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STUDY MATERIAL

EXECUTIVE PROGRAMME

**TAX LAWS**

MODULE 1

PAPER 4



**THE INSTITUTE OF  
Company Secretaries of India**

**भारतीय कम्पनी सचिव संस्थान**

**IN PURSUIT OF PROFESSIONAL EXCELLENCE**

Statutory body under an Act of Parliament

(Under the jurisdiction of Ministry of Corporate Affairs)

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# EXECUTIVE PROGRAMME

## TAX LAWS

This paper consists of two parts, namely Direct Tax and Indirect Tax. The tax that is levied directly on the income or wealth of a person is called direct tax. Indirect taxes were the taxes levied on goods and services on the basis of production, sale or purchase of goods or provision of services in the form of import and export duty, excise, customs, entertainment tax, electricity duty, tax on passenger fares and freight etc. and now Goods & Services Tax levies on supply of goods and/or services.

The purpose of this study material is to impart conceptual understanding to the students of the provisions of the Direct Tax Laws (Income Tax) and Indirect Tax Laws (GST and Customs) covered in the Syllabus. This study material has been published to aid the students in preparing for the Tax Laws paper of the CS Executive Programme. It is part of the educational kit and takes the students step by step through each phase of preparation stressing on key concepts, pointers and procedures. Company Secretaryship, being a professional course, the examination standards are set very high, with emphasis on knowledge of concepts, their applications, procedures under the tax laws and case laws therein, for which sole reliance on the contents of this study material may not be enough.

The subject of Tax Laws is inherently complicated and is subjected to constant refinement through new primary legislations, rules and regulations made thereunder, annual Budget and court decisions on specific legal issues. It therefore becomes necessary for every student to constantly update himself with the various changes made as well as judicial pronouncements rendered from time to time by referring to the Institute's journal 'Chartered Secretary' and 'Student Company Secretary e-bulletin' as well as other law/professional journals on tax laws. ICSI also brings out a monthly ICSI-GST Newsletter, dedicated solely to updates, current affairs and other reading material under the novel Goods and Services Tax regime.

Besides, as per the Company Secretaries Regulations, 1982, students are expected to be conversant with the amendments to the laws made upto six months preceding the date of examination.

The legislative changes made upto December 31st, 2019 have been incorporated in the study material. However, it may so happen that some developments might have taken place during the printing of the study material and its supply to the students. The students are therefore, advised to refer to the e-bulletin and other publications for updation of the study material.

In the event of any doubt, students may write to the Directorate of Academics of the Institute for clarification.

Although due care has been taken in publishing this study material, the possibility of errors, omissions and/or discrepancies cannot be ruled out. This publication is released with an understanding that the Institute shall not be responsible for any errors, omissions and/or discrepancies or any action taken in that behalf.

Should there be any discrepancy, error or omission noted in the study material, the Institute shall be obliged if the same is brought to its notice for issue of corrigendum in the e-bulletin 'Student Company Secretary'.

The study material contains a Model Test Paper at the end. This is for practice purpose only, and not to be sent to the institute.

Note: This study material is based on Finance Act, 2019 applicable for Assessment Year 2020-21 and is useful for students appearing in June, 2020 session onwards. The students are expected to update themselves from reference materials available on the Academic Corner and GST Corner of ICSI website. The students may also update themselves of the latest developments, notifications and circulars on Indirect Tax from *cbic.gov.in* and Direct Tax from *incometaxindia.gov.in*.

***The Institute has decided that the examination for this paper under new syllabus from December 2019 session will be conducted in Optical Mark Recognition (OMR) format.***

# EXECUTIVE PROGRAMME – TAX LAWS

The subject of Tax Laws at CS Executive Level is divided into two parts with equal weight age of marks.

- Part I – Direct Tax (50 Marks)
- Part II – Indirect Tax (50 Marks)

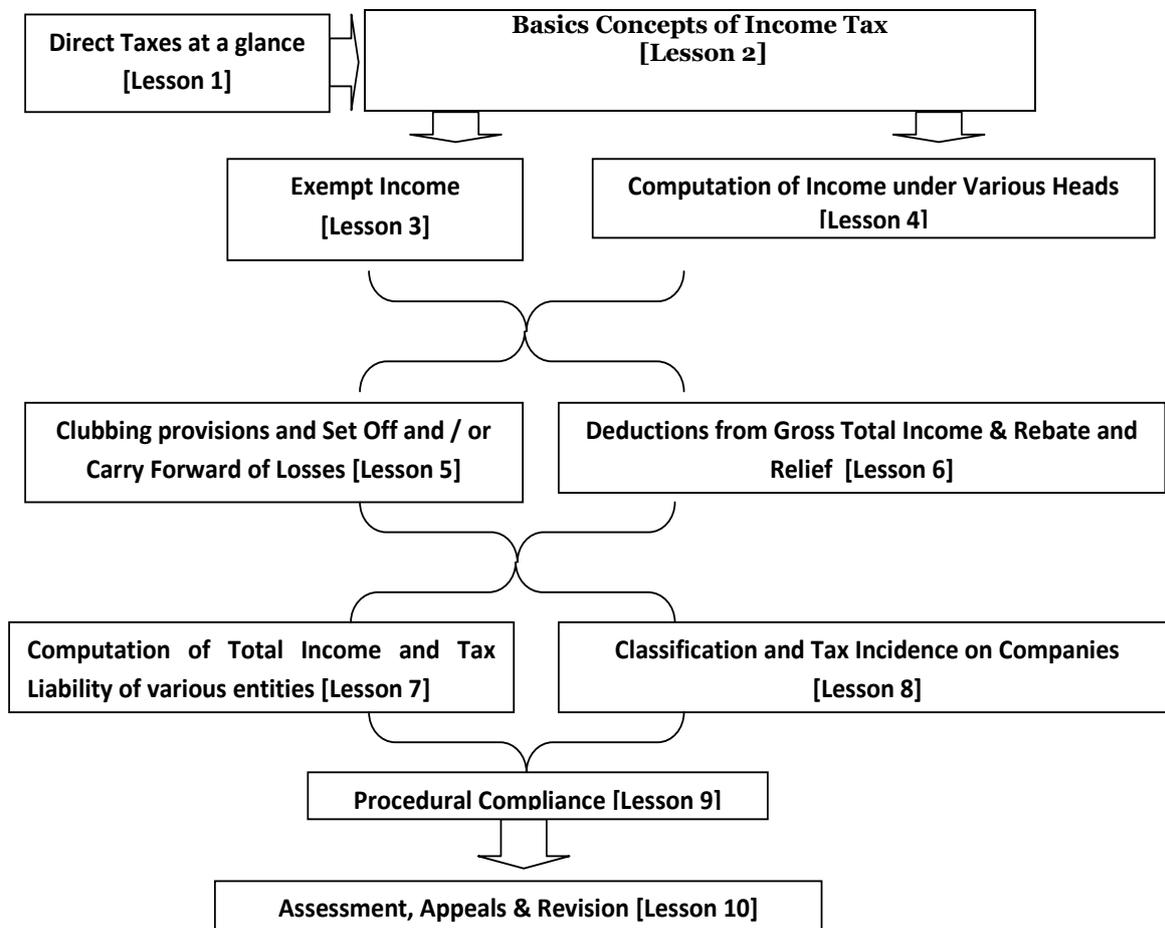
## PART I – DIRECT TAX (50 MARKS)

Income Tax Act, 1961 provides for levy, administration, collection and recovery of Income Tax. It provides progressive rate schedule, exemption limits, and incorporates number of incentive provisions. It provides sound tax system. Rate schedule & Exemption limits are prescribed by Finance Act.

Indian tax legislative and judicial environment is constantly evolving, along with globalization, economic shifts, and operational adjustments. Businesses are faced with a tax regime with greater complexities and challenges, nonetheless moving towards a globally cohesive tax world. Now, more than ever, businesses must have an ongoing system for adapting to and staying on top of these complex changes.

The tax laws of the country undergo significant changes every year on the passing of Annual Finance Act. Apart from the amendments coming out every year through the Finance Act, there are circulars / notifications issued by the CBDT / CBEC to implement the provision of the act, clarifying the scope of the provision.

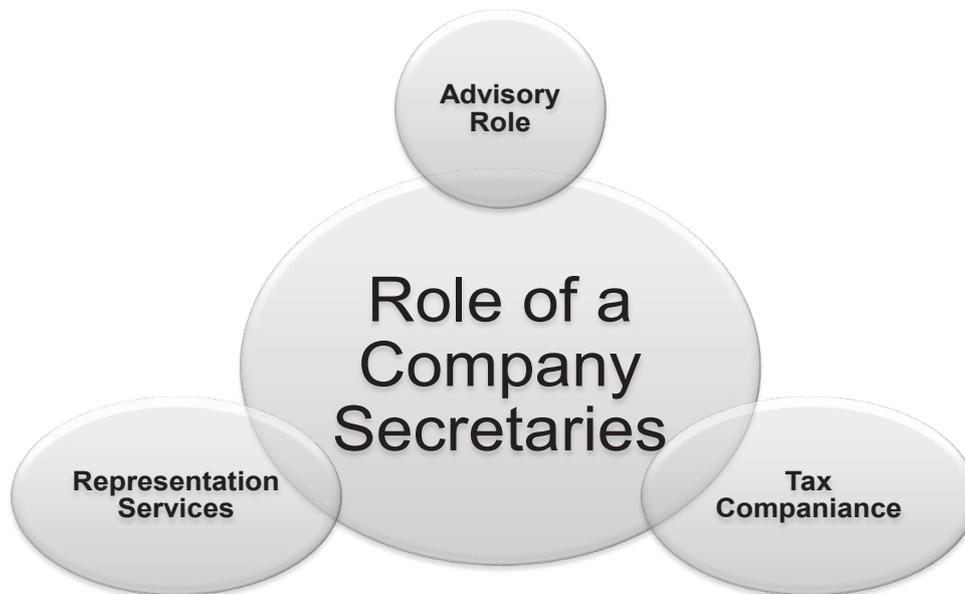
The part I of the study material is related to Direct Taxes and comprises of Total 10 lesson. The broad coverage of the lessons is summarized in the below chart.



## ROLE OF COMPANY SECRETARIES IN DIRECT TAX

The Company Secretaries as experienced tax professionals can assist in resolving various challenges such as keeping abreast with tax regulations, efficiently manage compliances, address uncertain tax positions, among many others. The Company Secretaries can provide with an insight into how to best work to meet the business needs.

The following are the key important areas under the direct tax regime where a Company Secretaries can play a vital role.



**Advisory** : Corporate taxation is an essential aspect of doing business in India and its importance cannot be undermined. The Company Secretaries can provide the corporate tax advisory services in the following areas:

- Establishing tax efficient Indian business presence for an MNC
- Assisting an entrepreneur in establishing business
- Expanding into new sectors
- Planning a heavy capital outlay in the existing business
- Addressing concerns about cash flow and examining tax inefficiencies
- Ensuring that the tax function is aligned with the business plan
- Assessing the impact of any tax and regulatory changes/ amendments

**Tax Compliance** : As the complexities of businesses increase, the amount of time spent by professionals in cracking up the law codes increases. However, tax and regulatory systems of even the most developed countries cannot keep pace with the developments across each industry as businesses emerge day by day. These also bring out the requirements for new compliances and the challenges of meeting them every single day. More detailed Income Tax Return forms including disclosures on tax residency certificates and details of foreign assets, and higher penalties for non disclosures require businesses to gear up for efficient tax compliance.

- Advising on withholding tax obligations on payments
- Obtaining no-objection certificates
- Assisting in filing various tax returns and making adequate disclosures.
- Tax diagnostic reviews

- Enhancing ERP systems to meet tax management requirements
- Tax implications on payments (local or overseas) to a host of parties
- Reporting of multilayered tax issues

**Representation Services** : The Company Secretaries can also represent the client before appellate authority at various levels.

- Representation before the income tax and withholding tax authorities
- Providing corporate tax litigation assistance, including representation services
- Obtaining advance rulings and opinion from senior counsels

**Note** : The Study material on Income tax Laws is based on the provisions of income tax law as amended by the Finance Act, 2019 and the significant circulars issued upto December 31, 2019. The computational / practical problems have been solved on the basis of the provisions of income tax laws applicable for AY 2020-21. The study material is relevant for the students for June, 2020 examinations onwards.

## PART II – INDIRECT TAX (50 MARKS)

Indirect taxes are the taxes levied on goods and services on the basis of production, sale or purchase of goods or provision of services, in the form of import and export duty, excise, sales tax, Value Added Tax (VAT), service tax, entertainment tax, electricity duty, tax on passenger fares and freights etc. They are called indirect taxes as the burden of tax is passed on to the consumer unlike direct taxes which are supposed to be borne by the persons on whom these taxes are levied.

Broadly, the earlier indirect tax regime can be looked at from the point of view of Central and State laws. For the Central Government, Central Excise, Customs and Service tax were the three main components of indirect taxes. Similarly, for the State Governments, Value Added Tax and Central Sales Tax were major taxes along with Octroi , Entertainment Tax etc.

The taxation reforms in India go back right from liberalization and globalization in the early 1990s to the recent Goods and Services Tax (GST). Goods and Services Tax is one of the most comprehensive single tax reforms of independent India. GST is a comprehensive indirect tax levied on goods as well as services at the national level. It consolidated multiple indirect tax levies into a single tax thus subsuming an array of tax levies. However, Basic Customs Duty continues to be levied on imports.



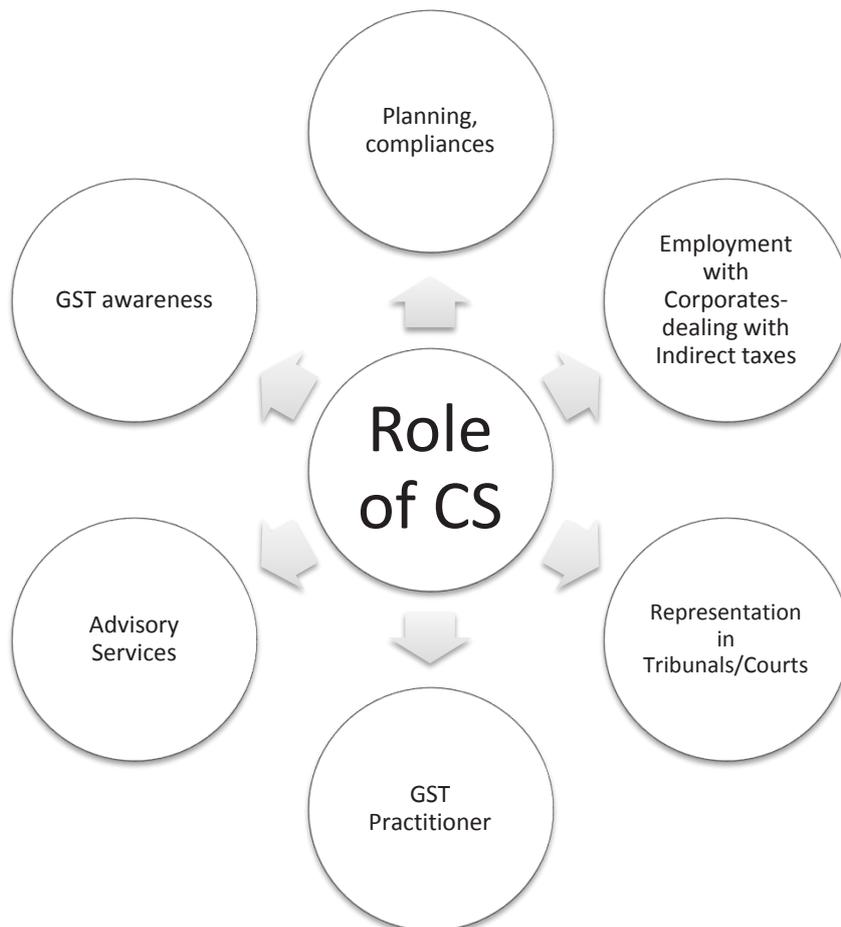
**GST consists of the following five Acts :**

- (1) Central Goods and Services Tax Act, 2017
- (2) Integrated Goods and Services Tax Act, 2017
- (3) State Goods and Services Tax Act, 2017
- (4) Union Territory Goods and Services Tax Act, 2017
- (5) Goods and Services (Compensation to States) Act, 2017

The study material broadly covers an overview of the GST Acts focusing upon the following key topics – Basics, Registration, Returns, Payments, Composition Scheme, Concept of Supply, Reverse Charge Mechanism and other aspects of GST. The purpose of this study material is to impart conceptual understanding to the students of the provisions of the novel indirect tax law along with an overview of provisions of Customs.

**GST and Opportunities Galore for Company Secretaries**

Company Secretaries, who practice in almost all the branches of law and possess a robust understanding on accounting, are competent professionals to handle the regulatory compliance under the GST laws. They are skilled professionals who understand legal, financial and compliance dimensions of business entity comprehensively. Company Secretaries are already acting as extended arms of the regulatory mechanism and are well equipped to partner in the tasks under GST Regime to facilitate the stakeholders in GST preparedness by extending their needful services.



## **GST and Governance Professionals-in-Making**

The students are expected to gear up to enhance their perceptive knowledge and involve in capacity building initiatives. They must make the best use of this opportunity to augment their professional ambit in future under indirect taxes. GST is subject to constant refinement through new rules and updated notifications as well as circulars. It is thus expected of the student to be regularly updated about the developments taking place under the Law.

**Note:** The study has been updated till December 31, 2019. The students are expected to update themselves from reference materials available on the Academic Corner and GST Corner of ICSI website. The students may also update themselves of the latest developments, notifications and circulars of GST from [cbic.gov.in](http://cbic.gov.in).

# EXECUTIVE PROGRAMME

## Module 1

### Paper 4

## Tax Laws (Max Marks 100)

### SYLLABUS

#### Objective

**Part I :** To provide working knowledge on practical application of Direct Tax Laws.

**Part II :** To provide conceptual knowledge of GST with practical application of GST Laws.

#### PART I: DIRECT TAXES (50 MARKS)

##### Detailed Contents

- 1. Direct Taxes at a Glance :** Background of Taxation system in India; Vital Statistics; Layout; Administration.
- 2. Basic concepts of Income Tax :** An overview of Finance Bill, ; Important definitions under Income Tax Act, 1961; Distinction between Capital and Revenue Receipts and Expenditure; Residential Status & Basis of Charge; Scope of Total Income; Tax Rates.
- 3. Incomes which do not form part of Total Income :** Incomes not included in Total Income; Tax holidays.
- 4. Computation of Income under Various Heads :** Income from Salary; Income from House Property; Profit and Gains of Business or Profession; Capital Gains; Income from Other Sources; Fair Market Value.
- 5. Clubbing provisions and Set Off and / or Carry Forward of Losses :** Income of other persons included in Assessee's Total Income; Aggregation of Income; Set off and / or Carry forward of losses.
- 6. Deductions from Gross Total Income & Rebate and Relief :** Deductions in respect of certain payments; Specific deductions in respect of certain income; Deductions in respect for donations for expenditure under CSR activities; Rebates and Reliefs.
- 7. Computation of Total Income and Tax Liability of various entities :** Individual; Hindu Undivided Family 'HUF'; Alternate Minimum Tax (AMT); Partnership Firm / LLP; Co-operative Societies; Association of Person 'AOP' and Body of Individual 'BOI'; Political Parties; Electoral Trusts; Exempt organization – Registration u/s 12A/ 12AA;
- 8. Classification and Tax Incidence on Companies :** Computation of taxable income and tax liability of Company; Dividend Distribution Tax; Minimum Alternate Tax 'MAT'; Other Special Provisions Relating to Companies; Equalization Levy.

9. **Procedural Compliance** : Permanent Account Number 'PAN' / Tax Collection Account Number 'TAN'; Tax Deduction at Source 'TDS' & Tax Collection at Source 'TCS'; Advance Tax & Self Assessment Tax 'SAT'; Returns, Signatures, E-Filing ; Fee and interest for default in furnishing return of Income ; Collection, Recovery of Tax, Refunds.
10. **Assessment, Appeals & Revision** : Assessment; Types of Assessment; Appeals; Revisions; Search, Seizure, Penalty and Offences.

**Case Laws, Case Studies & Practical Aspects.**

**PART II: INDIRECT TAXES (50 MARKS)**

**(A) Goods and Service Tax**

11. **Concept of Indirect Taxes at a glance** : Background; Constitutional powers of taxation; Indirect taxes in India – An overview; Pre-GST tax structure and deficiencies; Administration of Indirect Taxation in India; Existing tax structure.
12. **Basics of Goods and Services Tax 'GST'** : Basics concept and overview of GST; Constitutional Framework of GST; GST Model – CGST / IGST / SGST / UTGST; Taxable Event; Concept of supply including composite and mixed supply; Levy and collection of CGST and IGST; Composition scheme & Reverse Charge; Exemptions under GST.
13. **Concept of Time, Value & Place of Taxable Supply** : Basic concepts of Time and Value of Taxable Supply; Basics concept of Place of Taxable Supply.
14. **Input Tax Credit & Computation of GST Liability- Overview.**
15. **Procedural Compliance under GST** : Registration; Tax Invoice, Debit & Credit Note, Account and Record, Electronic way Bill; Return, Payment of Tax, Refund Procedures; Audit.
16. **Basic overview on Integrated Goods and Service Tax (IGST), Union Territory Goods and Service tax (UTGST), and GST Compensation to States.**

**(B) Customs Act**

17. **Overview of Customs Act** : Overview of Customs Law; Levy and collection of customs duties; Types of Custom duties; Classification and valuation of import and export goods; Exemption; Officers of customs; Administration of Customs Law; Import and Export Procedures; Transportation, and Warehousing; Duty Drawback; Demand and Recovery; Confiscation of Goods and Conveyances; Refund.

**Case Laws, Case Studies & Practical Aspects.**

# LESSON WISE SUMMARY

## TAX LAWS

### PART I – DIRECT TAX

#### Lesson 1 [Direct Taxes - At a Glance]

In the present time, taxation is not just a means of transferring money to the government to spend it for meeting the public expenditures or raise revenue to the government, but taxes have become beside that, as a tool for redistribution of income and wealth in the society. It also serves as a means of economic development and plays a significant role in stabilization of income. Taxation assist in finding solutions to the economic problems which are faced by a country, like unemployment, inflation, and depression. Countries practice sovereignty authority upon its citizens, through levying of Taxes.

The coverage of the lesson would include:

- Taxes – Types of taxes and its characteristics, objectives
- The Canons of Taxes
- Direct v/s Indirect Taxation
- The Background of Indian Taxation System and its structure
- Tax Administration
- The Vital Statistics and Layout of Tax

#### Lesson 2 [Basic Concepts of Income Tax]

Taxes are broadly divided into two parts i.e. direct taxes and indirect taxes. The tax that is levied directly on the income or wealth of a person is called direct tax. Income tax is one of the forms of direct taxes. The levy of income tax in India is governed by the Income Tax Act, 1961 and Income Tax Rules, 1962. It is charged on the Total Income and to derive the total income one must know certain concepts of the Income Tax Act, such as residential status, assessment year, previous year, assessee etc.

Income tax is leviable on the taxable income and to determine taxable income, ascertainment of the residential status of the person and scope of total income are required at an initial level. There are two types of taxpayers from residential point of view - Resident in India and Non-resident in India. Sourced based income in India is taxable in India whether the person earning income is resident or non-resident. Conversely, foreign sourced income of a person is taxable in India only if such person is resident in India. Therefore, the determination of the residential status of a person is very significant in order to find out his / her tax liability.

The coverage of the lesson would include:

- Overview of Finance Bill
- Some basic concepts like assessment year, previous year, income, person, assessee,
- Distinguish between capital and revenue receipts etc.
- Basic steps in the calculation of tax liability.

- Be able to determine the residential status of a person
- Be aware of the importance of residential status for tax purposes
- The scope of total income
- The rates of tax

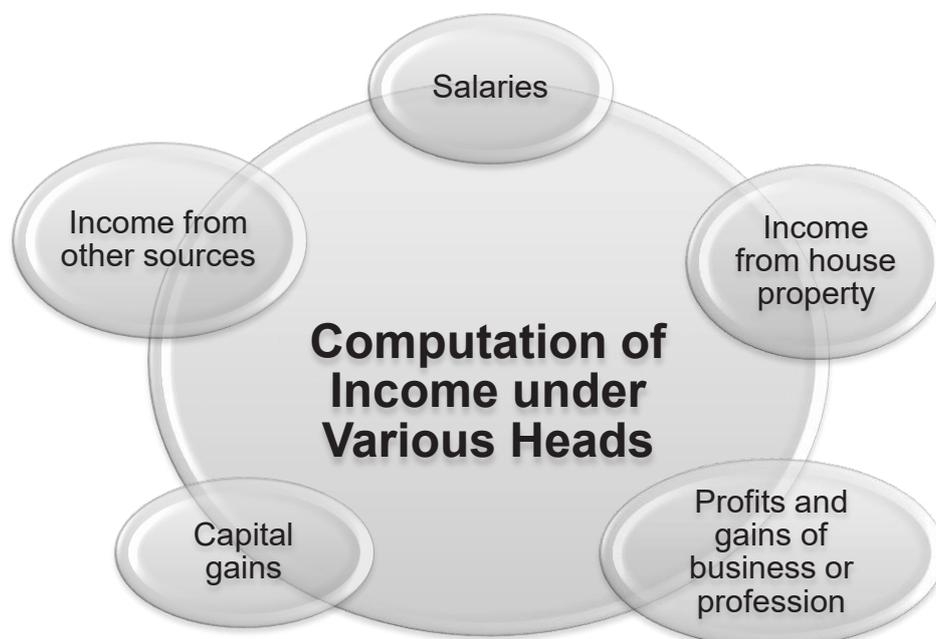
### Lesson 3 [Incomes which do not form Part of Total Income]

Tax is calculated on the income earned in the previous year. For providing relief to the tax payers from payment of tax, income tax law contains certain provisions relating to exemption and deduction. Exempted income means the income which is not charged to tax. Under Income Tax Act, section 10 provides for incomes which are exempted from levy of income tax for example Scholarship etc. Further, deduction means the amount which needs to be included in the income first and then they are allowed for deduction in full or in part on fulfillment of certain conditions. For example, deduction for payment of donations under section 80G. This lesson deals with incomes which do not form part of total income.

### Lesson 4 [Computation of Income under Various Heads]

The taxability of income of a person depends on the chargeability of such income under the Income tax Act 1961. The total income of an assessee (subject to statutory exemptions) is chargeable under Section 4(1). The scope of the total income, which varies with the residential status, is defined in Section 5. Section 14 enumerates the heads of income under which the income of an assessee will fall. The rules for computing income and the permissible deductions under different heads of income, are dealt in different sections of the Act.

The coverage of the lesson includes the heads of income (as mentioned below), along with their corresponding set of sections for the purpose of computation of income.



### Lesson 5 [Clubbing provisions and Set Off and / or Carry Forward of Losses]

In addition to the general provisions which are applicable for computation of total income, there are special provisions in Sections 60 to 65 of the Income-tax Act which provide for inclusion of income of other persons in the total income of assessee. The special provisions contained in these sections are designed

to counteract the various attempts of an individual for avoiding or reducing his liability to tax by transferring his assets or income to other person(s) while, at the same time, retaining certain powers or interest over the property or it's income. These provisions may also be termed as clubbing provisions and are covered under first part of the lesson. In the second part of this lesson provisions for set-off and carry forward of losses are discussed.

### Lesson 6 [Deductions from Gross Total Income & Rebate and Relief]

The aggregate of income computed under each head, after giving effect to the provisions for clubbing of income and set off of losses, is known as "Gross Total Income". Sections 80C to 80U of the Income-tax Act lay down the provisions relating to the deductions allowable to assesseees from their gross total income.

The coverage of the lesson would include:

- The type of deductions allowable from gross total income
- The permissible deductions in respect of payments
- The permissible deductions in respect of incomes
- Deductions allowable in the case of a person with disability.
- The provision related to Rebate & Relief

### Lesson 7 [Computation of Total Income and Tax Liability of various entities]

For calculation of income, amount received is classified under 5 heads of income; it is then to be adjusted with reference to the provisions of the Income Tax laws in the following manner.

Particulars	Amount (Rs.)
Income under the head:	
Income from Salaries	XXX
+ Income from House Property	XXX
+ Profits and gains of business or profession	XXX
+ Capital gains	XXX
+ Income from other sources	XXX
<b>Adjustment in respect of:</b>	
+ Clubbing of Income	XXX
– Set off and carry forward of losses	(XXX)
<b>= Gross Total Income</b>	<b>XXX</b>
– Deductions under section 80C to 80U (or Chapter VIA)	<u>(XXX)</u>
<b>= Total Income</b>	<b>XXX</b>

The coverage of the lesson would include the Income Tax Treatment with relation to Individual, Hindu Undivided Families (HUF), Firms, Associations of Persons and Cooperative Societies is being discussed. The tax implications, rates of tax and other issues relating to the above persons have been discussed elaboratory.

## **Lesson 8 [Classification and Tax Incidence on Companies]**

In the previous lessons we have learn the tax provisions of persons not being the company. Here, we will go through the income tax provisions of corporate entity.

The coverage of the lesson would include:

- The constitutional provisions for companies with regard to income tax,
- Domestic and Foreign companies,
- Provisions of Minimum Alternate Tax
- Dividend distribution tax
- Provision related to Equalization Levy
- Specific provisions related to,
  - Buyback of Shares Listed on Recognized Stock Exchange
  - Conversion of an Indian Branch of a foreign company into an Indian subsidiary company
  - Tax on Income distributed by specified company or Mutual Fund
  - Taxation aspects related to Conversion of Company into an LLP
  - Tax liability of company in the event of liquidation
  - Taxation of Share Premium
  - Taxation aspects of Amalgamation, Mergers and De-mergers

## **Lesson 9 (Procedural Compliance)**

The Income-tax Act provides for collection and recovery of income-tax in the following ways, namely:

- Deduction of tax at source
- Advance payment of Tax
- Self-assessment of Tax
- Payment made after the assessment of Tax.

Once the tax is deducted, it is duty to deposit the same to the credit of the Central Government under prescribed procedures stated under the Income Tax Act, 1961. In this chapter TDS related aspects of the Income Tax Act have been discussed at length with special emphasis on e-TDS and other relevant issues.

The coverage of the lesson would include

- The provisions related to tax deducted at source and tax collected at source
- The rates of Tax Deduction at Source 'TDS' and Tax Collection at Source 'TCS'
- The due dates for payment of TDS and TCS and Advance Tax
- The provision related to Returns, E-Filing, Signature
- Fee and Interest

## **Lesson 10 (Assessment, Appeals and Revision)**

The provisions of the Income-Tax Act contained in Sections 117 to 136 specify the procedure relating to the appointment of the various income-tax authorities, their powers, functions, jurisdiction and control. The procedure under the Income-tax Act for making an assessment of income begins with the filing of a return of income. Section 139 of the Act contains the relevant provisions relating to the furnishing of a return of income. On the basis of return of income the income tax authority makes the assessment.

The coverage of the lesson would include

- The various income-tax authorities, their powers, functions, jurisdiction and control.
- The types of assessment

The Income-tax Act provides for various remedies to an assessee on completion of the assessment. The main remedies available to an assessee on completion of the assessment are Appeals, Revision, and Rectification. All these remedies work in different areas. However, strictly speaking the remedies are not alternative to each other but at times more than one remedial proceeding may be used as complimentary to each other so as to achieve the best results.

The right to appeal arises where the taxpayer is aggrieved by the order passed by the income-tax authority. The coverage of the lesson would also include :

- The provisions for filing of appeal.
- The procedure to file an application before the appellate authority.
- The provisions related to offence and penalties

## **PART II – INDIRECT TAXES**

### **Lesson 11: Concept of Indirect Taxes at a glance**

Chapter 11 contains the Constitutional powers of taxation and an overview of indirect taxes in India along with pre GST tax structure and its shortcomings. It also lays an overview of administration of indirect taxation in India and the Existing tax structure.

Erstwhile indirect taxes consisted of various laws at Central and State level including VAT, Excise, Service Tax etc. which had some challenges that were required to be addressed like multiplicity of taxes and their cascading effects.

Goods & Services Tax brought a single tax regime which got levied on supply of goods or services or both thereby overcoming the gaps of previous indirect tax laws. Various Constitutional amendments have been made to enable Centre and States to levy GST simultaneously and new Articles got inserted.

### **Lesson 12: Basics of Goods and Services Tax**

The chapter covers basics of GST and GST models including CGST / IGST / SGST / UTGST, supply which is the taxable event under GST. It is to be noted that supply can be of two types i.e., composite and mixed supply. In a composite supply, the goods are naturally bundled. The chapter contains the levy and collection of CGST and IGST under the GST Law and broad rates prescribed therein.

Composition scheme is a scheme wherein GST is not collected from the recipients / customers subject to a prescribed threshold turnover. In a composition levy, the supplier cannot himself take Input Tax Credit. Under Reverse Charge, the recipient pays the GST on the supply on behalf of the supplier. Exemptions under GST may be by General or by Special Order.

### **Lesson 13: Concept of Time, Value & Place of Taxable Supply**

The chapter comprises of basic concepts of Time and Value of Taxable Supply. Taxable event is the point which gives rise to taxability and the point of levy is determined by time of supply and thus value of supply determines value on which GST is payable. Valuation includes determining the value on which GST is payable by following the Valuation Rules and principles, contained in the GST law.

Basic concepts of Place of Taxable Supply include intra state and interstate supply as well as determining the place of supply under various situations. When the location of supplier and the place of supply are within the same state, it is an Intra-State Supply, and if these are in different states, then it is Inter-State supply.

### **Lesson 14: Input Tax Credit & Computation of GST Liability – Overview**

Integrated GST, Central GST, State GST or Union Territory GST paid on inward supply of inputs, capital goods and services are called input taxes and its credit is Input Tax Credit (ITC). Company which distributes the input tax credit to various units on the basis of their previous year turnover is called input service distributor. There is no offset of ITC available between the CGST and the SGST.

GST is a consumption based tax levied on the basis of the “Destination principle.” It is an inclusive tax regime covering both goods and services, to be collected on value-added at each stage of the supply chain.

### **Lesson 15: Procedural Compliance under GST**

Procedural Compliances include the terms for eligibility of compulsory and voluntary Registration and the persons exempt from Registration and procedure thereby. The Chapter explains the concept of Tax Invoices, Debit & Credit Note including cases where Delivery Challan or Bill of Supply is needed instead.

The Act prescribes the Accounts and Records that an assessee should maintain. Electronic way Bills have been introduced under the GST Law for movement of goods. Under GST, various monthly, quarterly and annual returns are filed. Payment can be made via NEFT, RTGS, net banking, debit /credit card. The law prescribes two types of Audit under GST - General and Special. Refund Procedures are contained in the given Chapter.

### **Lesson 16: Basic overview on Integrated Goods and Service Tax (IGST), Union Territory Goods and Service tax (UTGST), and GST Compensation to States**

The President of India gave assent to the following four Acts, related to GST:

- Central Goods & Services Tax Act,2017
- Integrated Goods & Services Tax Act,2017
- Union Territory Goods & Services Tax Act,2017
- Goods & Services Tax (Compensation to States) Act,2017

Apart from these, every State has its own State GST Act. Delhi and Puducherry are two Union Territories but UTGST Act, governing GST for Union Territories shall not be applicable there as they have their own State Legislature and Government. State GST would be applicable in their case.

IGST Act, 2017 governs Integrated Goods & Services Tax, which is levied and collected by the Centre on inter-state supply of goods and services including imports into India and supplies made outside India along with supplies to / from SEZs.

The GST (Compensation to States) Act, 2017 ascertains the amount of compensation that shall be payable by the Government to states during the transition period of five years due to the revenue loss owing to levy of

Goods and Services Tax. The Act provides for calculation and ascertainment of base year, projected growth rate, compensation to be paid etc.

**Lesson 17: Overview of Customs Act**

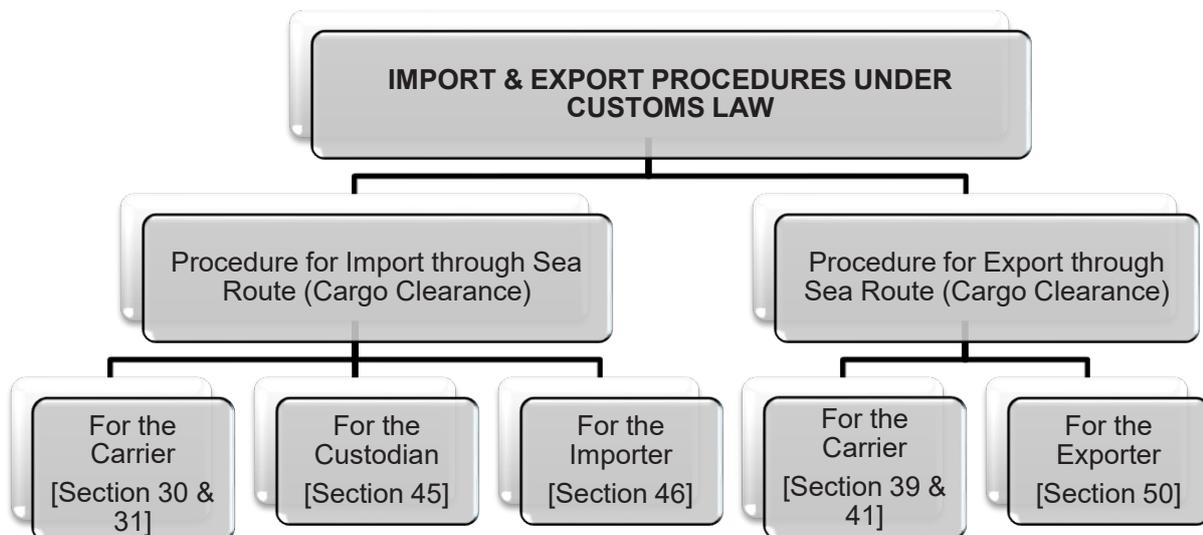
With the implementation of GST Law, the Basic Customs Duty is still levied on imports with other additional duties being subsumed under GST.

The basic and overview of Customs Act is contained in Chapter 17 which consists of provisions for levy and collection of customs duties and its types, Classification and valuation of import and export goods alongwith exemptions, administration of Customs Law including Officers under the Law. Valuation Rules are explained.

**Interpretation Rules under the Customs Tariff Act, 1975**



The Chapter also consists of Import and Export Procedures, provisions for Transportation and Warehousing and Duty Drawback. The Chapter states the conditions for Confiscation of Goods and Conveyances and procedures for Refund and Demand as well as Recovery.



## LIST OF RECOMMENDED BOOKS

### PAPER 4 – TAX LAWS

#### DIRECT TAX

##### READINGS

1. Mahendra B. Gabhawala: Direct Tax Ready Reckoner with Tax Planning
2. Bharat's Law House : Income Tax Act
3. Bharat's Law House : Income Tax Rules
4. Taxmann's : Income Tax Act
5. Taxmann's : Income Tax Rules
6. Dr. Vinod K. Singhania : Direct Taxes Law and Practice  
& Dr. Kapil Singhania
7. Dr. Girish Ahuja & : Direct Taxes Ready Reckoner with Tax Planning  
Dr. Ravi Gupta

#### INDIRECT TAX

##### READINGS

1. Dr. Sanjiv Agarwal : Goods & Services Tax, Laws, Concepts and Impact Analysis, Bloomsbury  
& Sanjeev Malhotra
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# ARRANGEMENT OF STUDY LESSON

Module-1 Paper-4

## TAX LAWS

### PART I (DIRECT TAX)

<b>S.No.</b>	<b>Lesson Tittle</b>
1.	Direct taxes – At a glance
2.	Basic concept of income tax
3.	Incomes which do not form part of total income
4.	Computation of income under various heads
5.	Clubbing provisions and set off and / or carry forward of losses
6.	Deductions from gross total income & rebate and relief
7.	Computation of total income and tax liability of various entities
8.	Classification and tax incidence on companies
9.	Procedural compliance
10.	Assessment, appeals & revision

### PART II (INDIRECT TAX)

11.	Concept of Indirect Taxes at a glance
12.	Basics of Goods and Services Tax 'GST'
13.	Concept of Time, Value & Place of Taxable Supply
14.	Input Tax Credit & Computation of GST Liability – Overview
15.	Procedural Compliance under GST
16.	Basic overview on Integrated Goods and Service Tax (IGST), Union Territory Goods and Service tax (UTGST), and GST Compensation to States
17.	Overview of Customs Act

# CONTENTS

## DIRECT TAX (PART I)

### LESSON 1

#### DIRECT TAXES – AT A GLANCE

Taxes - An Introduction	2
Characteristics of Taxes	4
Canons of Taxes	5
Objectives of Taxation	6
Direct Vs Indirect Taxes	8
Background of Taxation System in India	11
Tax Structure in India	12
Administration	13
Vital Statistics and Layout	14
SELF TEST QUESTIONS	16

### LESSON 2

#### BASIC CONCEPT OF INCOME TAX

Introduction	20
An Overview of Finance Bill	20
Heads of Income [Section 14]	22
Important Concepts	22
Assessee [Section 2(7)]	24
Assessment Year [Section 2(9)]	25
Previous Year [Section 3]	26
India [Section 2(25A)]	26
Maximum Marginal Rate and Average Rate of Tax	26
Income [Section 2(24)]	27
Capital and Revenue Receipts	30
Charge of Income Tax [Section 4]	33
Residential Status [Section 6]	34
Test of Residency for Individuals	34

Tests of Residence for Hindu Undivided Families	40
Test of Residence for Companies	42
Test of Residence for Firm and AOP	47
Meaning and Scope of Total Income [Section 5]	48
Income deemed to accrue or arise in India [Section 9]	51
Computation of Taxable Income and Tax Liability of an Assessee	60
Tax Rates For FY 2019-20 i.e. AY 2020-21	61
Case Laws	65
LESSON ROUND UP	65
SELF TEST QUESTIONS	67

### **LESSON 3**

#### **INCOMES WHICH DO NOT FORM PART OF TOTAL INCOME**

Background	72
Incomes which do not Form Part of Total Income	72
Summary Chart	99
LESSON ROUND UP	100
SELF TEST QUESTIONS	100

### **LESSON 4**

#### **COMPUTATION OF INCOME UNDER VARIOUS HEADS PART I – INCOME UNDER THE HEAD “SALARIES”**

Introduction	107
Basis of Charge	108
Salary [Section 17(1)]	109
Allowances	109
Retirement Benefits	113
Profits in lieu of Salary	116
Provident Funds - Treatment of Contributions to and Money Received From the Provident Fund	123
Deductions from Salary	126
Computation of Salary	126
Case Law	132
LESSON ROUND UP	133
SELF-TEST QUESTIONS	134

## LESSON 4

### PART II – INCOME UNDER THE HEAD HOUSE PROPERTY

Basis of Charge [Section 22]	138
Determination of Annual Value	138
Deductions from Net Annual Value (Section 24)	146
Deemed Ownership	150
House Property Incomes – Exempted From Tax	150
Case Law	155
LESSON ROUND UP	156
SELF-TEST QUESTIONS	157

## LESSON 4

### PART III – PROFIT AND GAINS FROM BUSINESS / PROFESSION

Business' or 'Profession'	162
Income Chargeable To Tax under the Head Business or Profession (Section 28)	162
Speculation Business	163
Computation of Profits of Business or Profession	168
Computation of Income under the Head "Profits and Gains from Business or Profession"	168
Admissible Deductions	169
Expenses Disallowed (Section 40)	193
Expenses Restricted	196
Deemed Profits	201
Special Provision In Case of Income of Public Financial Institutions, Etc. (Section 43D)	203
Special Provisions Related To Insurance Business (Section 44)	203
Compulsory Maintenance of Books of Account (Section 44AA)	204
Compulsory Audit of Books of Account (Section 44AB)	204
Special Provision for Computing Profits and Gains of Business on Presumptive Basis (Section 44AD)	205
Presumptive Taxation for Professionals [Section 44ADA]	206
Special Provisions for Computing Profits and Gains of Business of Plying, Hiring or Leasing Goods Carriages [Section 44AE]	206
Questions and Answers	207
Annexure	212
Case Law	219
LESSON ROUND UP	222
SELF TEST QUESTIONS	223

**LESSON 4**  
**PART IV – INCOME FROM CAPITAL GAINS**

Capital Gains	226
Capital Asset [Section 2(14)]	227
Short-Term & Long-Term Assets	228
Transfer [Section 2(47)]	230
Mode of Computation	236
Ascertainment of Cost in specified circumstances [Section 49]	240
Advance Money Received [Section 51]	248
Exemption of Capital Gains	249
Tax Rates	256
Case Law	260
LESSON ROUND UP	262
SELF TEST QUESTIONS	262

**LESSON 4**  
**PART V – INCOME FROM OTHER SOURCES**

Basis of Charge of Income from Other Sources [Section-56]	266
Casual Income [Section 56(2)(1b)]	270
Income from Family Pension	271
Taxation of Dividends	271
Deductions Allowable In Computing Income from Other Sources	274
Amounts Not Deductible [Section 58]	275
Deemed Income [Section 59]	275
Case Law	277
LESSON ROUND UP	278
SELF TEST QUESTIONS	278

**LESSON 5**  
**CLUBBING PROVISIONS AND SET OFF AND / OR CARRY FORWARD OF LOSSES**

Clubbing of Income	282
Transfer of Income [Section 60]	282
Revocable Transfer of Assets [Section 61]	283

Income of Spouse	284
Income From Assets Transferred To Son's Wife [Section 64(1)(vi)]	286
Transfer For Immediate Or Deferred Benefit Of Son's Wife [Section 64(1)(viii)]	286
Income to Spouse Through A Third Person [Section 64(1)(vii)]	287
Clubbing of Income of Minor Child [Section 64(1A)]	287
Income from the Converted Property [Section 64(2)]	287
Recovery of Tax	290
Set-Off and Carry-Forward of Losses	292
Carry-Forward of Losses	295
Carry Forward and Set-Off Of Accumulated Business Loss and Unabsorbed Depreciation in Certain Cases of Amalgamation or Demerger Etc. [Section 72A]	298
Carry Forward and Set Off Of Accumulated Loss and Unabsorbed Depreciation Allowance in Scheme of Amalgamation of Banking Company in Certain Cases [Section 72AA]	301
Treatment of Carry-Forward of Losses of Certain Assessees	301
Submission of Return for Loss [Section 80]	302
Summary of provisions regarding carry forward and set-off of losses	303
LESSON ROUND UP	304
SELF TEST QUESTIONS	306

## LESSON 6

### DEDUCTIONS FROM GROSS TOTAL INCOME, REBATE AND RELIEF

Introduction	310
Deductions	313
Illustration	338
Relief and Rebate	348
Case Law	352
LESSON ROUND UP	352
SELF TEST QUESTIONS	354

## LESSON 7

### COMPUTATION OF TOTAL INCOME AND TAX LIABILITY OF VARIOUS ENTITIES

Introduction	358
Taxation of Individuals	359
Taxation of Hindu Undivided Families	366

Computation of Income of HUF	369
Taxation of Firms	374
Alternate Minimum Tax (AMT) [Section 115JC]	379
Taxation of Association of Persons /Body of Individuals	390
Taxation of Co-Operative Societies	393
Tax Exemptions to Political Parties (Section 13A)	400
Electoral Trust	401
Tax Exemptions for Charitable Trusts and Institutions	401
LESSON ROUND UP	411
SELF TEST QUESTIONS	412

## LESSON 8

### CLASSIFICATION AND TAX INCIDENCE ON COMPANIES

Background & Types of Companies	416
Tax Incidence under Income Tax Act, 1961	419
Minimum Alternate Tax (MAT)	421
Mat Credit [Section 115JAA]	432
Dividend Distribution Tax [Section 115-O]	437
Carbon Credit [Section 115BG]	440
Buy-Back of Shares	440
Conversion of an Indian Branch of a Foreign Company into an Indian Subsidiary Company	442
Tax on Income Distributed by Specified Company or Mutual Fund	443
Equalization Levy	444
Taxation Aspects Related To Conversion of Company into an LLP	446
Tax Liability of Companies in the Event of Liquidation	448
Taxation of Share Premium	449
Taxation Aspects of Amalgamations, Mergers and Demergers	451
LESSON ROUND UP	453
SELF TEST QUESTIONS	454

## LESSON 9

### PROCEDURAL COMPLIANCE

Permanent Account Number [Section 139A]	458
Tax Deduction Account Number (TAN)	461

Tax Deducted At Source (TDS)	463
Tax Collection At Source (TCS) [Section 206C]	482
Time limit for the payment of TDS to the Government	483
TDS Forms	485
TDS Chart FY 2019-20 “AY 2020-21”	486
Minimum Threshold Limit Upton Which TDS not Applicable	493
Advance Payment of Tax	495
Self-Assessment Tax (SAT)	500
Returns	501
Signing of Return [Section 140]	507
Fee and Interest	508
Collection and Recovery of Tax	511
Refunds (Section 237 to Section 245)	512
Case Laws	515
LESSON ROUND UP	516
SELF TEST QUESTIONS	517

## LESSON 10

### ASSESSMENT, APPEALS & REVISION

Income-Tax Authorities (Appointment, Jurisdiction and Powers) [Section 116]	520
The Central Board of Direct Taxes (CBDT)	521
Commissioner of Income-Tax (Appeals)	527
Assessment	529
Appeal	539
Introduction	539
Appeals Orders before Commissioner (Appeals)	540
Procedure for Filing of Appeal [Section 249(1)]	541
Period of Limitation to Prefer an Appeal [Section 249(2)]	541
Payment of Tax before Filing Appeal [Section 249(4)]	542
Procedure in Appeal [Section 250]	543
Powers of the Commissioner (Appeals) [Section 251]	543
Revisions	544
Revision by the Commissioner of Income Tax [Sections 263 And 264]	544
Revision of orders prejudicial to the interest of Revenue [Section 263]	544

Revision of order in the interest of Assessee [Section 264]	547
Circumstances in Which No Revision can be Made [Section 264(4)]	548
Appellate Tribunal [Section 252]	549
Appealable Orders [Section 253(1) AND (2)]	549
Procedure For Filing Appeal [Section 253(3), (4)&(6)]	550
Order of Appellate Tribunal [SECTION 254]	551
Procedure of Appellate Tribunal [SECTION 255]	553
Appeal to High Court	553
Appeal to the Supreme Court [Section 261]	554
Offences and Penalties	556
Offences and Prosecution	565
LESSON ROUND UP	567
SELF TEST QUESTIONS	569

## LESSON 11

### CONCEPT OF INDIRECT TAXES AT A GLANCE

Background	572
Constitutional Powers of Taxation	572
Constitution Amendment Act, 2016	573
Goods and Services Tax Council	576
Compensation to States for deficit in Tax collections	579
Power to Remove Difficulties	579
Indirect Taxes in India – An Overview	580
Pre GST Tax Structure & Deficiencies	582
Administration of Indirect Taxation in India	584
Administrative Mechanism at the Central Level	585
Existing Tax Structure	585
LESSON ROUND UP	591
SELF TEST QUESTIONS	591

## LESSON 12

### BASICS OF GOODS AND SERVICES TAX

Basic Concepts and Overview Of Goods and Services Tax	594
GST MODEL	594

Constitutional Framework of Goods & Services Tax	595
Taxable Event	597
Concept of Supply	597
Levy & Collection of Tax	602
Composition Scheme	602
Liability to pay GST	609
Exemptions Under Goods & Services Tax	609
LESSON ROUND UP	612
SELF TEST QUESTIONS	612

### **LESSON 13**

#### **CONCEPT OF TIME, VALUE AND PLACE OF TAXABLE SUPPLY**

Concept of Supply	614
Place of Supply	616
Time of Supply	621
Value of Taxable Supply [Section 15 of CGST Act, 2017]	628
Valuation Rules : Chapter IV, CGST Rules, 2017	630
LESSON ROUND UP	636
SELF TEST QUESTIONS	636

### **LESSON 14**

#### **INPUT TAX CREDIT AND COMPUTATION OF GST LIABILITY**

Input Tax Credit	640
Goods Sent To Job Worker	652
Input Service Distributor	655
LESSON ROUND UP	661
SELF TEST QUESTION	662

### **LESSON 15**

#### **PROCEDURAL COMPLIANCE UNDER GST**

Registration	664
Tax Invoices, Debit & Credit Notes	683
Rules for Tax Invoices, Debit & Credit Notes	687

Accounts and Records	695
Electronic Way Bills	697
Returns	698
Payments	701
Payment Rules [Chapter IX]	704
Refunds	708
Audit	712
LESSON ROUND UP	714
SELF TEST QUESTIONS	715

## LESSON 16

### BASIC OVERVIEW ON IGST, UTGST AND GST COMPENSATION TO STATES ACT

Introduction to IGST	718
Integrated Goods & Services Tax Act, 2017	718
Introduction to Union Territory Goods & Services Tax Act, 2017	723
Applicability of the UTGST ACT, 2017	723
Administration & Powers of Officers [Section 4, 5 & 6]	725
Levy and Collection of UTGST [Section 7]	725
Exemption From GST [Section 8]	726
Payment of Tax [Section 9]	726
Input Tax Credit on Input Stocks [Section 18]	728
Input Tax Credit: Taxable as well as Exempted Goods	728
Switch Over from Composition Levy	729
Advance Ruling [Section 14 of UTGST Act, 2017]	729
Constitution of Authority for Advance Ruling [Section 15]	730
Constitution of Appellate Authority For Advance Ruling [Section 16]	730
Miscellaneous	730
Power to Make Rules [Section 22]	731
General Power To Make Regulations [Section 23]	731
Laying of Rules, Regulations and Notifications [Section 24]	732
Power to Issue Instructions or Directions [Section 25]	732
Removal of Difficulties [Section 26]	732
The Goods and Services Tax (Compensation to States) Act, 2017	732
Salient Features Of GST (Compensation To States) Act, 2017	732

Projected Growth Rate [Section 3]	734
Base Year [Section 4]	734
Base Year Revenue [Section 5]	735
Projected Revenue for any year [Section 6]	736
GST Compensation [Section 7]	736
Compensation Cess [Section 8]	737
Payments Return and Refund [Section 9]	738
Crediting Proceeds of Cess To Fund [Section 10]	738
Other Provisions Relating to Cess [Section 11]	739
Power to Make Rules [Section 12]	739
LESSON ROUND UP	741
SELF TEST QUESTIONS	741

## LESSON 17

### OVERVIEW OF CUSTOMS LAW

Overview of Customs Law	744
Levy & Collection of Customs Duties	746
Types of Customs Duties	746
Classification & Valuation of Import And Export Goods	749
Exemptions	758
Officers of Customs Law	758
Administration of Customs Law	758
Import & Export Procedures under Customs Law	760
Transportation & Warehousing	761
Duty Drawback	764
Demand & Recovery	766
Confiscation of Goods & Conveyances	766
Refund	768
Miscellaneous	769
LESSON ROUND UP	771
SELF-TEST QUESTIONS	772

## TEST PAPER

Model Test Papers	774
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# Lesson 1

## Direct Taxes – At a Glance

### LESSON OUTLINE

- Taxes – An Introduction
- Characteristics of Taxes
- Canons of Taxes
- Objectives of Taxation
- Direct v/s Indirect Taxation
- Background of Taxation System in India
- Tax Structure in India
- Administration
- Vital Statistics and Layout
- SELF TEST QUESTION

### LEARNING OBJECTIVES

In the present time, taxation is not just a means of transferring money to the government to spend it for meeting the public expenditures or raise revenue to the government, but taxes have become beside that, as a tool for reduce demand in the private sector, redistribution of income and wealth in the societies in the countries. It is also a means for economic development and for playing very important role in the case of stabilization of income, protection industrial home from foreign industrials. Taxation helps to find out solution for some economic problems that face the state, like unemployment, inflation, and depression. Taxation finds out solution for some economic problems, but not alone, there are also a lot of another fiscal instruments. They are working together for solution of those economic problem. Countries practice sovereignty authority upon its citizens, through levying of Taxes.

At the end of the lesson, you will be able to understand:

- Taxes – Types of taxes and its characteristics, objectives
- Canons of Taxes
- Direct v/s Indirect Taxation
- The Background of Indian Taxation System and its structure
- Tax Administration
- Vital Statistics and Layout of Tax

## TAXES - AN INTRODUCTION

The word tax is based on the latin word *taxo* which means to estimate. To tax means to impose a financial charge or other levy upon a taxpayer, an individual or legal entity, by a state or the functional equivalent of a state such that failure to pay is punishable by law.

Taxation has existed since the birth of early civilization. In ancient times taxes were either material or money like goods or services in the primitive society. The subjects used to pay a share of their income to the Head of a tribe or to the King who in return provided them with the administration security from foreign aggression and other civic amenities.

In the medieval centuries feudalism was founded, so the origin of modern tax system also was founded. Feudal market dues, tolls for protection and use of road, bridges, ferries, land rent, and other payment in goods and services were gradually transferred into money payment with the rise of money economy, Kings liked to receive money and the people preferred to pay money instead of goods and services. Step by step the old feudal revenue system changed into taxation.

Then with the development of economic sciences and with the passage of time, the functions of modern state appeared and taxation gradually became a tool of usage with more than one goal and became important source of revenue. During 19th and 20th centuries, there has been both qualitative and quantitative change in the public expenditures. Taxation has passed through the stages with passage of time, and tax's functions and objectives also have changed from the ancient communities to medieval societies to modern societies also, so the tax system has evolved with the evolution of the functions of the modern state.

Taxation is a payment from natural persons or legal entity and it is levied by government ,for which no goods or services is received directly in return, so taxes is that amount of money, the people pay which is not related directly to the benefit of people obtained from the provision of a particular goods or services.

Until the early 1930s, it was universally accepted in principle that governments should balance their budgets. Thus, the principle reason for taxation was to pay for government expenditures. Of course, governments had from time to time resorted to borrowing in order to pay for their expenditures and government borrowing was relatively quite large during some war periods. Government borrowing may be from the private sector or from abroad. Alternatively, governments may borrow from the central bank of the Country. A portion of taxes also goes to pay off the state's debt and the interest accumulates.

The taxes collected have been used by the government to carry out many functions. Some of these include:

- expenditures on war,
- the enforcement of law and public order,
- protection of property,
- economic infrastructure (roads, legal tender, enforcement of contracts, etc.),
- public works,
- social engineering, and
- the operation of government itself.

Governments also use taxes to fund welfare and public services. These services can include

- education systems,
- health care systems,
- pensions for the elderly,

- unemployment benefits, and
- public transportation, energy, water and waste management systems, common public utilities, etc.

Governments have also financed expenditures in recent years through the sale of publicly owned assets. Although asset sales were an important source of funds to the government, however, they are necessarily limited since assets can only be sold once. Thus, governments still have to raise most of the revenue needed to finance their expenditures through taxation or by charging directly for government services (user charges). Governments use different kinds of taxes and vary the tax rates, this is done to distribute the tax burden among individuals or classes of the population involved in taxable activities, such as business, or to redistribute resources between individuals or classes in the population.

Modern social security systems are intended to support the poor, the disabled, or the retired person by taxes on those who are still working. In addition, taxes are applied to fund foreign aid and military ventures, to influence the macroeconomic performance of the economy or to modify patterns of consumption or employment within an economy, by making some classes of transaction more or less attractive. Thus, there is no doubt that most government expenditures must be paid through the taxation system and it is reasonable to see this as the principle function of taxation. Yet there have always been a variety of subsidiary objectives of taxation.

In the present time, taxation is not just a means of transferring money to the government to spend it for meeting the public expenditures or raise revenue to the government, but taxes have become beside that, as a tool for reduce demand in the private sector, redistribution of income and wealth in the societies in the countries. It is also a means for economic development and for playing very important role in the case of stabilization of income, protection industrial home from foreign industrials. Taxation helps to find out solution for some economic problems that face the state, like unemployment, inflation, and depression. Taxation finds out solution for some economic problems, but not alone, but there are also a lot of another fiscal instruments. They are working together for solution of those economic problem. Countries practice sovereignty authority upon its citizens, through levying of Taxes.

### Definitions

There is no precise and accurate definition for the tax and the concept of tax has been defined differently by different economists. Some definitions are as follows.

**According to Prof Seligman** – A tax is compulsory contribution from the person to the government to defray the expense incurred in the common interest of all without reference to special benefits conferred.

**According to Bastable** – A tax as a compulsory contribution of the wealth of a person, or body of persons for the service of public powers.

**Deviti. De Marco defines** – A tax as a share of the income of citizens which the state appropriate in order to procure for itself the means necessary for the production of general public services.

**Hugh Dalton** – A tax is a compulsory charges imposed by a public authority irrespective of the exact amount of service rendered to the tax payer in return and not imposed as a penalty for legal offence.

**Jom Bouvier** defined a tax as “A pecuniary burden imposed for support of the government, the enforced proportional contribution of persons and property of the government and for all public needs”

**According to Trussing**, “The essence of Tax as distinguished from other charges by government is the absence direct quid pro quo- tit for tat between the tax payers and the public authority”.

From the above definitions we may conclude that a tax is compulsory contribution, levied by government from owner of income without direct benefit but for public benefit, and taxes should be arranged by the law.

## CHARACTERISTICS OF TAXES

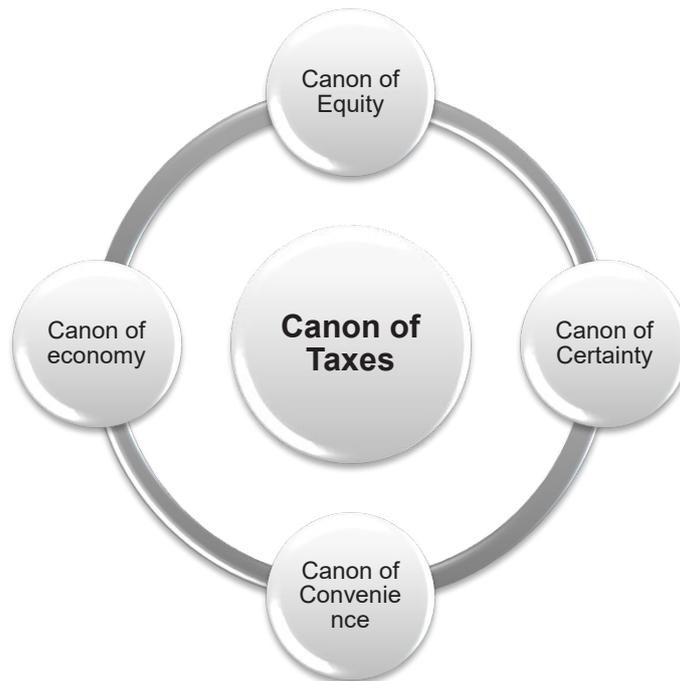
1. **Tax is compulsory** – A tax is imposed by law. So tax is compulsory payment to the governments from its citizens. Tax is duty from every citizen to bear his share for supporting the government. The tax is compulsory payment, refusal or objection for paying tax due leads to punishment or is an offence of the court of law. Government imposes tax when somebody buys commodities, or when uses services or earns income or any other condition for compulsion is found. The government practices its sovereign when levying the tax from its citizens.
2. **Tax is contribution** – Contribution means in order to help or provide something. Tax is contribution from members of community to the Government. A tax is the duty of every citizen to bear their due share for support to government to help it to face its expenditures. Some wants are common to everybody in the society like defence and security, so these wants cannot be satisfied by individuals. These social wants are satisfied by governments, hence the people support government for these social wants. Contribution involves loss or sacrifice from the side of contributor. These sacrifices affect his income.
3. **Tax is for public benefit** – Tax is levied for the common good of society without regard to benefit to special individual. Government proceeds are spent to extend common benefits to all the people such as natural disaster - like floods, famine - defence of the country, maintenance of law and establish infrastructure and order. Such benefits are given to all people.
4. **No direct benefit** – Government is compulsorily collecting all types of taxes and does not give any direct benefits to the tax payer for taxes paid. The essence of tax as distinguished from other charges by governments is the absence of a direct quid-pro-quo between the taxpayer and the public authority. Tax is different from another government charges which may give direct benefits to payers such as prices, fees, fines etc where the direct benefits are available. Taxes are for common benefits to all the members of the society.
5. **Tax is paid out of income of the tax payer** – Income means money received, especially on regular basis, for work or through investment. Tax is paid out of income as long as the income becomes realized, here the tax is imposed. Income owner has profit from any business, so he should pay his share for support to the government.
6. **Government has the power to levy tax** – Governments are practicing sovereign authority upon its citizens through levying of taxes. Only Govt. can collect tax from the people. Tax is transferring resources from the private sector to the public sector. Government is levying the tax to cover its expenditures. The government use these taxes for increasing social welfare & economy development.
7. **Tax is not the cost of the benefit** – Tax is not the cost of benefit conferred by the government on the public. Benefit and taxpayer are independent of each other, and payment of taxation is of course designed for conferring of benefits on general public.
8. **Tax is for the economic growth and public welfare** – Major objective of the government is to maximize economic growth and social welfare. Developmental activities of the nations generally involve two operations, the raising of revenue and the spending of revenue, so the government spent taxes for economic benefit, for entire community and for aggregate welfare of the society.

**Characteristic of Good Taxation System**



**CANONS OF TAXES**

Canons of taxation refer to the administrative aspect of a tax. They are related to the rate, amount, method of levy, and collection of a tax. Despite the modern development of economic sciences, Adam smith’s canons of taxation, still continue to be widely accepted as providing a good basis by which to judge taxes and these principles still apply today. The fundamental canons of taxation are as follows:



That the basic principle of taxation has reminded more or less unchanged for 220 years. Since then, there has been a lot of change in the economic activities, so modern economists like Charles F Bastable, H Dalton have added some canons to these to update and expand them.

1. **Canon of equity:** This canon implies that any tax system should be based on the principle of social justice. Equity refers to both horizontal and vertical equity. Horizontal equity describes the concept that, taxpayers with equal abilities to pay should pay the same amount of tax. Vertical equity means that taxpayers with a greater ability to pay should pay more tax.
2. **Canon of Certainty :** The tax rules should clearly specify when the tax is to be paid, how it is to be paid,

## 6 EP-TL

and how the amount to be paid is to be determined. Objective of this canon is to create trust between two parties, first party taxpayer who is to pay the tax and second party the authority whom receipt tax. If taxpayers have difficulty measuring the tax base or determining the applicable tax rate or the tax consequences of a transaction, then certainty doesn't exist. Certainty might also be viewed as the level of confidence a person has that the tax is being calculated correctly.

3. **Canon of Convenience** : A tax should be due at a time or in a manner that is most likely to be convenient for the taxpayer. Convenience in paying a tax helps to ensure compliance. The appropriate payment mechanism depends on the amount of the liability and the how easy or difficult it is to collect. Discussion of this principle in designing a particular rule or tax system would focus on whether it is best to collect the tax from the manufacturer, wholesaler, retailer or customer, as well as the frequency of collection.
4. **Canon of Economy** : This canon implies that decreasing the administrative cost of collection of the tax at the lowest level. The costs to collect a tax should be kept to a minimum for both the government and taxpayers. This principle considers the number of revenue officers needed to administer a tax. Compliance costs for taxpayers should also be considered. This principle is closely related to the principle of simplicity.

### OBJECTIVES OF TAXATION

Objectives of taxes have been developed when the functions of the Government are developed. In the primitive communities a member has to pay his share to the Head of the tribe, who in return provided them with administration, security from foreign aggression and other civic amenities. But today taxation besides being the main resource for supporting government has become a tool for economic growth, social welfare; attract foreigner investment, economic stability, and income distribution. The Objectives of taxation in brief are as under:-

- **Revenue** -This objective is the oldest, uppermost and primary objective. Taxes are imposed so as to produce the necessary amount of revenue to meet the requirement of the government, as the public expenditures is increasing in scope and size day by day. Therefore, the main objective of taxes is to raise revenue to meet the Govt. expenditures adequately.
- **Social objectives** – Taxes became a main goal for some of social objectives.
  - a) *Redistribution of income and wealth*: Income differs from one person to another in the society, Inequity in income leads to many evils, and the government aim to reduce inequalities between members of the society, to secure social justice. Tax is a means of ensuring the redistribution of income and wealth in order to reduce poverty and promote social welfare. For achieving these goals government adopts following:
    - i. Imposition of high rate tax upon luxury commodities.
    - ii. Applying progressive tax system when levying taxes from taxpayers.
    - iii. Imposition of tax exemption to basic goods.
  - b) *Social welfare*: Social welfare is the basic need of the society in the modern age. The government functions have become very important to the society, because the society needs saving, protection, education, health, and so on. All these functions are necessary to make social welfare, so the government receives revenue from tax, and expends it for those function. Therefore revenue from taxes is fuel to the government for social welfare. Social welfare is indicator for development of the countries, so almost all the countries have competition to introduce these services in the societies.

- c) *Safety of society from bad and injurious customs*: Fighting the bad customs in the society is the primary task of the government, so tax is a tool for fighting some of those customs. From this angle tax imposition of very high percentage on the goods like tobacco and alcohol is an effort to reduce these habits.
- **Economic significance of taxes**- Taxes are used from economic point of view, so taxation helps to encourage some economic activities, and as a tool to solve some economics problems. Tax is also a means for directing of scarce economic activities. Taxation helps to accelerate economic growth, and taxation plays very important role in case of economic stability.
  - **Economic growth**: Taxes are considered as a tool for economic growth and it helps to accelerate growth of economic development. Economic development has placed considerable emphasis on objectives of taxation policy. Economic development is the main objective in all the countries of the world. Economic development depends on mobilization of resources and efficient use of such resources between different sectors of the economy activities. Tax policy must be designed so as to mobilize the internal resources and use these resources in productive manner. Taxation policy helps to increase production through raising the rate of capital formation, so it helps improve the economic welfare through better distribution of income and it becomes an important instrument for removing regional inequalities. Tax policy may serve directly to mobilize resources for capital formation in the public sector and indirectly to promote private saving and investment.
  - **Enforcing government policy**: Government policy can be easily enforced by adoption of suitable tax policy. The Government can encourage investment, saving, consumption, export, protection of home industry, employment, production, protection of society from harmful customs, and economic stability through suitable tax policy. Therefore, the government gives tax exemption to the investment and saving.
  - **Directing limited scarce resources into effective and essential channels**: Tax policy plays crucial role for directing scarce resources into essential commodities. This is achieved by giving tax exemption to certain industries and imposition of heavy duties on other industries, so with the adoption of suitable tax policy, economic resources may be diverted to the production of necessary articles and investors will go to the exemption industries.
  - **Economic stability**: Maintaining economic stability is one of the tax objectives. Economic stability is a very important factor for the sustained economic growth. Government can effectively use taxes in the case of inflation and depression. These may be increased in inflationary situations. Increase in the rates of existing taxes and the imposition of new taxes would check consumption, decrease the level of effective demand and therefore help in bringing up stability in prices. Heavy taxation transfer purchasing power from the hand of people to the government which if used for productive purpose will increase the level of economic activity and employment.

In the case of depression taxes play a different role. Purchasing power in the hand of people is reduced and they are able to spend less and the demand for commodities and services is reduced. All these lead to a shrinkage of business activity and employment. In this case government should increase the purchasing power in the hand of public through reducing the burden of taxation on the people and impose tax upon saving and hoarding so that people may be encouraged to spend more and thus help to create more demand for goods and more business activity and employment.

**DIRECT VS INDIRECT TAXES**



**Direct Taxes:** Taxes which are directly levied on Income of the person and its burden can not be shifted; for example Income Tax.

**Indirect Taxes:** Indirect taxes are imposed on price of goods or services. Person paying the indirect tax can shift the incidence to another person; for example GST or Customs Duty.

To have a better understanding of the Direct and Indirect Taxes, let us understand the differences between the two:

**Differences between direct and indirect taxes**

Point of difference	Direct Tax	Indirect Tax
Incidence & Impact	A tax is said to be direct when impact and incidence of a tax are on one and same person.	If impact of tax is on one person and incidence on the another, the tax is called 'indirect'
Burden	Direct tax is imposed on the individual organisation and burden of tax cannot be shifted to others.	Indirect tax is imposed on commodities and allows the tax burden to shift.
Viability of payment	Direct taxes are lesser burden then Indirect taxes to people as direct taxes are based on Income earning ability of people.	Indirect taxes are borne by the consumers of commodities and services Irrespective of financial ability as the MRP Includes all taxes.
Administrative viability	The administrative cost of collecting direct taxes is more and Improper administration may result in tax evasion.	Cost of collecting Indirect taxes is very less as indirect taxes are wrapped up in prices of goods and services and cannot be evaded.
Penalty	It is levied on the assessee.	It is levied on supplier of Goods & Services.

**Merits of Direct Tax**

1. **Equity** : - Direct taxes have equity of sacrifice, depend upon the volume of income. They are based on the principle of progressive, so rates of tax increase as the level of income of a person rises.
2. **Elasticity and productivity** : - Direct taxes have elasticity because when the government faces some

emergency, like earthquake, floods and famine the government can collect money for facing those problems by direct tax.

3. **Certainty**:- Direct taxes have certainty on both sides' tax-payer and government. The tax- payers are aware of the quantity of tax. They have to pay and rate, time of payment, manner of payment, and punishment from the side of government is also certain about the total amount they are getting.
4. **Reduce inequality**: - Direct taxes follow progressive principles so it is taxing the rich people with higher of taxation and the poor people with a lower level of taxation.
5. **Good instrument in the case of inflation**:- Tax policy as fiscal instrument plays important role in the case of the inflation, so government can absorb the excess money by arising in the rate of existing taxes or imposition of new taxes.
6. **Simplicity**:- Direct taxes are simplicity, while levy the rules, procedures, regulations of income tax are very clear and simple.

**Demerits of Direct Taxes**

1. Evasion: - Direct tax is lump sum therefore tax payers try evasion.
2. Uneconomically:-Expenses of collection are larger in the case of direct taxes, because they require widely- spread staff for collection
3. Unpopular:-Direct tax is required to be paid in lump sum for the whole year, so the tax payers feel the painful payment, these taxes are therefore unpopular.
4. Little incentive to work and save:-In direct taxes, rates are of progressive nature. A person with higher earning is taxed more, in turn he is left little with amount. So the tax payer feels disincentive to work hard and save money after reaching a certain level of income.
5. Not suitable for a poor country:- Direct taxes are not enough to meet its expenditure.
6. Arbitrary:-Due to absence of logical or scientific principle to determine the degree of progression in the taxation, the direct taxes are arbitrary.

**Merits of Direct Taxes**

**Demerits of Direct Taxes**



Equity

Evasion

Elasticity and Productivity

Uneconomically

Certainty

Unpopular

Reduce inequality

Arbitrary

Simplicity

Not suitable to poor economy

**Merits of Indirect Taxes**

1. **High revenue production** :-Nature of indirect taxes is imposition on the commodities and services. Here indirect taxes cover a large number of essential goods and luxurious goods which are consumed by the mass both rich and poor people, these help in collecting large revenue.
2. **No evasion**. Nature of indirect tax is that, it is included in the price of commodity, so tax evasion or tax avoid is difficult.
3. **Convenient**:-Indirect taxes are small amount and indirect taxes are hidden in the price of goods and service, hence the burden of these taxes is not felt very much by the tax-payers, and not lump sum like direct taxes.
4. **Economy** - Indirect taxes are economical in collection and the administrations costs of collection are very low, also the procedure of collection of these taxes is very simply.
5. **Wide coverage**:-Indirect taxes cover almost all commodities like essential commodities, luxuries, and harmful ones.
6. **Elasticity**:-Since a large number of commodities and services are covered by indirect taxation there is great scope for modification of taxes, goods and tax rate, much depends on nature of goods and on its demands.

**Demerits of Indirect Taxes**

1. **Regressive in effect**:-Essential commodities are used from all members of community. When taxing these commodities the burden would be equal, and no distinction is made between the rich and poor people.
2. **Uncertainty in collection**- Discourage savings and Increase inflation:-Indirect taxes are payable when people spent their income or when people buy goods and services, so tax authorities cannot accurately estimate the total yield from different indirect taxes.
3. **Discourage savings**- Increase inflation:-Indirect taxes are included in the price of commodity, so people have to spend more money on essential commodities, when levied indirectly. In this case that means the customers cannot save some of their money.
4. **Increase inflation**:-Indirect taxes increase the cost of input and output, increase in production cost, push the price of goods. These reflect in increase in the wages of the workers.

**Merits of Indirect Tax**

**Demerits of Indirect Tax**



High Revenue Production

Regressive in effect

No Evasion

Uncertainty in collection

Convenient

Discourage savings

Economy

Increase inflation

Wide coverage

Elasticity

## BACKGROUND OF TAXATION SYSTEM IN INDIA

### Taxation in India during Ancient Time

In India, the system of direct taxation as it is known today, have been in force in one form or another even from ancient times. There are references both in Manu Smriti and Arthashastra to a variety of tax measures.

Manu, the ancient sage and law-giver stated that the king could levy taxes, according to Sastras. The wise sage advised that taxes should be related to the income and expenditure of the subject. He, however, cautioned the king against excessive taxation and stated that both extremes should be avoided namely either complete absence of taxes or exorbitant taxation. According to him, the king should arrange the collection of taxes in such a manner that the subjects did not feel the pinch of paying taxes.

He laid down that traders and artisans should pay 1/5th of their profits in silver and gold, while the agriculturists were to pay 1/6th, 1/8th and 1/10th of their produce depending upon their circumstances.

The detailed analysis given by Manu Smriti and Arthashastra on the subject clearly shows the existence of a well-planned taxation system, even in ancient times. Taxes were paid in the shape of gold-coins, cattle, grains, raw-materials and also by rendering personal service. Most of the taxes of Ancient India were highly productive. The admixture of direct taxes with indirect taxes secured elasticity in the tax system, although more emphasis was laid on direct tax. The tax-structure was a broad based one and covered most people within its fold. The taxes were varied and the large variety of taxes reflected the life of a large and composite population”.

### Establishment of Income tax in Modern India

#### Income Tax Act, 1860

Consequent upon the financial difficulties created by the events of 1857. Income Tax was introduced in India for the first time by the British in the year 1860. The Act of 1860 was passed only for five years and therefore it lapsed in 1865. It was replaced 1867 by a licence tax on professions and trades and the latter was converted into a certificate tax in the following year. It was latter abolished in 1873. Licence tax traders remained in operation till 1886 when it was merged in the income tax Act of that year.

#### Income Tax Act, 1886

The Act of 1886 levied a tax on the income of residents as well as non residents in India. The Act defined agricultural income and exempted it from tax liability in view of the already existing land revenue a kind of direct taxes. The Act of 1886 exempted life insurance premiums paid by assessee policies of his own life. Another important provision of this Act Hindu undivided family was treated as a distinct taxable entity.

#### Income Tax Act, 1918

The Act of 1918 brought under change also receipts of casual or non recurring nature pertaining to business or professions. Although income tax in India has been a charge on net income since inception, it was in the Act of 1918 that specific provisions were inserted for the first time pertaining to business deductions for the purpose of computing net income.

The Act of 1918 remained in force for a short period and was replaced by new Act (Act XI of 1922) in view of the reforms introduced by the Govt. of India Act, 1919 .

#### Income Tax Act, 1922

The organizational history of the income tax department dates back to the year 1922. “one of the important aspects of the 1922 Act was that, it laid down the basis, the mechanism of administering the tax and the rates at which the tax was to be levied would be laid down in annual finance acts. This is procedure brought in the much needed flexibility in adjusting the tax rates in accordance with the annual budgetary requirements and in securing a degree of elasticity

for the tax system. Before 1922 the tax rate were determined by the Income tax act itself and to revise the rates, the act itself had to be amended. The Income tax Act, 1922 gave for first time a specific nomenclature to various income tax authorities and laid the foundation of a proper system of administration as per provisions of income tax act 1922 thus, it is the income tax act 1961, which is currently operative in India.

### **Income Tax Act, 1961**

The present law of income tax in India is governed by the Income Tax Act, 1961 which is amended from time to time by the annual finance Act and other legislations pertaining to direct tax. The act which came into force on April 1, 1962, replaced the Indian income tax Act, 1922, which had remained in operation for 40 years. Furthermore, A set of rules known as Income Tax Rules, 1962 have been framed for implementing the various provisions of the Act.

## **TAX STRUCTURE IN INDIA**

### **Constitution of India**

The roots of every law in India lies in the Constitution, therefore understanding the provisions of Constitution is foremost to have clear understanding of any law. Let us first understand what it talks about tax:

- Article 265– No tax shall be levied or collected except by the Authority of Law.
- Article 246- Distributes legislative powers including taxation, between the Parliament of India and the State Legislature.
- Schedule VII- Enumerates powers under three lists
  - o Union List – Powers of Central Government
  - o Legislative List- Powers of State Government
  - o Concurrent List- Both Central and state Government have powers, in case of conflict; law made by Union Government prevails.

Some of the major taxes under respective lists are:-

#### **Central Government**

- Taxes on Income other than Agricultural Income
- Customs including export duties
- Excise on Tobacco and other goods manufactured in India except alcoholic liquors for human consumption, opium, narcotic drugs
- Corporation Tax
- Taxes on interstate trade of goods other than newspapers
- Taxes on interstate consignment of goods
- Any other matter not included in List II or III

#### **State Government**

- Taxes on agricultural income
- Excise duty on alcoholic liquors, opium and narcotics
- Octroi or Entry Tax
- Tax on intra state trade of goods other than newspapers
- Tax on advertisements other than that in newspapers
- Tax on goods and passengers carried by road or inland waterways
- Tax on professionals, trades, callings and employment

## ADMINISTRATION

The Central Board of Revenue or Department of Revenue is the apex body charged with the administration of taxes. It is a part of Ministry Of Finance which came into existence as a result of the Central Board of Revenue Act, 1924.

Initially the Board was in charge of both direct and indirect taxes. However, when the administration of taxes became too unwieldy for one Board to handle, the Board was split up into two, namely the Central Board of Direct Taxes (CBDT) and Central Board of Excise and Customs (CBEC) with effect from 1 January 1964. This bifurcation was brought about by constitution of the two Boards under Section 3 of the Central Boards of Revenue Act, 1963.

### Central Board of Direct Taxes

The Central Board of Direct Taxes (CBDT) provides essential inputs for policy and planning of direct taxes in India and is also responsible for administration of the direct tax laws through Income Tax Department. The CBDT is a statutory authority functioning under the Central Board of Revenue Act, 1963. It is India's official Financial Action Task Force (FATF) unit.

### Organisational Structure

The CBDT is headed by CBDT Chairman and also comprises six members. The Chairperson holds the rank of Special Secretary to Government of India while the members rank of Additional Secretary to Government of India.

- Member (Income Tax)
- Member (Legislation and Computerisation)
- Member (Revenue)
- Member (Personnel & Vigilance)
- Member (Investigation)
- Member (Audit & Judicial)

The CBDT Chairman and Members of CBDT are selected from Indian Revenue Service (IRS), a premier civil service of India, whose members constitute the top management of Income Tax Department.

### Income Tax Department

Income Tax Department functions under the Department of Revenue in Ministry of Finance. It is responsible for administering following direct taxation acts passed by Parliament.

- Income Tax Act, 1961
- Various Finance Acts (Passed Every Year in Budget Session)

Income Tax Department is also responsible for enforcing Double Taxation Avoidance Agreements and deals with various aspects of international taxation such as Transfer Pricing. Income Tax Department has powers to combat aggressive Tax avoidance by enforcing General Anti Avoidance Rules.

### Central Board of Indirect Taxes and Customs

Central Board of Excise and Customs (CBIC) is a part of the Department of Revenue under the Ministry of Finance, Government of India. It deals with the tasks of formulation of policy concerning levy and collection of Customs & and GST, prevention of smuggling and administration of matters relating to Customs, GST and Narcotics to the extent under CBIC's purview.

### GST Council

A GST Council consisting of representatives from the Centre as well as State has been formulated under the GST Law of indirect taxes. The Council will make recommendations to the Union and the States on Goods and Service Tax laws, on any other matter relating to GST.

Till date, numerous conclusive meetings of GST Council have been undertaken. Decisions have been taken regarding rates, Composition Scheme, exemption schemes to North-Eastern and hilly areas, compensation method for loss of revenue to states etc. Rules regarding return, refund, registration, payment, invoicing and the like have been finalized by the same. However, various other issues and modalities regarding the GST are constantly being discussed at the GST Council Meetings for smoothening the law and making it easy to implement for society at large.

### VITAL STATISTICS AND LAYOUT

#### Contribution of Direct Taxes to Total Tax Revenue

(Rs. in crore)

Financial Year	Direct Taxes	Indirect Taxes	Total Taxes	Direct Tax As % Of Total Taxes
2000-01	68305	119814	188119	36.31%
2001-02	69198	117318	186516	37.10%
2002-03	83088	132608	215696	38.52%
2003-04	105088	148608	253696	41.42%
2004-05	132771	170936	303707	43.72%
2005-06	165216	199348	364564	45.32%
2006-07	230181	241538	471719	48.80%
2007-08	314330	279031	593361	52.97%
2008-09	333818	269433	603251	55.34%
2009-10	378063	243939	622002	60.78%
2010-11	445995	343716	789711	56.48%
2011-12	493987	390953	884940	55.82%
2012-13	558989	472915	1031904	54.17%
2013-14	638596	495347	1133943	56.32%
2014-15	695792	543215	1239007	56.16%
2015-16	741945	711885	1454180	51.03%
2016-17	849818	861515	1711333	49.66%
2017-18	1002037	915256	1918210	52.24%
2018-19*	1137685	939018	2076703	54.78%

\* Provisional

(Source - <https://www.incometaxindia.gov.in/Documents/Direct%20Tax%20Data/IT-Department-Time-Series-Data-FY-2000-01-to-2018-19.pdf>)

**Direct-Tax GDP Ratio**

(Rs. in crore)

Financial year	Net Collection of Direct Taxes	GDP Current Market Price	Direct Tax GDP Ratio	GDP Growth Rate	Tax Growth Rate	Buoyancy Factor
2000-01	68305	2102376	3.25%	7.7%	17.85%	2.32
2001-02	69198	2281058	3.03%	8.5%	1.31%	0.15
2002-03	83088	2458084	3.38%	7.76%	20.07%	2.59
2003-04	105088	2754621	3.81%	12.06%	26.48%	2.19
2004-05	132771	3242209	4.1%	17.7%	26.34%	1.49
2005-06	165216	3693369	4.47%	13.92%	24.44%	1.76
2006-07	230181	4294706	5.36%	16.28%	39.32%	2.42
2007-08	314330	4987090	6.3%	16.12%	35.56%	2.27
2008-09	333818	5630063	5.93%	12.89%	6.20%	0.48
2009-10	378063	6457352	5.85%	14.69%	13.25%	0.90
2010-11	445995	7674148	5.81%	18.84%	17.97%	0.95
2011-12	493987	9009722	5.48%	17.4%	10.76%	0.62
2012-13	558989	10113281	5.53%	12.25%	13.16%	1.07
2013-14	638596	11355073	5.62%	12.28%	14.24%	1.16
2014-15	695792	12541208	5.55%	10.45%	8.96%	0.86
2015-16	741945	13567192	5.47%	8.25%	6.63%	0.80
2016-17	849818	1,53,62,386	5.53%	13.23%	14.53%	1.10
2017-18	10,02,037	1,70,95,005	5.86%	11.28%	17.93%	1.59
2018-19	11,37,685	1,90,10,164@	5.98%	11.20%	13.54%	1.21

\* Provisional

@ Advance Estimates as per Press Release dated 31.05.2019 of MOSPI.

(Source - <https://www.incometaxindia.gov.in/Documents/Direct%20Tax%20Data/IT-Department-Time-Series-Data-FY-2000-01-to-2018-19.pdf>)**Cost of Collection**

(Rs. in crore)

Financial Year	Total Collections	Total Expenditure	Cost of Collection
2000-01	68305	929	1.36%
2001-02	69198	933	1.35%
2002-03	83088	984	1.18%
2003-04	105088	1050	1.00%
2004-05	132771	1138	0.86%
2005-06	165216	1194	0.72%
2006-07	230181	1349	0.59%
2007-08	314330	1687	0.54%
2008-09	333818	2248	0.67%
2009-10	378063	2726	0.72%

2010-11	445995	2698	0.60%
2011-12	493987	2976	0.60%
2012-13	558989	3283	0.59%
2013-14	638596	3641	0.57%
2014-15	695792	4101	0.59%
2015-16	741945	4593	0.61%
2016-17	849818	5578	0.66%
2017-18	10,02,037	6,087	0.61%
2018-19*	11,37,685	7074	0.62%

\* Provisional

\*(Source - <https://www.incometaxindia.gov.in/Documents/Direct%20Tax%20Data/IT-Department-Time-Series-Data-FY-2000-01-to-2018-19.pdf>)

### SELF TEST QUESTIONS

1. CBDT Full Form:
  - a) Central Board of Digital Taxes
  - b) Common Board of Direct Taxes
  - c) Central Board of Direct Taxes
  - d) Common Board of Digital Taxes
2. Merits of Direct Taxes:
  - a) Equity
  - b) Elasticity and Productivity
  - c) Certainty
  - d) All of the above

Answer: 1 (c) , 2 (d)

### SUGGESTED READINGS

1. **Direct Taxes Law and Practice**  
 Author : Dr. Vinod K. Singhania & Dr. Kapil Singhania  
 Publisher : Taxmann  
 Year : 2019  
 Edition : 2019
2. **Direct Taxes Ready Reckoner with Tax Planning**  
 Author : Dr. Girish Ahuja & Dr. Ravi Gupta  
 Publisher : Wolters Kluwer  
 Year : 2019  
 Edition : 20th Edition





# Lesson 2

## Basic Concept of Income Tax

### LESSON OUTLINE

- Introduction
- An Overview of Finance Bill
- Heads of Income [Section 14]
- Important Concept
- Person [Section 2(31)]
- Assessee [Section 2(7)]
- Assessment year [Section 2(9)]
- Previous year [Section 3]
- India [Section 2(25A)]
- Maximum Marginal Rate and Average Rate of Tax
- Income [Section 2(24)]
- Total Income [Section 2(45A)]
- Capital and Revenue Receipts
- Charge of Income Tax (Section 4)
- Residential Status and Tax Liability (Section 6)
- Test for residence of Individuals
- Test for residence of HUF
- Test for residence of Companies
- Test for residence for Firm, AOP / BOI
- Meaning and Scope of total Income (Section 5)
- Scope of total income on the basis of residential status
- Income received in India
- Income deemed to be received Income accrued in India
- Income deemed to accrue or arise in India
- Tax incident vis-a-vis residential status
- Computation of Taxable Income and Tax Liability of an Assessee
- Tax Rates
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

The taxes are the basic source of revenue for the Government. Revenue raised from the taxes are utilized for meeting expense of Government like, provision for education, infrastructure facilities such as roads, dams etc. Taxes are broadly divided into two parts i.e. direct taxes and indirect taxes. The tax that is levied directly on the income or wealth of a person is called direct tax. Income tax is one of form of direct taxes. The levy of income tax in India is governed by the Income Tax Act, 1961 and Income Tax Rules, 1962. It is charged on the Total Income and to derive the total income one must know certain concepts of the Income Tax Act, such as residential status, assessment year, previous year, assessee etc.

Income tax is leviable on taxable income and to determine taxable income, residential status of the person and scope of total income are the initial steps. There are two types of taxpayers from residential point of view - Resident in India and Non-resident in India. Sourced based income in India is taxable in India whether the person earning income is resident or non-resident. Conversely, foreign sourced income of a person is taxable in India only if such person is resident in India. Therefore, the determination of the residential status of a person is very significant in order to find out his tax liability.

At the end of this lesson, you will understand:

- Overview of Finance Bill
- Some basic concepts like assessment year, previous year, income, person, assessee,
- Distinguish between capital and revenue receipts etc.
- Basic steps in the calculation of tax liability.
- Be able to determine the residential status of a person
- Be aware of the importance of residential status for tax purposes
- The scope of total income
- The rates of tax

***The Income Tax Department is governed by Central Board of Direct Taxes (CBDT) and it is the part of the Department of Revenue under the Ministry of Finance, Government of India***

## INTRODUCTION

Tax is the financial charge imposed by the Government on income, commodity or activity. Government imposes two types of taxes namely Direct taxes and Indirect taxes. Direct tax is one where burden of tax is directly on the payer e.g. income tax, whereas Indirect tax is paid by the person other than the one who utilizes the product or service e.g. Custom duty, Goods and Service Tax (GST).

Article 265 of the Constitution provides that no tax shall be levied or collected except by authority of law. Thus, the tax proposed to be levied or collected must be within the legislative competence of the legislature imposing the tax. Further, the law imposing the tax, like other laws, must not violate any fundamental right.

Income tax being direct tax happens to be the major source of revenue for the Central Government. The responsibility for collection of income-tax vests with the Central Government. This tax is leviable and collected under Income-tax Act, 1961 (hereinafter referred to as 'the Act'). The entire amount of income tax collected by the Central Government is classified under the head :

1. Corporation Tax (Tax on the income of the companies); and
2. Income Tax (Tax on income of the non-corporate assesseees)

The Income tax Act contains the provisions for determination of taxable income, determination of tax liability, procedure for assessment, appeal, penalties and prosecutions. It also lays down the powers and duties of various income tax authorities. The income tax law in India consists of the following components.

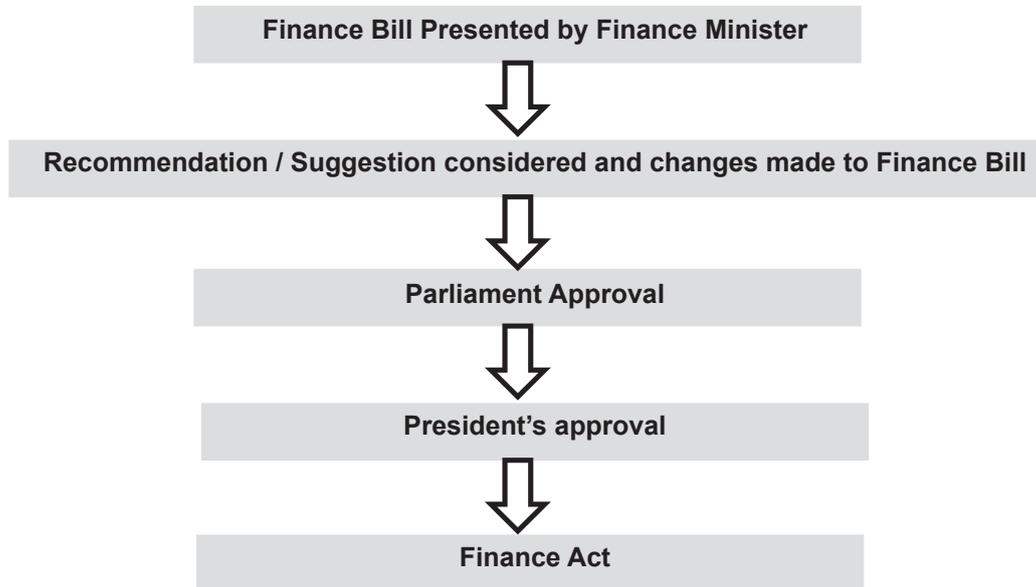
- **Income Tax Act, 1961** : This Act came into force on 1st April, 1962. It contains sections 1 to 298, wherein each section may have sub-sections, clauses or sub-clauses and may also have Provisos and Explanations.
- **Annual Finance Act** : Every year a Budget is presented before the parliament by the Finance Minister. One of the important components of the Budget is the Finance Bill. This Bill contains various amendments in the Income-Tax Act and other tax laws to prescribe the additions and deletions therein. When the Finance Bill is approved by both the houses of parliament and receives the assent of President, it becomes the Finance Act.
- **Income Tax Rules, 1962** : For implementation of the Act and for administration of the direct taxes Central Board of Direct Taxes (CBDT) is empowered to frame these rules from time to time. These rules are collectively called as the Income-tax Rules, 1962. These rules are made applicable by notification in the Official Gazette of India.
- **Notifications** : Notifications are issued either by Central Government or by CBDT to take care the procedural aspects of the Act from time to time. These notifications are binding on everyone i.e. on Income Tax Authorities as well as on the assesseees.
- **Circulars/Clarifications** : Circulars and clarifications are issued by the CBDT to clarify the doubts regarding the scope and meaning of certain provisions of the law and primarily to provide guidance to the Income Tax officers. These circulars are binding on the Income Tax Authorities but not on the assessee however an assessee can take benefit of these circulars.
- **Judicial Decisions (Case Laws)** : Decisions pronounced by Supreme Court become Judicial Precedent and are binding on all the courts, Appellate Tribunal, Income Tax Authorities and on assesseees. Further, High Court decisions are binding on assesseees and Income Tax Authorities which come under its jurisdiction unless it is overruled by a higher authority. The decision of a High Court can not bind other High Court.

## AN OVERVIEW OF FINANCE BILL

Finance Bill as part of the Union Budget is presented usually in the month of February every year and this bill

contains amendments in direct as well as indirect taxes. It is presented in the Parliament by the Union Finance Minister.

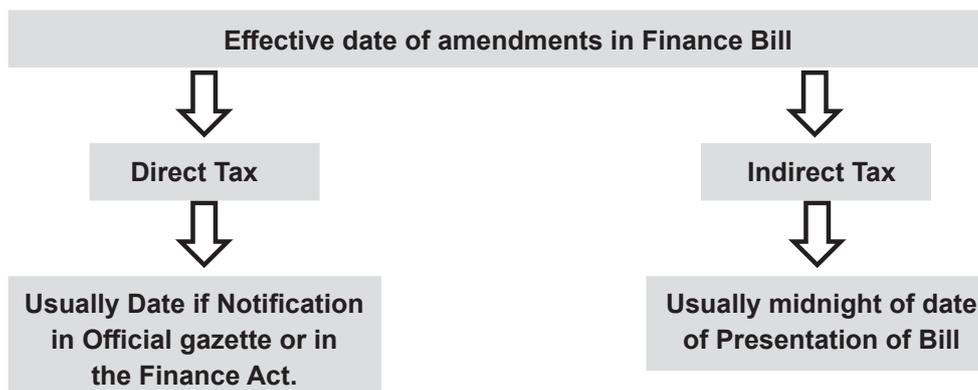
The finance bill is passed by both the houses of Parliament after it is being tabled and necessary recommendation / amendments have been made in it. Once the bill has been passed by the Parliament, it goes to the President for his assent. After Presidents assent, the finance bill becomes the Finance Act.



The Finance Bill is presented at the time of presentation of the Annual Financial Statement before Parliament, in fulfillment of the requirement of Article 110 (1)(a) of the Constitution, detailing the imposition, abolition, remission, alteration or regulation of taxes proposed in the Budget. It is through the Finance Act that amendments are made to the various Acts like Income Tax Act 1961, Customs Act 1962 etc. In short, Finance Bill can be considered as an umbrella Act.

When the proposals are introduced to the Parliament it is called as a Finance Bill. Once it is passed by the Parliament and assented to by the President, Finance Bill becomes the Finance Act for that year. Finance Bills for various years may be seen at the website <http://indiabudget.nic.in/>

The different clauses in the Finance Act may get notified eventually, but at different times based on the readiness of the stakeholders and implementing agencies. The effective date of applicability of provisions of the Finance Act is usually mentioned in the notification in the official gazette or in the Act itself. Generally, the amendments by the Finance Act are made applicable from the first day of the next financial year. Likewise, amendments by Finance Act, 2019 are effective from 1st April, 2019. Regarding indirect taxes, the ad valorem tax rates (tax rates based on value) are effective from the midnight of the date of presentation of the Union Budget.



## HEADS OF INCOME [SECTION 14]

Under Income Tax Act all incomes are categorized under 5 Heads of Income. There is a charging section under each head of income which defines the scope of income chargeable under that head. These heads of income cover all possible avenues for a person to earn any income. Accordingly income earned is classified under the following heads:

- a. Income under the head Salary : Earned by employee from his employer
- b. Income under the head House Property : Rental income earned by a landlord from house property
- c. Income under the head Profits and Gains from Business and Profession(PGBP) : Business income
- d. Income under the head Capital Gains: Income by sale/transfer of Capital Asset
- e. Income under the head Other Sources: Residual head of income.

Every person whose Total Income of the previous year exceeds the maximum amount which is not chargeable to tax, is an assessee and such total income shall be chargeable to Income Tax at the rates prescribed in the Act for that relevant assessment year. However this Total income shall be determined on the basis of the residential status of the assessee in India.

To levy income tax, one must have an understanding of the various concepts related to the charge of tax like previous year, assessment year, Income, total income, person, maximum amount not chargeable to tax etc.

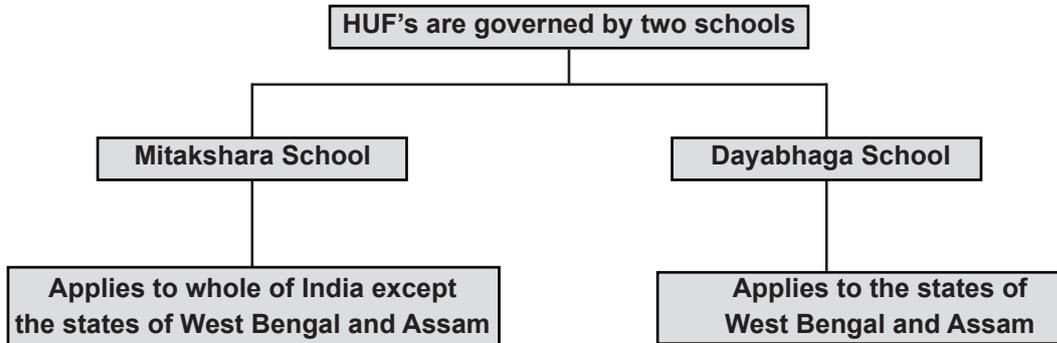
## IMPORTANT CONCEPTS

**PERSON [SECTION 2(31)]** : Income-tax is charged in respect of the total income of the previous year of every person. Hence, it is important to know the definition of the word person. As per section 2(31), Person includes :



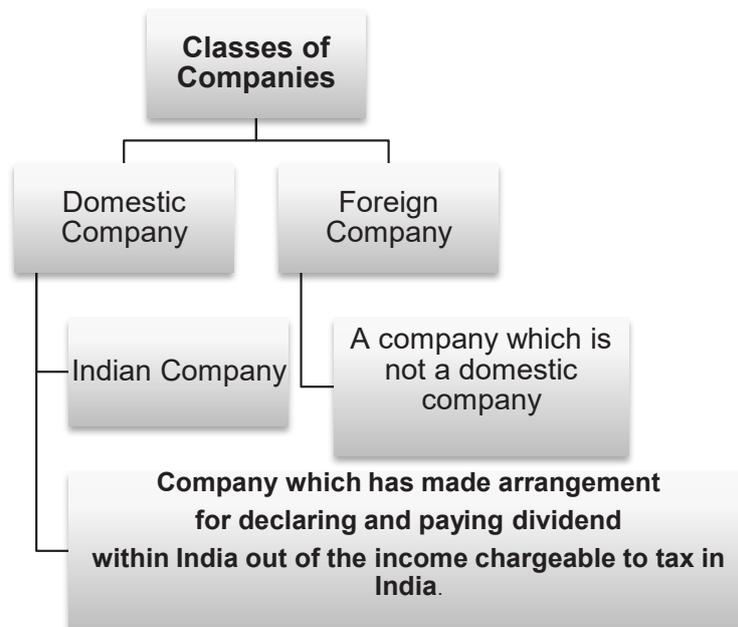
- **Individual** : An individual is a natural human being i.e. male, female, minor or a person of sound or unsound mind.
- **HUF** : Under Income Tax Act, 1961 a Hindu Undivided Family (HUF) is treated as separate entity for the purposes of assessment. It consists of all persons lineally descended from a common ancestor and includes their wives and unmarried daughters and also a stranger who has been adopted by the family. Members of the HUF are called as co-parceners which includes the head of the HUF who is called as Karta. A Hindu Coparcenary includes those persons who acquire an interest in joint family property by

birth. The relation of a HUF does not arise from a contract but arises from status. Only the coparceners have a right to partition. However, other female members of the family, for example, wife or daughter-in-law of a coparcener are not eligible for such coparcenary rights. Jain undivided families and Sikh undivided families would also be assessed as a HUF.



➤ **Company** : It include Domestic company, Foreign company, company in which public are substantially interested. Section 2(17) defines the term company to mean :

- i. any Indian company, or
- ii. any body corporate incorporated by or under the laws of a country outside India i.e. a foreign company, or
- iii. any institution, association or body which is or was assessable or was assessed as a company for any assessment year under the Indian Income Tax Act, 1922 or which is or was assessable or was assessed under this Act as a company for any assessment year commencing on or before the 1st day of April, 1970, or
- iv. any institution, association or body, whether incorporated or not and whether Indian or non-Indian, which is declared by general or special order of the CBDT to be a company only for such assessment year or assessment years as may be specified by the order of CBDT.



➤ **Firm** : It includes a partnership firm whether registered or not and shall include a Limited Liability Partnership as defined in the Limited Liability Partnership Act,2008.

According to Section 4 of the Partnership Act, 1932 persons who have entered into partnership with one another are called individually, 'partners' and collectively 'a firm'.

- **Association of Person** : Two or more persons join in for a common purpose or common action to produce income, profits or gains.

It may consist of individuals, HUF, companies, firms, etc. as members

The object must be to produce income. It is not enough that the persons receive the income jointly.

- **Body of Individuals** denote the status of persons who are assessable in like manner and to the same extent as the beneficiaries individually.

Only individuals can be the members

Individuals join together for common purposes



The difference between Association of persons and body of individuals is that whereas an association implies a voluntary getting together for a definite purpose, a body of individuals would be just a body without an intention to get-together. Moreover, the members of body of individuals can be individuals only whereas the members of an association of persons can be individual or non-individuals (i.e. artificial persons).

**A local authority**

It means a municipal committee, district board, body of port commissioners, or other authority legally entitled to or entrusted by the Government with the control and management of a Municipal or local fund.

**Every artificial, juridical person, not falling within any of the above categories**

This is a residuary clause. If the assessee does not fall in any of the first six categories, he is assessed under this clause. Generally, a statutory corporation, deity or charitable institution or an endowment for charitable or religious purposes falls under artificial juridical person.

**ASSESSEE [SECTION 2(7)]**

- In layman language tax payer is assessee, he may be the person of any of the above categories
- As per Section 2(7) of Income Tax Act, assessee is A person
  - by whom any tax or
  - any other sum of money

is payable under Income Tax Act. It includes every person :

- (a) in respect of whom any proceeding under Income Tax Act has been taken for assessment of
  - his income or
  - fringe benefits or
  - 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
  - the amount of refund due to him or to such other person
- (b) who is deemed to be an assessee under any provision of Income Tax Act;
- (c) who is deemed to be an assessee in default under any provision of Income Tax Act;

Accordingly, assessee is a person by whom tax or any other sum is payable under the Act. The expression “other sum of money” includes

- fine, interest, penalty and tax or
- person to whom any refund of tax etc. is due under the Act or
- if any proceeding under the Act has been taken against any person, he is also an assessee. Remember, the proceedings must be initiated under the provisions of the Act. In other words, a single enquiry letter issued by the Income-tax Department without reference to any specific provision of the Act does not constitute proceeding under the Act and, as such, till proceedings are initiated under the Act, the person may not become an assessee within the ambit of Section 2(7) of the Act.

### ASSESSMENT YEAR [SECTION 2(9)]

“Assessment year” means the period of twelve months commencing on 1st April every year. Therefore, the period beginning on 1st April of one year and ending on 31st March of the next year. Income of previous year of an assessee is taxed during the following assessment year at the rates prescribed by the relevant Finance Act.

**Exception to the General Rule :** In the following situation, the Income of previous year of an assessee is assessed in the previous year itself:

1. Income of Non-Resident from Shipping: [Section 172]- A non resident who is carrying on a shipping business and earns income any port in India, shall be charged to tax before the ship is allowed to leave Indian Port. Hence income is deemed and computed at a presumptive rate of 7.5% of the amount of the fare/freight charged by the non-resident ship from the Indian port.
2. Income of persons leaving India either permanently or for long duration: [Section 174]- When it appears to the Assessing Officer (A.O.) that an individual may leave India and has no intentions of returning back during an assessment year, then the income is charged to tax during the same Assessment year.
3. Income of bodies formed for short duration: [Section 174A]- When it appears to the Assessing Officer (A.O.) that any organization is formed for a particular event and is likely to be dissolved during the current assessment year.
4. Income of person trying to transfer his assets with a view to avoid tax: [Section 175]- When it appears to the Assessing Officer (A.O.) that during the current assessment year any person is likely to charge, sell, transfer, dispose of or otherwise part with any of his assets to avoid payment of any liability under this Act, the total income of such person for the period from the expiry of the previous year to the date, when the Assessing Officer commences proceedings under this section is chargeable to tax in that assessment year.
5. Income of discontinued business: [Section 176]- Where any business or profession is discontinued in any assessment year, the income of the period from the expiry of the previous year up to the date

of such discontinuance may, at the discretion of the Assessing Officer, be charged to tax in that assessment year.

### PREVIOUS YEAR [SECTION 3]

Income tax is payable on the income which is earned during the Previous Year and it is assessed in the immediately succeeding financial year which is called an Assessment Year.

All assesses are required to follow a uniform previous year i.e. The Financial Year (1st April to 31st March) as their Previous year. Although assessee may maintain books of accounts on calendar year basis (1st January to 31st December) but his previous year for income tax purposes shall be the Financial year.

Each financial year is both, a previous year as well as an assessment year. It is the previous year for the income earned during the financial year and assessment year for the income earned during the preceding previous year. For example financial year 2019-20 is the previous year for the income earned during the financial year 2019-20 and assessment year for the income earned during the previous year 2018-19.

In case of newly set up business or profession or a source of income newly coming into existence, the first previous year will be the period commencing from the date of setting up of business/profession or as the case may be, the date on which the source of income newly comes into existence and ending on the immediately following March, 31.

Examples of previous year in the case of newly set-up business/profession.

**Example 1** : Y sets up a new business on May 15, 2019. What is the previous year for the assessment year 2020-21.

**Answer** : Previous year for the assessment year 2020-21 is the period commencing on May 15, 2019 and ending on March 31, 2020.

**Example 2** : A joins an Indian company on February 17, 2019. Prior to joining this Indian company he was not in employment nor does he have any other source of income. Determine the previous year of A for the assessment years 2019-20 and 2020-21.

**Answer** : Previous years for the assessment years 2018-19 and 2019-20 will be as follows.

Previous year	Assessment year
Feb. 17, 2019 to March 31, 2019	2019-20
April 1, 2019 to March 31, 2020	2020-21

### INDIA [SECTION 2(25A)]

The term 'India' means –

- (i) the territory of India as per Article 1 of the Constitution,
- (ii) its territorial waters, seabed and subsoil underlying such waters,
- (iii) continental shelf,
- (iv) exclusive economic zone or
- (v) any other specified maritime zone and the air space above its territory and territorial waters.

Specified maritime zone means the maritime zone as referred to in the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976.

### MAXIMUM MARGINAL RATE AND AVERAGE RATE OF TAX

As per section 2(10), "Average Rate of income-tax" means the rate arrived at by dividing the amount of income-tax calculated on the total income, by such total income.

Section 2(29C) defines “Maximum Marginal Rate” to mean the rate of income-tax (including surcharge on the income-tax, if any) applicable in relation to the highest slab of income in the case of an individual, AOP or BOI, as the case may be, as specified in Finance Act of the relevant year.

**INCOME [SECTION 2(24)]**

“Income is the consumption and savings opportunity gained by an entity within a specified timeframe, which is generally expressed in monetary terms. However, for households and individuals, “income is the sum of all the wages, salaries, profits, interests payments, rents, and other forms of earnings received in a given period of time.”

In general terms, Income is a periodical monetary return with some sort of regularity. However, the Income Tax Act, even certain income which does not arise regularly are treated as income for tax purposes e.g. Winnings from lotteries, crossword puzzles.

The definition of Income as given in Section 2(24) of the Act starts with the word includes therefore the list is inclusive not exhaustive. The definition enumerates certain items, including those which cannot ordinarily be considered as income but are treated statutorily as such.

As per section 2(24), the term income includes :

S. No.	Income under Section 2(24)	Head Of Income
1.	Profits and gains	PGBP
2.	Dividend	Other Sources
3.	Voluntary contributions received by a trust/institution created wholly or partly for charitable or religious purposes or by certain research association or universities and other educational institutions or hospitals and other medical institutions or an electoral trust.	Generally exempt under Section 11 and 12
4.	The value of any perquisite or profit in lieu of salary taxable	Salary
5.	<b>Any special allowance</b> or benefit 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.	Salary (Generally exempt)
6.	<b>City Compensatory Allowance/ Dearness allowance</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.	Salary
7.	<b>Benefit or Perquisite to a Director</b> : The value of any benefit or perquisite, whether convertible into money or not, obtained from a company by. (a) a director, or (b) a person having substantial interest in the company, or (c) a relative of the director or of the person having substantial interest, and any sum paid by any such company in respect of any obligation which, but for such payment, would have been payable by the director or other person aforesaid;	Salary (If as per employment agreement) Else under Other Sources (If not in the terms of employment agreement)

8.	<b>Any Benefit or perquisite to a Representative Assessee</b> : The value of any benefit or perquisite (whether convertible into money or not) obtained by any representative assessee under Section 160(1) (iii)/ (iv) or beneficiary, or any amount paid by the representative assessee in respect of any obligation which, but for such payment, would have been payable by the beneficiary;	Other Sources
9.	Deemed profits chargeable to tax under section 28 or section 41 or section 59	PGBP
10.	<b>Capital Gain</b> : Any capital gains chargeable to tax under Section 45; since the definition of income in Section 2(24) is inclusive and not exhaustive capital gains chargeable under Section 46(2) are also assessable as income.	Capital Gains
11.	<b>Insurance Profit</b> : The profits and gains of any Insurance business carried on by a mutual insurance company or by a co-operative society computed in accordance with the provisions of Section 44 or any surplus taken to be such profits and gains by virtue of the profits contained in the First Schedule to the Income-tax Act	PGBP
12.	<b>Banking income of a Co-operative Society</b> : The profits and gains of any business of banking (including) providing credit facilities carried on by a cooperative society with its members.	PGBP
13.	<b>Winnings from Lottery</b> : Any winnings from lotteries, crossword puzzles, races, including horse-races, card-games and games of any sort or from gambling or betting of any form.	Other Sources
14.	<b>Employees Contribution Towards Provident Fund</b> : 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 (34 of 1948) or any other fund for the welfare of such employees.	PGBP if not deposited by the assessee to the specified fund
15.	<b>Amount Received under Keyman Insurance Policy</b> : Any sum received under a Keyman Insurance Policy including the sum allocated by way of bonus on such policy. Keyman Insurance Policy means a life insurance policy taken by a person on the life of another person who is or was the employee of the first mentioned person or is or was connected with the business of the first mentioned person in any manner whatsoever.	PGBP
16.	<b>Amount received for not carrying out any activity</b> : Any sum referred to in Section 28(va), i.e. any sum, whether received or receivable in cash or kind, under an agreement for -  (i) not carrying out any activity in relation to any business or profession; [Amendment vide Finance Act, 2016]  (ii) not sharing any know-how, patent, copyright, trade-mark, license, franchise or any other business or commercial right of similar nature or information or technique likely to assist in the manufacture or processing of goods or provision for services	PGBP

17.	Any sum referred to in clause (v) or (vi) of sub-section (2) of section 56	Other sources
18.	<b>Gift received for an amount exceeding Rs. 50,000</b> : Any sum of money or value of property referred to in clause (vii) or clause (viiia) of sub-section (2) of Section 56	Other sources
19.	Any consideration received for issue of shares as exceeds the fair market value of the shares referred in section 56(2)(viib).	Other sources
20.	Amount received as an advance or otherwise in the course of negotiation for transfer of a capital asset referred to in clause (ix) of section 56(2).	Other sources
21.	Any sum of money or value of property received without consideration or for inadequate consideration as referred to in clause (x) of Section 56(2)	Other sources
22.	Any compensation or payment in connection with termination of employment as referred under clause (xi) of Section 56(2).	Other sources
23.	Assistance in the form of a subsidy or grant or cash incentive or duty drawback or waiver or concession or reimbursement (by whatever name called) by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee other than the subsidy or grant or reimbursement which is taken into account for determination of the actual cost of the asset in accordance with the provisions of Explanation 10 to clause (1) of section 43.	PGBP

### TOTAL INCOME [SECTION 2(45)]

Total income is computed under the 5 heads of income. Income computed under each head of income is aggregated and the aggregate income is called as the Gross Total Income, certain deductions are allowed under Chapter VIA and the balance income taxable after deductions is called as Total Income.

A study of some of the broad principles given below will help to understand the concept of income.

#### 1. Cash or kind

Income may be received in cash or kind. When the income is received in kind, its valuation will be made in accordance with the rules prescribed in the Income-tax Rules, 1962.

#### 2. Receipt basis/ Accrual basis

Income arises either on receipt basis or on accrual basis. It may accrue to a taxpayer without its actual receipt. The income in some cases is deemed to accrue or arise to a person without its actual accrual or receipt. Income accrues where the right to receive arises.

#### 3. Legal or illegal source

The income-tax law does not make any distinction between income accrued or arisen from a legal source and income tainted with illegality. In *CIT v. Piara Singh* (1980) 3 Taxman 67, the Supreme Court has held that if smuggling activity can be regarded as a business, the confiscation of currency notes by customs authorities is a loss which springs directly from the carrying on of the business and is, therefore, permissible as a deduction.

#### 4. Temporary/Permanent

There is no difference between temporary and permanent income under the Act. Even temporary income is taxable under the Income Tax Act.

**5. Lumpsum/instalments**

Income whether received in lump sum or in installment is liable to tax. For example : arrears of salary or bonus received in lump sum is income and charged to tax as salary.

**6. Gifts**

Normally, gifts constitute a capital receipt in the hands of the recipient. However, certain gifts are brought within the purview of income- tax, for example, receipt of property without consideration is brought to tax under section 56(2)(x). Gifts of personal nature do not constitute income subject to maximum of Rs. 50,000 received in cash. The recipient of gifts like birthday, marriage gifts, etc., is not liable to income-tax as received in kind however as per the Finance Act, 2009 gifts in kind having fair value upto Rs. 50,000 are not liable to tax but having fair value of more than Rs. 50,000 is wholly taxable.

**7. Revenue or Capital receipt**

Income-tax, as the name implies, is a tax on income and not a tax on every item of money received. Therefore, unless the receipt in question constitutes income as distinguished from capital, it cannot be charged to tax. For this purpose, income should be distinguished from capital which gives rise to income. However, some capital receipts have been specifically included in the definition of income.

**CAPITAL AND REVENUE RECEIPTS**

The Act contemplates a levy of tax on income and not on capital and hence it is very essential to distinguish between capital and revenue receipts. Capital receipts cannot be taxed, unless they fall within the scope of the definition of “income” and so the distinction between capital and revenue receipts is material for tax purposes.

Certain capital receipts which have been specifically included in the definition of income are compensation for modification or termination of services, income by way of capital gains etc.

It is not possible to lay down any single test as infallible or any single criterion as decisive, final and universal in application to determine whether a particular receipt is capital or revenue in nature. Hence, the capital or revenue nature of the receipt must be determined with reference to the facts and circumstances of each case.

**Criteria for determining whether a receipt is capital or revenue in nature:**

An amount referable to fixed capital is a capital receipt whereas a receipt referable to circulating capital would be a revenue receipt. While the latter is chargeable to tax, the former is not subject to income-tax unless otherwise expressly provided.

**TYPE OF CAPITAL**

Fixed capital	Circulating Capital
Fixed capital is that which is not involved directly in the process of business but remains unaffected by the process.	Circulating capital is that part of the capital which is turned over in the business and which ultimately results in profit or loss. For instance, the proceeds of sale of stock-in-trade is a revenue receipt while the sale proceeds of building, machinery or plant will be capital receipt.

The Income-tax Act does not define the term “Capital receipt” & “Revenue receipt”. Also, it has not laid down the criterion for differentiating the capital and revenue receipt. Yet, it has exempted certain capital receipts from taxation while certain capital receipts have been taken into ambit of capital receipts chargeable as capital gains.

Whether a particular receipt is of the nature of income or capital is explained below by the following examples.

The following test can be applied to determine the nature of particular receipt.

Base	Explanation	Example
<b>Type of capital will depend upon the nature of business</b>	The very same thing may be fixed capital in the hands of one business but circulating capital in the hands of another.	An amount received on account of sale of trading goods or receipts in respect of circulating capital or of flowing capital is revenue receipt, for example sale of a motor car by a dealer. On the other hand a receipt on account of sale of fixed assets is a capital receipt, for example, amount received on sale of a motor car by a person who is not a car dealer.
<b>Nature of receipt also depends upon the reference to the recipient</b>	Whether a particular receipt is capital or revenue in nature must be determined with reference to the recipient who is sought to be taxed as the assessee. For tax purposes the capital or revenue character of the receipt must be determined on the basis of the nature of the trade in the course of which or in connection with which it arises.	<ul style="list-style-type: none"> <li>• The reimbursement of capital outlay is a capital receipt even if the total amount received exceeds the cost of the outlay itself.</li> <li>• Compensation received for the loss of a capital asset is a receipt of a capital nature whereas the compensation received for damage to or loss of a trading asset is a revenue receipt.</li> <li>• A capital asset is converted into income and the price realized on its sale takes form of the periodic payments of a revenue nature;</li> <li>• Where a person sells his properties and the sale price is payable to him by the purchaser in the form of annuities of a fixed sum so long as the seller is alive or until he attains a particular age.</li> </ul>
<b>Capital and Revenue Receipts in Relation To Business Activities</b>	<p>Profits and gains arising from the various transactions which are entered into in the ordinary course of the business of the tax payers or those which are incidental to or closely associated with his business would be revenue receipts chargeable to tax.</p> <p>But even in these cases the receipts may be of a capital nature in certain circumstances.</p>	<ul style="list-style-type: none"> <li>• profits on purchase and sale of shares by a share broker on his own account;</li> <li>• profits arising from dealings in foreign exchange by a banker or other financial institutions,</li> <li>• income from letting out buildings owned by a company to its employees etc.</li> </ul> <p>For instance, profit on sale of shares and securities held by a bank as investments would be of a capital nature. Where profits arise from transactions which are outside the normal dealing of the assessee, although connected with his business, the taxable nature or otherwise of the profits would depend upon the fact whether or not the transaction(s) in question constitute(s) trading activity.</p>

### Factors that do not determine the nature or character of receipt

The capital or revenue nature of a receipt must be determined with reference to each receipt on the basis of the facts and circumstances of each case., the ultimate conclusion as to the capital or revenue character of the receipt would be of the High Court or the Supreme Court and the principles laid down by the Court. However, while determining the question whether a particular receipt is capital or revenue in nature, care must be taken to ensure that the following are not taken as the basis for determination although these factors may, to a certain extent, be helpful to arrive at the conclusion.

Factors	Explanation
<b>Character and source of income</b>	<p>The nature of receipt should be decided entirely on the basis of its character in the hands of the recipient, the source from which the payment has been received being immaterial for the purpose.</p> <p>There may be cases where the payer makes the payment out of capital while the recipient gets it as income. This may happen in a case where there is a businessman who deals in plant and machinery; while the purchaser of the machinery would pay the price out of his capital, the seller would get it as income from business. Therefore, the taxability of the receipt does not depend upon the character of payment in the hands of the payer.</p>
<b>Application of Income</b>	The application of the income after its receipt by the recipient is immaterial for purposes of taxability.
<b>Allowance or disallowance of the amount to the payer</b>	The payment may represent expenditure in the hands of the payer and in certain cases may be disallowed in computing the taxable income of the payer. But the disallowance in the payer's hands would not in any way affect the taxability of the entire amount of remuneration in the employees or directors hands although there may be double taxation of the same amount in two hands for the same period. Thus, the allowance or disallowance of the amount to the payer is immaterial for taxing the recipient.
<b>Treatment given in the books</b>	<p>The name by which the payment is called by the parties concerned and the treatment given to it in the books of accounts of the parties would also be irrelevant.</p> <p>For instance, every item of income from employment is taxable as salary income whether it is called salary, wages, bonus, pension, and annuity or by any other name. In other words, it is only the real character of the receipt and not what the parties call it that would determine its taxability.</p>
<b>Magnitude and method of payment</b>	The quantum of the payment, whether it is paid in installments or in lump sum and also whether it is paid at regular intervals of time or otherwise and even the magnitude of the payment are not the factors that determine the capital or revenue character of the receipt for tax purpose.
<b>Basis for measurement of the receipt</b>	The basis for measurement of the receipt (a specified percentage of the estimated profit taken as the basis for measuring damages) should not be taken as the deciding factor for determining the capital or revenue character of the receipt.
<b>Ways or devices resorted by payer</b>	The various devices resorted to by tax payers in arranging their financial affairs do not also conclusively establish the nature of the receipt because a tax payer is legally entitled to arrange his affairs in such a way as to reduce his tax burden to the minimum. In the light of the aforesaid principles the capital or revenue nature of the receipt should be first determined before proceeding to compute the taxable income.

**Illustration :** State whether the following are capital or revenue receipts/expenses and give your reasons :

1. ABC & Co. received Rs. 5,00,000 as compensation from XYZ & Co. for premature termination of contract of agency.
2. Sales-tax collected from the buyer of goods.
3. PQR Company Ltd. instead of receiving royalty year by year, received it in advance in lump sum.
4. An amount of Rs. 1,50,000 was spent by a company for sending its production manager abroad to study new methods of production.
5. Payment of Rs. 50,000 as compensation for cancellation of a contract for the purchase of machinery with a view to avoid an unnecessary expenditure.
6. An employee director of a company was paid Rs. 3,50,000 as a lump sum consideration for not resigning from the directorship.

**Solution**

1. Receipt in substitution of a source of income is a capital receipt. Therefore, the amount received by ABC & Co. from XYZ & Co. for premature termination of an agency contract is a capital receipt though the same is taxable under Section 28(ii)(c).
2. Sales-tax is the liability of a seller to pay to the Government on the sale of goods made by him, which is allowed as deduction as revenue expenditure. If any part of Sales-tax is collected from the buyer of goods that may be treated as a revenue receipt. Thus the sales-tax collected from the buyer of goods is a revenue receipt.
3. Receipt of lump sum royalty in lieu of future royalties is a revenue receipt, as it is an income from royalty.
4. Amount spent by a company for sending its production manager abroad to study new methods of production is revenue expenditure to be allowed as a deduction. Because the new knowledge and exposure of that manager will assist the company in improving its existing methods of production etc.
5. This is a capital expenditure, as any expenditure incurred by a person to free himself from a capital liability is a capital expenditure. In the given case, the payment of Rs. 50,000 for cancelling the order for purchase of the machinery, has helped the assessee to become free from an unnecessary capital liability.
6. The amount of Rs. 3,50,000 received for not resigning from the directorship is a reward received from the employer. Therefore it is a revenue receipt.

**CHARGE OF INCOME TAX [SECTION 4]**

Section 4 of the Act is the charging section. It lays down the basis on which tax is imposed. Section 4 of Income tax act is the most effective and operative of the various provisions in the Act since, it is because of this section alone all other sections become enforceable. The charging section is the backbone of the act, it lays down the provisions as to what are taxable and at what rates; income of which period is taxable and in whose hands. Accordingly, the section provides that :

- a) Income tax shall be charged at the rate or rates prescribed in the finance act for the relevant previous year,
- b) the charge of tax is on various persons specified u/s 2(31);
- c) the income sought to be taxed is that of the previous year and not of the of assessment year
- d) the levy of tax on the assessee is on his total or taxable income computed in accordance with and subject to the appropriate provisions of the income tax Act, including provisions for the levy of additional income-tax

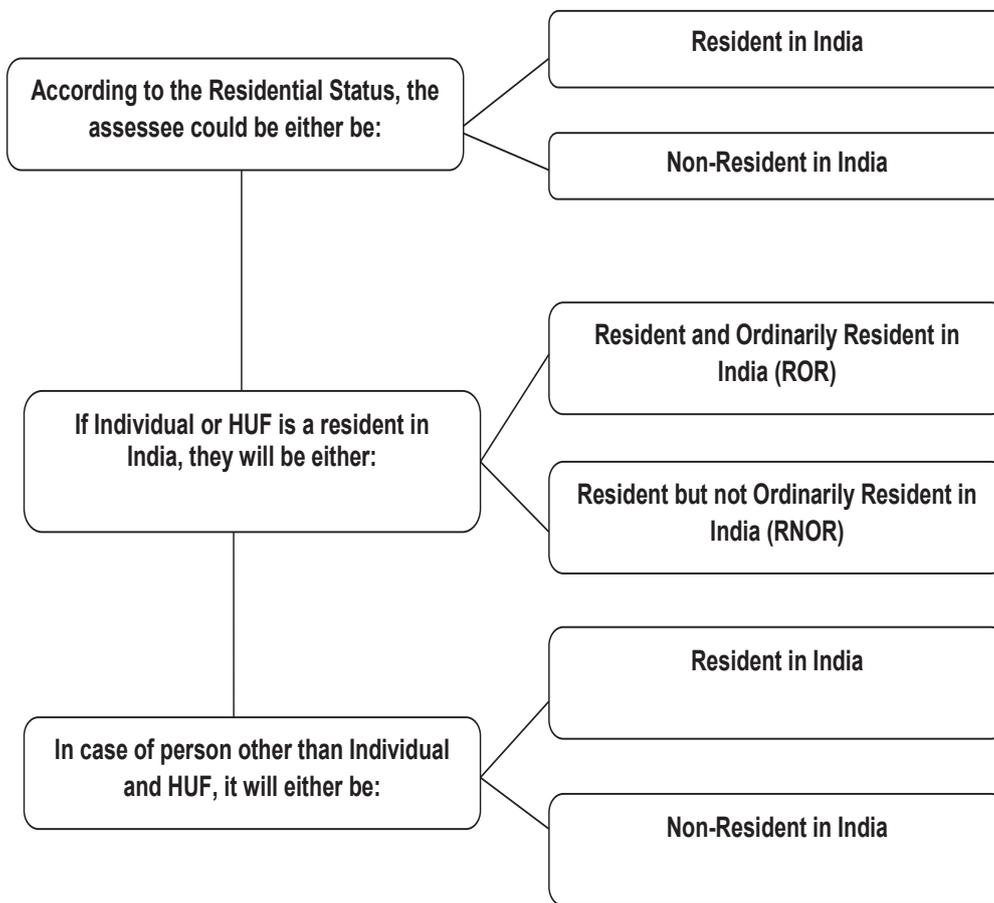
Provided that where by virtue of any provision of this Act income-tax is to be charged in respect of the income of a period other than the previous year, income-tax shall be charged accordingly.

**RESIDENTIAL STATUS [SECTION 6]**

Total income of an assessee cannot be computed unless the person’s residential status in India during the previous year is known. Thus, determining residential status of a person is important for calculating tax liability of a person.

Section 6 of the Income tax Act prescribes the tests to be applied to determine the residential status of all tax payers for purposes of income-tax. An assessee’s residential status must be determined with reference to the previous year in respect of which the income is sought to be taxed.

Residential status of a person could be :



There are different test to be applied for different types of person, let us understand test for each category of person :

**TEST OF RESIDENCY FOR INDIVIDUALS**

**Basic Condition for a person to be Resident**

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

- (a) is in India in the previous year for a period or periods amounting in all to one hundred and eighty-two days or more i.e., he has been in India for at least 182 days during the previous year; or,

- (b) has been in India for at least three hundred and sixty-five days (365 days) during the four years preceding the previous year and has been in India for at least sixty days (60 days) during the previous year.

### Exception to the basic condition

In the case of following individual –

- (a) being a citizen of India, who leaves India in any previous year as a member of the crew of an Indian ship as defined in clause (18) of section 3 of the Merchant Shipping Act, 1958 (44 of 1958), or for the purposes of employment outside India,

#### Rule 126 Computation of period of stay in India in certain cases

An individual, being a citizen of India and a member of the crew of a ship, the period of stay in India in respect of an eligible voyage shall not include the period beginning from the date of joining till the date of signing off as mentioned in the Continuous Discharge Certificate under the Merchant Shipping Act, 1958

“eligible voyage” shall mean a voyage undertaken by a ship engaged in the carriage of passengers or freight in international traffic where –

- (i) for the voyage having originated from any port in India, has as its destination any port outside India; and
  - (ii) for the voyage having originated from any port outside India, has as its destination any port in India.
- (b) being a citizen of India, or a person of Indian origin within the meaning of Explanation to clause (e) of section 115C, who, being outside India, comes on a visit to India in any previous year,

The provisions of the second condition shall apply in relation to that year as if for the words “sixty days (60 days)”, occurring therein, the words “one hundred and eighty-two days (182 days)” had been substituted.

*A person is deemed to be of Indian origin if he, or either of his parents or any of his grandparents, was born in Undivided India. It may be noted that grandparents include both maternal and paternal grand parents.*

### Non-Resident

If an individual does not satisfy any of the above basic condition then, he will be treated as Non-Resident. It must be noted that the fulfillment of any one of the above conditions (a) or (b) as applicable will make an individual resident in India for tax purposes. Further it is to be noted that these conditions are alternative and not cumulative in their application.

### Resident and Ordinarily Resident (ROR)

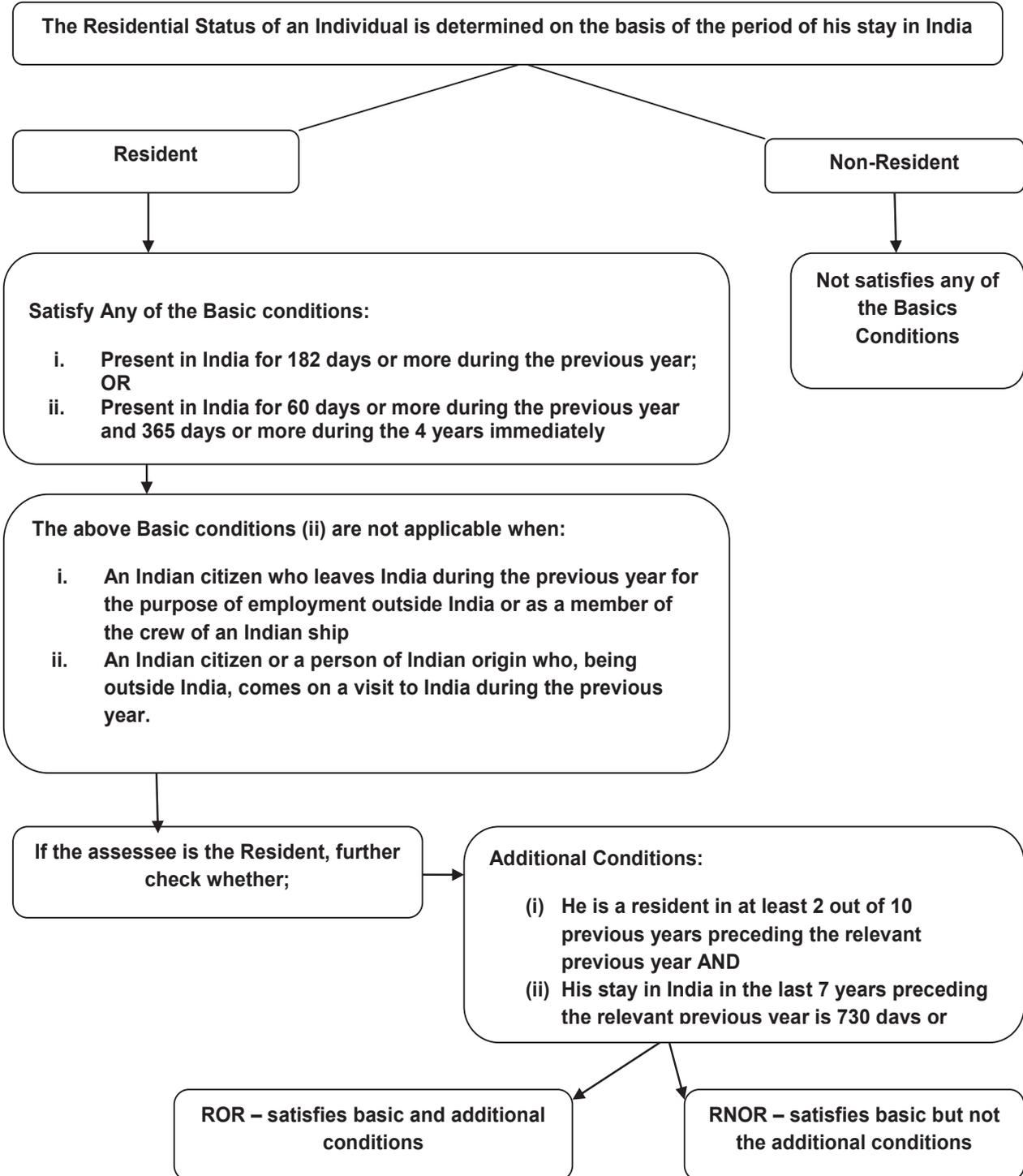
An individual may become a resident and ordinarily resident in India if he satisfy both the following conditions given u/s 6(1) besides satisfying any one of the above mentioned conditions:

- (i) he is a resident in atleast any two out of the ten previous years immediately preceding the relevant previous year, and
- (ii) he has been in India for 730 days or more during the seven previous years immediately preceding the relevant previous year.

### Resident but Not Ordinarily Resident (RNOR)

An individual is not ordinarily resident in any previous year if –

- (a) he has been a non-resident in India in nine out of the ten previous years preceding that year, or
- (b) he has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, seven hundred and twenty-nine days (729 days) or less.



**Important Points**

- The fact that an assessee is resident in India in respect of one year does not automatically mean that

he would be resident in the preceding or succeeding years as well. Consequently, the residential status of the assessee should be determined for each year separately. This is in view of the fact that a person resident in one year may become non-resident or not ordinarily resident in another year and vice versa.

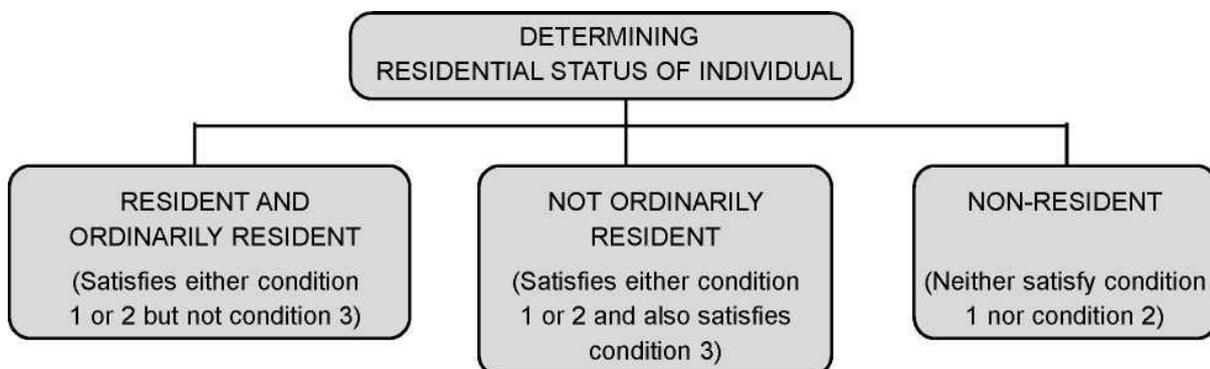
- It must also be noted that the residential status of an individual for tax purposes is neither based upon nor determined by his citizenship, nationality and place of birth or domicile. This is because of the fact that, for tax purposes, an individual may be resident in more than one country in respect of the same year.
- The common feature in both the above conditions is the stay of the individual in India for a specified period. The period of stay required in each of the conditions need not necessarily be continuous or consecutive nor it is stipulated that the stay should be at the usual place of residence, business or employment of the individual. Purpose of stay is immaterial in determining the residential status.
- The stay may be anywhere in India and for any length of time at each place in cases where the stay in India is at more places than one, what is required is the total period of stay should not be less than the number of days specified in each condition.
- While determining residential status, the day of leaving and returning to India should be considered as a stay in India.
- Person of Indian Origin is one who is, or either of his parents or grandparents was born in Undivided India.
- India means territory of India, its territorial waters, continental shelf, Exclusive Economic Zone (upto 200 nautical miles) and airspace above its territory and territorial waters.
- Where the exact arrival and departure time is not available then the day he comes to India and the day he leaves India is counted as stay in India.

### Steps to solve residential status of an Individual :

**Step 1 :** Determine whether the individual falls under exception to basic condition;

**Step 2 :** If yes, apply only first basic condition, if satisfied, then he will be resident otherwise non-resident. If no, then apply both basic conditions and Individual becomes Resident on satisfaction of any one of the conditions.

**Step 3 :** Check if satisfy the test of Ordinarily Residents , if yes, then he will be called ROR, otherwise he will be called RNOR.



**Condition 1 :** If individual is in India in the previous year for a total period of 182 days or more.

**Condition 2 :** If he has been in India for at least 365 days during the 4 years preceding the previous year and

**38 EP-TL**

has been in India for at least 60 days during the previous year. However, this 60 days shall be read as 182 days, if he is a :

- Citizen of India, who leaves India in any previous year as a member of the crew of an Indian ship, or for the purpose of employment outside India or
- Citizen of India or of Indian origin engaged outside India (whether for rendering service outside or not) and who comes on a visit to India in the any previous year.

**Condition 3 :** An individual who has been a non-resident in India in at least nine out of the ten previous years preceding that year, and has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to 729 days or less.

**Illustration 1**

Mr. A, an Indian Citizen, is living in Mumbai since 1950, he left for China on July 1, 2014 and comes back on August 7, 2019. Determine his residential status for the assessment year 2020-21.

**Solution :**

Stay in India for a minimum period of 182 days in the previous year :

Mr. A has stayed in India for 237 (viz. 25 + 30 + 31 + 30 + 31 + 31 + 28 + 31) days in the Previous year 2019-20. So, this test is satisfied.

So, Mr. A shall be a resident in India during the previous year 2019-20. (Assessment year 2020-21).

Keeping in view the facts of the given case, Mr. A satisfies the two additional conditions also namely :

He is resident in two out of ten previous years preceding the relevant previous year.

PY	Stay in PY (days)	Stay during PY (days)	Basic Condition Satisfied	Resident/Non-Resident
2018-19	Nil	-	None	Non-Resident
2017-18	Nil	-	None	Non-Resident
2016-17	Nil	-	None	Non-Resident
2015-16	Nil	-	None	Non-Resident
2014-15	30+31+30+1= 92	365 days	Second	Resident
2013-14	365	365	First	Resident

His stay in India is also more than 730 days in 7 previous years preceding the relevant previous year. As he left for Japan on 1st July 2014.

PY	Stay (days)
2018-19	Nil
2017-18	Nil
2016-17	Nil
2015-16	Nil
2014-15	92
2013-14	365
2012-13	366
Total Stay in 7 Previous Years	823

Hence, Mr. A is resident and ordinary resident in India for the assessment year 2020-21.

**Illustration 2**

Mr. Steve Waugh, the Australian cricketers comes to India for 100 days every year. Find out his residential status for AY 2020-21.

**Solution :**

**Step 1 :** The total stay of Steve Waugh in the last 4 preceding years is 400 days and his stay in India during the previous year is 100 days. Since, he satisfied the second condition in section 6(1), he is resident.

**Step 2 :** Since his total stay in India in the last 7 years preceding the previous years is 700 days, he does not satisfy the minimum requirements of 730 days in 7 years.

Therefore the residential status of Mr. Steve Waugh for the assessment year 2020-21 is Resident but not ordinarily resident in India.

**Illustration 3**

Dr. A, an Indian Citizen and a Professor in IIM, Lucknow, left India on September 15, 2019 for USA to take up Professors job in MIT, USA. Determine his residential status for the assessment year 2020-21.

**Solution :**

Dr. A being a citizen of India and who has gone out of the country for employment, will be governed by 182 days test only and therefore the second condition under section 6(1), i.e. 60 days during relevant previous year shall not be applicable.

Dr. A stayed in India for 168 (viz. 30 + 31 + 30 + 31 + 31 + 15) days only in the relevant previous year.

Hence, Dr. A shall be a non-resident in India for the assessment year 2020-21 as condition by stay of 182 days in relevant previous year is not satisfied.

**Illustration 4**

Mr. X is a foreign citizen. His father was born in Mumbai in 1960 and mother was born in USA in 1965. His grandfather was born in Chennai in 1935. Mr. X is coming to India to see Taj Mahal and visit other historical places in India. He comes to India on 1st November, 2019 for 200 days. He has never come to India before. Determine his residential status for AY 2019-20.

**Solution :**

Mr. X falls in exception to basic conditions as he is a Person of Indian Origin (as his grandfather was born in undivided India) and he comes on a visit to India during relevant Previous year. Therefore, only first basic condition of 182 days during relevant previous year would be checked.

Stay during relevant PY 2019-20 = 1st Nov, 2019 to 31st March, 2020 = 30+31+31+28+31 = 151 days Mr. X is Non-resident in India for AY 2020-21 as he does not satisfy first basic condition.

**Illustration 5**

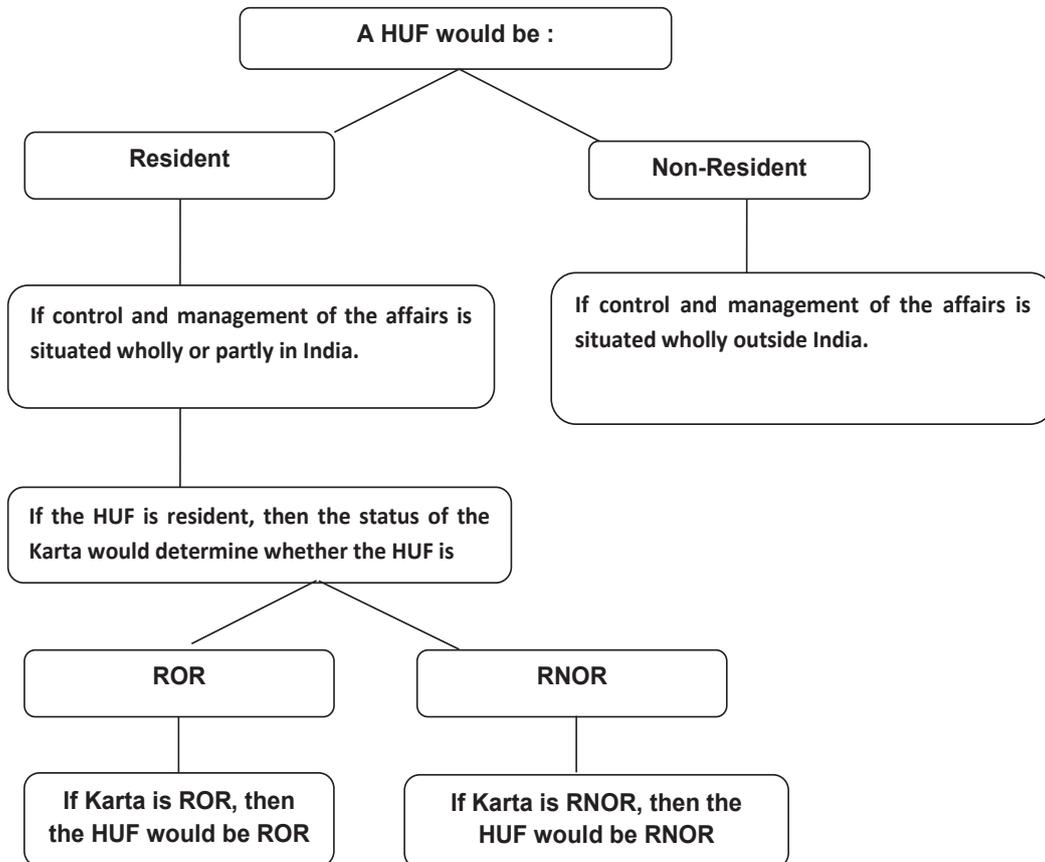
Mr. Anil, an Indian citizen, leaves India on 22nd September, 2019 for the first time to work as an Engineer in France. Determine his residential status for AY 2020-21.

**Solutions :**

During the previous year 2019-20, Mr. Anil, an Indian citizen, was in India for 175 days (i.e. 30+31+30+31+31+22). He does not satisfy the minimum criteria of 182 days. Also since he is an Indian citizen leaving India for the purpose of employment outside India, the second condition u/s 6(1) is not applicable to him.

Therefore Mr. Anil is non-resident for the AY 2020-21.

## TESTS OF RESIDENCE FOR HINDU UNDIVIDED FAMILIES



The test to be applied to determine the residential status of a HUF is based upon the control and management of the affairs of the assessee concerned. The tests based on the period of stay in India applicable to individuals cannot be applied to these assessees for obvious reasons.

### Meaning of place of control and management :

The expression control and management refers to the functions of decision-making and issuing directions but not the places where from the business is carried on.

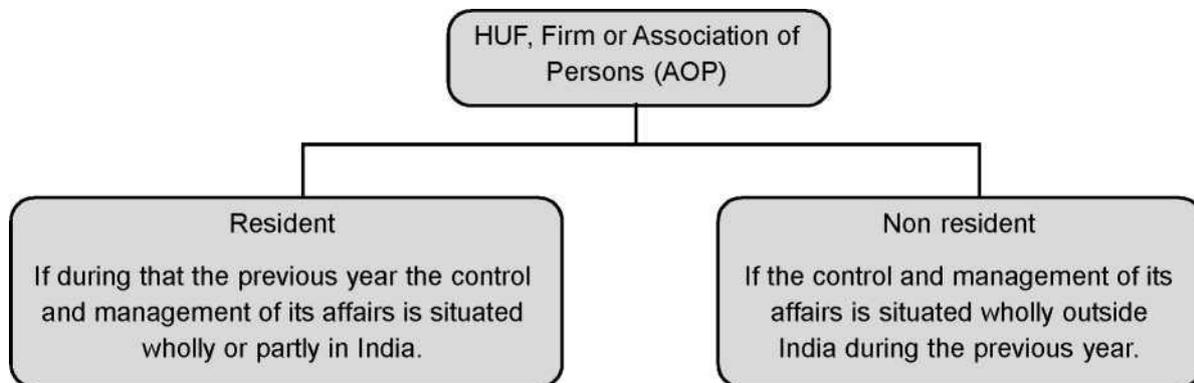
In other words, the Control and Management means taking policy decisions relating to business. Policy decisions are concerning finance, marketing, production, advertising, personnel etc. It does not mean day to day operations of the concern/assessee. The control and management is situated at that place where policy decisions are taken.

The business may be done from outside India and yet its control and management may be wholly within India. Therefore, control and management of a business is said to be situated at a place where the head and brain of the business is situated. The place of control and may be different from the usual place of running the businesses and sometimes even the registered office of the assessee. But control and management do imply the functioning of the controlling and directing power at a particular place with some degree of permanence.

- Control and Management of HUF : It is with Karta or its Manager.
- Control and Management of Firm/AOP : It is with Partners/Members.

A HUF, firm or other association of persons is said to be resident in India within the meaning of Section 6(2)

in any previous year, if during that year the control and management of its affairs is situated wholly or partly in India. If the control and management of its affairs is situated wholly outside India during the relevant previous year, it is considered non resident.



### An HUF can be “not ordinarily resident”

If manager/karta has been a not ordinarily resident in India in the previous year in accordance with the tests applicable to individuals. Where, during the last ten years the kartas of the H.U.F. had been different from one another, the total period of stay of successive kartas of the same family should be aggregated to determine the residential status of the karta and consequently the H.U.F.

In other words, if Karta of Resident HUF satisfies both the following additional conditions (as applicable in case of Individual) then Resident HUF will be ROR, otherwise it will be RNOR :

#### Additional Conditions :

- (1) Karta of Resident HUF should be resident in atleast 2 previous years out of 10 previous year immediately preceding relevant previous year.
- (2) Stay of Karta during 7 previous year immediately preceding relevant previous year should be 730 days or more.

#### Important Note :

- It is immaterial whether Karta is Resident or Non-Resident during relevant previous year, for the purpose of determining whether HUF is ROR or RNOR. If Karta satisfies both the additional conditions, then HUF will be ROR, otherwise RNOR.
- Firms, association of persons, local authorities and other artificial juridical persons can be either resident (ordinarily resident) or non-resident in India but they cannot be not ordinarily resident in India.
- Even if negligible portion of the control and management of the affairs is exercised from India, it will be sufficient to make the family, firm or the association resident in India for tax purposes. For instance, if the affairs of a firm are controlled partly from India and partly from Bangladesh, the firm would be resident in India.
- While the control and management of the affairs of the firm or family would necessarily be exercised by the partners of the firm or members of the family, the residential status of the members or partners is generally irrelevant for determining the residential status of the firm or family. But in cases where the residential status of the partners materially affects or determines the place of control and management of the affairs of the firm, the residential status of the member or partners should also be taken into account in determining the residential status of the firm or the family.

## 42 EP-TL

- The mere fact that all the partners are resident in India does not necessarily lead to the conclusion that the firm is resident in India because there may be cases where even though the partners are resident in India, control and management of the affairs of the firm is exercised from outside India.
- A Hindu Undivided Family would generally be presumed to be resident in India unless the assessee proves to the tax authorities that the control and management of its affairs is situated wholly outside India during the relevant accounting year.

### Illustration 1

An HUF, whose affairs of business are completely controlled from India. Determine its Residential status for AY 2020-21 (a) if Karta is ROR in India for that year (b) If Karta is NR in India but he satisfies both the additional conditions (c) If Karta is RNOR in India.

#### Solution :

HUF would be Resident in India as Control and Management is wholly situated in India. Determination of whether HUF is ROR or RNOR :

- a) HUF is ROR in India as Karta would be satisfying both the additional conditions (because he is ROR).
- b) HUF is ROR in India as Karta is satisfying both the additional conditions. Karta's Residential status during relevant previous year (i.e. resident/non-resident) is irrelevant.
- c) HUF is RNOR as Karta does not satisfy both the additional conditions.

### Illustration 2

Karta of an Hindu Undivided Family comes to India every year for a minimum period of 60 days and maximum 91 days. Determine residential status of the HUF for the assessment year 2020-21.

#### Solutions :

Hindu Undivided Family is resident since the karta has come to India for at least 60 days but the stay of karta during seven years can be maximum 637 days. Hence HUF can be considered as resident but not ordinarily resident.

### Illustration 3

Hindu Undivided Family is being managed partly from Mumbai and partly from Japan. The Karta of HUF is a foreign citizen and comes to visit in India every year since 1980 in the month of April for 105 days.

Determine residential status of HUF for AY 2020-21.

#### Solutions :

Since the control and management of the affairs of HUF is partly managed from Mumbai and therefore HUF is resident in India. Further, the Karta of HUF is also satisfying both of additional conditions of section 6 (6)(b) and therefore HUF is resident and ordinarily resident in India during the AY 2020-21.

## TEST OF RESIDENCE FOR COMPANIES

All Indian companies within the meaning of Section 2(26) of the Act are always resident in India regardless of the place of control and management of its affairs.

In the case of a foreign company the place of control and management of its affairs is the basis on which the company's residential status is determinable.

Accordingly a company shall be said to be resident in India in any previous year, if –

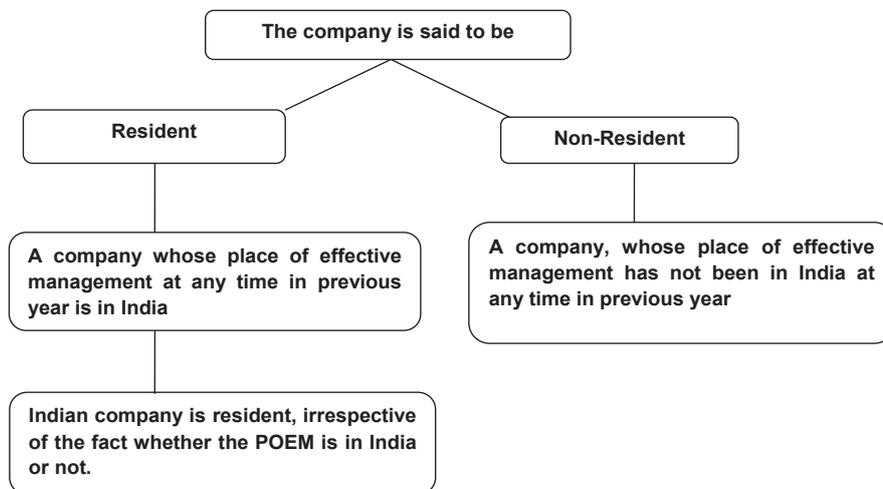
- (i) it is an Indian company; or

(ii) its place of effective management, in that year, is in India.

It must be noted that only an individual or a HUF can be resident, not ordinarily resident or non-resident in India. All other assesses can be either resident or non-resident in India but cannot be not ordinarily resident in the matter of their residential status for all purposes of income tax.

The assessment should, in every case, be made in accordance with the provisions of the law in force in the relevant assessment year and not the law applicable to the previous year.

From Assessment Year 2017-18 a foreign company will be resident in India if its Place Of Effective Management (POEM) during the previous year is in India. For this purpose, the Place Of Effective Management means a place where Key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance are made.



Place of Effective Management (POEM) means a place where key management and commercial decisions, necessary for the conduct of the business of an entity as a whole are, in substance made.

**Note :** Vide Circular No 08 of 2017 dated 23rd February, 2017. it has been clarified that the POEM provisions shall not apply to a company having turnover or gross receipts of Rs 50 crore or less in a financial year. *Please refer details: [https://www.incometaxindia.gov.in/communications/circular/circular25\\_2017.pdf](https://www.incometaxindia.gov.in/communications/circular/circular25_2017.pdf)*

**Guiding Principles for Determination of Place of Effective Management (POEM) of a Company**

Place of effective management (POEM) is an internationally recognised test for determination of residence of a company incorporated in a foreign jurisdiction. Most of the tax treaties entered into by India recognises the concept of place of effective management for determination of residence of a company as a tie-breaker rule for avoidance of double taxation. The guiding principles to be followed for determination of POEM are enumerated as follows :

A company shall be said to be engaged in “active business outside India” if the passive income is not more than 50% of its total income; and

- (i) less than 50% of its total assets are situated in India; and
- (ii) less than 50% of total number of employees are situated in India or are resident in India; and
- (iii) the payroll expenses incurred on such employees is less than 50% of its total payroll expenditure.

**Explanation :** For the aforesaid purpose :

the income shall be	As computed for tax purpose in accordance with the laws of the country of incorporation; or as per books of account, where the laws of the country of incorporation does not require such a computation.
the value of assets	<ul style="list-style-type: none"> <li>• In case of an individually depreciable asset, shall be the average of its value for tax purposes in the country of incorporation of the company at the beginning and at end of the previous year; and</li> <li>• In case of pool of a fixed assets being treated as a block for depreciation, shall be the average of its value for tax purposes in the country of incorporation of the company at the beginning and at end of the year;</li> <li>• In case of any other asset, shall be its value as per books of account;</li> </ul>
the number of employees	the number of employees shall be the average of the number of employees as at the beginning and at the end of the year and shall include persons, who though not employed directly by the company, perform tasks similar to those performed by the employees;
pay roll	the term “pay roll” shall include the cost of salaries, wages, bonus and all other employee compensation including related pension and social costs borne by the employer.
Head Office	<p>“Head Office” of a company would be the place where the company senior management and their direct support staff are located or, if they are located at more than one location, the place where they are primarily or predominantly located.</p> <p>A company head office is not necessarily the same as the place where the majority of its employees work or where its board typically meets;</p>
Passive income	<p>“Passive income” of a company shall be aggregate of, income from the transactions where both the purchase and sale of goods is from / to its associated enterprises; and income by way of royalty, dividend, capital gains, interest or rental income;</p> <p><i>Note</i> : any income by way of interest shall not be considered to be passive income in case of a company which is engaged in the business of banking or is a public financial institution, and its activities are regulated as such under the applicable laws of the country of incorporation.</p>
Senior Management	“Senior Management” in respect of a company means the person or persons who are generally responsible for developing and formulating key strategies and policies for the company and for ensuring or overseeing the execution and implementation of those strategies on a regular and on-going basis. While designation may vary, these persons may include : (i) Managing Director or Chief Executive Officer; (ii) Financial Director or Chief Financial Officer; (iii) Chief Operating Officer; and (iv) The heads of various divisions or departments.

The determination of the POEM will depend upon the facts and circumstances of a given case. The POEM concept is one of substance over form. It may be noted that an entity may have more than one place of management, but it can have only one place of effective management at any point of time. Since “residence” is to be determined for each year, POEM will also be required to be determined on year to year basis. The process of determination of POEM would be primarily based on the fact as to whether or not the company is engaged in active business outside India.

### Determination of POEM if active business outside India

The place of effective management in case of a company engaged in active business outside India shall be presumed to be outside India if the majority meetings of the board of directors of the company are held outside India. However, it is established that the Board of directors of the company are standing aside and not exercising their powers of management and such powers are being exercised by either the holding company or any other person (s) resident in India, then the place of effective management shall be considered to be in India. For the purpose of determining whether the company is engaged in active business outside India, the average of the data of the previous year and two years prior to that shall be taken into account. In case the company has been in existence for a shorter period, then data of such period shall be considered.

### Determination of POEM other than those that are engaged in active business outside India

In this case, the determination of POEM would be a two stage process as follows :

**First Stage** : Identification or ascertaining the person or persons who actually make the key management and commercial decision for conduct of the company business as a whole.

**Second Stage** : Determination of place where these decisions are in fact being made.

**Note** : The place where these management decisions are taken would be more important than the place where such decisions are implemented. For the purpose of determination of POEM it is the substance which would be conclusive rather than the form.

### Some of the guiding principles for determining the POEM

- (a) The location where a company's Board regularly meets and makes decisions may be the company place of effective management provided, the Board retains and exercises its authority to govern the company; and in substance, make the key management and commercial decisions necessary for the conduct of the company business as a whole. Mere formal holding of board meetings at a place would by itself not be conclusive for determination of POEM being located at that place.

**Note** : A company's board may delegate some or all of its authority to one or more committees such as an executive committee consisting of key members of senior management. In these situations, the location where the members of the executive committee are based and where that committee develops and formulates the key strategies and policies for mere formal approval by the full board will often be considered to be the company's place of effective management.

- (b) The location of a company's head office will be a very important factor in the determination of the company's place of effective management because it often represents the place where key company decisions are made. The following points need to be considered for determining the location of the head office of the company :

If the company's senior management and their support staff are based in a single location and that location is held out to the public as the company's principal place of business or headquarters then that location is the place where head office is located. If the company is more decentralized (for example where various members of senior management may operate, from time to time, at offices

located in the various countries) then the company's head office would be the location where these senior managers :

- i. are primarily or predominantly based; or
- ii. normally return to following travel to other locations; or
- iii. meet when formulating or deciding key strategies and policies for the company as a whole.

In situations where the senior management is so decentralised that it is not possible to determine the company's head office with a reasonable degree of certainty, the location of a company's head office would not be of much relevance in determining that company's place of effective management.

- c) The use of modern technology impacts the place of effective management in many ways. It is no longer necessary for the persons taking decision to be physically present at a particular location. Therefore physical location of board meeting or executive committee meeting or meeting of senior management may not be where the key decisions are in substance being made. In such cases the place where the directors or the persons taking the decisions or majority of them usually reside may also be a relevant factor.

It may be clarified that day to day routine operational decisions undertaken by junior and middle management shall not be relevant for the purpose of determination of POEM.

If the above factors do not lead to clear identification of POEM then the following secondary factors can be considered :

- i. Place where main and substantial activity of the company is carried out; or
- ii. Place where the accounting records of the company are kept.

The determination of POEM is to be based on all relevant facts related to the management and control of the company, and is not to be determined on the basis of isolated facts that by itself do not establish effective management, as illustrated by the following examples :

- i. The fact that a foreign company is completely owned by an Indian company will not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.
- ii. The fact that there exists a Permanent Establishment of a foreign entity in India would itself not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.
- iii. The fact that one or some of the Directors of a foreign company reside in India will not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.
- iv. The fact of, local management being situated in India in respect of activities carried out by a foreign company in India will not , by itself, be conclusive evidence that the conditions for establishing POEM have been satisfied.
- v. The existence in India of support functions that are preparatory and auxiliary in character will not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.

Further, based on the facts and circumstances if it is determined that during the previous year the POEM is in India and also outside India then POEM shall be presumed to be in India if it has been mainly /predominantly in India.

**Example 1** : Company A Co. is a sourcing entity, for an Indian multinational group, incorporated in country X and is 100% subsidiary of Indian company (B Co.). The warehouses and stock in them are the only assets of the company and are located in country X. All the employees of the company are also in country X. The average income wise breakup of the company's total income for three years is, :

- i. 30% of income is from transaction where purchases are made from parties which are non-associated enterprises and sold to associated enterprises;

- ii. 30% of income is from transaction where purchases are made from associated enterprises and sold to associated enterprises;
- iii. 30% of income is from transaction where purchases are made from associated enterprises and sold to non-associated enterprises; and
- iv. 10% of the income is by way of interest.

**Interpretation :** In this case passive income is 40% of the total income of the company. The passive income consists of :

- i. 30% income from the transaction where both purchase and sale is from/to associated enterprises; and
- ii. 10% income from interest.

The A Co. satisfies the first requirement of the test of active business outside India. Since no assets or employees of A Co. are in India the other requirements of the test is also satisfied. Therefore company is engaged in active business outside India.

**Example 2 :** The other facts remain same as that in Example 1 with the variation that A Co. has a total of 50 employees. 47 employees, managing the warehouse, storekeeping and accounts of the company, are located in country X. The Managing Director (MD), Chief Executive Officer (CEO) and sales head are resident in India. The total annual payroll expenditure on these 50 employees is of Rs. 5 crore. The annual payroll expenditure in respect of MD, CEO and sales head is of Rs. 3 crore.

**Interpretation :** Although the first limb of active business test is satisfied by A Co. as only 40% of its total income is passive in nature. Further, more than 50% of the employees are also situated outside India. All the assets are situated outside India. However, the payroll expenditure in respect of the MD, the CEO and the sales head being employees resident in India exceeds 50% of the total payroll expenditure. Therefore, A Co. is not engaged in active business outside India.

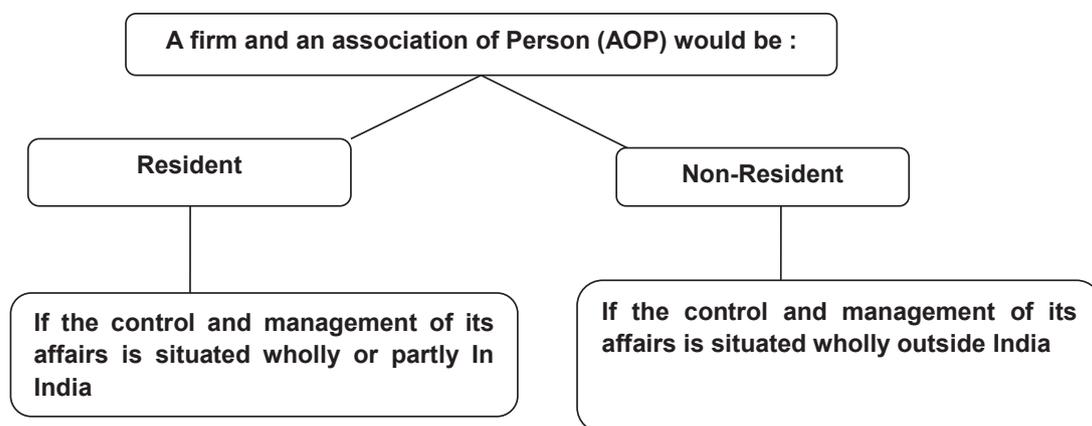
**Example 3 :** The basic facts are same as in Example 1. Further facts are that all the directors of the A Co. are Indian residents. During the relevant previous year 5 meetings of the Board of Directors is held of which two were held in India and 3 outside India with two in country X and one in country Y.

**Interpretation :** The A Co. is engaged in active business outside India as the facts indicated in Example 1 establish. The majority of board meetings have been held outside India. Therefore, the POEM of A Co. shall be presumed to be outside India.

**For Detailed POEM Guidelines :**

<http://www.incometaxindia.gov.in/news/circular06/2017.pdf>

### TEST OF RESIDENCE FOR FIRM AND AOP



- Business and the whole of it may be done outside India and yet the control and management of that business may be wholly within India.
- It is entirely irrelevant where the business is done and where the income has been earned. What is relevant and material is from which place has that business been controlled and managed.

### Illustration 1

AB & Co. is a partnership firm whose operations are carried out in India. However, all meetings of partners take place outside India as all the partners are settled abroad. Determine Residential status of firm for AY 2020-21.

#### Solution :

AB & Co. is Non-Resident in India during relevant previous year as Control and Management (place where policy decisions are taken, here it is the place where meetings are held) is wholly situated outside India.

Once the residential status of an individual is identified, the rule of taxation could be applied to determine whether an income is to be taxed or not.

## MEANING AND SCOPE OF TOTAL INCOME [SECTION 5]

To calculate the total income, it is essential to understand :

- A. Residential status of person by whom the income is earned vis-a vis place where it is earned/ received or deemed to be earned/ received
- B. Time when the income is earned/ received or deemed to be earned or received
- C. What is to be included in income

Section 4 of the Act imposes a charge of tax on the total or taxable income of the assessee. The meaning and scope of the expression of total income is contained in Section 5. The total income of an assessee cannot be determined unless we know the residential status in India during the previous year. The scope of total income and consequently the liability to income-tax also depends upon the following facts :

- (a) whether the income accrues or is received in India or outside,
- (b) the exact place and point of time at which the accrual or receipt of income takes place, and
- (c) the residential status of the assessee.

Scope of total income has been defined on the basis of Residential status

### (A) Resident and Ordinarily Resident Assessee

According to Sub-section (1) of Section 5 of the Act the total income of a resident and ordinarily resident assessee would consist of :

- (i) income received or deemed to be received in India during the accounting year by or on behalf of such person;
- (ii) income which accrues or arises or is deemed to accrue or arise to him in India during the accounting year;
- (iii) income which accrues or arises to him outside India during the accounting year.

*It is important to note that under clause (iii) only income accruing or arising outside India is included. Income deemed to accrue or arise outside India is not includible.*

### (B) Resident but Not Ordinarily Resident In India

Proviso to section (1) of section 5 the total income in case of resident but not ordinarily resident in India

- (i) income received or deemed to be received in India during the accounting year by or on behalf of such person;

- (ii) income which accrues or arises or is deemed to accrue or arise to him in India during the accounting year;
- (iii) income which accrues or arises to him outside India during the previous year if it is derived from a business controlled in or a profession set up in India.

**(C) Non-Resident**

Sub-section (2) of Section 5 provides that the total income of a non-resident would comprise of :

- (i) income received or deemed to be received in India in the accounting year by or on behalf of such person;
- (ii) income which accrues or arises or is deemed to accrue or arise to him in India during the previous year.

**Rule of taxation on the basis of residential status**

Nature of Income	ROR	RNOR	NR
Income received in India (Whether accrued in or outside India)	Taxed	Taxed	Taxed
Income deemed to be received in India (Whether accrued in or outside India)	Taxed	Taxed	Taxed
Income accruing or arising in India (Whether received in India or outside India)	Taxed	Taxed	Taxed
Income deemed to accrue or arise in India (Whether received in India or outside India)	Taxed	Taxed	Taxed
Income received and accrued outside India from a business controlled or a profession set up in India	Taxed	Taxed	Not Taxed
Income received and accrued outside India from a business controlled from outside India or a profession set up outside India	Taxed	Not Taxed	Not Taxed
Income earned and received outside India but later on remitted to India (Whether tax incidence arises at the time of remittance)	Not Taxed	Not Taxed	Not Taxed

**Explanation 1.** - Income accruing or arising outside India shall not be deemed to be received in India within the meaning of this section by reason only of the fact that it is taken into account in a balance sheet prepared in India.

**Explanation 2.** - For the removal of doubts, it is hereby declared that income which has been included in the total income of a person on the basis that it has accrued or arisen or is deemed to have accrued or arisen to him shall not again be so included on the basis that it is received or deemed to be received by him in India.

**Place of receipt of income**

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

- (i) The receipt contemplated for this purpose refers to the first receipt of the amount in question as the income of the assessee.

For instance, if A receives his salary at Delhi and sends the same to his father, the salary income of A is a receipt for tax purposes only in the hands of A; his father cannot also be said to have received income when he receives a part of the income of A. In the hands of ARs. s father it is only a receipt of a sum of money but not a receipt of income.

- (ii) Method of Accounting : Although receipt of income is not the sole test of its taxability, the receipt of income would be the primary basis for determining the taxability of the amount in cases where the assessee follows the cash system of accounting; however, where the assessee follows the mercantile system of accounting the income would become taxable as the income of the accounting year in which it falls due to the assessee regardless of the date or place of its actual receipt.
- (iii) While considering the receipt of income for tax purposes both the place and the date of its receipt must be taken into account. The income in question should be not only received during the accounting year relevant to the assessment year but must also be received in India in order to constitute the basis of taxation. Thus, if an item of income is first received outside India and after a few years is brought into India the subsequent receipt of the same amount in India should not be taken as the basis of taxing the same since the same income cannot be received twice and it will be known as Remittances.
- (iv) For the purpose of taxation both actual and constructive receipt must be taken into account. Receipt by some other person on behalf of the assessee should be treated as receipt by the assessee for being taxed in his hands.
- (v) The question of taxability of a particular income received by the assessee depends upon the nature of income. For instance, income from salaries and interest on securities would attract liability to tax immediately when it falls due to the assessee regardless of its actual receipt by or on behalf of the assessee.

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

- (i) All sums deducted by way of taxes at source (Section 198).
- (ii) Incomes of other persons which are included in the income of the assessee under Sections 60 to 64.
- (iii) The amount of unexplained or unrecorded investments (Section 69).
- (iv) The amount of unexplained or unrecorded moneys, etc. (Section 69A).
- (v) The annual accretion in the previous year to the balance standing at the credit of an employee participating in a Recognised Provident fund to the extent provided in Rule 6 of Part A of the Fourth Schedule [Section 7(i)]. The contributions made by the employer to Recognised Provident Fund in excess of 12% of the employees salary and the interest credited to the Provident Fund account of the employee in excess of the prescribed rate shall be included in the salary income of the employee. This amount is known as annual accretion.
- (vi) The transferred balance in a Recognised Provident Fund to the extent provided in Rule 11(4) of Part A - Fourth Schedule [Section 7(ii)].

When provident fund is recognised for the first time in a particular year, the existing balance to the credit of an employee on the date of recognition, which is carried into the recognised provident fund, is called the transferred balance. The amount of the transferred balance, less the employees own contributions included therein, is deemed to be the income of the year in which recognition takes place. The amount contributed by the employer to the provident fund and the interest on his contribution is included in the income under the head Salaries and the interest on the contributions made by the employee is included in the income under the head "Income from other sources".

- (vii) Any dividend declared by a Company or distributed or paid by it within the meaning of Section 2(22) [Section 8(a)].

- (viii) Any interim dividend unconditionally made available by the Company to the member who is entitled to it [Section 8(b)].

**Income accrued in India :** The accrual of income is different and distinct from the receipt of income discussed above. Sometimes in the context of accrual or arisal the word earned is used. A person may be said to have earned his income in the sense that he has contributed to the production by rendering of goods or services. But in order that the income may be said to have accrued to him, an additional element is necessary, that is, he must have created a debt in his favour. Income is said to accrue when it comes into existence for the first time or at the point of time when the right to receive the income arises although the right may be exercised or exercisable at a future date. Income is said to be received when it reaches the assessee. When the right to receive the income becomes vested in the assessee, it is said to accrue or arise.

Income is said to accrue only to that person who is lawfully entitled to that income. Income accrues at the place where the source of the income is situated, which may or may not be the same as the place from which the business activities are carried on. Normally, income accrues at the place where the contract yielding the income is entered into and for this purpose the contract should be taken to have been entered into at the place where the offer is accepted.

### **INCOME DEEMED TO ACCRUE OR ARISE IN INDIA [SECTION 9]**

Certain types of income are deemed to accrue or arise in India even though they may actually accrue or arise outside India. The categories of income which are deemed to accrue or arise in India are :

- (1) Any income accruing or arising to an assessee in any place outside India whether directly or indirectly
  - (a) through or from any business connection in India,
  - (b) through or from any property in India,
  - (c) through or from any asset or source of income in India or
  - (d) through the transfer of a capital asset situated in India [Section 9(1)(i)].
- (2) Income, which falls under the head "Salaries", if it is earned in India. Salary payable for service rendered in India would be treated as earned in India. Further, any income under the head "Salaries" payable for rest period or leave period which is preceded and succeeded by services rendered in India, and forms part of the service contract of employment, shall be regarded as income earned in India [Section 9(1)(ii)].
- (3) Income from Salaries which is payable by the Government to a citizen of India for services rendered outside India (However, allowances and perquisites paid outside India by the Government is exempt) [Section 9(1)(iii)].
- (4) Dividend paid by a Indian company outside India [Section 9(1)(iv)].
- (5) Interest [Section 9(1)(v)]
- (6) Royalty [Section 9(1)(vi)]
- (7) Fees for technical services [Section 9(1)(vii)]

#### **(a) Income by virtue of business connection**

In cases where all the operations or activities of a business are not carried on in India but a part of them arise by virtue of the business connection in India, the income which is deemed to accrue or arise in India, should be taken to be only that part which could reasonably be attributed to the operations carried on in India. Rule 10 of the Income-tax Rules contains the basis on which the income attributable to the operations carried out in India could be deemed to accrue or arise in India.

However, where a substantial part of a non-residents output is sold in the Indian market through brokers to

various customers in India, or mere rendering of services outside India to a person carrying on business in India does not amount to a business connection in India.

Similarly, where an Indian exporter selling goods through non-resident selling agents, receives sale price in India, credits commission on sales to non-resident agents in his books of account and remits the amount to them later, such commission to non-residents is neither received or deemed to be received in India nor deemed to accrue or arise in India [C.I.T. v. Toshoku Ltd. (1980) 125 ITR p. 525 (S.C.)].

### **THE MEANING OF THE EXPRESSION “BUSINESS CONNECTION”**

The expression business connection includes :

- (i) the maintenance of a branch office, factory, agency, receivership, management or other establishment for the purchase or sale of goods or for transacting any other business;
- (ii) the erection of a factory where the raw products purchased locally are processed or converted into some form suitable for export outside India;
- (iii) appointing an agent or agents in India for the systematic and regular purchase of raw materials or other commodities or for the sale of the non-residents goods, or for any other purpose;
- (iv) the formation of a close financial association between a resident and a non-resident company which may or may not be related to one another as a holding and subsidiary company;
- (v) the formation of a subsidiary company to sell or otherwise deal with the products of the non-resident parent company;
- (vi) the grant of a continuing licence to a non-resident for the purpose of exploitation for profit of an asset belonging to the non-resident even though the transaction in question may be treated as an
  - Business connection shall include any business activity carried out through a person acting on behalf of the non-resident.
  - He must have an authority which is habitually exercised to conclude contracts on behalf of the non-resident. However, if his activities are limited to the purchase of goods or merchandise for the non-resident, this provision will not apply.
  - Where he has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident, a business connection is established.
  - Business connection is also established where he habitually secures orders in India, mainly or wholly for the non-resident. Further, there may be situations when other non-residents control the above-mentioned non-resident. Secondly, this non-resident may also control other non-residents. Thirdly, all other non-residents may be subject to the same common control, as that of the non-resident. In all the three situations, business connection is established, where a person habitually secures orders in India, mainly or wholly for such non-residents. Exception : “Business connection”, however, shall not be held to be established in cases where the non-resident carries on business through a broker, general commission agent or any other agent of an independent status, if such a person is acting in the ordinary course of his business. A broker, general commission agent or any other agent shall be deemed to have an independent status where he does not work mainly or wholly for the non-resident. He will however, not be considered to have an independent status in the three situations explained in

No Business connection in India in following cases of Non-Resident.

1. **Tax Exemption for encouraging Export** : For the purpose of encouraging exports, a specific tax concession has been given by providing that no income shall be deemed to accrue or arise in India

to a non-resident through or from his operations which are confined to the purchase of goods in India for the purpose of export. Consequently, the exemption would not be available if the goods purchased in India are sold in India or are not exported outside India. Further, if the non-resident works up the raw-materials into finished or semi-finished products, the exemption would be withdrawn and he would become chargeable on such portion of the profits as is attributable to his manufacturing it in India.

2. Operations confined to collection of news and views for transmission outside India by or on behalf of Non Resident who is engaged in the business of running news agency or of publishing newspapers, magazines or out and out sale by the parties concerned journals;
3. Operations confined to shooting of cinematograph films in India if such Non-Resident is :
  - (a) an Individual - he should not be a citizen of India; or
  - (b) a firm - the firm should not have any partner who is a citizen of India or who is resident in India; or
  - (c) a company - the company does not have any shareholder who is a citizen of India or who is resident in India

**(b) Income arising from any asset or property in India :**

- Income arising in a foreign country from any property situated in India would be deemed to accrue or arise in India.
- In this context, the term property does not refer to house property alone but it refers to all tangible properties whether movable or immovable. For instance, the rent or hire charges for the use of buildings or machinery of the assessee which, under an agreement are payable only outside India, would be deemed to accrue or arise in India.
- Income arising through or from any asset or source of income in India would also be deemed to accrue or arise in India.
- In this context, the term source means not a legal concept but something which a practical man would regard as a real source of income.
- The term property does not refer to the property dealt with by Sections 22 and 23, but it includes any tangible movable or immovable property. The term asset would, however, include all intangible rights and, consequently, interests, dividends, patents and copyrights, royalties, rents etc. will be an Income from assets.

**(c) Capital asset :**

- Capital gains arising to an assessee from the transfer of a capital asset situated in India would be deemed to accrue or arise in India irrespective of the fact whether the capital asset in question represents a movable or immovable property or a tangible or intangible asset.
- It is also immaterial whether the consideration for the transfer of the capital asset is actually paid or payable in India or outside.
- The place of registration of the document of transfer of property is equally immaterial.
- However, if the capital asset, prior to the transfer, is situated outside India, the provisions of Section 9(1) would not apply to deem the capital gains arising on the transfer as accruing or arising in India for purposes of its taxation in India.

**(d) Income from salaries**

- Income which is chargeable under the head Salaries is deemed to accrue or arise in India in all cases

when earned in India. For this purpose income is said to be earned in India if the services are rendered in India.

- The actual place of accrual of the salaries, the residential status of the employer, the citizenship or nationality of the employee and whether the employee is a Government servant or an employee of private enterprise are immaterial.
- However, under Sub-section (2) of Section 9, any pension payable outside India to a person residing permanently outside India should not be deemed to accrue or arise in India if the pension is payable to civil servants and retired judges provided they were appointed before the 15th August, 1947 and continued to serve after the constitution came into operation.
- Barring this exception, non-residents and not ordinarily residents entitled to receive salary or pension earned by them in India would be deemed to receive income which has accrued in India even though the income may be actually accruing and received outside India.
- Income from salaries payable by the Government to a citizen of India outside India for his services rendered outside India, is deemed to accrue or arise in India even though the income is actually accruing outside India and is also received outside India. Thus, under this provision, salary income of all Government servants, working outside India is deemed to accrue in India. In the absence of this provision they would not be chargeable to tax in respect of such income as they would, after some time, become non-residents.
- This provision to deem income as accruing in India applies only in respect of their income from salary but not in respect of the allowances and perquisites to which they are entitled to while serving in a foreign country.
- Section 10(7) of the Income-tax Act, 1961 contains a specific provision to exempt Government servants from tax on their services in a foreign country partly to meet the higher cost of living in that country.
- Salaries paid by the Indian Government in a foreign country to citizens of the foreign country should not, however, be deemed to accrue in India since this provision applies only to Indian citizens employed by the Government who are rendering service outside India.

**(e) Taxability of Interest :** Interest payable in following cases will be deemed to accrue or arise in India and will be taxable in the hands of recipient irrespective of his residential status (i.e. ROR, RNOR or NR).

Interest payable by :

- (i) Government; or
- (ii) A Resident in India, except where interest is payable in respect of moneys borrowed and used for the purpose of business or profession carried outside India or earning any income from any source outside India (i.e. Interest payable by a Resident for loan used in India for any purpose, whether for business or profession or otherwise);
- (iii) A Non-Resident in India provided interest is payable in respect of moneys borrowed and used for a business or profession carried on in India (i.e. Interest payable by a Non-Resident for loan used for only business or profession in India)

**(f) Taxability of Royalty :** Royalty payable in following cases will be deemed to accrue or arise in India and will be taxable in the hands of recipient irrespective of his residential status (i.e. ROR, RNOR or NR).

Royalty payable by :

- (i) Government; or
- (ii) A Resident in India except where it is payable in respect of any right/information/property used for the

purpose of a business or profession carried on outside India or earning any income from any source outside India (i.e. Royalty payable by a Resident for right/information/property used for any purpose in India whether business or profession or for earning other incomes);

- (iii) A Non-Resident in India provided royalty is payable in respect of any right/information/property used for the purpose of the business or profession carried on in India or earning any income from any source in India (i.e. Royalty payable by a Non-Resident for right/information/property used for any purpose in India whether business or profession or for earning other incomes)

**(g) Taxability of Fees for Technical Services :** Fees for technical services payable in following cases will be deemed to accrue or arise in India and will be taxable in the hands of recipient irrespective of his residential status (i.e. ROR, RNOR or NR).

Fees for technical services payable by :

- (i) Government; or
- (ii) A Resident in India except where services are utilized for the purpose of a business or profession carried on outside India or earning any income from any source outside India (i.e. Fees for technical services payable by a Resident for services utilised for any purpose in India whether business or profession or for earning other incomes);
- (iii) A Non-Resident in India provided fee is payable in respect of services for the purpose of a business or profession carried on in India or earning any income from any source in India (i.e. Fees for technical services payable by a Resident for services utilised for any purpose in India whether business or profession or for earning other incomes);

**(h) Taxability of Dividend :**

- Dividend paid by any Indian company outside India is deemed to accrue or arise in India and the income is consequently chargeable to income-tax irrespective of the fact whether the dividend is interim dividend or a final dividend and whether it is an actual dividend or a notional dividend.
- The place of declaration of the dividend is immaterial and the date of payment is equally immaterial for deeming the income to accrue in India.
- Normally, dividend income arises at the place where the source of income is situated, i.e., where the shares yielding the income are kept. Shares are said to be situated at the place where the share register of the company is kept. While the share register of a company should ordinarily be kept at the place where its registered office is located, even if the share register is kept outside India and the dividends are declared outside India, the dividend would still be deemed to accrue in India because the company is an Indian company. It is another matter that dividend paid/payable by Indian companies has been exempted vide Section 10(34) with the introduction of the system of distribution tax which has shifted the incidence of tax on dividend to the company from the shareholder.
- Dividends declared by foreign companies outside India would not, however, be deemed to accrue or arise in India even in cases where the foreign company is resident in India because of the control and management of its affairs being situated wholly in India.

In order to deem the dividend income as arising in India, the residential status of the shareholder as also the status of the assessee, whether he is an individual, company or local authority, are irrelevant.

### **Tax incidence vis-a-vis residential status**

Tax incidence is vis-a-vis residential status of all assesses is indicated in the following table.

Where tax incidence arises in case of	Resident or Resident & Ordinarily Resident	Resident but not Ordinarily Resident	Non-Resident
Income received in India (Whether accrued in or outside India)	YES	YES	YES
Income deemed to be received in India (Whether accrued in or outside India)	YES	YES	YES
Income accruing or arising in India (Whether received in India or outside India)	YES	YES	YES
Income deemed to accrue or arise in India (Whether received in India or outside India)	YES	YES	YES
Income received and accrued outside India from a business controlled or a profession set up in India	YES	YES	NO
Income received and accrued outside India from a business controlled from outside India or a profession set up outside India	YES	NO	NO
Income earned and received outside India but later on remitted to India (whether tax incidence arises at the time of remittance?)	NO	NO	NO
Past untaxed profits (not taxable as relates to past years)	NO	NO	NO
Agricultural Income in India [Exempt under Section 10(1)]	NO	NO	NO
Long term capital gain [on STT paid shares or on shares sold through stock exchange] Exempt u/s 10(38) arising before 1st April, 2018	NO	NO	NO
Long term capital gain u/s 10(38) on or after 1st April, 2018	YES	YES	YES
Dividend from a Domestic Company [Exempt u/s 10(34)] or Income from Mutual funds specified u/s 10(23D) [Exempt u/s 10(35)]	NO	NO	NO
Gifts from relatives or on marriage or under will etc. (or gifts from others upto Rs. 50,000 in a year)	NO	NO	NO

The above table depicts that the first four incomes are chargeable to tax in India in respect of all assesses, irrespective of their residential status. In the case of a resident or resident and ordinarily resident assessee, tax incidence is the highest as income accruing in any part of the world attracts tax incidence in India. The tax incidence, on the other hand, is the lowest in the case of non-resident as only such income as accrued or is received or deemed to be received in India is liable to tax.

In respect of incomes which are deemed to accrue or arise in India, it is immaterial as to who the assessee is or what the nature or status of the assessee's position in India. Since income which is deemed to accrue or arise in India is taxable in the hands of all assesses regardless of their residential status, nationality, citizenship, place of birth, the domicile or business. However, the above table has a major role in determining the tax incidence in case of non-residents and also in cases where the income is actually accruing or arising outside India.

**Illustration 1 :** Mr. X earns the following income during the previous year ended 31st March, 2020. Determine the income liable to tax for the assessment year 2020-21 if Mr. X is (a) resident and ordinarily resident in India,

(b) resident and not ordinarily resident in India, and (c) non-resident in India during the previous year ended 31st March, 2019.

- Profits on sale of a building in India but received in Holland – Rs. 20,000
- Pension from former employer in India received in Holland – Rs. 14,000
- Interest on U.K. Development Bonds (1/4 being received in India) – Rs. 20,000
- Income from property in Australia and received in U.S.A. – Rs. 15,000
- Income earned from a business in Abyssinia which is controlled from Zambia (Rs. 30,000 received in India) – Rs. 70,000
- Dividend on shares of an Indian company but received in Holland [not qualifying for exemption under Section 10(34)] – Rs. 10,000
- Profits not taxed previously brought into India – Rs. 40,000
- Profits from a business in Nagpur which is controlled from Holland – Rs. 27,000

**Solution :** Computation of income liable to tax :

Particular	Resident & Ordinarily (Rs.)	Resident but not Ordinarily Resident (Rs.)	Non-Resident (Rs.)
Profits on sale of a building in India but received in Holland (accrued in India received outside India)	20,000	20,000	20,000
Pension from former employer in India received in Holland (accrued in India, received out of India)	14,000	14,000	14,000
Interest on U.K. Development Bonds (Accrued out of India, 1/4th received in India)	5,000	5,000	5,000
Interest on U.K. Development Bonds (Accrued out of India, 3/4th received out of India)	15,000	Nil	Nil
Income from property in Australia and received in U.S.A. (Accrued and received out of India)	15,000	Nil	Nil
Income earned from a business in Abyssinia which is controlled from Zambia (Business controlled outside India)	70,000	30,000	30,000
Dividend on shares of an Indian company but received in Holland (Accrued in India)	10,000	10,000	10,000
Profits not taxed previously brought into India (Not an income so not taxable)	Nil	Nil	Nil
Profits from a business in Nagpur which is controlled from Holland (Accrued in India)	27,000	27,000	27,000
<b>Total</b>	<b>1,76,000</b>	<b>1,06,000</b>	<b>1,06,000</b>

**Illustration 2 :** A had the following income during the previous year ended 31st March, 2020 :

- Salary Received in India for three Months - Rs. 9,000
- Income from house property in India- Rs. 13,470

58 EP-TL

- Interest on Saving Bank Deposit in State Bank of India-Rs. 1,000
- Amount brought into India out of the past untaxed profits earned in Germany- Rs. 20,000
- Income from agriculture in Indonesia being invested there-Rs. 12,350
- Income from business in Bangladesh, being controlled from India- Rs. 10,150
- Dividends received in Belgium from French companies, out of which Rs. 2,500 were remitted to India-Rs. 23,000

You are required to compute his total income for the assessment year 2020-21 if he is : (1) a resident; (ii) a not ordinarily resident, and (iii) a Non-resident.

**Solution :** Computation of total income of A is given below :

Particular	Resident & Ordinarily Resident (Rs.)	Resident but not Ordinarily Resident (Rs.)	Non-Resident (Rs.)
Salary Received in India for three Months (Indian received in India)	9,000	9,000	9,000
Income from house property in India (Income accrue or arise in India)	13,470	13,470	13,470
Interest on Saving Bank Deposit in State Bank of India (Income accrue or arise in India)	1,000	1,000	1,000
Amount brought into India out of the past untaxed profits earned in Germany ( not an income, hence not taxable)	Nil	Nil	Nil
Income from agriculture in Indonesia being invested there (Income accrue or arise in outside India)	12,350	Nil	Nil
Income from business in Bangladesh, being controlled from India (it is supposed that the money is not received in India) (Income accrued outside India from a business controlled from India)	10,150	10,150	Nil
Dividends received in Belgium from French companies (Income accrue outside India India remittance is irrelevant)	23,000	Nil	Nil
<b>Total</b>	<b>68,970</b>	<b>33,620</b>	<b>23,470</b>

**Illustration 3 :** Mr. Y earns the following income during the previous year ended on 31st March, 2020. Determine the income liable to tax for the assessment year 2020-21 if Mr. Y is (a) resident and ordinary resident (b) resident and not ordinary resident, and (c) non-resident in India during the previous year ended on 31st March, 2020.

- (i) Honorarium received from Government of India (Travelling and other incidental expenses of Rs. 7,000 were incurred in this connection)- Rs. 20,000
- (ii) Profits earned from a business in Tamilnadu controlled from Pakistan - Rs. 50,000
- (iii) Profits earned from a business in U.K. controlled from Delhi-Rs. 30,000
- (iv) Profits earned from a business in U.S.A. controlled from Pakistan and amount deposited in a bank there- Rs. 40,000
- (v) Income from a house property in France, received in India-Rs. 10,000

- (vi) Past untaxed foreign income brought into India during the year-Rs. 25,000
- (vii) Dividends from a German company credited to his account in Pakistan- Rs. 35,000
- (viii) Dividends declared but not received from an Indian company- Rs. 20,000
- (ix) Agricultural income from Burma not remitted to India-Rs. 40,000
- (x) Pension for services rendered in India, but received in Pakistan-Rs. 30,000

**Solution :** Computation of Income liable to tax of Mr. Y is given below :

Particular	Resident & Ordinarily Resident (Rs.)	Resident but not Ordinarily Resident (Rs.)	Non-Resident (Rs.)
Honorarium received from Govt. of India	20,000	20,000	20,000
Profits earned from a business in Tamilnadu controlled from Pakistan (Income accrue or arise in India)	50,000	50,000	50,000
Profits earned from a business in U.K. controlled from Delhi (Income accrue or arise outside India from a business controlled from India)	30,000	30,000	-
Profits earned from a business in USA controlled from Pakistan and amount deposited in a Bank there (Income accrue outside India)	40,000	-	-
Income from a house property in France, received in India (Income received in India)	10,000	10,000	10,000
Past untaxed foreign income brought into India during the year (Not taxable as profit of past years, also remittance is irrelevant)	-	-	-
Dividends from a foreign company credited to his account in Pakistan (Income accrue outside India)	35,000	-	-
Dividends declared but not received from an Indian company [u/s 10(33) enjoys exemption]	-	-	-
Agricultural income from Burma not remitted to India (Income accrue outside India)	40,000	-	-
Pension for Services rendered in India, but received in Pakistan (Income deemed to accrue or arise in India)	30,000	30,000	30,000
<b>Total</b>	<b>2,55,000</b>	<b>1,40,000</b>	<b>1,10,000</b>

Computation of Tax Liability include following steps :

1. Determine the category of person
2. Determine the residential status of the person as per section 6
3. Calculate the Total income as per the provisions
4. Calculate the tax on income

## COMPUTATION OF TAXABLE INCOME AND TAX LIABILITY OF AN ASSESSEE

Income tax is a charge on the assessee's income. Income Tax law lays down the provisions for computing the taxable income on which tax is to be charged. Taxable income of an assessee shall be calculated in the following manner.

1. Determine the residential status of the person as per section 6 of the Act.
2. Calculate the income as per the provisions of respective heads of income. Section 14 classifies the income under five heads.
  - (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
3. Consider all the deductions and allowances given under the respective heads before arriving at the net under each head.
4. Exclude the income exempt under section 10 of the Act.
5. Aggregate of incomes computed under the 5 heads of income after applying clubbing provisions and making adjustments of set off and carry forward of losses is known as Gross Total Income.
6. Deduct therefrom the deductions admissible under Sections 80C to 80U. The balance is called Total income.
7. The total income is rounded off to the nearest multiple of Rupees ten. (Section 288A)
8. Add agriculture income (if any) in the total income calculated in (6) above. Then calculate tax on the aggregate as if such aggregate income is the Total Income.
9. Calculate income tax on the net agricultural income as increased by Rs. 2,50,000/3,00,000/5,00,000 as the case may be, as if such increased net agricultural income were the total income.
10. The amount of income tax determined under (9) above will be deducted from the amount of income tax determined under (8) above.
11. Calculate income tax on capital gains under Section 112, and on other income at specified rates.
12. The balance of amount of income tax left as per (10) above plus the amount of income tax at (11) above will be the income tax in respect of the total income.
13. Deduct the following from the amount of tax calculated under (12) above.
  - Rebate under section 87A (if applicable).
  - Tax deducted and collected at source.
  - Advance tax paid.
  - Double taxation relief (Section 90 or 91).
14. The balance of amount left after deduction of items given in (13) above, shall be the net tax payable or net tax refundable for the assessee. Net tax payable/refundable shall be rounded off to the nearest multiple of Ten rupees (Section 288B).
15. Along with the amount of net tax payable, the assessee shall have to pay penalties or fines, if any, imposed on him under the Income-tax Act.

For calculation of income, amount received is classified under 5 heads of income; it is then to be adjusted with reference to the provisions of the Income Tax laws in the following manner.

Particulars	Amount (Rs.)
<b>Income under the head :</b>	
+ Income from Salaries	XXX
+ Income from House Property	XXX
+ Profits and gains of business or profession	XXX
+ Capital gains	XXX
+ Income from other sources	XXX
<b>Adjustment in respect of :</b>	
+ Clubbing of Income	XXX
– Set off and carry forward of losses	(XXX)
<b>= Gross Total Income</b>	<b>XXX</b>
– Deductions under section 80C to 80U (or Chapter VIA)	(XXX)
<b>= Total Income</b>	<b>XXX</b>

### TAX RATES FOR FY 2019-20 i.e. AY 2020-21

Calculation of Tax on Income

- Tax rate depends upon the category of person
- Amount of income
- Residential status of person
- Age of individual
- Type of Income

Components of Tax are



**Tax Rates for Different types of person depending upon various parameters :**

**1. For :**

- Resident Individual of the age below 60 years
- Non Residents Individual
- Hindu undivided family
- Association of Persons
- Body of Individuals (other than Co-operative society)
- Artificial Juridical Person

Total Income (Rs.)	Tax Rate	Tax liability (Rs.)
Upto 2,50,000	Nil	Nil
2,50,001 – 5,00,000	5%	5% of (Total Income – 2,50,000)
5,00,001 – 10,00,000	20%	20% of (Total Income – 5,00,000) + 12,500
Above 10,00,000	30%	30% of (Total Income – 10,00,000) + 1,12,500

**2. Applicable for :**

Resident individual of the age of 60 years or more but less than eighty years at any time during the previous year

Total Income (Rs.)	Tax Rate	Tax liability (Rs.)
Upto 3,00,000	Nil	Nil
3,00,001 – 5,00,000	5%	5% of (Total Income – 3,00,000)
5,00,001 – 10,00,000	20%	20% of (Total Income – 5,00,000) + 10,000
Above 10,00,000	30%	30% of (Total Income – 10,00,000) + 1,10,000

**3. Applicable for :**

Resident Individual of the age of 80 years or more at anytime during the previous year

Total Income (Rs.)	Tax Rate	Tax liability (Rs.)
Upto 5,00,000	Nil	Nil
5,00,001 – 10,00,000	20%	20% of (Total Income – 5,00,000)
Above 10,00,000	30%	30% of (Total Income – 10,00,000) + 1,00,000

CBDT has clarified vide Circular No. 28/2016 27.07.2016, that a person born on 1st April would be considered to have attained a particular age on 31st March, the day preceding the anniversary of his birthday.

Therefore a resident individual, whose 60th / 80th birthday falls on 1st April, 2020 would be treated as having attained the age of 60 years/80 years in the P. Yr. 2019-20.

**4. For firm and local authorities:**

	Types of person	Tax Rates
i.	Firms (including LLP)	30% of total Income
ii.	Local Authorities	30% of total Income

**Good to Know :** Entity or individual other than a company whose adjusted total income exceeds Rs. 20 lakhs is liable to pay Alternate Minimum tax @18.5%.

**5. For Company**

<b>Domestic Company</b>	<b>Assessment Year 2020-21</b>
- Where it opted for Section 115BAA [This benefit shall be available when total income of the company is computed without claiming specified deductions, incentives, exemptions and additional depreciation available under the Income-tax Act.]	22%
- Where it opted for Section 115BAB [This regime shall be available only for the manufacturing companies incorporated in India on or after 01-10-2019. Hence, old companies will not be able to take the benefit of this section.]	15%
- Where it has not opted for Section 115BAA and the Total Turnover or Gross receipts of the company in the last previous year does not exceeds 400 crore rupees	25%
- Any other domestic company	30%
<b>Foreign Company</b>	40%

**Good to Know : A company is liable to pay MAT @ 15%.**

**6. For Co-operative Society :**

	Income Slabs	Tax Rates
i.	Where the taxable income does not exceed Rs. 10,000/-	10% of the income
ii.	Where the taxable income exceeds Rs. 10,000/- but does not exceed Rs. 20,000/-	Rs. 1,000/- + 20% of income in excess of Rs. 10,000/-
	Where the taxable income exceeds Rs. 20,000/-	Rs. 3,000/- + 30% of the amount by which the taxable income exceeds Rs. 20,000/-

**Surcharge**

Surcharge is an additional tax imposed on certain cases. It is imposed over the basic tax rate calculated on the income.

*For example :* Suppose total taxable income of an individual of 45 years is Rs. 1,30,00,000, then Base tax will be : Rs. 1,12,500 + 30% of (1,20,00,000) = Rs. 37,12,500.

Surcharge @12%\* of Rs. 37,12,500 = Rs. 4,45,500. There are different rate of surcharge prescribed in the following manner :

	Types of person		Surcharge Rates
i.	Individuals, HUF, AOP, BOI	If Income exceeds Rs. 50 lakhs but does not exceed Rs. 1 crore	10% of income tax
		If income exceeds Rs. 1 crore but does not exceed Rs. 2 crore	15% of income tax
		If income exceeds Rs. 2 crore but does not exceed Rs. 5 crore	25% of income tax
		If total income exceeds Rs. 5 crore	37% of income tax
ii.	Firm / Local Authority / Co-operative Society	If income exceeds Rs. 1 crore	12% of income tax
iii.	Domestic Companies*	If income exceeds Rs. 1 crore but does not exceed Rs. 10 crores	7% of income tax
		If income exceeds Rs. 10 crore	12% of income tax
iv.	Companies other than a domestic company	If income exceeds Rs. 1 crore but does not exceed Rs. 10 crores	2% of income tax
		If income exceeds Rs. 10 crore	5% of income tax

\*The rate of surcharge in case of a company opting for taxability under Section 115BAA or Section 115BAB shall be 10% irrespective of amount of total income.

**Marginal Relief in Surcharge :** When an assessee's taxable income exceeds Rs. 1 crore, he is liable to pay Surcharge at prescribed rates mentioned above on Income Tax payable by him. However, the amount of Income Tax and surcharge on total income shall not exceed the amount of income that exceeds Rs. 1 crore.

**Example :** Suppose Mr. Ram an individual assessee of 42 years is having taxable income of Rs. 1,00,01,000/-

1.	Income Tax	Rs. 28,12,800
2.	Surcharge @15% of Income Tax	Rs. 4,21,920

3.	Income Tax on income of Rs. 1 crore	Rs. 28,12,500
4.	Maximum Surcharge payable (Income over Rs. 1 crore i.e. Rs. 1,000)	Rs. 1,000
5.	(Income Tax + Surcharge) payable	Rs. 28,13,500

Thus, in the above case, though the surcharge @15% is Rs. 421920. However, since the income of Mr. Ram exceeds Rs. 1 crore by just Rs. 1,000, Ram will be eligible for marginal relief and maximum surcharge will be restricted to Rs. 1,000 only.

#### Cess

- Governments resort to imposition of cess for meeting specific expenditure
- Education Cess and Senior and Higher Education Cess are additional levy on the basic tax liability + surcharge, if applicable.
- Rate of Education Cess is 2%
- Rate of SHEC is 1%.
- Rate of Health Cess is 1%.

#### Rebate under section 87A

An assessee, being an individual resident in India, whose total income does not exceed Rs. 5,00,000 shall be entitled to a deduction, from the amount of income-tax (as computed before allowing the deductions under this Chapter) on his total income with which he is chargeable for any assessment year, of an amount equal to 100% of such income-tax or an amount of Rs. 12,500, whichever is less.

#### Steps involved in calculation of Tax on Total Income

Particulars	Amount Rs.
Tax on Special Incomes @ specified tax rates (Long term capital gains @ 20%; Casual Income @ 30% and Short term capital gains (on Securities transaction tax paid securities) @ 15%;	XXX
Add : Tax on Balance Income @ Slab Rate/Flat Rate (as applicable)	XXX
<b>Total Tax</b>	<b>XXX</b>
Add : Surcharge, if any	XXX
Less : Marginal Relief, if applicable	XXX
<b>Tax including Surcharge</b>	<b>(XXX)</b>
Add : Education Cess @ 2% on tax including surcharge	XXX
Add : SHEC @ 1% on tax including surcharge	XXX
Add : Health Cess @ 1% on tax including surcharge	XXX
(Combinedly Health and Education Cess on income tax is levied @ 4%)	XXX
<b>Tax liability</b>	<b>XXX</b>
Add : Interest under Section 234A/234B/ 234C	XXX
<b>Net tax liability</b>	<b>XXX</b>
<b>Less : Taxes paid by way of :</b>	
– Tax deducted at source (TDS)	(XXX)
– Advance tax	(XXX)
– Self Assessment Tax	(XXX)
– Double Taxation Relief	(XXX)
<b>Tax Payable/Refundable</b>	<b>XXX</b>

### CASE LAWS

**1. Can capital contribution of the individual partners credited to their accounts in the books of the firm be taxed as cash credit in the hands of the firm, where the partners have admitted their capital contribution but failed to explain satisfactorily the source of receipt in their individual hands?**

**CIT v. M. Venkateswara Rao (2015 T & AP)**

The High Court held that the view taken by the AO that the partnership firm has to explain the source of income of the partners as regards the amount contributed by them towards capital of the firm, in the absence of which the same would be treated as the income of the firm, was not tenable.

**2. Liquidated damages – whether capital or revenue receipt**

**Commissioner of Income-tax, Gujarat v. Saurashtra Cement Ltd. [2010] [233 CTR 209]**

On a question whether the liquidated damages received by the assessee from the supplier of the plant and machinery on account of delay in the supply of plant is a capital or a revenue receipt, the Supreme Court held that it was clear from the agreement that the liquidated damages were to be calculated at 0.5 per cent of the price of the respective machinery and equipment which were delivered late, for each month of delay, without proof of the actual damages suffered by the assessee on account of the delay. The delay in supply could be of the whole plant or a part thereof but the determination of damages was not based upon the calculation made in respect of loss of profit on account of supply of a particular part of the plant. It was evident that the damages to the assessee were directly and intimately linked with the procurement of a capital asset, i.e., the cement plant, which would obviously lead to delay in coming into existence of the profit-making apparatus, rather than a receipt in the course of profit-earning process. Compensation paid for the delay in procurement of capital asset amounted to sterilization of the capital asset of the assessee as supplier had failed to supply the plant within time as stipulated in the agreement. The amount received by the assessee towards compensation for sterilization of the profit-earning source and not in the ordinary course of its business, was a capital receipt in the hands of the assessee.

### LESSON ROUND UP

- Tax is the financial charge imposed by the Government on income, commodity or activity. Government imposes two types of taxes namely Direct taxes and Indirect taxes. Direct tax is one where burden of tax is directly on the payer. While Indirect tax is paid by the person other than the person who utilizes the product or service.
- The Income tax Act contains the provisions for determination of taxable income, determination of tax liability, procedure for assessment, appeal, penalties and prosecutions.
- Every year a Budget is presented before the parliament by the Finance Minister. One of the important components of the Budget is the Finance Bill. The Bill contains various amendments such as the rates of income tax and other taxes. When the Finance Bill is approved by both the houses of parliament and receives the assent of President, it becomes the Finance Act.
- To levy income tax, one must have the understanding of the various concepts related to the charge of tax like previous year, assessment year, Income, total income, person etc.
- **Income** : No precise definition of the word 'Income' is available under the Income-tax Act, 1961. The definition of Income as given in Section 2(24) of the Act starts with the word includes therefore the list is inclusive not exhaustive.
- **Assessee** : In common parlance every tax payer is an assessee. However, the word assessee has been defined in Section 2(7) of the Act according to which assessee means a person by whom any tax or any other sum of money (i.e. interest, penalty etc.) is payable under the Act.

- Person : Income-tax is charged in respect of the total income of the previous year of every person. Hence, it is important to know the definition of the word person.
- Assessment year means the period of twelve months commencing on 1st April every year.
- Previous year : Income earned in a year is taxable in the next year. The year in which income is earned is known as previous year.
- Computation of income : Income tax is a charge on the assessee's income. Income Tax law lays down the provisions for computing the taxable income on which tax is to be charged.
- Total income of an assessee cannot be computed unless the person's residential status in India during the previous year is known. According to the residential status, the assessee can either be;
  - (i) Resident in India or
  - (ii) Non-resident in India
- Section 6 of the Income-tax Act prescribes the tests to be applied to determine the residential status of all tax payers for purposes of income-tax. There are three alternative tests to be applied for individuals, two for companies and Hindu Undivided Families and firms, associations of persons, bodies of individuals and artificial juridical persons.
- Residential status of Individual : The residential status of individual is determined on the basis of the following conditions :
  - (i) *Condition 1* : If individual is in India in the previous year for a total period of 182 days or more.
  - (ii) *Condition 2* : If he has been in India for at least 365 days during the 4 years preceding the previous year and has been in India for at least 60 days during the previous year. However, the clause of 60 days is not applicable if a person is :
    - Citizen of India, who leaves India in any previous year as a member of the crew of an Indian ship, or for the purpose of employment outside India. OR
    - Citizen of India or of Indian origin engaged outside India (whether for rendering service outside or not) and who comes on a visit to India in any previous year.
  - (iii) *Condition 3* : An individual who has been a non-resident in India in at least nine out of the ten previous years preceding that year, and has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to 729 days or less.

Resident and Ordinarily Resident - Satisfies either condition 1 or 2; But does not satisfies condition 3

Not ordinarily resident - Satisfies any one condition from 1 & 2 and condition 3

Non-resident - Does not satisfy any condition from 1 and 2
- Residential status of HUF : The test to be applied to determine the residential status of a HUF, Firm or other Association of Persons is based upon the control and management of the affairs of the assessee concerned. A HUF, firm or other association of persons is said to be resident in India within the meaning of Section 6(2) in any previous year, if during that year the control and management of its affairs is situated wholly or partly in India during the relevant previous year. If the control and management of its affairs is situated wholly outside India during the relevant previous year, it is considered non resident.
- A HUF can be "not ordinarily resident"
- If manager/karta has been a not ordinarily resident in India in the previous year in accordance with the tests applicable to individuals.

- Firms, association of persons, local authorities and other artificial juridical persons can be either resident (ordinarily resident) or non-resident in India but they cannot be not ordinarily resident in India.
- Residential status of Companies : All Indian companies within the meaning of Section 2(26) of the Act are always resident in India regardless of the place of effective management.

In the case of a foreign company the place of effective management (POEM) of the affairs is the basis on which the company's residential status is determinable.

- Basis of charge : Section 4 of the Act is the charging section which imposes a charge and provides rules for working out the charge so imposed.

Section 4 of the Act imposes a charge of tax on the total or taxable income of the assessee. The meaning and scope of the expression of total income is contained in Section 5. The total income of an assessee cannot be determined unless we know the residential status in India during the previous year. The scope of total income and consequently the liability to income-tax also depends upon the following facts :

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

### SELF TEST QUESTIONS

*These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.*

#### Multiple Choice Questions 'MCQs'

1. Basic exemption for a co-operative society for the assessment year 2018-19 is :
  - a) Rs. 10000
  - b) Rs. 15000
  - c) Rs. 20000
  - d) Nil

Answer: d

2. Person is defined under section \_\_\_\_\_ of the Income Tax Act, 1961
  - a) 2(31)
  - b) 2(7)
  - c) 2(9)
  - d) 3

Answer: a

3. Income earned by a LLP is taxable at the rate of:
  - a) 10%
  - b) 20%

- c) 30%
- d) None of the above

Answer: c

4. Income is defined under section \_\_\_\_\_ of the Income Tax Act, 1961

- a) 2(31)
- b) 2(24)
- c) 2(9)
- d) 3

Answer: b

5. Which of the following is not a revenue receipt? (i) Compensation received for the loss of a capital asset (ii) Compensation received for damage to or loss of a trading asset. (iii) Profits on purchase and sale of shares by a share broker on his own account. (iv) Income from letting out buildings owned by a company to its employees etc

- a) i only
- b) i and ii both
- c) i , ii, and iii
- d) All of the above

Answer: a

### SUGGESTED READINGS

**1. Direct Taxes Law and Practice**

Author : Dr. Vinod K. Singhania & Dr. Kapil Singhania

Publisher : Taxmann

Year : 2019

Edition : 2019

**2. Direct Taxes Ready Reckoner with Tax Planning**

Author : Dr. Girish Ahuja & Dr. Ravi Gupta

Publisher : Wolters Kluwer

Year : 2019

Edition : 20th Edition





# Lesson 3

## Incomes which do not form Part of Total Income

### LESSON OUTLINE

- Background
- General Exemption
- Exemption under section 10
- Specific Exemption
- Special provisions in respect of newly established Units in Special Economic Zone (Section 10AA)
- LESSON ROUND UP
- SELF TEST QUESTION

### LEARNING OBJECTIVES

Tax is calculated on the income earned in the previous year. For providing relief to the tax payers from payment of tax, income tax law contains certain provisions relating to exemption and deduction. Exempted income means the income which are not charged to tax. Under Income Tax Act, section 10 provides for incomes which are exempted from levy of income tax for example Scholarship. Further, deduction means the amount which needs to be included in the income first and then they are allowed for deduction in full or in part on fulfillment of certain conditions. For example, deduction for payment of donations under section 80G.

This lesson deals with incomes which do not form part of total income. Section 10 provides for various categories of income that are exempt from tax. Section 10AA, deals with exemption in respect of income of industrial units in special economic zones.

After going through this lesson, you will learn:

- about the income which does not form part of the total income
- the conditions to be satisfied for availing exemption under section 10, 10AA.

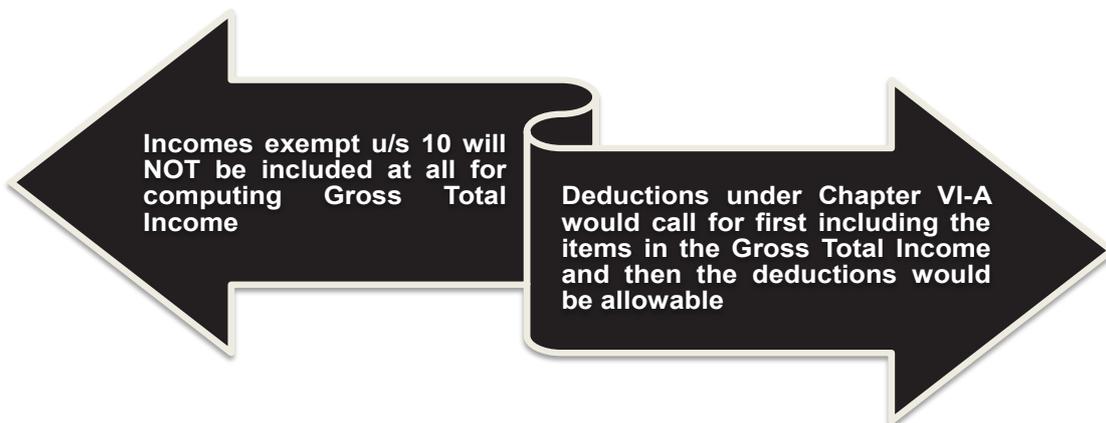
**BACKGROUND**

Tax is calculated on the total income of an person for the previous year. For providing relief to the tax payer, Income Tax laws provides for exemption, deduction and rebate. The exempt income is often confused with the deductions and rebate. However there is difference between these concepts. The same has been explained in the table below:

<b>Exemptions</b>	<ul style="list-style-type: none"> <li>• Exemptions are claimed on the basis of the source of income.</li> <li>• The exempted income is not included in the total Income of the assessee.</li> </ul>
<b>Deductions</b>	<ul style="list-style-type: none"> <li>• Deductions are allowed on the basis of the payments/ investments made.</li> <li>• The tax deductions are allowed under different heads of income as well as from the gross income.</li> </ul>
<b>Rebate</b>	<ul style="list-style-type: none"> <li>• Rebate is a percentage amount reduced from total income tax payable.</li> <li>• Tax rebate is allowed as a reduction to the total tax payable.</li> </ul>

There are several incomes that do not form part of the total income of the assesseees, which are entailed u/s 10 of the Act. Being exempt, these do not enter the computation of taxable incomes therefore.

There is a major difference between incomes u/s 10 and the deductions under Chapter-VI-A, although and it is therefore imperative to note that the incomes u/s 10 do not enter the computation of taxable income for assesseees at all, they are exempt; whereas Chapter for VI-A, first incomes are added and form part of Gross Total Income (GTI) and only then these deductions under the Chapter are allowed.



**INCOMES WHICH DO NOT FORM PART OF TOTAL INCOME**

**Agricultural Income [Section 10(1)]**

Section 10(1) states that agricultural incomes are not included in the total income of the assesseees.

The term Agricultural Income can be quite wide in scope as under:

- It could take the form of rent or revenues derives from a land in India(If agricultural land is situated in a foreign country, the entire income would be taxable), and used for agricultural purposes

- ✓ The amount received in money or in kind, by one person from another for right to use land is termed as **Rent**. The rent can either be received by the owner of the land or by the original tenant from the sub-tenant. It implies that ownership of land is not necessary. Thus, the rent received by the original tenant from sub-tenant would also be agricultural income subject the other conditions mentioned above.
- It could take the form of income through agriculture / cultivation to render the produce fit for being taken in to the market for sale
  - ✓ Agriculture would include **basic operations** which are absolutely necessary for raising produce, and **subsequent operations** which are performed after the produce sprouts from the land.
  - ✓ Therefore, activities like tilling of the land, sowing seeds, and both the basic and subsequent operations performed together in conjunction with each other would be construed as the agricultural purpose.
  - ✓ In order to render the produce, fit for being taken to market for sale, the activities would include all activities, like cleaning, drying, winnowing, crushing etc. Example, let's assume the process being referred to is obtaining rice from paddy, the process ordinarily employed by the cultivator would include:
    - Removing hay from basic grains
    - Removing chaff from the grains
    - Filtering the grain to remove stones
    - Packing the rice in gunny bags

Therefore, all activities, manual or otherwise, all the processes would be included in and therefore constitute the activities deployed to render the produce fit for being taken to the market.

- It could take the form of sale of agricultural produce itself
  - ✓ Here, the most important part to be understood is that the produce must be sold in it's raw form, and then that will constitute agricultural income. However, if the produce is further subjected to processes other than the processes ordinarily employed to render the produce fit for the market, example, for tobacco, cotton, tea, these are subjected to further manufacturing processes before being commercially sold, and therefore the income so arising from such sale would be treated as a mix of agricultural and business income.

**Reference Case Law** : Assessee acquired land from agriculturist on lease and constructed a greenhouse floriculture project on said land. It started growing of rose flowers / plants on bridge of plastic trays erected with help of M.S. stand 2.3 ft. above land. The assessee claimed the income from rose flowers as exempt. The Assessing Officer held that the rose plants were not planted on earth land and no basis operation was carried out by assessee on land hence, not eligible for exemption. According to assessee, for plantation of roses a very well treated soil was required, manures were mixed in soil for preparing a base for growing rose plants trays were filed with mixture of soil, insecticides were sprinkled on plants to save plants from any disease, root stocks were brought from market and planted in green house, mother plant was otherwise reared on earth, subsequently saplings were planted on plastic trays which were kept at height of 2-3 ft. placed on M.S. stand, purpose of growing rose plants at a height was primarily to avoid pest and to develop in a controlled atmosphere and green house was used for various benefits so that sunlight and humidity level both could be maintained. The Tribunal held that the claim of exemption was justified. Refer, *Dy. CIT v. Best Roses Biotech (P) Ltd.*, 49 SOT 277.

**Whether income from nursery constitutes agricultural income?**

Yes, as per *Explanation 3* to section 2(1A), income derived from saplings or seedlings grown in a nursery would be deemed to be agricultural income, whether or not the basic operations were carried out on land.

**Rule 7** - Where the income is partially agricultural income and partially business income, **the market value** of any agricultural produce so raised by the assessee, which has been further utilised / processed in such business will be allowed as a deduction in such business.

**Determination of market value** - There are two possibilities here:

- (I) The agricultural produce is capable of being sold in the market either in its raw stage or after application of any ordinary process to make it fit to be taken to the market. In such a case, the value calculated at the average price at which it has been so sold during the relevant previous year will be the market value.
- (II) It is possible that the agricultural produce is not capable of being ordinarily sold in the market in its raw form or after application of any ordinary process. In such case the market value will be the total of the following:—
  - The expenses of cultivation;
  - The land revenue or rent paid for the area in which it was grown; and
  - Such amount as the Assessing Officer finds having regard to the circumstances in each case to represent at reasonable profit.

**Illustration 1 :**

Kundan Lal grows sugarcane and uses the same for the purpose of manufacturing sugar in his factory.

40% of the sugarcane produce is sold for INR 15,00,000 and the cost of cultivation of this part is INR 8,00,000.

60% of the sugarcane produce is further subjected to manufacturing sugar and the Market Value (MV) of the same was INR 33,00,000 and the cost of cultivation of this part was INR 21,00,000.

Post incurring INR 3,00,000 in the manufacturing process for sugar, that the sugarcane was subjected to, the sugar was sold for INR 40,00,000.

You are required to advise on his Agricultural and Business Income.

**Solution :**

Particulars	In Lakhs	In Lakhs
Item	Sugarcane	Sugar
Sale	48.0	40.0
Cost of cultivation	29.0	33.0
Further Mfg.	0.0	3.0
<b>Agriculture Income</b>	<b>19.0</b>	
<b>Business Income</b>		<b>4.0</b>

**Notes:**

- a) 40% of the sugarcane produce was sold raw @ INR 15,00,000 and 60% of the sugarcane produce was subjected to further manufacturing, MV was INR 33,00,000. Therefore, for the purposes of agricultural income, the entire produce was disposed at a consideration of INR 48,00,000
- b) The cost of 100% produce is INR 800,000 and INR 21,00,000 for the 40% and 60% respectively, which is INR 29,00,000

- c) For sugar, the MV of the 60% produce would be taken as the cost hence, and therefore the cost of cultivation would be INR 33,00,000

### Income from manufacture of rubber [Rule 7A]

This rule applies on income from sale of latex, or crepes derived from latex, coagulum obtained from rubber plants, grown by the seller in India. In such cases, 35% of profits on sales is taxable as business income and 65% as agricultural income, which stands exempt.

#### Illustration 2:

Nikhil manufactures latex from rubber plants grown by him in India. These are subsequently sold in the market at INR 50,00,000. The costs incurred are as under:

- Manufacturing Latex: INR 12,00,000
- Growing Rubber Plants: INR 18,00,000

The treatment is explained as under:

Particulars	INR
Total Income	50,00,000
Total Costs	30,00,000
Profits	20,00,000
Business Income	7,00,000
Agricultural Income	13,00,000

**Note :** the business income chargeable to tax under the head “Profits and Gains from Business / Profession” is taken @ 35% of the profits and the agricultural income is taken @ 65%, which is subsequently exempt from tax.

#### Illustration 3

Mr. A manufactures latex from the rubber plants grown by him in India. These are then sold in the market for Rs. 50 lacs. The cost of growing rubber plants is Rs. 20 lacs and that of manufacturing latex is Rs. 10 lacs. Compute his total income.

#### Solution:

The total income of Mr. A comprises of agricultural income and business income.

Total profits from the sale of latex= Rs. 50 lacs – Rs. 20 lacs – Rs. 10 lacs = Rs. 20 lacs.

Agricultural income = 65% of Rs. 20 lac = Rs. 13 lacs

Business income = 35% of Rs. 20 lacs = Rs. 7 lacs

### Income from the manufacture of coffee [Rule 7B]

This rule applies on income from sale of coffee grown & cured by the seller in India. In such cases, 25% of profits on sales is taxable as business income and 75% as agricultural income, which stands exempt.

However, in case of income from sale of coffee, grown, cured, roasted and grounded by the seller in India, with / without mixing flavoured ingredients, 40% of the income would be taken as taxable as business income and 60% as agricultural income, which stands exempt.

### Income from growing and manufacturing of tea [Rule 8]

This rule applies on income, where the assessee themselves grow tea leaves and manufacture tea in India. In such cases, 40% of profits on sales is taxable as business income and 60% as agricultural income, which stands exempt.

Nature of income	Income tax Rule applicable	Amount of agricultural income	Amount of non-agricultural income
Income from growing and manufacturing of rubber	Rule 7A	65% of such income	35% of such income
Income derived from sale of coffee grown and manufactured in India	Rule 7B(1)	75% of such income	25% of such income
Income derived from sale of coffee grown, cured, roasted and grounded in India	Rule 7B(1A)	60% of such income	40% of such income
Income from sale of tea manufactured or grown in India	Rule 8	60% of such income	40% of such income

### Income from farm building:

Income arising from the use of farm building for any purpose (including letting for residential purpose or for the purpose of business or profession) other than agriculture would not be agricultural income.

Further, the income from farm building would be agricultural income only if the following conditions are satisfied:

- (a) The building should be on or in the immediate vicinity of the land; and
- (b) The receiver of the rent or revenue or the cultivator or the receiver of rent in kind should, by reason of his connection with such land require it as a dwelling house or as a store house.

In addition to the above conditions any one of the following two conditions should also be satisfied:

- (i) The land should either be assessed to land revenue in India or be subject to a local rate assessed and collected by the officers of the Government as such or;
- (ii) Where the land is not so assessed to land revenue in India or is not subject to local rate:-
  - a. It should not be situated in any area as comprised within the jurisdiction of a municipality or a cantonment board and which has a population not less than 10,000 or
  - b. It should not be situated in any area within such distance, measured aerially, in relation to the range of population as shown hereunder –

Sl. No.	Shortest aerial distance from the local limits of a municipality or cantonment board referred to in item a.	Population according to the last preceding census of which the relevant figures have been published before the first day of the previous year
(i)	≤ 2 kilometers	> 10,000 ≤ 1,00,000
(ii)	≤ 6 kilometers	> 1,00,000 ≤ 10,00,000
(iii)	≤ 8 kilometers	> 10,00,000

### Whether income arising from transfer of agricultural land situated in urban area be agricultural income?

No, as per Explanation 1 to section 2(1A), the capital gains arising from the transfer of urban agricultural land would not be treated as agricultural income under section 10 but will be taxable under section 45.

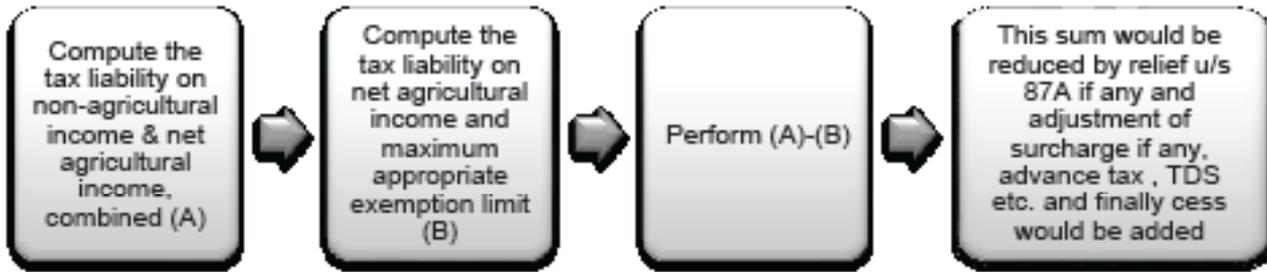
### Where there is a combination of agricultural and non-agricultural income

This is applicable to Individuals, HUF, AOP, BOI, and artificial juridical person.

Two conditions which needs to be satisfied for partial integration of agricultural income with non-agricultural income are:

- 1) The net agricultural income must be > INR 5000/- p.a.; &
- 2) The non-agricultural income must be > the maximum amount not chargeable to tax (which is INR 250,000 for all individuals / HUF's; INR 300,000 for senior citizens and INR 500,000 for very senior citizens)

The manner of computation of Income in such cases would be as under:



Refer to the illustration below which will explain this better.

Income of Mr. A for the previous year 2019-20 is as follows: Compute Tax Liability for the Assessment year 2020-21.

Particulars	INR
Income from salary (computed)	2,50,000
Income from house property (computed)	1,25,000
Net Agricultural Income	1,00,000
Total (A)	4,75,000
Tax Liability	11,250
Total (B)	3,50,000
Tax Liability	5,000
(A)-(B)	6,250
Less: Rebate 87A[12500 or tax payable i.e. 6,250 whichever is lower]	6,250
Total tax payable	Nil

**Note:**

- 1) The (A) would be the combined income and the tax liability is computed per the current slabs and rates
- 2) The (B) would be the net agricultural income as increased by the minimum exemption amount and the tax liability is computed per the current slabs and rates
- 3) The (A)-(B) would be the tax liability on which rebate 87A is allowed to determine the final total tax liability

**Amount received by a member of the HUF from the income of the HUF [Section 10(2)]**

As per section 10(2), amount received out of family income, or in case of impartible estate, amount received out of income of family estate by any member of such HUF is exempt from tax. This is allowable only when the payments are made by the HUF to it's members, out of the income of the family or out of the impartible estate belonging to the family.

**Illustration:**

Mr. P, a member of a HUF, received Rs. 5,000 as his share from the income of the HUF. Is such income includible in his chargeable income?

**Answer:**

No. Such income is not includible in Mr. P's chargeable income since section 10(2) exempts any sum received by an individual as a member of a HUF where such sum has been paid out of the income of the family.

**Share of profit received by a partner from the firm [Section 10(2A)]**

As per section 10(2A), share of profit received by a partner from a firm is exempt from tax in the hands of the partner. Further, share of profit received by a partner of LLP from the LLP will be exempt from tax in the hands of such partner. This exemption is limited only to share of profit and does not apply to interest on capital and remuneration received by the partner from the firm/LLP.

**Interest to non-residents [Section 10(4)]**

- ▶ As per section 10(4)(i), in the case of a non-resident; any income by way of interest on certain notified securities or bonds (including income by way of premium on the redemption of such bonds) is exempt from tax.
- ▶ As per section 10(4)(ii),
  - in the case of an individual,
  - any income by way of interest on money standing to his credit in a Non-Resident (External) Account
  - in any bank in India in accordance with the Foreign Exchange Management Act, 1999, and the rules made thereunder is exempt from tax.
  - Exemption under section 10(4)(ii) is available only if such individual is a person resident outside India as defined in clause (w) of section 2 of the Foreign Exchange Management Act, 1999 or is a person who has been permitted by the Reserve Bank of India to maintain the aforesaid Account.

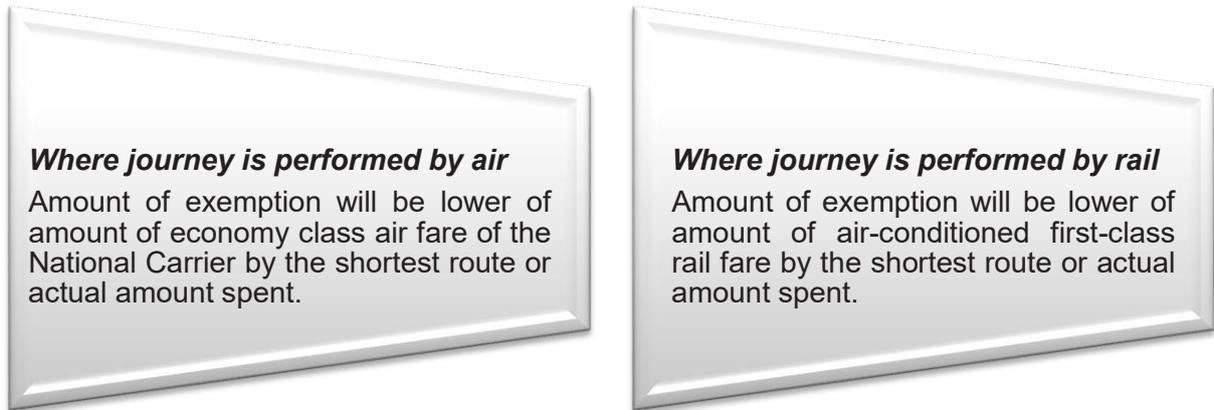
**Interest on notified savings certificates [Section 10(4B)]**

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

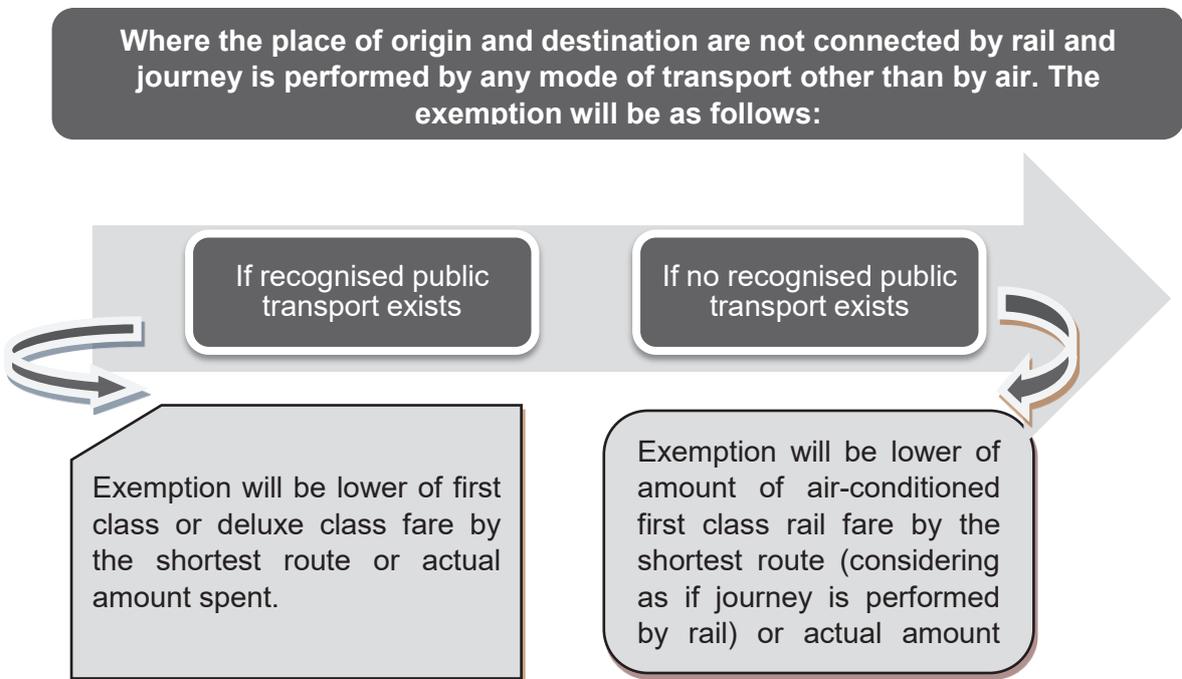
**Leave travel concession [Section 10(5)]**

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

Other provisions to be kept in mind in this regard are as follows:



The same rule will apply where journey is performed by any other mode and the place of origin of journey and destination are connected by rail.



**Block:** Exemption is available for 2 journeys in a block of 4 years. The block applicable for current period is calendar year 2018-21. The previous block was of calendar year 2014-2017.

**Carry over:** If an employee has not availed of travel concession or assistance in respect of one or two permitted journeys in a particular block of 4 years, then he is entitled to carry over one journey to the next block. In this situation, exemption will be available for 3 journeys in the next block. However, to avail of this benefit, exemption in respect of journey should be utilised in the first calendar year of the next block. In other words, in case of carry over, exemption is available in respect of 3 journeys in a block, provided exemption in respect of at least 1 journey is claimed in the first year of the next block. Exemption is in respect of actual expenditure on fare, hence, if no journey is performed, then no exemption is available.

**Family:** Family will include spouse and children of the individual, whether dependent or not and parents, brothers, sisters of the individual or any of them who are wholly or mainly dependent on him. Exemption is restricted to only 2 surviving children born after October 1, 1998 (multiple births after first single child will be considered as one child only), however, such restriction is not applicable to children born before October 1, 1998.

**Reference Case Law:** In a recent judgment in case of Commissioner of Income tax & ANR vs M/s Larsen & Toubro Ltd, the Honourable Supreme Court of India has considered the question whether the employer has any obligation under the Act/Rules to collect evidence to show that the employee had actually utilized the amount paid towards LTA. The Honourable Supreme Court of India observed that the beneficiary of exemption under Section 10(5) is the individual employee. It also referred to the annual circular issued by the CBDT under Section 192 where under guidance is given to employers on the manner in which tax is required to be deducted from salary paid to employees. The Court has held that the said Circular did not require an employer to examine the supporting evidence to the declaration submitted by an employee as far as LTA is concerned. Based on this, the Court has held that the employer has no obligation to collect such evidence or to verify the claim.

### **Remuneration received by individuals, who are not citizens of India [Section 10(6)]**

In case of an individual who are not a citizen of India are entitled to certain exemptions under section 10(6) which are discussed as follows:

#### **Remuneration received by specified diplomats and their staff [Section 10(6)(ii)]**

As per section 10(6)(ii)

- in case of an individual who is not a citizen of India,
- remuneration received by him as an official (by whatever name called) of an Embassy, High Commission, Legation, Commission, Consulate or Trade Representative of a Foreign State, or member of the staff of any of that official is exempt from tax, if corresponding Indian official in that foreign country enjoys a similar exemption.

#### **Salary of a foreign employee and non-resident member of crew [Section 10(6)(vi), (viii)]**

As per section 10(6)(vi),

- the remuneration received by
- a foreign national as an employee of a foreign enterprise
- for services rendered by him during his stay in India is exempt from tax,
- provided the following conditions are fulfilled:
  - (a) the foreign enterprise is not engaged in any trade or business in India ;
  - (b) his stay in India does not exceed in the aggregate a period of 90 days in such year ; and
  - (c) such remuneration is not liable to be deducted from the income of the employer.

As per section 10(6)(viii),

- any salaries received by or due to a
- non-resident foreign national for
- services rendered in connection with his employment on a foreign ship
- where his total stay in India does not exceed in the aggregate a period of 90 days in the year

is exempt from tax.

#### **Remuneration of a foreign trainee [Section 10(6)(xi)]**

As per section 10(6)(xi),

- the remuneration received by a

- foreign trainee as an employee of foreign Government
- during his stay in India in connection with his training in any establishment or office of, or in any undertaking owned
- by the Government ; or any company owned by the Central Government, or any State Government or any company which is a subsidiary of a company referred to above or any corporation established by or under a Central, State or Provincial Act or any co-operative society wholly financed by the Central Government, or any State Government Tax,

is exempt from tax

**Tax paid on behalf of foreign company deriving income by way of royalty or fees for technical services [Section 10(6A)]**

Tax paid by Central Government, State Government or an Indian concern on behalf of a foreign company deriving income by way of royalty or fees for technical services in pursuance of an agreement made after March 31, 1976 but before June 1, 2002 will be exempt from tax in the hands of such foreign company provided such agreement is in accordance with the industrial policy of the Indian Government or it is approved by the Central Government.

**Tax paid on behalf of foreign company or non-resident in respect of other income [Section 10(6B)]**

Tax paid by Central Government, State Government or an Indian concern on behalf of a foreign company or non-resident in respect of any income (not being salary, royalty or fees for technical services) will be exempt from tax in the hands of such foreign company or non-resident if such income is received in pursuance of an agreement entered into before June 1, 2002 by the Central Government with the Government of a foreign State or international organisation or any other related agreement approved by the Central Government.

**Tax paid on behalf of foreign Government or foreign enterprise deriving income by way of lease of aircraft or aircraft engine [Section 10(6BB)]**

Tax paid by an Indian company, engaged in the business of operation of aircraft, on behalf of foreign Government or foreign enterprise deriving income by way of lease of aircraft or aircraft engine will be exempt from tax in the hands of such foreign Government or foreign enterprise if such lease rental is received under an agreement which is approved by Central Government and entered during the period between 31-3-1997 to 1-4-1999, or after 31-3-2007.

**Technical fees received by a notified foreign company [Section 10(6C)]**

Section 10(6C) grants exemption from tax in respect of income arising to notified foreign company by way of royalty or fees for technical services received in pursuance of an agreement entered into with that Government for providing services in or outside India in projects connected with security of India.

**Royalty or fees for technical services payment by NTRO to a non resident Section 10 (6D)**

Any income arising to a

- non-resident, not being a company, or a foreign company,
- by way of royalty from, or fees for technical services rendered in or outside India to the National Technical Research Organisation (NTRO).
- Consequently NTRO will not be required to deduct tax on such payments.

**Allowance/perquisites to Government employee outside India [Section 10(7)]**

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

**Income of foreign Government employee under co-operative technical assistance programme [Section 10(8)]**

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

**Remuneration or fees received by a non-resident consultant/its foreign employees [Section 10(8A), (8B)]**

Under section 10(8A), (a) remuneration or fees received by a consultant directly or indirectly out of the funds made available to an international organisation, under a technical assistance agreement between such organisation and the Government of a foreign State and (b) any other income which accrues or arises to him outside India and is not deemed to accrue or arise in India, in respect of which such consultant is required to pay income-tax/social security tax to the foreign Government of the country of his origin, is exempt from tax.

**Income of a family member of an employee serving under co-operative technical assistance programme [Section 10(9)]**

As per section 10(9), the income of any member of the family of any such individual as is referred to in section 10(8)/(8A)/(8B) accompanying him to India, which accrues or arises outside India and is not deemed to accrue or arise in India, in respect of which such member is required to pay any income or social security tax to the Government of that foreign State or country of origin of such member, as the case may be, is exempt from tax.

**Retrenchment compensation [Section 10(10B)]**

As per section 10(10B), compensation received at the time of retrenchment is exempt from tax to the extent of lower of the following: (a) An amount calculated in accordance with the provisions of section 25F(b) of the Industrial Dispute Act, 1947; or (b) Maximum amount specified by the Central Government (Rs. 5,00,000); (c) Actual amount received.

Under the Industrial Dispute Act, a workman is entitled to retrenchment compensation, equal to 15 days' average pay for each completed year of continuous service or any part in excess of six months. Compensation in excess of aforesaid limits is taxable as salary. However, the aforesaid limit is not applicable in cases where compensation is paid under any scheme approved by the Central Government.

**Compensation for Bhopal Gas Leak Disaster [Section 10(10BB)]**

Compensation [in accordance with Bhopal Gas Leak Disaster (Processing of Claims) Act, 1985] received by

- victims of Bhopal gas leak disaster is exempt from tax.
- However, compensation received for any expenditure which is allowed as deduction from taxable income is not exempt.

**Compensation on account of any disaster [Section 10(10BC)]**

Any amount received from the

- Central Government or
- State Government or
- a Local Authority by
- an individual or his legal heirs
- as compensation on account of any disaster

is exempt from tax.

However, no deduction is available in respect of the amount received or receivable to the extent such individual or his legal heirs has been allowed a deduction under the Act on account of loss or damage caused due to such disaster.

**Disaster here means**

- any disaster due to any natural or
- man-made causes or
- by accident/negligence which results in substantial loss of human life or
- damage to property or environment and
- the magnitude of such disaster is beyond coping capacity of community of the affected area.

**Payment at the time of voluntary retirement [Section 10(10C)]**

As per section 10(10C), any compensation received at the time of voluntary retirement or termination of service is exempt from tax, if the following conditions are satisfied:

- ✓ Compensation is received at the time of voluntary retirement or termination (or in the case of an employee of public sector Company, at the time of voluntary separation)
- ✓ Compensation is received by an employee of following undertakings- a) public sector company; or b) any other company; or c) an authority established under a Central, State or Provincial Act; or d) a local authority; or e) a co-operative society ; or f) a University established or incorporated by or under a Central, State or Provincial Act and an institution declared to be a University under section 3 of the University Grants Commission Act, 1956 (3 of 1956) ; or g) an Indian Institute of Technology within the meaning of clause (g) of section 3 of the Institutes of Technology Act, 1961 (59 of 1961) ; or h) any State Government; or i) the Central Government; or j) Notified institutes having importance throughout India or in any State or States, k) Notified institute of management
- ✓ Compensation is received in accordance with the scheme of voluntary retirement/separation, which is framed in accordance with guidelines prescribed under Rule 2BA of Income-tax Rules, 1962. Maximum amount of exemption is Rs. 5,00,000. Where exemption is allowed to an employee under section 10(10C) for any assessment year, no exemption under this section shall be allowed to him for any other assessment year. With effect from assessment year 2010-11, section 10(10C) has been amended to provide that where any relief has been allowed to assessee under section 89 for any assessment year in respect of any amount received or receivable on his voluntary retirement or termination of service or voluntary separation, no exemption under section 10(10C) shall be allowed to him in relation to such or any other assessment year.

**Tax on perquisites paid by the employer [Section 10(10CC)]**

Perquisites to employees mean any facility provided by the employer to the employees. There are two types of perquisites, viz., monetary and non-monetary. Value of perquisite is charged to tax in the hands of the employees, however, the employer may at his will pay tax (on behalf of employees) on such perquisites. In such a case, the amount of tax paid on such perquisites by the employer on behalf of the employees will be treated as income of the employees and is charged to tax in his (i.e., in employee's) hands. However, by virtue of section 10(10CC) tax paid by employer (on behalf of employee) on non-monetary perquisites will be exempt from tax in the hands of employees. Such tax paid by the employer shall not be allowed as a deductible expenditure in the hands of employer under section 40. Section 10(10CC) provides exemption only in respect of tax on nonmonetary perquisites. In other words, this section does not provide exemption in respect of perquisites or tax paid on monetary perquisites.

**Reference Case Law:** The assessee, an employee, claimed that the tax paid by the employer on his salary income is not liable to be included in his total income as it is exempt under section 10(10CC). Assessing Officer disallowed the claim. The Tribunal following the Special bench in RBF Rigs Corpn. LIC (RBFRC) v. ACIT (2007) 109 ITD 141 (SB) (Delhi)(Trib.) held that tax borne by the employer on behalf of the employee would constitute a non-monetary payment as such the same is exempt under section 10(10CC).

**Amount paid on life insurance policy [Section 10(10D)]**

As per section 10(10D), any amount received under a life insurance policy, including bonus is exempt from tax.

Following points should be noted in this regard:

Situation	Exemption u/s 10(10D)
In respect of policies issued before 1.4.2003	Any sum received under a LIP including the sum allocated by way of bonus is exempt.
In respect of policies issued between 1.4.2003 and 31.3.2012	Any sum received under a LIP including the sum allocated by way of bonus is exempt. However, exemption would not be available if the premium payable for any of the years during the term of the policy exceeds 20% of "actual capital sum assured".
In respect of policies issued on or after 1.4.2012 but before 1.4.2013	Any sum received under a LIP including the sum allocated by way of bonus is exempt. However, exemption would not be available if the premium payable for any of the years during the term of the policy exceeds 10% of "minimum capital sum assured" under the policy on the happening of the insured event at any time during the term of the policy.
In respect of policies issued on or after 1.4.2013	(a) Where the insurance is on the life of a person with disability or severe disability as referred to in section 80U or a person suffering from disease or ailment as specified under section 80DDB.  Any sum received under a LIP including the sum allocated by way of bonus is exempt. However, exemption would not be available if the premium payable for any of the years during the term of the policy exceeds 15% of "minimum capital sum assured" under the policy on the happening of the insured event at any time during the term of the policy.
	(b) Where the insurance is on the life of any person, other than mentioned in (a) above

	Any sum received under a LIP including the sum allocated by way of bonus is exempt. However, exemption would not be available if the premium payable for any of the years during the term of the policy exceeds 10% of “minimum capital sum assured” under the policy on the happening of the insured event at any time during the term of the policy.
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**Notes:**

- (a) Amounts not to be considered while computing actual capital sum assured: For the purpose of calculating the actual capital sum assured,
- (1) the value of any premiums agreed to be returned or
  - (2) the value of any benefit by way of bonus or otherwise, over and above the sum actually assured, shall not be taken into account.
- (b) Meaning of actual capital sum assured: In respect of the life insurance policies to be issued on or after 1st April, 2012, the actual capital sum assured shall mean the minimum amount assured under the policy on happening of the insured event at any time during the term of the policy, not taking into account -
- (1) the value of any premium agreed to be returned; or
  - (2) any benefit by way of bonus or otherwise over and above the sum actually assured which is to be or may be received under the policy by any person.

In effect, in case the insurance policy has varied sum assured during the term of policy then the minimum of the sum assured during the life time of the policy shall be taken into consideration for calculation of the “actual capital sum assured”, in respect of life insurance policies to be issued on or after 1st April, 2012.

Exemption is not available in respect of amount received from an insurance policy taken for disabled person under section 80DD: Any sum received under section 80DD(3) shall not be exempt under section 10(10D). Accordingly, if the dependent disabled, in respect of whom an individual has paid or deposited any amount in any scheme of LIC or any other insurer, predeceases the individual, the amount so paid or deposited shall be deemed to be the income of the individual of the previous year in which such amount is received. Such amount would not be exempt under 10(10D).

- (c) Exemption is not available in respect of the sum received under a Keyman insurance policy: Any sum received under a Keyman insurance policy shall also not be exempt.

Explanation 1 to section 10(10D) defines “Keyman insurance policy” as a life insurance policy taken by one person on the life of another person who is or was the employee of the first-mentioned person or is or was connected in any manner whatsoever with the business of the first-mentioned person. The term includes within its scope a keyman insurance policy which has been assigned to any person during its term, with or without consideration. Therefore, such policies shall continue to be treated as a keyman insurance policy even after the same is assigned to the keyman. Consequently, the sum received by the keyman on such policies, being “keyman insurance policies”, would not be exempt under section 10(10D).

**Payment from account opened in accordance with the Sukanya Samridhi Account Rules, 2014 [Section 10(11A)]**

As per section 10(11A), any payment from an

- account opened in accordance with the Sukanya Samriddhi Account Rules, 2014 made under the Government Savings Bank Act, 1873 is exempt from tax.
- In other words, interest and withdrawals from such account will be exempt from tax under section 10(11A).

### **Payment from the National Pension System Trust to an employee [Section 10(12A)]**

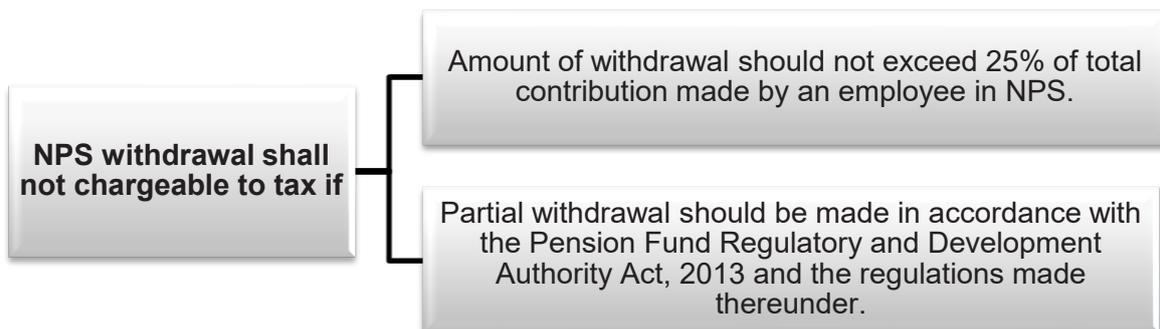
Any payment from the National Pension System Trust to

- an assessee (Word assessee is substituted in place of employee to extend benefit to non-employees)
- on closure of account or his opting out of the pension scheme referred to in section 80CCD,
- to the extent it does not exceed 60% of the total amount payable to him at the time of closure or
- his opting out of the scheme,

is exempt from tax.

### **Partial withdrawal from NPS [Section 10(12B)]**

To provide relief to an employee withdrawing partial amount from National Pension System (NPS) Trust. A new clause (12B) is inserted under section 10 with effect from assessment year 2018-19 to provide that the withdrawal from NPS will not be chargeable to tax if the following conditions are satisfied: -



### **Payment from approved superannuation fund in specified circumstances and subject to certain limits [Section 10(13)]**

Approved superannuation fund means superannuation fund which is approved by the Commissioner of Income-tax. Tax treatment of such fund is as follows:

Employer's contribution is exempt from tax, however, from assessment year 2010-11 employer's contribution in excess of Rs. 1,50,000 per annum is charged to tax as perquisite. Employee's contribution qualifies for deduction under section 80C and interest on accumulated balance is not liable to tax.

Payments made from the fund are exempt from tax under section 10(13) in following cases:

- ✓ Payment on death of beneficiary; or
- ✓ Payment to employee in lieu of, or in commutation of an annuity on his retirement at or after the specified age or on his becoming incapable prior to such retirement; or
- ✓ Payment by way of refund of contributions on the death of a beneficiary; or
- ✓ Payment to employee by way of refund of his contributions on leaving the service in connection with which the fund is established otherwise than by retirement at or after a specified age or on his becoming incapacitated prior to such retirement; or Payment to employee by way of transfer to his account under a pension scheme referred to in section 80CCD

**Allowances for meeting business expenditure [Section 10(14)]**

Discuss in Lesson No. 4 [Income under the head Salary]

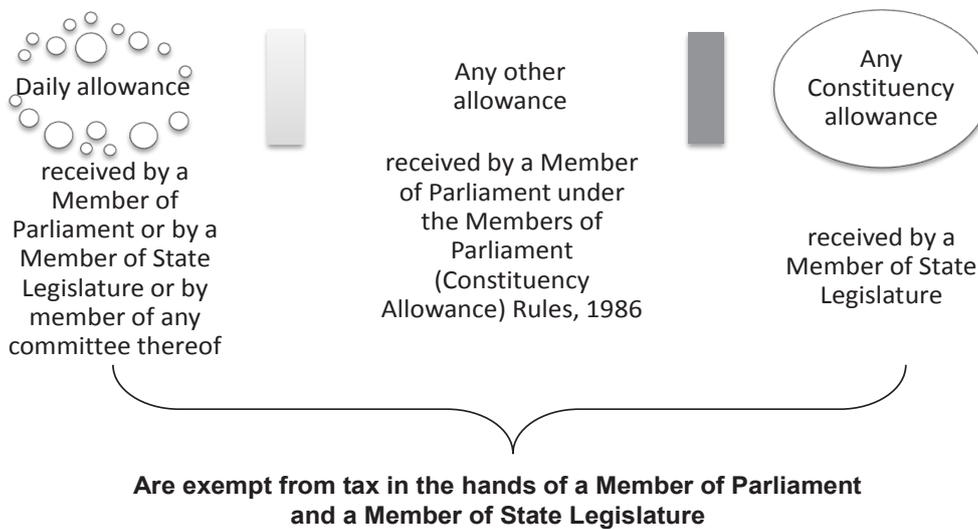
**Interest Incomes [Section 10(15)]**

Interest, Redemption Premium, on notified securities, bonds, certificates, deposits etc., are exempt for all assessees.

**Educational scholarship [Section 10(16)]**

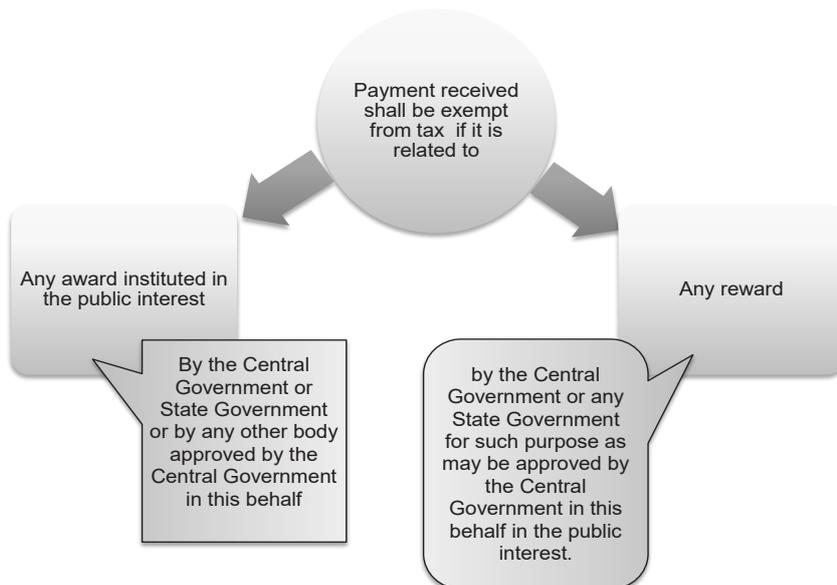
Any amount received as educational scholarship (i.e., scholarship to meet the cost of education) is exempt from tax in the hands of recipient.

**Daily allowance to a Member of Parliament [Section 10(17)]**



**Awards [Section 10(17A)]**

Any payment received in pursuance of following (whether paid in cash or in kind) is exempt from tax:



**Pension to gallantry award winner [Section 10(18)]**

Pension received by an

- individual who was employee of the Central Government or State Government and
- who has been awarded Param Vir Chakra or Maha Vir Chakra or Vir Chakra or any other notified gallantry award

is exempt from tax.

In case of death of such individual, any income by way of Family pension received by any member of the family\*\*of such individual is also exempt.

\*\*Meaning of Family:

Family, in relation to an individual, means –

- The spouse and children of the individual; and
- The parents, brothers and sisters of the individuals or any of them, wholly or mainly dependent on the individual.

**Family pension received by the family members of armed forces [Section 10(19)]**

From the assessment year 2005-06, family pension received by

- the widow or children or nominated heirs,
- of a member of armed forces (including paramilitary forces) of the
- Union,

is exempt from tax in the hands of such family members, if

- the death of such member of armed forces has occurred in the course of
- operational duty in prescribed circumstances and subject to such conditions as may be prescribed.

**Exemption of disability pension granted to disabled personnel of armed forces who have been invalided on account of disability attributable to or aggravated by such service [Circular No. 13/2019, dated 24.6.2019]**

The entire disability pension, i.e. “disability element” and “service element” of pension granted to members of naval, military or air forces who have been invalided out of naval, military or air force service on account of bodily disability attributable to or aggravated by such service would be exempt from tax.

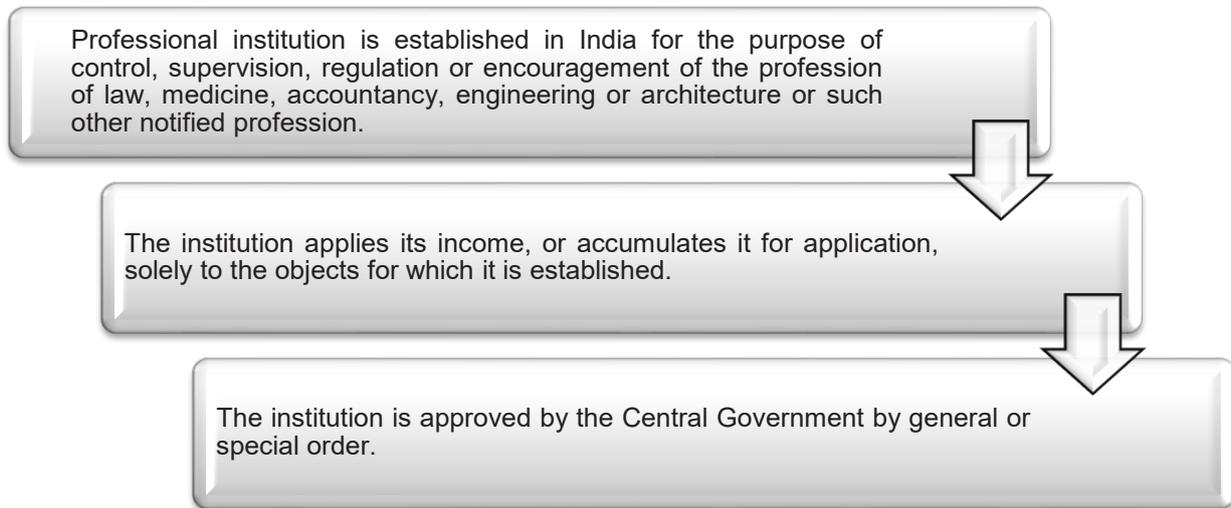
The CBDT has, vide this circular, clarified that exemption in respect of disability pension would be available to all armed forces personnel (irrespective of rank) who have been invalided out of such service on account of bodily disability attributable to or aggravated by such service. However, such tax exemption will be available only to armed forces personnel who have been invalided out of service on account of bodily disability attributable to or aggravated by such service and not to personnel who have been retired on superannuation or otherwise.

**Income of a news agency [Section 10(22B)]**

Any income of a notified news agency, set-up in India solely for collection and distribution of news is exempt from tax provided that the news agency applies its income or accumulates it for application solely for collection and distribution of news and does not distribute its income in any manner to its members.

### Income of a professional association [Section 10(23A)]

Any income (other than income from house property and income from rendering any specific service or income by way of interest or dividend on investment) of an professional institution/association is exempt from tax, if the following conditions are satisfied:



### Income received on behalf of Regimental Fund [Section 10(23AA)]

Any income received by any person on behalf of any Regimental Fund or Non-Public Fund established by the armed forces of the Union for the welfare of the past and present members of such forces or their dependents, is exempt from tax.

### Income of a fund established for welfare of employees [Section 10(23AAA)]

Any income received by any person on behalf of a fund established, for such purpose as may be notified by the Board in Official Gazette, for the welfare of employees or their dependents and of which fund such employees are members, is exempt from tax, if such fund applies or accumulates its income for exclusive application towards its objects, invests its funds in the modes specified in section 11(5) and such fund is approved by the Principal Commissioner or Commissioner in accordance with rule made in this behalf (see rule 16C and Form No. 9).

### Income of pension fund [Section 10(23AAB)]

Any income of a fund set-up by the Life Insurance Corporation of India on or after August 1, 1996 or any other insurer to which contribution is made by any person for receiving pension from such fund, and which is approved by the Controller of Insurance or the Insurance Regulatory and Development Authority, is exempt from tax.

### Income from Khadi or village industry [Section 10(23B)]

Income of an institution constituted as a public charitable trust or society which is established for the development of khadi and village industries (not for profit purpose) is exempt from tax, if following conditions are satisfied: 1) Income is attributable to the business of production, sale, or marketing, of khadi or products of village industries. 2) Institution applies its income, or accumulates it for application, solely for the development of khadi or village industries or both 3) Institution is approved by the Khadi and Village Industries Commission.

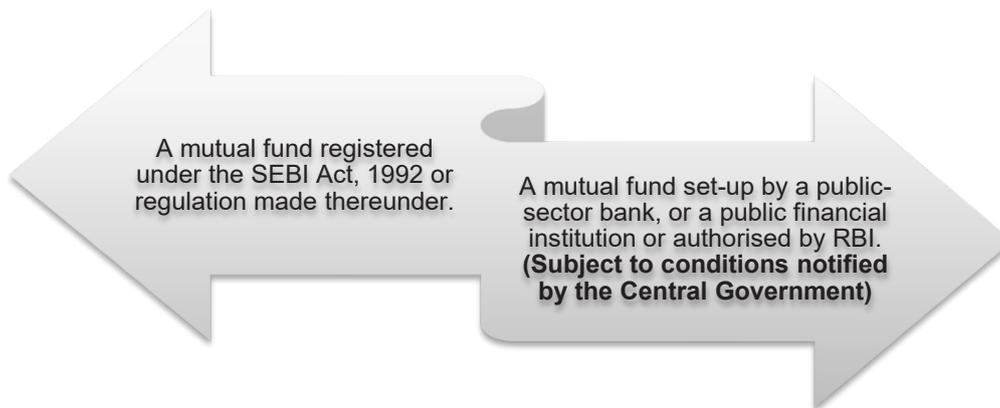
### Income of Hospital [Section 10(23C)]

Income arises to any hospital or other institution for the reception and treatment of persons suffering from illness

or mental defectiveness or for the reception and treatment of persons during convalescence or of persons requiring medical attention or rehabilitation, existing solely for philanthropic purposes and not for purposes of profit, shall be exempt from tax under following situations: 1) If the hospital or other institution is wholly or substantially financed by the Government then exemption would be available under section 10(23C). 2) If the aggregate annual receipt of such hospital or institution do not exceed Rs. 1 Crore then exemption would be available under section 10(23C). 3) If the hospital is approved by the prescribed authority

### **Income of mutual fund [Section 10(23D)]**

Any income of following mutual funds (subject to provisions of sections 115R to 115T) is exempt from tax:



### **Income of notified investor protection fund [Section 10(23EA)]**

Any income by way of contributions received from recognised stock exchanges and the members thereof, of a notified Investor Protection Fund set up by recognised stock exchanges in India is exempt from tax. Provided that where any amount standing to the credit of the Fund and not charged to income-tax during any previous year is shared, either wholly or in part, with a recognised stock exchange, the whole of the amount so shared shall be deemed to be the income of the previous year in which such amount is so shared and shall accordingly be chargeable to income-tax.

### **Income of the notified investor protection fund set-up by commodity exchange [Section 10(23EC)]**

Any income by way of contributions received from commodity exchanges and the members thereof, of a notified Investor Protection Fund set up by commodity exchanges in India is exempt from tax. Provided that where any amount standing to the credit of the Fund and not charged to income-tax during any previous year is shared, either wholly or in part, with a commodity exchange, the whole of the amount so shared shall be deemed to be the income of the previous year in which such amount is so shared and shall accordingly be chargeable to income-tax.

### **Income of Investor Protection Fund set by a depository [Section 10(23ED)]**

Any income, by way of contributions received from a depository, of notified Investor Protection Fund set up by a depository in accordance with the regulations made under the SEBI Act and Depository Act is exempt from tax. Provided that where any amount standing to the credit of the Fund and not charged to income-tax during any previous year is shared, either wholly or in part with a depository, the whole of the amount so shared shall be deemed to be the income of the previous year in which such amount is so shared and shall, accordingly, be chargeable to income-tax.

**Income of a venture capital fund or a venture capital company from investment in a venture capital undertaking [Section 10(23FB)]**

Income of a venture capital fund or a venture capital company from investment in a venture capital undertaking is exempt from tax from assessment year 2001-02. However, this exemption is subject to satisfaction of conditions specified in section 10(23FB). These provisions shall not apply in respect of any income of a venture capital company or venture capital fund, being an investment fund specified in clause (a) of the Explanation 1 to section 115UB, of the previous year relevant to the assessment year beginning on or after the 1st day of April, 2016.

**Income of an investment fund [Section 10(23FBA)]**

Any income of an investment fund other than the income chargeable under the head “Profits and gains of business or profession” is exempt under Section 10(23FBA). “Investment fund” shall have the same meaning assigned to it in clause (a) of the Explanation 1 to section 115UB. Income referred to in section 115UB of a unit holder of an investment fund [Section 10(23FBB)] Any income referred to in section 115UB, accruing or arising to, or received by, a unit holder of an investment fund, being that proportion of income, which is of the same nature as income chargeable under the head “Profits and gains of business or profession” is exempt under section 10(23FBB). “Investment fund” shall have the same meaning assigned to it in clause (a) of the Explanation 1 to section 115UB.

**Income of a registered trade union [Section 10(24)]**

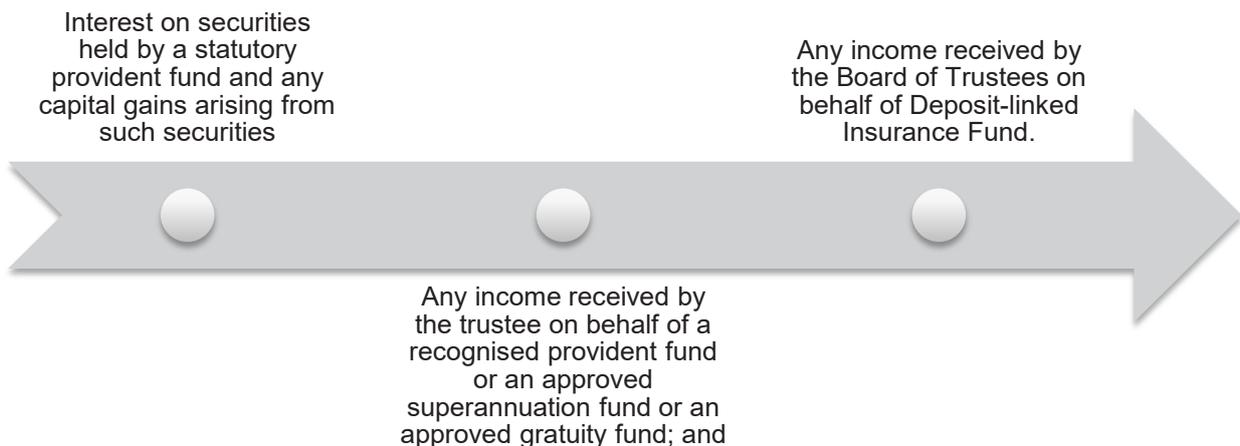
Any income chargeable under the head

- “Income from house property” and
- “Income from other sources” of a registered union within the meaning of the Indian Trade Union Act, 1926, formed primarily for the purpose of regulating the relation between workmen and employers or between workmen and workmen

is exempt from tax. Similar exemption is available to an association of registered unions.

**Income of provident fund [Section 10(25)]**

Following income is exempt from tax under this section:



**Income of the Employees’ State Insurance Fund [Section 10(25A)]**

Any income of the Employees’ State Insurance Fund of the Employees’ State Insurance Corporation set-up under the provisions of the Employees’ State Insurance Act, 1948 is exempt from tax under section 10(25A).

**Income of a member of a Scheduled Tribe [Section 10(26)]**

Income of a member of a Scheduled Tribe [as per article 366(25) of the Constitution] is exempt from tax, if following conditions are satisfied:

- ✓ Such member resides in any area in the State of Nagaland, Manipur, Tripura, Arunachal Pradesh, Mizoram or district of North Cachar Hills, Mikir Hills, Khasi Hills, Jaintia Hills and Garo Hills or in the Ladakh region of the State of Jammu and Kashmir.
- ✓ Such exemption is available in respect of income which accrues/arises from any source in such areas or income by way of dividends/interest on securities arises from any area.

**Specified income of a Sikkimese Individual [Section 10(26AAA)]**

- (i) The following income, which accrues or arises to a Sikkimese individual, would be exempt from income-tax –
  - (a) income from any source in the State of Sikkim; or
  - (b) income by way of dividend or interest on securities.
- (ii) However, this exemption will not be available to a Sikkimese woman who, on or after 1st April, 2008, marries a non-Sikkimese individual.

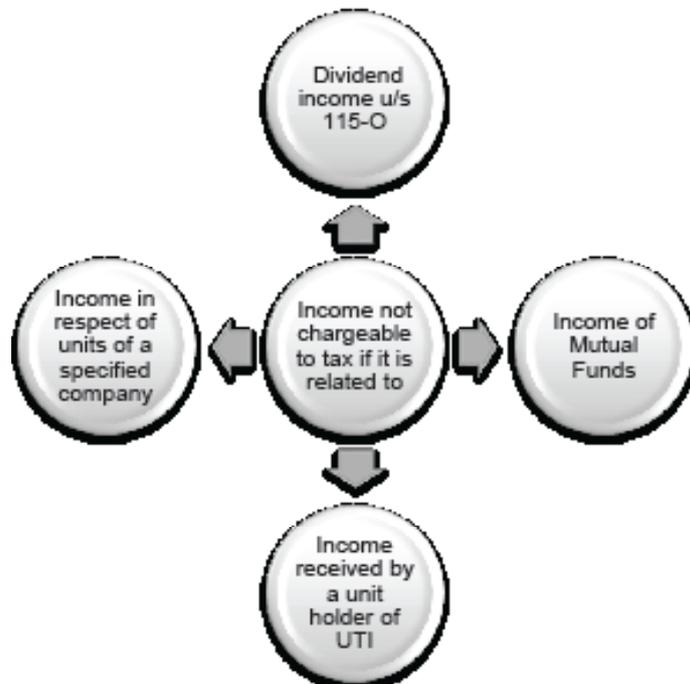
**Income of Minor [Section 10(32)]**

Under section 64(1A) income of a minor child is clubbed along with the income of his/her parent, subject to certain conditions. If the income of an individual includes any income of his/her minor child (dependent or not, adopted child), then such individual can claim exemption (in respect of each minor child) of lower of following amount:

- (a) Rs. 1,500 per minor child; or
- (b) Amount of income of each minor child (which is clubbed).

**Dividends and interest on units [Section 10(34)/(35)]**

Following incomes are not chargeable to tax from the assessment year 2004-05:



- Any income by way of dividends covered by section 115-O @ 15% [i.e., any dividends from a domestic company including dividends covered under section 2(22)(e)] at special rate of 30% ; However, as per section 115BBDA (as inserted by Finance Act, 2016), in the case of resident individual/HUF/firm, dividend shall be chargeable to tax at the rate of 10% if aggregate amount of dividend received during the year exceeds Rs. 10,00,000.
- Any income in respect of units of a mutual fund;
- Income received by a unit holder of UTI;
- Income in respect of units of a specified company.

**Note** : 1. Under section 115-O and section 115R, the person paying the dividends on share or income on units will have to pay distribution tax on dividend/income distributed.

2. It should be noted that under this clause, Income on transfer of units is not exempt.

#### **Income on Buyback of Shares [Section 10(34A)]**

Any income arising to an assessee, being a shareholder, on account of buy back of shares by the company as referred to in section 115QA is exempt from tax.

#### **Income from international sporting event [Section 10(39)]**

From the assessment year 2006-07, any specified income of notified person, arising from an international sporting event held in India is exempt from tax, if the event is approved by the international body and is notified by the Central Government and has participation by more than two countries.

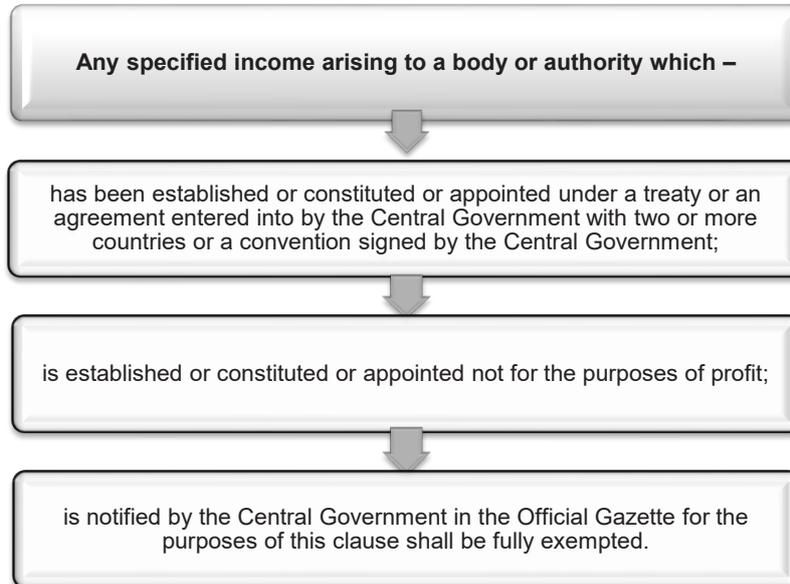
#### **Income received as grant by a subsidiary company [Section 10(40)]**

Income of any subsidiary company by way of grant or otherwise received from its Indian holding company which is engaged in the business of generation/ transmission/distribution of power is exempt, if such receipt is for settlement of dues in connection with reconstruction or revival of an existing business of power generation. The exemption is available, if the reconstruction or revival is by way of transfer of business to the Indian company notified under section 80 IA(4)(v)(a).

#### **Income from transfer of asset of an undertaking engaged in the business of generation, transmission or distribution of power [Section 10(41)]**

Under section 10(41), any capital gain arising in the above case is not chargeable to tax, if the transfer has taken place before April 1, 2006

Income from transfer of capital asset of an undertaking engaged in the business of generation, transmission or distribution of power where such transfer takes place on or before 31.3.2006 and transfer is made to the Indian company as notified u/s 801A.

**Income of a body or authority set up by two countries [Section 10(42)]****Reverse Mortgage [Section 10(43)]**

Any amount received by an individual as a loan, either in lump-sum or in installment in a transaction of reverse mortgage referred in clause (xvi) of Section 47 shall be exempted.

**New Pension System Trust [Section 10(44)]**

Any income received by any person for, or on behalf of the New Pension System Trust established on 27th February, 2008 shall be exempted.

**Exemption of Allowance or perquisite to chairman/member of UPSC [Section 10 (45)]**

Any allowance or perquisite, as may be notified by the Central Government in the Official Gazette, in this behalf, paid to the chairman or a retired chairman or any other member or retired member of the Union Public Service Commission, shall be exempt.

**Exemption of 'specified income' of certain bodies or authorities [Section 10(46)]**

Any specified income arising to a body or authority or Board or Trust or Commission which:

- is constituted or established by or under a Central, State or Provincial Act, or has been constituted by the Central Government or a State Government with the object of regulating or administering an activity for the benefit of general public;
- is not engaged in commercial activity; and
- is specified by the Central Government by notification in the Official Gazette in this behalf, shall be exempt.

The Central Government has the power to notify the nature and extent of the income of a class of such body or authority or Board or Trust or Commission which shall constitute the specified income, by single notification.

**Exemption of Income of notified 'Infrastructure debt fund' [Section 10(47)]**

Any income of notified 'infrastructure debt fund', which is set up in accordance with the guidelines as may be prescribed, shall be exempt from income-tax.

**Exemption of Income of a foreign company from sale of Crude Oil in India [Section 10 (48)]**

Any income of a foreign Co. received in India in Indian currency on account of sale of crude oil to any person in India shall be exempt if the following conditions are satisfied.

- Such Income is in pursuant to an agreement or an arrangement entered into by the Central Govt. or approved by the Central Govt.;
- having regard to the national interest, the foreign company and the agreement or arrangement are notified by the Central Govt. in this behalf; and
- the foreign company is not engaged in any activity, other than receipt of such income, in India.

**Exemption of income of foreign company from sale of leftover stock of crude oil on termination of agreement or arrangement [ Section 10(48B) ]**

Any income of foreign company on account of sale of leftover stock of crude oil from the facility in India after the expiry or on termination of the agreement or the arrangement shall be exempt, in accordance with the terms mentioned therein.

**Exemption of income of National Financial Holdings Company [Section 10(49)]**

Any income of the National Financial Holdings Company, being a company set-up by the Central Government, shall be exempt.

**Other important exemptions**

Apart from above discussed exemption of section 10, following is the list of other important exemptions:

- 1) **Section 10AA provides for exemption in respect of income of newly established units in Special Economic Zones**

**Applicability**

A deduction of profits and gains which are derived by an assessee being an entrepreneur from the export of articles or things or providing any service, shall be allowed from the total income of the assessee.

**Which assessee is eligible for exemption:**

Exemption is available to

- all categories of assesseees who derive any profits or gains from an undertaking, being a unit,
- engaged in the manufacturing or production of articles or things or provision of any service.

Such assessee should be an entrepreneur referred to in section 2(j) of the SEZ Act, 2005 i.e., a person who has been granted a letter of approval by the Development Commissioner under section 15(9) of the said Act.

This section applies to any undertaking, being the Unit, which fulfils all the following conditions, namely:

- (i) it has begun or begins to manufacture or produce articles or things or provide services during the previous year relevant to the assessment year commencing on or after the 1st day of April, 2006 in any Special Economic Zone;
- (ii) it is not formed by the splitting up, or the reconstruction, of a business already in existence:  

Provided that this condition shall not apply in respect of any undertaking, being the Unit, which is formed as a result of the re-establishment, reconstruction or revival by the assessment of the business of any such undertaking as is referred to in section 33B, in the circumstances and within the period specified in that section;
- (iii) it is not formed by the transfer to a new business, of machinery plant previously used for any purpose.

However, deduction under section 10AA will be available if total value of the machinery or plant transferred does not exceed 20% of the total value of machinery or plant used in the business.

For this purpose, any machinery or plant which was used outside India by any person other than the assessee shall not be regarded as machinery or plant previously used for any purpose if the following conditions are fulfilled:

- (a) such machinery or plant was not at any time used in India;
  - (b) such machinery or plant is imported into India from any country outside India; and
  - (c) no deduction on account of depreciation has been allowed in respect of such machinery or plant to any person earlier.
- (iv) The assessee should furnish in the prescribed form, alongwith the return of income, the report of a chartered accountant certifying that the deduction has been correctly claimed.

### Deduction

- (i) 100% of profits and gains derived from the **export, of such articles or things or from services for a period of five consecutive assessment years[1st to 5th year]** beginning with the assessment year relevant to the previous year in which the Unit begins to manufacture or produce such articles or things or provide services, as the case may be, and fifty per cent of such profits and gains for further five assessment years and thereafter;

- (ii) 50% of such profits and gains for further 5 assessment years[ 6th to 10 th year]

for further next five consecutive assessment years[11th to 15th year], so much of the amount not exceeding fifty per cent of the profit as is debited to the profit and loss account of the previous year in respect of which the deduction is to be allowed and credited to a reserve account (to be called the "Special Economic Zone Re-investment Reserve Account") to be created and utilized for the purposes of the business of the assessee in the manner laid down in sub-section (2).

### Computation of profits and gains from exports of such undertakings

The profits derived from export of articles or things or services (including computer software) shall be the amount which bears to the profits of the business of the undertaking, being the unit, the same proportion as the export turnover in respect of such articles or things or services bears to the total turnover of the business carried on by the undertaking i.e.

$$\text{Profits of Unit in SEZ} \times \frac{\text{Export turnover of Unit SEZ}}{\text{Total turnover of Unit SEZ}}$$

### Clarification on issues relating to export of computer software

Section 10AA provides deduction to assesseees who derive any profits and gains from export of articles or things or services (including computer software) from the year in which the Unit begins to manufacture or produce such articles or things or provide services, as the case may be, subject to fulfillment of the prescribed conditions. The profits and gains derived from on site development of computer software (including services for development of software) outside India shall be deemed to be the profits and gains derived from the export of computer software outside India.

**Meaning of Export turnover:** It means the consideration received in India or brought into India by the assessee in respect of export by the undertaking being the unit of articles or things or services.

However, it does not include

- freight

- telecommunication charges
- insurance

attributable to the delivery of the articles or things outside India or expenses incurred in foreign exchange in rendering of services (including computer software) outside India.

**Clarification on issues relating to deduction of freight, telecommunication charges and other expenses from total turnover [Circular No. 4/2018, dated 14/08/2018]**

“Export turnover”, inter alia, does not include freight, telecommunication charges or insurance attributable to the delivery of the articles or things outside India or expenses, if any, incurred in foreign exchange in rendering of services (including computer software) outside India.

CBDT has, vide this notification, clarified that freight, telecommunication charges and insurance expenses are to be excluded both from “export turnover” and “total turnover”, while working out deduction admissible under section 10AA to the extent they are attributable to the delivery of articles or things outside India.

Similarly, expenses incurred in foreign exchange for rendering services outside India are to be excluded from both “export turnover” and “total turnover” while computing deduction admissible under section 10AA.

**Calculation of Deduction**

**Step 1:** Calculate the total income of the assessee as per the provisions of the act, but before allowing deduction under section 10AA.

**Step 2 :** From the amount calculated in Step 1, allow the deduction under section 10AA, which is least of the following:

- Amount calculated under step 1; or
- Amount deductible under section 10AA

**Conditions:**

- a) the amount credited to the Special Economic Zone Re-investment Reserve Account is to be utilised -
  - (i) for the purpose of acquiring machinery or plant which is first put to use before the expiry of a period of three years following the previous year in which the reserve was created; and
  - (ii) until the acquisition of the machinery or plant as aforesaid, for the purposes of the business of the undertaking other than for distribution by way of dividends or profits or for remittance outside India as profits or for the creation of any asset outside India;
- b) the particulars, as may be specified by the Central Board of Direct Taxes in this behalf, under clause (b) of sub-section (1B) of section 10A have been furnished by the assessee in respect of machinery or plant along with the return of income for the assessment year relevant to the previous year in which such plant or machinery was first put to use.

Where any amount credited to the Special Economic Zone Re-investment Reserve Account has been utilised for any purpose other than those referred, the amount so utilised; or has not been utilised before the expiry of the period specified, the amount not so utilised, shall be deemed to be the profits,

- (i) in a case referred to in clause (a), in the year in which the amount was so utilised; or
- (ii) in a case referred to in clause (b), in the year immediately following the period of three years specified in sub-clause (i) of clause (a) of sub-section (2),

and shall be charged to tax accordingly

**Restriction on other tax benefits**

- (i) The business loss under section 72(1) or loss under the head “Capital Gains” under section 74(1), in

so far as such loss relates to the business of the undertaking, being the Unit shall be allowed to be carried forward or set off.

- (ii) In order to claim deduction under this section, the assessee should furnish report from a Chartered Accountant in the prescribed form along with the return of income certifying that the deduction is correct.
- (iii) During the period of deduction, depreciation is deemed to have been allowed on the assets. Written Down Value shall accordingly be reduced.
- (iv) No deduction under section 80-IA and 80-IB shall be allowed in relation to the profits and gains of the undertaking.
- (v) Where a deduction under this section is claimed and allowed in relation to any specified business eligible for investment-linked deduction under section 35AD, no deduction shall be allowed under section 35AD in relation to such specified business for the same or any other assessment year.

### Deduction allowable in case of amalgamation and demerger

In the event of any undertaking, being the Unit which is entitled to deduction under this section, being transferred, before the expiry of the period specified in this section, to another undertaking, being the Unit in a scheme of amalgamation or demerger, -

- (a) no deduction shall be admissible under this section to the amalgamating or the demerged Unit for the previous year in which the amalgamation or the demerger takes place; and
- (b) the provisions of this section would apply to the amalgamated or resulting Unit, as they would have applied to the amalgamating or the demerged Unit had the amalgamation or demerger had not taken place.

### Illustration to explain exemption u/s 10 AA

Rajveer Turbines has 2 undertakings, one in a SEZ and one in a normal zone. The summarised results are as under:

Item	SEZ	Normal
Domestic turnover	50	125
Export turnover	200	0
Gross Profit	75	25
Expenses & Depreciation	15	10
Net profit	60	15

Compute the business income of the assessee.

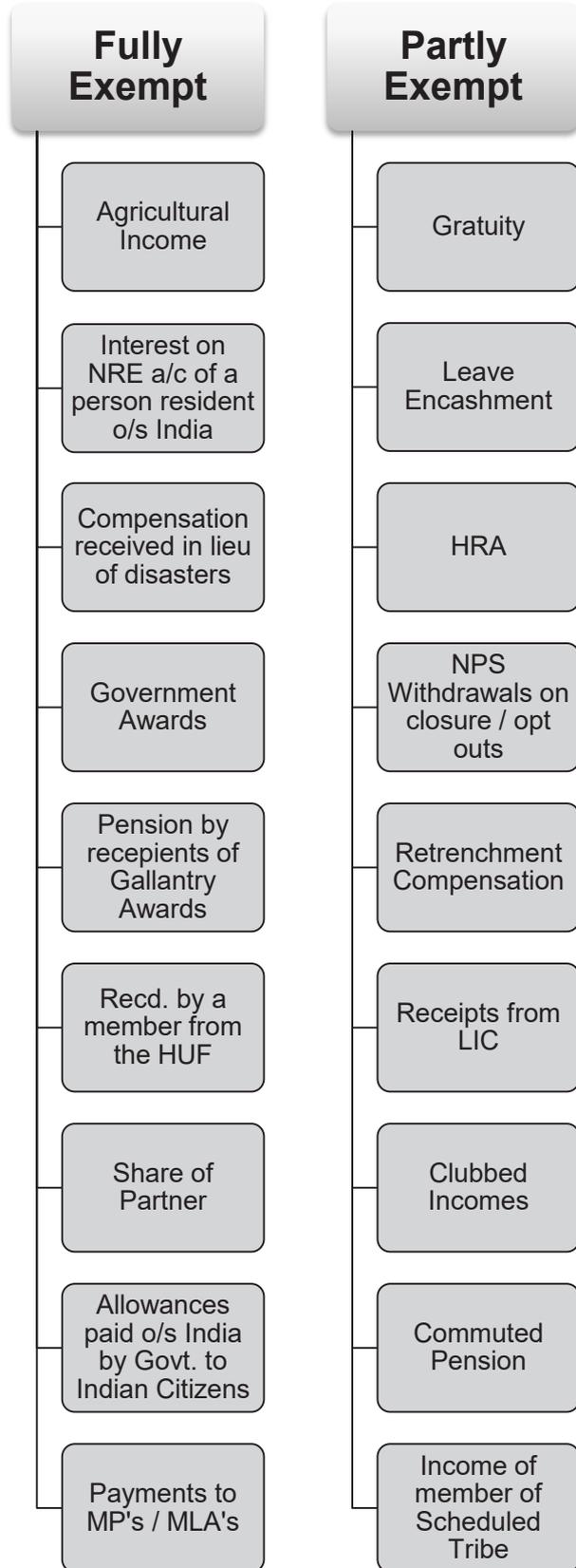
The treatment is as under:

Total profit	75
Less : Exempt u/s 10AA	48
Taxable profits	27

### Note:

1. Total profits is the sum of the respective net profits for both the units
2. The exemption is in the proportion of the export turnover to total turnover
3. It is assumed that the current FY falls within the 1st 5 years commencing from the year of manufacture of goods / provision of services by the SEZ Unit, as the quantum of deduction available is 100% of export profits for the first 5 years and 50% for the next 5 years and 50% of the next 5 years as is credited to a special reserve a/c.

**SUMMARY CHART**



### LESSON ROUND UP

- This Lesson discusses the general exempted incomes enumerated under section 10 and other specific exempted income dealt under section 10A, 10AA.
- The scheme applies only to those assesseees (being an individual, association of persons or body of individuals) who have simultaneously net agricultural income exceeding Rs. 5,000 and non agricultural income exceeds the basis exemption limit of Rs. 2,50,000 or Rs.3,00,000 or Rs. 5,00,000 the case may be.
- Leave salary means the salary for the period of leave not availed by the employee. The encashment of accumulated leave can be at the time of retirement or during the continuation of service.
- In case of a Government employee, any death-cum-retirement gratuity received is wholly exempt under section 10(10)(i). Employees of statutory corporation will not fall under this category.
- Any payment received from an account, opened in accordance with the Sukanya Samriddhi Account Rules, 2014 made under the Government Savings Bank Act, 1873 is exempt income.

### SELF TEST QUESTIONS

These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.

#### Multiple Choice Questions (MCQs)

Choose the most appropriate answer from the given options in respect of the following:

- (i) Any rent or revenue derived from land may be treated as agricultural income if-
- (a) It is derived from land
  - (b) The land is situated in India
  - (c) The land is used for agricultural purpose
  - (d) All the above conditions are satisfied.

Ans: (d)

- (ii) Which of the following income is agricultural income—
- (a) Rent received from agricultural land
  - (b) Income from dairy farm
  - (c) Income from poultry farm
  - (d) Dividend from a company engaged in agriculture.

Ans: (a)

- (iii) Income of an assessee engaged in the business of growing and manufacturing tea in India is taxable to the extent of-
- (a) 40% of such income
  - (b) 60% of such income
  - (c) 70% of such income
  - (d) 30% of such income.

Answer: (a)

- (iv) If non-agricultural income is Rs. 2,02,000 and net agricultural income is Rs. 40,000, the tax liability of an individual assessee will be:

- (a) Nil (b) Rs. 200  
 (c) Rs. 206 (d) Rs. 4,326.

Answer: (a)

- (v) Which of the following additional incomes will not be treated as agricultural income under the Income-Tax Act, 1961:

- (a) Additional income from selling ginned cotton as compared to unginned cotton  
 (b) Additional income from selling dried-up coffee as compared to raw coffee  
 (c) Additional income from selling cured tobacco as compared to green tobacco leaves  
 (d) Additional income from selling dried-up tea leaves as compared to raw tea leaves.

Answer: (a)

- (vi) Pawan reports net income of Rs. 5 lakh from the activity of growing and manufacturing rubber. How much of such income is to be treated as non-agricultural income:

- (a) Rs. 1,75,000 (b) Rs. 2,00,000  
 (c) Rs. 1,25,000 (d) Nil

Answer: (a) Rs.1,75,000

- (vii) Tax holiday under section 10AA in respect of newly established units in SEZ is allowed for a total period of —

- (a) 5 Years (b) 10 Years  
 (c) 15 Years (d) 20 Years.

Answer: (c) 15 Years.

- (viii) Mr. Vinayak derived income from sale of tea manufactured and grown in Coorg, Karnataka. His income for the previous year 2017-18 from the said activity is Rs. 20 lakhs. The amount exempt from tax by way of agricultural income is:

- (a) Rs. 8 lakhs (40%) (b) Rs. 5 lakhs (25%)  
 (c) Rs. 12 lakhs (60%) (d) Rs. 7 lakhs (35%) (1 mark)

Answer: (c) Rs. 12 lakhs (60%)

- (ix) Mr. Sankar received Rs. 50,000 as educational scholarship from Nehru Memorial Trust (a charitable trust). The scholarship is to assist Mr. Sankar for pursuing M.A. (History) at Jawaharlal Nehru University, New Delhi. The amount of scholarship liable to tax is:

- (a) Rs. 50,000 (b) Rs. 10,000  
 (c) Rs. 25,000 (d) Nil

Answer: (d) Nil

- (x) Mr. Chandan (age 70) received Rs. 30,000 every month during the financial year 2017-18 on reverse mortgage of his property with State Bank of India. The amount of receipt liable to tax in the hands of Mr. Chandan is:

- (a) Rs. 3,60,000 (b) Rs. 2,52,000  
 (c) Rs. 40,000 (d) Nil

Answer: (d) Nil

- (xi) Mr. Menon having tea estate in Munnar (Kerala) earned Rs. 5 lakhs by way of growing tea leaves and manufacturing tea. The income chargeable to tax would be:

- (a) Rs. 2,00,000      (b) Rs. 1,75,000  
(b) Rs. 1,25,000      (d) None of the above

Answer: (a) Rs. 2,00,000

- (xii) Ms. Laxmi received Rs. 60,000 by way of family pension from State Government. The amount of family pension eligible for exemption under section 10(19) is:

- (a) Rs. 60,000      (b) Rs. 40,000  
(c) Rs. 20,000      (d) Nil

Answer: As per section 10(19) family pension received by the widow or children or nominated heirs, as the case may be, of a member of the armed forces (including paramilitary forces) of the Union, where the death of such member has occurred in the course of operational duties, in such circumstances and subject to such conditions, as may be prescribed shall be fully exempted. Exemption is available only to union and not state, hence exemption under 10(19) is NIL.

- (xiii) A registered trade union earned income by way of interest on fixed deposit held with State Bank of India of Rs. 5,60,000. The interest income chargeable to tax in the hands of trade union would be:

- (a) Rs. 5,60,000      (b) Nil  
(c) Rs. 2,60,000      (d) Rs. 3,10,000

Answer: (b) Nil

- (xiv) The income derived from growing, manufacturing and sale of Centrifuged latex or Cenex or Latex based cops as per Rule 7A of the Income-tax Rules, 1962 shall be taken as agricultural and non-agricultural income in the following ratio:

- (a) 75% and 25%      (b) 60% and 40%  
(c) 65% and 35%      (d) None of the above

Answer: (c) 65% and 35%

## SUGGESTED READINGS

### 1. Direct Taxes Law and Practice

Author : Dr. Vinod K. Singhania & Dr. Kapil Singhania

Publisher : Taxmann

Year : 2019

Edition : 2019

### 2. Direct Taxes Ready Reckoner with Tax Planning

Author : Dr. Girish Ahuja & Dr. Ravi Gupta

Publisher : Wolters Kluwer

Year : 2019

Edition : 20th Edition





# Lesson 4

## Computation of Income under Various Heads

### LESSON OUTLINE

- Part I Salaries (Sections 15 to 17);
- Part II Income from house property (Sections 22 to 27);
- Part III Profits and gains from business or profession (Sections 28 to 44D);
- Part IV Capital gains (Sections 45 to 55A); and
- Part V Income from other sources (Sections 56 to 59).

### LEARNING OBJECTIVES

The taxability of income of a person depends on the chargeability of such income under the Income tax Act 1961. The total income of an assessee (subject to statutory exemptions) is chargeable under Section 4(1). The scope of the total income, which varies with the residential status, is defined in Section 5. Section 14 enumerates the heads of income under which the income of an assessee will fall. The rules for computing income and the permissible deductions under different heads of income, are dealt in different sections of the Act. The heads of income, along with their corresponding set of sections for the purpose of computation of income, are given below :

- (A) Salaries (Sections 15 to 17);
- (B) Income from house property (Sections 22 to 27);
- (C) Profits and gains of business or profession (Sections 28 to 44D);
- (D) Capital gains (Sections 45 to 55A); and
- (E) Income from other sources (Sections 56 to 59).

# Lesson 4

## Part I – Income under the Head “Salaries”

### LESSON OUTLINE

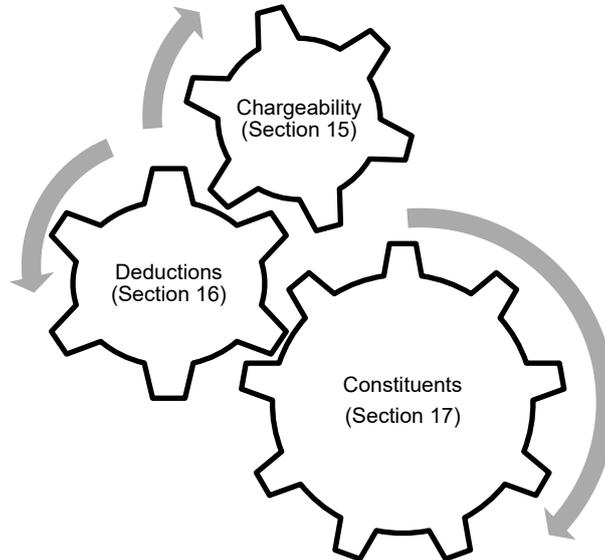
- Introduction
- Basis of Charge
- Salary [Section 17(1)]
- Allowances
- Perquisites [Section 17(2)]
  - (A) Tax-free perquisites (in all cases)
  - (B) Taxable perquisites (in all cases)
- Valuation of Perquisites
- Retirement Benefits
- Provident funds - Treatment of Contributions to and Money Received from the Provident Fund
- Deductions Allowed from Salaries (Section 16)
- Computation of Salary
- Illustrations
- LESSON ROUND UP
- SELF TEST QUESTION

### LEARNING OBJECTIVES

At the end of this lesson, you will learn how to calculate income under the head salaries, what are the deductions, exemptions available from salaries.

## INTRODUCTION

The provisions related to “Salaries” are contained as under:



The most fundamental of all aspects is to know that it is a pre-requisite that an *employer-employee relationship* exists, and that is the premise basis which the Income can be charged as “Salaries”. It is also important to note that the employment could be full time or part time, that really doesn’t matter, what matters is that the relationship should be *employer-employee*.

The question whether a particular person receives the income in his capacity as an employee or not has to be decided from the facts of each case.

Let’s examine the following cases, whether payments are chargeable under head salaries;

- (i) **Professor** : The professor of university would be receiving income by way of monthly salary from the university which is chargeable to tax under this head. But this does not mean that every item of income received by the employee from his employer would be taxable under this head. Thus, income by way of examinership fees received by a professor from the same university in which he is employed would not be chargeable to tax under this head but must be taxed as Income from other sources under Section 56. This is because of the fact that the essential condition that the income in question must be received for services rendered in the ordinary course of employment would not be fulfilled in the case of examinership fees.
- (ii) **Director** :A director of a company may, in some cases, be an employee of a company where there is a specific contract of employment between him and the company. The fact that the same person has dual capacity in his relationship with the company does not mean that he cannot be taxed under this head. Every item of income arising to such a director who is also an employee of the company (e.g. a managing director or other whole-time director) by virtue of his employment would be taxable as his income from salary. Thus, income by way of remuneration received by a managing director would be taxable as his salary income whereas the income received by him as director’s fees in his capacity as director for attending the meetings of the Board would be assessable under the head “Income from other sources”.
- (iii) **Official Liquidator** : An official liquidator appointed by the Court or by the Central Government would also become an employee of the Central Government under Section 448 of the Companies Act, 1956 and consequently the remuneration due to him would also be assessable under the head ‘Salaries’.

- (iv) **Manager** : Remuneration received by a manager of a company even if he is wrongly designated as a director or by any other name would be chargeable to tax under this head regardless of the fact that the amount is payable to him monthly or is calculated at a certain percentage of the company's profits.
- (v) **Partner of a firm** : Salary paid to a partner by a firm is nothing but appropriation of profits. Any salary, bonus, commission, or remuneration by whatever name called due to or received by partner of a firm shall not be regarded as salary but has to be charged as income from business. It is because of the fact that the relationship between the firm and its partner is not of employer and employee.
- (vi) **Member of Parliament** : According to a circular of the Board dated 22-5-1967, the salary received by a person as Member of Parliament will not be chargeable to income-tax under the head "Salaries" but as "Income from other sources" because a Member of Parliament is not an employee of the Government but only an elected representative of the people.
- (vii) **Treasurer of a bank** : The income received by a treasurer of a bank would be taxable as his salary income if the treasurer is an employee of the bank. If he does not happen to be an employee, the income received by him would be taxable as "Income from other sources". For this purpose, the question whether in a particular case the treasurer is an employee or not has to be decided on the basis of the facts and circumstances of each case having due regard to his powers, responsibilities and functions.
- (viii) **Person carrying on a profession or vocation** : Income derived by any person from carrying on a profession or vocation must be taxed as business income and not as salary income because employment is different from profession.

But, if an employee receives any money from his employer as part of the terms of employment for not carrying on any profession, such income must be taxed as salary income. For instance, the allowance given by employer to a doctor employed by him for not carrying on a profession in addition to the employment would be income arising from employment in accordance with the terms and conditions of such employment and must, therefore, be taxed as salary income. If an employee gets money from persons other than his employer and if such money is not in any way related to the contract of services with the employer under whom he is working, the receipts, if taxable as income, must be assessed under the head "Income from other sources".

However, gratuity, bonus, commission or other items of payment made by the employer without any specific stipulation in the contract of employment to this effect, would still be taxable as salary, because they are paid by the employer for the services rendered by the employee. The fact that such payments are voluntary and in certain circumstances may qualify for exemption from income-tax in the hands of the employee, would not affect the income being computed under the head salary.

## BASIS OF CHARGE

*The charging section, Section 15* states that, salary is taxable on "due" or "paid" basis whichever is earlier. That is, if it is due, it is included in taxable salary, irrespective of whether it is paid or not, and if it is paid, it is taxable, irrespective of whether it is due or not. Therefore, it is only logical to note that if it has already been taxed on due basis, the same cannot be taxed again when it is paid. Similarly, if a salary which was paid in advance, if it has already been taxed in the year of payment, it cannot subsequently be taxed when it becomes due.

### KEY POINTS

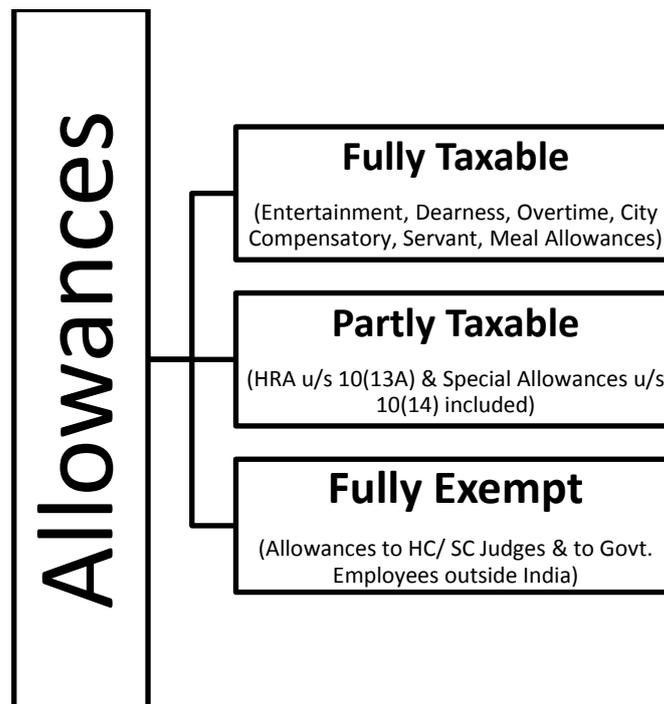
- Advance salary is taxable; however, an Advance against Salary is essentially a loan which will be recovered later from the Employee and therefore that is n't taxable.
- Salary, if earned in India, is deemed to accrue / arise in India, even if it is paid outside India

**SALARY [SECTION 17(1)]**

Salary would include wages, allowances, annuity, pension, gratuity, fees, commission, advance, leave encashment and also perquisites and profits in lieu of salary etc.

**ALLOWANCES**

An allowance is defined as a fixed amount of money given periodically in addition to the salary for the purpose of meeting some specific requirements connected with the service rendered by the employee or by way of compensation for some unusual conditions of employment. It is taxable on due/accrued basis whether it is paid in addition to the salary or in lieu thereon. These allowances are generally taxable and are to be included in the gross salary unless a specific exemption has been provided in respect of allowances provided under the Act.

**Fully Taxable Allowances**

- (1) **Dearness Allowance, Additional Dearness Allowance and Dearness Pay:** This is a very common allowance these days on account of high prices. Sometimes Additional Dearness Allowance is also given. It is included in the income from salary and is taxable in full. Sometimes it is given under the terms of employment and sometimes without it. When it is given under the terms of employment it is included in salary for purposes of determining the exemption limits of house rent allowance, recognised provident fund, gratuity and value of rent free house and is also taken into account for the purposes of retirement benefits.

Sometimes dearness allowance is given as ‘Dearness Pay’. It means that it is being given under the terms of employment.

- (2) **Fixed Medical Allowance:** It is fully taxable.
- (3) **Tiffin Allowance:** It is given for lunch and refreshments to the employees. It is taxable.
- (4) **Servant Allowance:** It is fully taxable even if it is given to a low paid employee, not being an officer, i.e., it is taxable for all categories of employees.

- (5) **Non-practising Allowance:** It is generally given to those medical doctors who are in government service and they are banned from doing private practice. It is to compensate them for this ban. It is fully taxable.
- (6) **Hill Allowance:** It is given to employees working in hilly areas on account of high cost of living in hilly areas as compared to plains. It is fully taxable, if the place is located at less than 1,000 metres height from sea level.
- (7) **Warden Allowance and Proctor Allowance:** These allowances are given in educational institutions for working as Warden of the hostel and/or working as Proctor in the institution. These allowances are fully taxable.
- (8) **Deputation Allowance:** When an employee is sent from his permanent place of service to some other place or institution or organisation on deputation for a temporary period, he is given this allowance. It is fully taxable.
- (9) **Overtime Allowance:** When an employee works for extra hours over and above his normal hours of duty he is given overtime allowance as extra wages. It is fully taxable.
- (10) **Other Allowances** like Family allowance, Project allowance, Marriage allowance, City Compensatory allowance, Dinner allowance, Telephone allowance etc. These are fully taxable.

### Allowances not fully taxable

#### House Rent Allowance u/s 10(13A)

House Rent Allowance (HRA) received by any employee is exempt to the extent of least of the following:

- 50% of Salary for Metro Cities (Delhi, Mumbai, Kolkata and Chennai), else 40% of Salary
- HRA actually received
- Rent paid minus 10% of Salary

*Note: Salary for the purposes of HRA = Basic + DA (if forming part of salary/retirement benefit) + Commission as a fixed % of Turnover*

#### **Illustration:**

*Vir is employed with Happiness Solutions Ltd. and during the FY 2019-20. He had a Basic Pay of INR 75000 per month. Owing to his good performance at workplace, he was given an annual increment in his Salary of 20% effective Feb 2020. He also received during the year, a Dearness Allowance of 100% of Basic (however only 50% of which was included per his terms of employment). The Company also gave him HRA of INR 30000 per month, which was increased to INR 35000 per month effective Jan 2020. He stayed at his parental home in Ahmedabad for Apr and May 2019, post which he took up a Rented Accommodation at Surat at a monthly rental of INR 26000. Effective Nov 19, he was moved to Mumbai to the Corporate Office, and he took up an accommodation at Mumbai at a monthly rental of INR 36000. You are required to compute the HRA exempt from Tax and the Gross Salary.*

#### **Solution**

*The computation of HRA exempt from tax would have to be done on a monthly basis as the salary and rental figures changed during the year, in the manner provided below.*

Item	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Total
Basic	75,000	75,000	75,000	75,000	75,000	75,000	75,000	75,000	75,000	75,000	90,000	90,000	9,30,000
D.A.	37,500	37,500	37,500	37,500	37,500	37,500	37,500	37,500	37,500	37,500	45,000	45,000	
Salary for HRA	1,12,500	1,12,500	1,12,500	1,12,500	1,12,500	1,12,500	1,12,500	1,12,500	1,12,500	1,12,500	1,35,000	1,35,000	
Accommodation	Own	Own	Surat	Surat	Surat	Surat	Surat	Mumbai	Mumbai	Mumbai	Mumbai	Mumbai	
40% or 50% of Salary	–	–	45,000	45,000	45,000	45,000	45,000	56,250	56,250	56,250	67,500	67,500	
HRA Actually Recd	30,000	30,000	30,000	30,000	30,000	30,000	30,000	30,000	30,000	35,000	35,000	35,000	3,75,000
Rent - 10% Salary	–	–	14,750	14,750	14,750	14,750	14,750	24,750	24,750	24,750	22,500	22,500	
Min	–	–	14,750	14,750	14,750	14,750	14,750	24,750	24,750	24,750	22,500	22,500	1,93,000

Note:

- (1) For the stay at Surat, 40% of Salary and for stay at Mumbai, 50% of Salary is considered for one of the parameters for exemption.
- (2) DA, only to the extent of it being included per terms of employment, is included in Salary for the purposes of HRA.

Please note the Gross Salary Computation below.

Particulars	Rs.	Rs.
Basic Salary (75000 x 10 + 90000 x 2)		9,30,000
Dearness Allowance (100% of Basic)		9,30,000
HRA	3,75,000	
Less : Exempt	1,93,000	1,82,000
<b>Gross Salary</b>		<b>20,42,000</b>

### Special Allowances [Section 10(14)]

- i) All special allowances specifically granted to meet expenses, incurred, for the purposes of performance of duties
  - a) Wholly
  - b) Exclusively &
  - c) Necessarily

These are exempt to the extent such expenses are actually incurred or the amount received whichever is less. *Examples include, Travelling & Conveyance, Relocation, Helper & Uniform Allowances. (no cap or upper limit)*

- ii) Special allowances granted to an assessee either to meet his personal expenses at the place of duty OR to compensate for increased cost of living. Allowances which are granted to meet personal expenses are exempt to the extent of amount received or the limits specified whichever is less.

Examples include,

- a) Tribal Area Allowance capped to INR 200 per month is exempt.
- b) Children Education Allowance capped to INR 100 per month (per child, max 2 children) is exempt.
- c) Hostel Expenditure Allowance capped to INR 300 per month (per child, max 2 children) is exempt.
- d) Transport Allowance for handicapped capped at INR 3200 per month is exempt.

112 EP-TL

Besides the above there are compensatory allowances for hilly areas, and for work in difficult conditions too.

As per section 10(14), read with rule 2BB following allowances granted to an employee are exempt from tax subject to certain limit:

Allowances	Exemption Limit
Children Education Allowance	Up to Rs. 100 per month per child up to a maximum of 2 children is exempt
Hostel Expenditure Allowance	Up to Rs. 300 per month per child up to a maximum of 2 children is exempt
Transport Allowance granted to an employee to meet expenditure on commuting between place of residence and place of duty. Consequent to introduction of Standard Deduction under section 16, exemption of transport allowance of Rs. 1600 P.M. is withdrawn.	Only Rs. 3,200 per month for blind and handicapped employees is exempt
Allowance granted to an employee working in any transport business to meet his personal expenditure during his duty performed in the course of running of such transport from one place to another place provided employee is not in receipt of daily allowance	Amount of exemption shall be lower of following: a) 70% of such allowance; or b) Rs. 10,000 per month
Conveyance Allowance granted to meet the expenditure on conveyance in performance of duties of an office	Exempt to the extent of expenditure incurred for official purposes
Travelling Allowance to meet the cost of travel on tour or on transfer	Exempt to the extent of expenditure incurred for official purposes
Daily Allowance to meet the ordinary daily charges incurred by an employee on account of absence from his normal place of duty	Exempt to the extent of expenditure incurred for official purposes
Helper/Assistant Allowance	Exempt to the extent of expenditure incurred for official purposes
Research Allowance granted for encouraging the academic research and other professional pursuits	Exempt to the extent of expenditure incurred for official purposes
Uniform Allowance	Exempt to the extent of expenditure incurred for official purposes
Special compensatory Allowance (Hilly A r e a s ) (Subject to certain conditions and locations)	Amount exempt from tax varies from Rs. 300 to Rs. 7,000 per month.
Border area, Remote Locality or Disturbed Area or Difficult Area Allowance (Subject to certain conditions and locations)	Amount exempt from tax varies from Rs. 200 to Rs. 1,300 per month.
Tribal area allowance in (a) Madhya Pradesh (b) Tamil Nadu (c) Uttar Pradesh (d) Karnataka (e) Tripura (f) Assam (g) West Bengal (h) Bihar (i) Orissa	Up to Rs. 200 per month

Compensatory Field Area Allowance. If this exemption is taken, employee cannot claim any exemption in respect of border area allowance (Subject to certain conditions and locations)	Up to Rs. 2,600 per month
Compensatory Modified Area Allowance. If this exemption is taken, employee cannot claim any exemption in respect of border area allowance (Subject to certain conditions and locations)	Up to Rs. 1,000 per month
Counter Insurgency Allowance granted to members of Armed Forces operating in areas away from their permanent locations. If this exemption is taken, employee cannot claim any exemption in respect of border area allowance (Subject to certain conditions and locations)	Up to Rs. 3,900 per month
Underground Allowance to employees working in uncongenial, unnatural climate in underground mines	Up to Rs. 800 per month
High Altitude Allowance granted to armed forces operating in high altitude areas (Subject to certain conditions and locations)	a) Up to Rs. 1,060 per month (for altitude of 9,000 to 15,000 feet)  b) Up to Rs. 1,600 per month (for altitude above 15,000 feet)

**RETIREMENT BENEFITS**

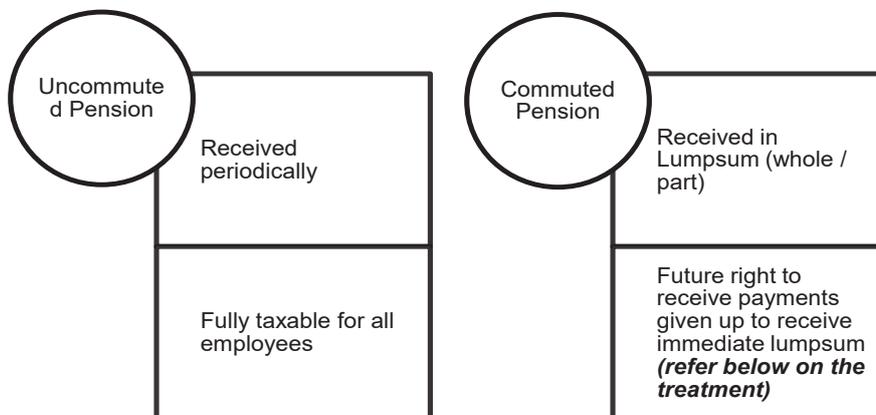
**Annuity / Pension**

Annuity is a yearly payment to an employee post his retirement on account of the funds that were saved by him by way of subscription to the annuity fund vide his salary when he was in employment.

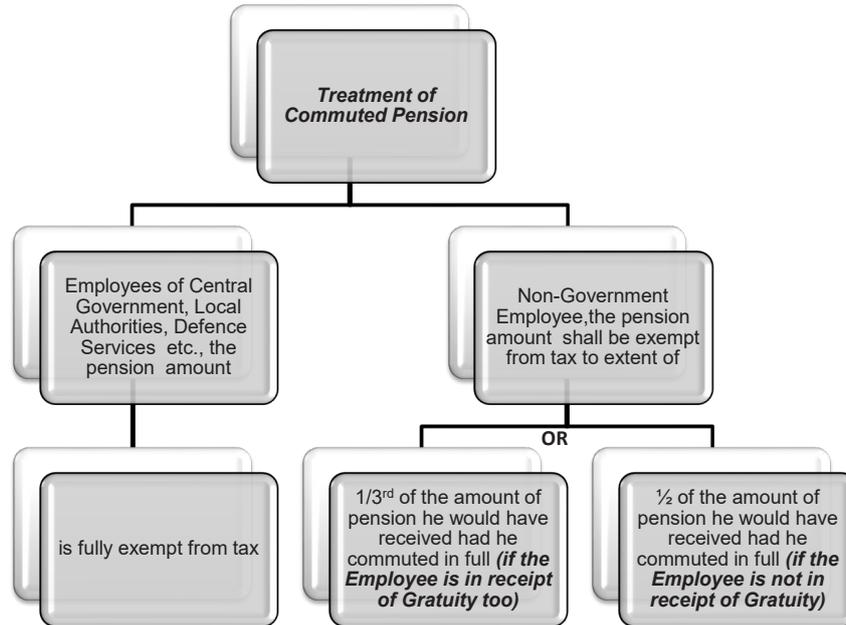
Annuity received from the *present employer is chargeable to tax as Salary and any amount received from the past employer is chargeable to tax as Profits In lieu of Salary.*

Pension however is generally paid by the Government or a Company to the employee for his past service and this too is payable after the retirement.

This pension so received could be commuted / uncommuted, explained as under:



## Treatment of Commuted Pension



## Gratuity

Gratuity is normally paid in lieu of the long-term service of an employee (usually > 5 years), but is a voluntary payment by the employer, as an appreciation of the long-standing services.

The Gratuity so received at the time of retirement or termination of employment or death of employee, is exempt as under:

- a) For the Central / State Government employees and for the members of the Defence Services, any amount received as Gratuity at the time of retirement/death is fully exempt
- b) For all other employees in the private sector:
  - In case the employee is covered under the Payment of Gratuity Act, 1972, any death-cum-retirement Gratuity is exempt to the extent of least of the following:
    - i. INR 20,00,000
    - ii. Gratuity actually received
    - iii. 15 days' Salary based on salary last drawn for each year of service or part thereof in excess of 6 months

*Note: Here Salary would mean (Basic + DA) and number of days in the month to be assumed to be 26.*

- In case the employee is NOT covered under the Payment of Gratuity Act, 1972, any death-cum-retirement Gratuity is exempt to the extent of least of the following:
  - i. INR 20,00,000
  - ii. Gratuity actually received
  - iii. Half months' Salary based on last 10 months' average salary drawn immediately preceding the month of retirement / death, for each completed year of service (fraction of year to be ignored)

**Note :** Here Salary would mean Basic + DA (only to the extent of forming part of the retirement benefits) + Commission as a % of Turnover and number of days in the month to be taken at 30.

**Note :**

- (i) If employee has received gratuity from any of his past employer, then the amount of gratuity exempted earlier shall be reduced from Rs. 20,00,000.
- (ii) If employee has not received gratuity from any of his past employer, then the period of past employment shall also be considered for calculating years of service.

**Leave Encashment**

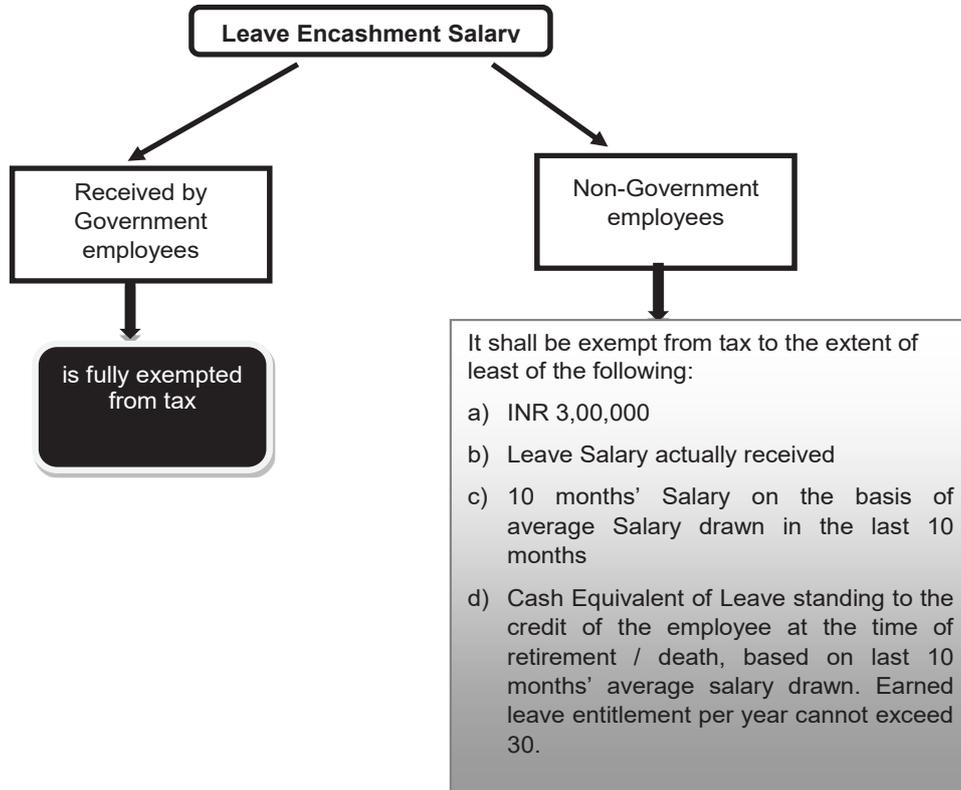
Leave encashment means getting salary equivalent to the number of leaves which were entitled to an employee but not availed (i.e. earned). Leave Encashment taken during employment is fully taxable for all employees. Leave Encashment taken at the time of retirement is exempted as follows :-

Leave Encashment Salary received by employees of the Government, is fully exempt from tax.

For the Non-Government employees, the Leave Encashment Salary so received is exempt from tax to the extent of least of the following:

- a) INR 3,00,000
- b) Leave Salary actually received
- c) 10 month’s Salary on the basis of average Salary drawn in the last 10 months
- d) Cash Equivalent of Leave standing to the credit of the employee at the time of retirement / death, based on last 10 month’s average salary drawn. Earned leave entitlement per year cannot exceed 30.

**Note:** Here Salary would mean Basic + DA (only to the extent of forming part of the retirement benefits) + Commission as a % of Turnover and number of days in the month to be taken at 30.



### Profits in lieu of Salary

Under this the following items are included:

- (i) The amount of any compensation due to or received by an assessee from the employer or former employer at or in connection with the termination of his employment. The termination of employment means retirement, premature termination of employment, termination by death or voluntary resignation. Generally, under the Income- tax Act, the income that is chargeable to tax is only a receipt which is revenue in nature; receipts of a capital nature are not chargeable to tax but this provision constitutes an exception to this rule because compensation received by an employee for termination of his employment would be a capital receipt since it is received in replacement of the sources of income itself. Still it is chargeable to tax because of the specific provision in the Act. However, relief under Section 89(1) would be available to the assessee in cases where he gets money which represents a profit in lieu of salary.
- (ii) The amount of any compensation due to or received by any assessee from his employer in connection with the modification of the terms and conditions relating to employment. For example, where an employer wants to cut down the salary payable to the employee, the lump sum paid to compensate the employee shall be treated as profits in lieu of salary. In the same way, where the remuneration for services is paid at the end of the period of employment or a lump sum remuneration is paid at the beginning of employment for a number of years, such payment shall be treated as profits in lieu of salary.
- (iii) Any amount due to or received, whether in lump sum or otherwise, by any assessee from any person - (A) before his joining any employment with that person; or (B) after cessation of his employment with that person.
- (iv) Any payment other than the following payment due to or received by assessee from an employer or a former employer or from a provident or other fund, **other than** Gratuity [Section 10(10)], Pension [Section 10(10A)], HRA [Section 10(13A)], Provident Fund / Public Provident Fund/ Recognised Provident Fund.
- (v) Any sum received under Keyman Insurance Policy

### PERQUISITES

Perquisite may be defined as any casual emolument or benefit attached to an office or position in addition to salary or wages. It also denotes something that benefits a man by going into his own pocket. Perquisites may be provided in cash or in kind. However, perquisites are taxable under the head "Salaries" only if they are

- a. allowed by an employer to his employee;
- b. allowed during the continuance of employment;
- c. directly dependent upon service;
- d. resulting in the nature of personal advantage to the employee; and
- e. derived by virtue of employer's authority.

It is not necessary that a recurring and regular receipt alone is a perquisite. Even a casual and non-recurring receipt can be perquisite if the aforesaid conditions are satisfied.

Any facility / benefit that is granted by the employer, the use of which is enjoyed by the employee or any member of the employee's household, is construed as a perquisite under the Income Tax Act, and hence attracts tax.

**Taxable Perquisites**

- Rent Free Residential Accommodation
- Interest Free / Concessional Loan
- Use of movable assets by employee / any member of his household
- Transfer of movable assets
- Provision of gas / electricity / water
- Provision of free / concessional educational facilities
- Credit Card Expenses
- Club expenditure
- Health Club, Sports, Similar facilities
- Sweat Equity

**Tax-free Perquisites (in all cases)**

- Medical Facilities
- Refreshment
- Subsidized lunch or dinner
- Recreational facilities
- Telephone facility
- Transport
- Personal accident insurance
- Refresher Course
- Free rations
- Computer/laptops
- Rent free houses / conveyance
- Employers' Contribution
- Annual Premium

**(A) Taxable Perquisites:** We need to understand the valuation of perquisites. The table appended below, summarises the taxable value of various perquisites in the hands of the employee assessee.

Sl. No.	Perquisite	Category of Employee	Value of perquisites
1	Rent Free Residential Accommodation	Government Employee	<p>Licence Fee determined as per the Government Rules, as reduced by rent actually paid by the employee for unfurnished accommodation.</p> <p><i>For a furnished accommodation, 10% p.a. of the furniture cost is added to the value obtained above for unfurnished.</i></p> <p>In case the <i>furniture is hired</i>, the actual hire charges would be added to the value obtained above for unfurnished.</p>

		Non-Government Employee	<p><b>In case of <i>Unfurnished Accommodation</i>;</b></p> <p>a) If the accommodation is owned by the employer, the value would be based on the population, i.e.,</p> <ul style="list-style-type: none"> <li>i) if in cities having a population of &gt; 25 Lacs (2001 Census) - 15% of Salary;</li> <li>ii) if the population is between 10 Lacs up to 25 Lacs – 10% of Salary;</li> <li>iii) else 7.5% of Salary</li> </ul> <p>b) If the accommodation is taken on lease by the employer, the actual value of lease rentals paid by the employer subject to a maximum of 15% of Salary is considered as Value.</p> <p><b>For a <i>furnished accommodation</i>,</b> 10% p.a. of the furniture cost is added to the value obtained above for unfurnished.</p> <p><b>In case the <i>furniture is hired</i>,</b> the actual hire charges would be added to the value obtained above for unfurnished.</p> <p>In all cases, any amount recovered from the employee should be reduced to arrive at the taxable value of the perquisite</p> <p>Where the accommodation is provided by the employer in a hotel (except where the employee is provided such accommodation for a period not exceeding in aggregate 15 days on the transfer from one place to another); The perquisites value would be 24% of salary paid or payable for the previous year or the actual charges paid or payable to such hotel, which is lower, for the period during which such accommodation is provided as reduced by the rent, if any, actually paid or payable by the employees.</p>
2	Interest Free / Concessional Loan	All employees	Where the employer grants a loan to an employee, exceeding INR 20000, the interest at the rate charged by SBI, as on the first date of the relevant PY, at maximum outstanding monthly balance as reduced by the Interest actually charged to the employee; would be the taxable value of the perquisite. Known for medical purpose is exempted.

3	Use of movable assets by employee / any member of his household	All employees	10% p.a. of the actual cost of the asset, if it is owned by the employer OR the actual hire charges incurred by the employer if the asset is hired as reduced by the amount, if any, paid or recovered from the employee for such use would be the taxable value of the perquisite.  <b>Note:</b> Use of laptops and computers wouldn't attract taxability as perquisites.
4	Transfer of movable assets	All employees	If Computers / electronic items are transferred, 50% Depreciation p.a. (WDV) for every completed year of usage; if Motor cars are transferred, 20% Depreciation p.a. (WDV) for every completed year of usage; and for all other assets transferred, 10% Depreciation p.a. (SLM) for every completed year of usage would be treated as the taxable value of perquisite net of any amount so recovered from the employee.
5	Provision of gas / electricity / water	All employees	The value of benefit to the employee resulting from the supply of gas, electric energy or water for his household consumption shall be determined as the sum equal to the amount paid on that account by the employer to the agency supplying the gas, electric energy or water. Where such supply is made from the sources owned by the employer, without purchasing them from any other outside agency, the value of perquisites would be the manufacturing cost per unit incurred by the employer. Where the employee is paying any amount in respect of such services, the amount so paid shall be deducted from the value so arrived at.
6	Provision of free / concessional educational facilities	All employees	Amount actually expended by the employer net of the amount so recovered. However, if the educational institution is owned by the employer, and free educational facilities are provided to the employee's children, there wouldn't be any perquisite as long as the value of benefit in a month is < INR 1000. Any amount recovered from the employee would be reduced.
7	Credit Card Expenses	All employees	Membership fees / Annual fees incurred by the employer, on a card provided to the employee, would be the taxable value of perquisite net of the amount, if any, recovered from him.
8	Club expenditure	All employees	Cost incurred by the employer at actual, net of recovery from the employee would be the taxable value of perquisite. However, in case the employee enjoys Corporate Membership in a club, the value of benefit wouldn't include the initial membership paid by the Employer to acquire the corporate membership.

9	Health Club, Sports, Similar facilities	All employees	No perquisite if provided uniformly by the employer to all employees.
10	Sweat Equity	All employees	<p><b><i>In case where, on the date of exercising the option, the share of the company is listed on a recognised stock exchange</i></b>, the fair market value (FMV) would be the average of the opening and closing price of the share on that date on the said stock exchange. If the shares of the company are listed on more than one stock exchange, the FMV would be the average of the opening and closing prices of the share on the recognised stock exchange which records the highest volume of trading in the share. In case on the date of the exercising of the option, if there was no trading in the share, the FMV would be the closing price on the recognised stock exchange, on a date closest to exercising the option, immediately before that date, and if the shares of the company are listed on more than one stock exchange, the FMV would be the closing price of the share on the recognised stock exchange which records the highest volume of trading in the share.</p> <p>In case the shares of the company are not listed on any recognised stock exchange, the FMV would be that as determined by the Merchant Banker on the specified date, i.e., the date of exercising the option or any date earlier not exceeding 180 days prior to the date of exercise of the option.</p>

### Motor Cars – Perquisites Valuation

The taxable value of use of motor cars are dealt with separately, as it is situational, as under:

#### **Where the Expenses are met by the employer**

- ✓ If the Car is owned / hired by the **employer**; expenses met by the employer & is used by the employee **wholly for Official purposes**, there is no perquisite.
- ✓ If the Car is owned / hired by the **employer**; expenses met by the employer & is used by the employee **wholly for Personal purposes**, the running and maintenance charges / wear & tear / hire charges / driver's salary would be treated as the taxable value of the perquisite net of the amount so recovered from the employee. (Including Depreciation @ 10% p.a. on SLM basis)
- ✓ If the Car is owned / hired by the **employer**; expenses met by the employer & is used by the employee **partly for Official and partly for Personal purposes**, the taxable value of the perquisite would be based on the cc (cubic capacity) of the engine, as under:
  - Up to 1.6 litres, the taxable value of the perquisite would be INR 1800 pm
  - > 1.6 litres, the taxable value of the perquisite would be INR 2400 pm
  - If chauffer is also provided, INR 900 pm is to be added to either of the above, depending on the engine capacity. (In this case recovery is not deductible)

- ✓ If the Car is owned / hired by the **employee**; expenses met by the employer & is used by the employee **wholly for Official purposes**, there is no perquisite.
- ✓ If the Car is owned / hired by the **employee**; expenses met by the employer & is used by the employee **wholly for Personal purposes**, the actual expenditure so incurred would be treated as the taxable value of the perquisite.
- ✓ If the Car is owned / hired by the **employee**; expenses met by the employer & is used by the employee **partly for Official and partly for Personal purposes**, the taxable value of the perquisite would be the actual expenditure incurred by the employer as reduced by the taxable value of the perquisite determined above basis the engine capacity.

**Where the Expenses are met by the employee**

- ✓ If the Car is owned / hired by the **employer**; expenses met by the employee & is used by the employee **wholly for Official purposes**, there is no perquisite
- ✓ If the Car is owned / hired by the **employer**; expenses met by the employee & is used by the employee **wholly for Personal purposes**, the wear & tear / hire charges / driver’s salary would be treated as the taxable value of the perquisite. (Including Depreciation @ 10% p.a. on SLM basis)
- ✓ If the Car is owned / hired by the **employer**; expenses met by the employee & is used by the employee **partly for Official and partly for Personal purposes**, the taxable value of the perquisite would be based on the cc of the engine, as under:
  - Up to 1.6 litres, the taxable value of the perquisite would be INR 600 pm
  - > 1.6 litres, the taxable value of the perquisite would be INR 900 pm
  - If chauffer is also provided, INR 900 pm is to be added to either of the above, depending on the engine capacity. (In this case recovery is not deductible)

**Illustration on Perquisites**

ABC Ltd. provided the following perquisites to its employee Srinivasan, for the FY 2019-20.

- 1) Leased accommodation provided to the employee. Hire Charges INR 50000 pm; recovered from employee INR 20000 pm
- 2) Accommodation was furnished and the actual hire charges paid by the Employer was INR 4050/- pm
- 3) He was also provided a Hyundai Santro with Chauffer and a Gift Voucher worth INR 9000/-

Salary for the purposes of valuation of perquisites is INR 25,00,000/-.

Compute the taxable value of the perquisites.

**Solution :**

<b>Accomodation on lease</b>					
Salary for the purposes of Valuation of Perquisites	25,00,000				
Actual Lease Charges	6,00,000				
15% of the above (Cap)	3,75,000				
Hence, Gross Taxable Value of the Perquisite		3,75,000			
Less: Amount recovered from the employee		<u>2,40,000</u>			
Taxable value of unfurnished leased accomodation			1,35,000		
Add: Actual hire charges of furniture hired			<u>48,600</u>		

<i>Taxable value of Furnished Accomodation</i>				<u>1,83,600</u>	
<b><i>Car used partly for Official &amp; partly for Personal</i></b>					
Engine Capacity is within 1.6 l (Santro)					
Taxable Value of Perquisite @ 1800 pm			21,600		
Chauffer @ 900 pm			<u>10,800</u>		
Taxable value of Motor Car provided				<u>32,400</u>	
Gift Voucher				<u>9,000</u>	
<b>Total Value of Perquisites</b>					<b>2,25,000</b>

**Note:**

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

**Tax-free perquisites (in all cases)**

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

**1. Medical Facilities**

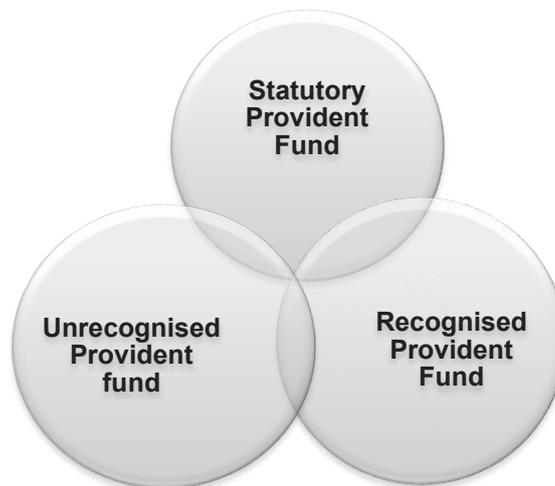
- a) The value of any Medical facility provided to an employee or his family member in any hospitals, clinics, etc. maintained by the employer.
- b) Reimbursement of expenditure actually incurred by the employee on medical treatment for self or for his family members in any hospitals, dispensaries etc. maintained by the Government or local authority or in a hospital approved under the Central Health Scheme or any similar scheme of the state Government or in a hospital, approved by the chief commissioner having regard to the prescribed guidelines for the purposes of medical treatment of the prescribed diseases or ailments.
- c) Group medical insurance obtained by the employer for his employees (including family members of the employees) or all medical insurance payments made directly or reimbursement of insurance premium to such employees who take such insurance.
- d) Any expenditure incurred or paid by the employer on the medical treatment of the employee or any family member of the employee outside India, the travel and stay abroad of such employee or any family member of such employee or any travel or stay abroad of one attendant who accompanies the patient in connection with such treatment will not be included in perquisites of the employee. However, the travel expenditure shall be excluded from the perquisites only when the employee's gross total income as computed before including the said expenditure does not exceed two lakh rupees and further to such conditions and limits as the Board may prescribe having regard to guidelines, if any, issued by the Reserve Bank of India.

**2. Refreshment :** The value of refreshment provided by the employer during office hours and in office premises is fully exempt

3. **Subsidized lunch or dinner** provided by employer is exempt
4. **Recreational facilities** : The value of recreational facilities provided is exempt. However, the facility should not be restricted to a selected few.
5. **Telephone facility** provided at the residence of the employee is exempt to the extent of the amount of telephone bills paid by the employer when it is used for official and personal purposes of the employee.
6. **Transport** provided by the employer to the employees as a group (and not to any individual or a few employees alone) from their place of residence to the place of work and back in the case of an employer engaged in the business of carriage of goods or passengers, to his employees either free of charge or at a concessional rate. Also from the assessment year 1990-91, conveyance facility provided for the journey between office and residence and back at free of charge or at concessional rate.
7. **Personal accident insurance**, i.e. payment of annual premium by employer on personal accident policy effected by him to his employee
8. **Refresher Course**: Where the employee attends any refresher course in management and the fees are paid by the employer, the amount spent by employer for the purpose.
9. **Free rations**: The value of free rations given to the armed forces personnel.
10. **Computer/laptops** provided only for use, ownership is retained by the employer
11. **Rent free houses / conveyance** to High Court & Supreme Court Judges
12. **Employers’ Contribution** to Group Insurance Schemes, to recognised Provident Funds
13. **Annual Premium** by employer on policy taken on life of employee

**PROVIDENT FUNDS - TREATMENT OF CONTRIBUTIONS TO AND MONEY RECEIVED FROM THE PROVIDENT FUND**

For purposes of Income-tax, provident funds are grouped under three heads:



**(A) Statutory provident fund**

**Meaning:** All provident funds which are set up under the Provident Funds Act, 1925 are called Statutory Provident Funds. Provident funds of institutions such as Universities, Colleges or other Educational Institutions, Reserve Bank of India, State Bank of India, the Central Government and State Government would constitute Statutory Provident Funds.

**Treatment:** In case of Statutory Provident Fund, the entire amount of employer's contribution without any limit or restriction whatsoever and the interest thereon received by the employee shall not be includible in the total income of the employee both at the time when the contribution is made and at the time when the money is received by or on behalf of the employee on his retirement, death or otherwise. This exemption is specifically conferred by Sub-section (11) of Section 10 of the Income-tax Act. The employee can contribute to this fund out of his salary as much as he likes.

**(B) Recognised provident fund**

**Meaning:** All Provident Funds recognised by the Commissioner of Income-tax under Rule 3 of Part 'A' of the Fourth Schedule to the Income-tax Act, 1961 and also Provident Funds established under a scheme framed under the Employees Provident Funds Act, 1952 are known under the Income-tax Act as Recognised Provident Funds. For the purposes of being treated as Recognised Provident Fund, the Fund in question must be recognised by the Commissioner of Income-tax at the time of its setting up and must continue to be so recognised even subsequently. The moment the recognition is withdrawn by the Commissioner, the Fund ceases to be a Recognised Provident Fund. The Provident Funds of various Public Sector Undertakings, Semi-Government bodies and other institutions and organisations including companies which are recognised by the Commissioner for income-tax purposes, would be treated as Recognised Provident Funds.

**Treatment:** In the case of a Recognised Provident Fund, the employer's contribution to the Provident Fund is not treated as the employee's income so long as the contribution by the employer does not exceed 12% of the salary of the employee. But if the contribution of the employer exceeds 12% of the employee's salary, the excess of the contribution over 12% of the salary of the employee is to be treated as part of the taxable income from salaries in the hands of the employee in respect of the financial year in which the contributions were made by the employer. The fact that the employee concerned does not receive the money in hand nor is he entitled to get the money immediately does not in any way affect the taxability of the excess over 12% of the employee's salary. The employee's own contribution qualifies for deduction under Section 80C of the Income-tax Act. [Salary for this purpose, includes basic salary; dearness allowance/pay (if the terms of employment so provide) and commission (if based on a fixed percentage of turnover achieved by the employee)]. As regards interest on the contributions to the Provident Fund, only an amount exceeding a sum calculated at 12% per annum on the balance standing to the credit of the employee would be treated as part of the taxable income of the employee. In other words, so long as the amount of interest does not exceed this limit, the interest does not become chargeable to tax in the hands of the employee.

**(C) Unrecognised provident Fund**

**Meaning:** The Provident Fund which is neither Statutory nor recognised by the Commissioner of Income-tax nor Public Provident Fund, would be an Unrecognised Provident Fund for income-tax purposes.

**Treatment:** In the case of an Unrecognised Provident Fund, the employee's own contribution to the Fund would not be allowed as a deduction. The employer's contribution and the interest thereon would, however, be exempt from tax as and when the contributions are being made. But when the money in lump sum is received back by the employee, that part of the amount attributable to the employer's contribution would be taxable as income from salaries and the interest on the employer's contribution would also be taxable as salary income in the hands of the employee. The employee's own contributions when received back would not be taxable because they do not contain an element of income. However, the interest thereon would be chargeable to tax as income from other sources and not as income from salaries.

**Relief when salary is paid in arrears or advance (section 89)**

Tax is calculated on total income earned or received during the year. If any portion received ‘salary in arrears or in advance’, or have received a family pension in arrears, assessee is allowed some tax relief under section 89(1) of the Income Tax Act, 1961.

Relief under section 89(1) for arrears of salary are available in the following cases:

- Salary received in advance or as arrears
- Gratuity
- Compensation on Termination of employment
- Commutation of Pension

**Calculating Relief under Section 89(1)**

Steps to be followed to calculate relief under section 89 (1)

**Step 1:** Calculate the tax payable on his total income including arrears of the relevant previous year in which the same is received. (Ex: X)

**Step 2:** Calculate the tax payable on his total income excluding arrears. (Ex: Y)

**Step 3:** Subtract the value obtained in step 1 from the value obtained in step 2. (e., A-B) and keep the result value as Z.

**Step 4:** Calculate the tax payable on the total income (including arrears) of the year to which the arrears are related. (Ex: “A”)

**Step 5:** Calculate tax payable on the total income (excluding arrears) of the year to which the arrears are related. (Ex: “B”)

**Step 6:** Subtract the value obtained in step 5 from the value obtained in step 4 (i.e., A – B). (Ex: “C”).

Excess of tax computed at step 3 over tax computed at step 7 is the amount of relief allowable under section 89. If tax computed at step 3 is less than tax computed at step 7 the taxpayer will not be eligible for any relief.

<b>Tax Liability in the PY in which adv / arrears are received</b>	
a) Incl. adv / arrears	A
b) Excl. adv / arrears	B
Differential	A-B
<b>Tax Liability of the PY to which such addl salary relates</b>	
a) Incl. adv / arrears	C
b) Excl. adv / arrears	D
Differential	C-D
<b>Relief u/s 89</b>	<b>(A-B)-(C-D)</b>

The Finance (No. 2) Act, 2019 has amended sections 140A (self assessment), 143 (regular assessment), section 234A, 234B, 234C (interests on late payment of tax) so as to provide that computation of tax liability shall be made after allowing relief under section 89.

## DEDUCTIONS FROM SALARY

### **Standard Deduction**

Standard deduction of Rs. 50,000 (fifty thousand) or the amount of the salary, whichever is less w.e.f. **Finance Act 2019** w.e.f. Assessment year 2020-21 [clause (ia) to section 16].

### **Entertainment Allowance**

- ✓ Fully taxable
- ✓ First to be included in salary and then deduction to be made.
- ✓ In case of Government Employees, the deduction is available, which would be lower of:
  - 1/5th of Basic Salary Or
  - INR 5000/- Or
  - Actual Entertainment Allowance received

### **Profession Tax**

- ✓ Allowed as a deduction when paid by the employee (recovered from salary) during the previous year

## COMPUTATION OF SALARY

Particulars	Rs.
Income From Salary	
Salary	xxxxx
Allowances received (taxable allowances)	xxxxx
Taxable value of perquisite	xxxxx
	=====
Gross Salary	xxxxx
Less: Deduction under section 16	
Professional Tax	xxxxx
Entertainment allowance	Xxxxx
	=====
Income From Salary (1)	

### **Illustration 1:**

Niteen is an employee of XYZ Ltd. He was appointed on 1st Mar 2019 at a scale of 50000 – 5000 – 70000. He is paid DA (which form part of retirement benefits) @ 15% of Basic Pay and Bonus equivalent to 2 month's salary at end of FY. He contributes 18% of his Basic + DA to a recognised provident fund, and the contribution is matched by the employer.

He is provided rent free accommodation, hired by the employer, @ 25000 pm. He is also provided the following benefits / amenities:

- a) Medical Treatment of his dependant spouse INR 40000
- b) Monthly salary to housekeeper INR 4000
- c) Telephone Allowance INR 1200 pm

- d) Gift Voucher of INR 4500 on account of his marriage anniversary
- e) Medical Insurance Premium for Niteen, paid by his employer INR 15000
- f) Motor Car owned and driven by Niteen, and engine capacity within 1.6 L; used partly for official and partly for personal purposes. Running & maintenance expenses borne by the employer INR 36,600/-.
- g) Lunch during office hours valued at INR 2200/-.

He was also allotted 2000 sweat equity shares in Sep 2019. The shares were allotted @ INR 227 per share against the FMV of INR 377 per share as on the date of exercise of the Option.

Compute the Salary Chargeable to tax.

### Solution

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

### Note:

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

If the Car is owned / hired by the employee; expenses met by the employer & is used by the employee partly for Official and partly for Personal purposes, the taxable value of the perquisite would be the actual expenditure incurred by the employer as reduced by the taxable

value of the perquisite determined basis the engine capacity, i.e., INR 36600 – INR (1800\*12)  
= INR 15000

**Illustration 2 :**

Mr. Ram is employed at Bombay. His basic Salary is Rs. 5,000 per month. He receives Rs. 5,000 p.a. as house rent allowance. Rent paid by him is Rs. 12,000 p.a. Find out the amount of taxable house rent allowance.

**Solution:**

As per Rule 2A, the least of the following is exempt from tax:

- (i) the actual house rent allowance;
- (ii) excess of rent paid over 10% of salary;
- (iii) where the accommodation is situated at Bombay, Delhi, Calcutta or Madras, one-half of the amount of salary due to the assessee for the relevant period;
- (iv) Where the accommodation is situate at any other place, two-fifth of the salary due to the assessee for the relevant period.

Accordingly, Mr. Ram would be entitled to the least of :

- (i) Rs. 5,000 or
- (ii) Rs. 6,000 being excess of rent over 1/10th of salary; or
- (iii) Rs. 30,000 (being one-half of the salary of the assessee).

Rs. 5,000, being the least, would not be included in the total income of Mr. Ram. So the entire amount of HRA would be exempt from tax.

Salary for this purpose includes basic salary as well as dearness allowance if the terms of employment so provide. It also includes commission based on a fixed percentage of turnover achieved by an employee as per terms of contract of employment but excludes all other allowances and perquisites and these are determined on due basis for the period during which rental accommodation is occupied by the employee in the previous year.

**Illustration 3 :**

Mr. Shyam, employed at Mumbai, receives the following from his employer during the previous year:

Particulars	Rs.
Basic Salary	60,000
Bonus	1,800
Entertainment allowance (taxable)	6,000
Electricity expenses	2,000
Professional tax paid by the employer	2,000
<i>Rent free house (owned by Employer):</i>	
Fair rent	48,000
Salary of gardener	2,400
Garden Maintenance	1,200
Salary of watchman	1,800

Determine the value of taxable perquisites in respect of rent free house assuming (a) Mr. Shyam is a Government

Officer and the fair rent as arrived at by the Government is Rs. 6,000 p.a (b) Mr. Shyam is a semi-Government employee, and (c) Mr. Shyam is employed by a private company.

**Solution:**

- (a) If Mr. Shyam is a Government Officer: As per Rule 3(1) of Income-tax Rules, Rs. 6,000 p.a being the rent of the house as per Government rules, will be the taxable value of the perquisite.
- (b) If Mr. Shyam is a semi-Government employee : As per Rule 3(1) of the Income-tax Rules, the value of the perquisite in respect of rent free accommodation is taken at 15% of salary of the employee (as the house is owned by the Employer and provided in Mumbai).

Salary = Rs. 67,800 ('Rs. 60,000 + 1,800 + 6,000)

15% of salary = Rs. 10,170 and

Therefore, Rs. 10,170 is taxable value of the perquisite.

Further, the value of Electricity expenses and Professional Tax paid by the employer, being perquisites, are not included in the salary for valuation of Rent Free House Accommodation.

- (c) If Mr. Shyam is employed in Private Company: The value of perquisite in this case shall also be Rs. 10,170. Under the new rules there is no difference between the semi-Govt. and other employees.

**Illustration 4 :**

Mr. Ramamoorthy, an employee of M/s. Gopalkrishnan & Co. of Chennai receives during the previous year ended March 31, 2020 the following payments:

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

Compute his taxable income for the Assessment Year 2020-21.

**Solution:**

Computation of taxable income of Mr. Ramamoorthy for the Assessment Year 2020-21

Basic Pay	40,000
Dearness allowance	3,000
Leave salary	5,400
Professional tax paid by employer	1,000

Perquisite for House :	
15% of salary (Rs. 40,000 + 3,000 + 5,400) 7,260	
Add: Furniture rent 1,000	
Less: Rent recovered (-) 3,000	5,260
	54,660
Less: Standard Deduction under section 16(ia)	(50,000)
Less: Professional tax u/s 16	1,000
Gross Total Income	3,660
Less: Deduction under Section 80C	(3,660)
Total income	NIL
Total tax payable	NIL

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

**Illustration 5 :**

Raman, an employee of the Gas Supply Ltd., Agra, receives the following emoluments during the previous year 2019-20.

Particulars	(Rs.)
Basic pay	10,000
Project allowance	1,800
Arrears of project allowance of May, 1984	150
Professional tax paid by the employer	200
Rent free furnished house	
- Fair rent of the house	2,000
- Rent of furniture	500
Free gas supply	400
Service of sweeper	600
Services of gardener	1,000
Service of cook	800
Free lunch	2,400

Free use of chauffeur driven Fiat car which is used partly for official and partly for private purposes.

He is a member of recognised provident fund to which he contributes Rs.1,500. His employer also contributes an equal amount. He deposits Rs. 600 per month in 10 year account under the Post Office Savings Bank (CTD) Rules. Determine his taxable income and tax payable thereon for the assessment year 2020-21. (a) If Raman is a director in the employer company and the rent-free house is owned by it, (b) If Raman is neither a director nor a shareholder in the employer company and the rent-free house is not owned by it.

**Solution:**

His taxable income will be computed as under :

	<i>If Raman is a director and rent-free house is owned by the company not owned by the Company</i> ‘A’	<i>If Raman is neither a director nor a shareholder and rent-free house is</i> ‘B’
(1)	(2)	(3)
	Rs.	Rs.
Basic Pay	10,000	10,000
Project allowance	1,800	1,800
Arrears of project allowance of May, 1984	150	150
Professional tax paid by the employer	200	200
Rent free furnished house :		
– 15% of Salary	1,770	1,770
– Rent of furniture	500	500
Free gas supply	400	Nil
Service of sweeper	600	Nil
Service of gardener	1,000	Nil
Service of cook	800	Nil
Free lunch	Nil	Nil
Excess of employer’s contribution towards provident fund over 12% of salary (1,500 - 12% of 10,000)	300	300
Gross salary	18,110	15,310
Deduction : Standard Deduction (Maximum Rs. 50,000)	18,110	15,310
Net Income from Salary	Nil	Nil
Tax on total income	Nil	Nil

**Notes:**

- (1) It is assumed that the arrears of project allowance are taxable on receipt basis.
- (2) Perquisite in respect of Rent Free house is taxable in the hands of all the assesseees. In this case fair market value has no relevancy (w.e.f. AY 2002-03) and assumed that the house is owned by the employer. Since the house is provided in Agra, population is assumed as exceeding 25 lakhs. Salary for valuation of perquisite is (10,000 + 1,800).
- (3) The free sweeper, gardener, cook, lunch, car etc. are not taxable in the second case, because Raman does not fall in the category of specified employee under Section 17(2)(iii) of the Act i.e., he is neither a director nor his salary is Rs. 50,000 p.a. or more.
- (4) Free lunch provided is not taxable to the extent of Rs. 50 per day.
- (5) Since Raman is employed in a Gas supply company, the value of gas supplied is taxable as cost to the employer. And it is assumed that the cost of supply is same as Rs. 400 as given.

**Illustration 6 :**

For the financial year 2019-20, 'A', a Central Government Officer receives salary of Rs. 77,000 (including dearness allowance of Rs. 42,000) and entertainment allowance of Rs.18,000. His contribution to provident fund during this period is Rs. 7,200. In addition, he has purchased National Savings Certificates (VIII Issue) for Rs. 6,000. He has been provided with accommodation by the Government for which the rent determined is Rs. 375 per month and this is recovered from A's salary. Compute A's tax liability for the assessment year 2020-21 assuming that he has no other income.

**Solution:**

Name of assessee : Mr. A  
Assessment Year : 2020-21  
Status: Resident/Individual  
Statement of assessable income

Salary from Central Government		77,000
Entertainment allowance	18,000	
Less: Entertainment Allowance under Section 16(ii) Rs. 5,000 or [1/5th of salary exclusive of any allowance, benefit or perquisite]	(5,000)	(13,000)
Less : Standard Deduction under section 16(ia)		(50,000)
<b>GROSS TOTAL INCOME</b>		<b>14,000</b>
Less : Deduction under Section 80C (7,200 + 6,000)		(13,200)
Total Income		800
Tax liability		Nil
Net tax payable		Nil

**CASE LAW**

**1. Can notional interest on security deposit given to the landlord in respect of residential premises taken on rent by the employer and provided to the employee, be included in the perquisite value of rent-free accommodation given to the employee?**

**CIT v. Shankar Krishnan (2012) (Bom.)**

On appeal by the Revenue, the Bombay High Court held that the Assessing Officer is not right in adding the notional interest on the security deposit given by the employer to the landlord in valuing the perquisite of rent-free accommodation, since the perquisite value has to be computed as per Rule 3 and Rule 3 does not require addition of such notional interest. Thus, the perquisite value of the residential accommodation provided by the employer would be the actual amount of lease rental paid or payable by the employer, since the same was lower than 10% (now 15%) of salary.

**2. Can the limit of INR 1,000 per month per child be allowed as standard deduction, while computing the perquisite value of free or concessional education facility provided to the employee by the employer?**

**CIT (TDS) v. Director, Delhi Public School (2011) (Punj. & Har.)**

The Punjab and Haryana High Court held that on a plain reading of Rule 3(5), it flows that, in case the value

of perquisite for free/concessional educational facility arising to an employee exceeds Rs. 1,000 per month per child, the whole perquisite shall be taxable in the hands of the employee and no standard deduction of INR 1,000 per month per child can be provided from the same. It is only in case the perquisite value is less than INR 1,000 per month per child, the perquisite value shall be nil. Therefore, INR 1,000 per month per child is not a standard deduction to be provided while calculating such a perquisite.

### LESSON ROUND UP

- Basis of Charge: As per section 15, salary is taxable on due or receipt basis whichever is earlier. Under Section 15 the income chargeable to income tax under the head salaries would include any salary due to an employee from an employer or a former employer during the previous year irrespective of the fact whether it is paid or not.
- Different forms of salary:
  - (A) Basic Salary: Basic salary is taxable in the hands of an employee.
  - (B) Allowance: An allowance is defined as a fixed amount of money given periodically in addition to the salary for the purpose of meeting some specific requirements connected with the service rendered by the employee or by way of compensation for some unusual conditions of employment. It is taxable on due/accrued basis whether it is paid in addition to the salary or in lieu thereon.
  - (C) Perquisites: The term “perquisites” includes all benefits and amenities provided by the employer to the employee in addition to salary and wages either in cash or in kind which are convertible into money. These benefits or amenities may be provided either voluntarily or under service contract. For income-tax purposes, the perquisites are of three types:
    - (i) Tax-free perquisites
    - (ii) Taxable perquisites
    - (iii) Perquisites taxable under specified cases.
- Valuation of perquisites: The basic principles governing valuation of perquisites are as follows:
  - The valuation is done on the basis of their value to the employee and not the employer’s cost for providing the same - *Wilkins v. Rogerson* (1963) 49 ITR 395 (CA).
  - The value of perquisite is included in the salary income only if the perquisite is actually provided to the employee.
  - Perquisite which is not actually enjoyed by the employee (though the terms of employment provide for the same) cannot be valued and taxed in the employee’s hands. Therefore, where the employee waives his right of perquisite, he cannot be taxed thereon.
- Allowable deductions under the head Salaries: The following amounts shall be deducted in order to arrive at the chargeable income under the head “Salaries”.
  - (A) Standard deduction: Rs. 50,000 or salary whichever is less.
  - (B) Entertainment allowance
  - (C) Tax on employment or Professional Tax
- Meaning of Salary under various circumstances:

Circumstance	Definition
Gratuity (Non-Government Employees covered by Payment of Gratuity Act, 1972)	Basic + DA
Gratuity (Non-Government Employees NOT covered by Payment of Gratuity Act, 1972)	Basic + DA (if terms of employment so provide) + Commission as a % of Turnover
Leave Salary	Basic + DA (if terms of employment so provide) + Commission as a % of Turnover
HRA	Basic + DA (if terms of employment so provide) + Commission as a % of Turnover
Rent Free Accommodation	Basic + DA (forming part of retirement benefits) + Bonus + all Taxable Allowances

### SELF-TEST QUESTIONS

#### Multiple Choice Questions (MCQs)

- The definition of Salary for the purposes of computing income under the head "Salaries" is Basic + Dearness Allowance + Commission as a % of Turnover?
  - Always
  - In some cases
  - The definition is irrelevant
  - None of the above

Answer: (b)

- Conveyance Allowance is exempt to the extent of \_\_\_\_\_ per month?
  - INR 800
  - INR 1600
  - Nil
  - None of the above

Answer: (c)

- Uncommuted pension is always taxable irrespective of whether the assessee is a Private Sector or a Public-Sector employee?
  - Yes
  - Yes, like commuted pension
  - It depends on whether the person is in receipt of Gratuity
  - FALSE

Answer: (a)

- For the purposes of taxability of Commuted Pension, this is independent of whether you have received Gratuity or not as these are anyways taxed separately?
  - Incorrect, it depends on whether you are a Government employee or not

- b) Incorrect, it depends on whether you are in receipt of Gratuity
- c) Both a & b
- d) None of the above

Answer: (c)

5. No. of days in a month for purposes of computing taxable Gratuity in case the employee is covered under the Payment of Gratuity Act, 1972, are?
- a) 26
  - b) 25
  - c) 30
  - d) 31

Answer: (a)

### SUGGESTED READING

**1. Direct Taxes Law and Practice**

Author : Dr. Vinod K. Singhanian & Dr. Kapil Singhanian

Publisher : Taxmann

Year : 2019

Edition : 2019

**2. Direct Taxes Ready Reckoner with Tax Planning**

Author : Dr. Girish Ahuja & Dr. Ravi Gupta

Publisher : Wolters Kluwer

Year : 2019

Edition : 20th Edition



# Lesson 4

## Part II – Income under the head House Property

### LESSON OUTLINE

- Basis of Charge
- Determination of Annual Value
- Deductions from Net Annual Value [Section 24]
- Inadmissible deductions [Section 25]
- Treatment of unrealized rent/Arrear of rent [Section 25A]
- Properties owned by Co-owners [Section 26]
- Deemed Ownership [Section 27]
- House Property Income Exempt form Tax
- Case Law
- LESSON ROUND UP
- SELF TEST QUESTION

### LEARNING OBJECTIVES

The provisions for computation of Income from house property are covered under sections 22 to 27. This chapter deals with the provisions for computation of Income from house property. Section 22 is the charging section that identifies the basis of charge wherein the annual value is prescribed as the basis for computation of Income from House Property. The process of computation of “Income from House Property” starts with the determination of annual value of the property. The concept of annual value and the method of determination are laid down in section 23. The admissible deductions available from house property are mentioned in section 24.

At the end of this lesson, you will learn

- the conditions to be satisfied for income to be chargeable under the head house property
- how to determine the annual value of different type of house properties,
- admissible deductions and inadmissible deductions from annual value,
- tax treatment of unrealized rent,
- who are deemed owners,
- what is meant by co-ownership and what is its tax treatment etc.

## BASIS OF CHARGE [SECTION 22]

The **annual value** of property consisting of any **buildings or lands appurtenant thereto** of which the assessee is the **owner**, other than such portions of such property as he may occupy **for the purposes of any business or profession carried on by him**, the profits of which are chargeable to income-tax, shall be chargeable to income-tax under the head Income from House Property”

In other words a house property is taxable under this head if following conditions are satisfied:-

1. There should be a property consisting of any buildings or lands appurtenant thereto;
2. Assessee should be the owner of such property (including deemed owner as given u/s 27)
3. Such property should not be occupied by the assessee for the purposes of any business or profession carried on by him, the profit of which are chargeable to income tax.

Income from house property is one of the important heads of income under the Income Tax Act. The tax payers have been, in particular, keen to know about the exemptions and deductions available to them on repayment of interest and principal of the loan obtained to purchase the house property, if that house property is let out or self-occupied. The amount of interest on borrowed capital of the current year is available under the head house property further repayment of principal is available under section 80C to individuals and Hindu Undivided Families.

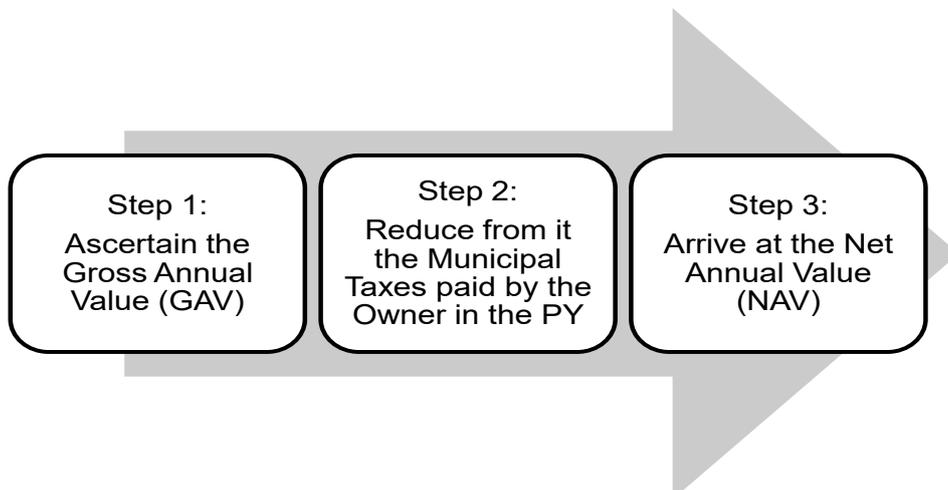
The annual value (AV) of the property of which the assessee is the owner is chargeable to Income Tax, under the head “house property”. It is imperative to note though, that the purpose of occupation is also a determinant, for example, a property that is occupied for the purpose of business / profession carried on by him is not chargeable under “Income from House Property”, which deals with self-occupied or let out properties for residential use.

### Exceptions

- Income from letting out a vacant land is chargeable to tax under the head “**Income From Other Sources**”
- Income earned by an assessee who is engaged in the business of letting out properties on rent, would be chargeable to tax under the head “**Profits / Gains from Business / Profession**”

## DETERMINATION OF ANNUAL VALUE

The process of determination of Annual Value is exhibited below.



**Annual Value:** The measure of charging income-tax under this head is the annual value of the property, i.e., the inherent capacity of a building to yield income. The expression 'annual value' has been defined in Section 23(1) of the Income-tax Act as:

(1) the annual value of any property shall be deemed to be:

- (a) the sum for which the property might reasonably be expected to let from year to year; or
- (b) where the property or any part of the property is let and the actual rent received or receivable by the owner in respect thereof is in excess of the sum referred to in clause (a), the amount so received or receivable; or
- (c) where the property or any part of the property is let and was vacant during the whole or any part of the previous year and owing to such vacancy the actual rent received or receivable by the owner in respect thereof is less than the sum referred to in clause (a), the amount so received or receivable.

Provided that the taxes levied by any local authority in respect of the property shall be deducted (irrespective of the previous year in which the liability to pay such taxes was incurred by the owner according to the method of accounting regularly employed by him) in determining the annual value of the property of that previous year in which such taxes are actually paid by him, i.e., municipal taxes will be allowed only in the year in which it was paid.

**Explanation :** For the purposes of clause (b) or clause (c) of this sub-section, the amount of actual rent received or receivable by the owner shall not include, the amount of unrealized rent.

(2) Where the property consists of a house or part of a house-

- (a) which is in the occupation of the owner for the purposes of his own residence;
- (b) or cannot actually be occupied by the owner by reason of the fact that owing to his employment, business or profession carried on at any other place, he has to reside at that other place in a building not belonging to him,

the annual value of such house or part of the house shall be taken to be nil.

(3) However, the provisions of sub-section (2) shall not apply if:

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

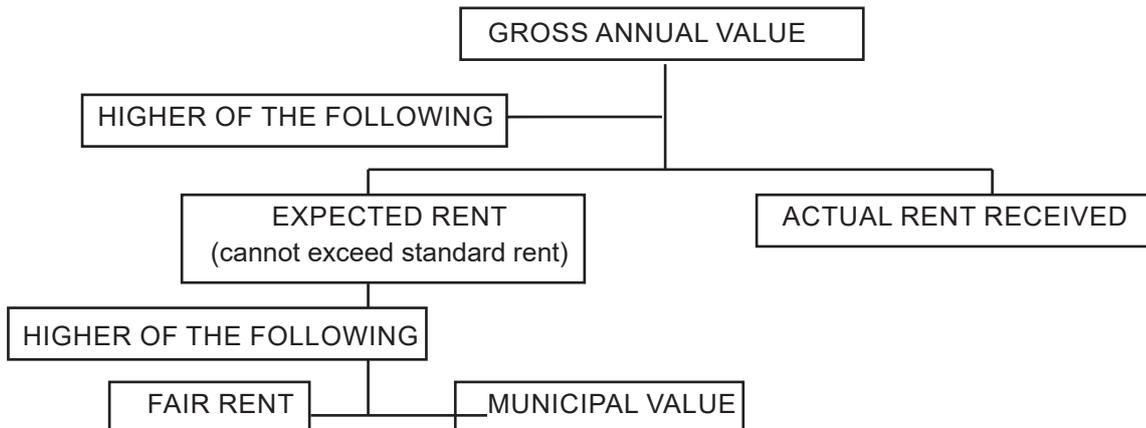
(4) Where the property referred to in Sub-section (2) consists of more than two houses:

- (a) the provisions of that sub-section shall apply only in respect of two of such houses, which the assessee may, at his option, specify in this behalf;
- (b) the annual value of the house or houses, other than the house or houses in respect of which the assessee has exercised an option under clause (a), shall be determined under Sub-section (1) as if such house or houses had been let.

**Unrealized Rent:** The amount of rent which the owner cannot realise shall be equal to the amount of rent payable but not paid by a tenant of the assessee and so proved to be lost and irrevocable only if following conditions under **Rule 4** are satisfied:

- (a) tenancy is bonafide;
- (b) the defaulting tenant has vacated, or steps have been taken to compel him to vacate the property;
- (c) the defaulting tenant is not in occupation of any other property of the assessee;
- (d) the assessee has taken all reasonable steps to institute legal proceedings for the recovery of the unpaid rent or satisfied the Assessing Officer that legal proceedings would be useless.

**Where the property is let out for the whole year [Section 23(1)]**



The GAV is the higher of

- o Expected Rent (ER) and
- o Actual Rent received / receivable (AR)

**Note:**

- ✓ The Expected Rent is the higher of Fair Rent (FR) and the Municipal Value (MV), but capped to Standard Rent (SR).
- ✓ Fair Rent is the rental fetched by a similar property in the adjoining neighbourhood.
- ✓ the Municipal Value is the value determined by the Municipal Authorities.
- ✓ the Standard Rent is the rent fixed by the Rent Control Act.

**MUNICIPAL TAXES:** The taxes including service taxes (fire tax, conservancy tax, education, water tax, etc.) levied by any municipality or local authority in respect of any house property to the extent to which such taxes are borne and paid by the owner, and include enhanced municipal tax finally determined on appeal and payable by assessee - *Clive Buildings Cola Ltd. v. CIT* (1989) 44 Taxman 160. However, deduction in respect of municipal taxes will be allowed in determining the annual value of the property only in the year in which municipal taxes are actually paid by the owner.

Where the tax on property is enhanced with retrospective effect by municipal or local authorities and the enhanced tax relating to the prior year is demanded during the assessment year, the entire demand is deductible in the assessment year [*C.I.T. v. L. Kuppu Swamy Chettiar* (1981) 132 ITR 416 (Mad.)].

Even where the property is situated outside the country taxes levied by local authority is that country are deductible is deciding the annual value of the property. [*CIT v. R Venugopala Riddiar* (1965) 58 ITR 439 (Mad.)]

**Illustration 1**

Mr. X is the owner of three houses, which are all let out and not governed by the Rent Control Act. From the following particulars find out the gross annual value in each case:

Particulars	I	II	III
Municipal Value	30,000	20,000	35,000
Actual (De facto) Rent	32,000	28,000	30,000
Fair Rent	36,000	24,000	32,000

**Solution:**

Gross Annual Value (GAV): Higher of Expected or Actual Rent

Expected Rent: Higher of Municipal Valuation or Fair Rent

House I: Rs. 36,000

House II: Rs. 24,000

House III: Rs. 35,000

Actual Rent (given)

GAV:

House I: Rs. 36,000 House II: Rs. 28,000 House III: Rs. 35,000

**Illustration 2**

Mr. X is the owner of four houses, which are all let out and are covered by the Rent Control Act. From the following particulars find out the gross annual value in each case, giving reasons for your answer:

Particulars	I	II	III	IV
Municipal Value	30,000	26,000	35,000	30,000
Actual (De Facto) Rent	40,000	30,000	32,000	32,000
Fair Rent	36,000	28,000	30,000	36,000
Standard Rent	30,000	35,000	36,000	40,000

**Solution**

As all the houses are covered by the Rent Control Act, their gross annual value will be higher of expected Rent or Actual Rent. Expected Rent shall be higher of Municipal Value or Fair rent but subject to Standard Rent:

Particulars	I	II	III	IV
Expected Rent	30,000	28,000	35,000	36,000
Actual (De Facto) Rent	40,000	30,000	32,000	32,000
G.A.V.	40,000	30,000	35,000	36,000

- Annual letting value of self occupied property, subject to Rent Control Act is to be fixed on basis of standard rent and not on basis of open market *Tilak Raj v. CIT (1989) 45 Taxman 279/178 ITR 327 (Punj. & Har.)*.
- In determining annual value salary paid to caretaker cannot be taken into account *CIT v. Smt. Sreelekha Banerjee (1989) 45 Taxman 358/179 ITR 46 (Cal.)*.
- Loss relating to self occupied house property could be set off against income from other sources *CIT v. K.K. Dhanda (HUF) (1989) 45 Taxman 346/178 ITR 602 (Punj. & Har.)*.

**Where let out property is vacant for part of the year [Section 23(1)]**

In a scenario of vacancy for a part of the year, it is quite probable that the Actual Rent received / receivable would fall lower than Expected Rent and in such an eventuality; therefore the Actual Rent becomes the Gross Annual Value.

**Illustration 3 :**

(i.e. No vacancy but there is unrealized rent)

Mr. A owns two houses. The expected rent of the house one is Rs. 65,000. This house was let out for Rs. 7,500 p.m. But the rent for the months of February and March, 2019 could not be realized.

The expected rent of another house is Rs. 1,50,000. This house was let out for Rs.12,000 p.m. But the rent for the last three months could not be realized.

In the both cases, Mr. A fulfills the conditions of Rule 4. You are required to compute the Gross Annual Value of both the houses.

**Solution**

	House I	House II
Expected Rent	65,000	1,50,000
Annual Rent	90,000	144000
Unrealized Rent	15,000	36,000

**Computation of Gross Annual Value**

Step 1: Expected Rent	65,000	1,50,000
Step 2: Actual Rent (After deducting unrealized rent) if higher than Expected Rent then Actual rent otherwise Expected rent	75,000	N.A.
Step 3: Applicable only in case of vacancy	N.A.	N.A.
Gross Annual Value	75,000	1,50,000

**Illustration 4 :****(There is vacancy but no unrealized rent)**

Find out the gross annual value in the case of the following properties for the Assessment year 2020-21

	Rs. in thousands			
	P	Q	R	S
Expected Rent	70	55	85	125
Rent Per Month (if let out)	7	5	8	8
Let out period (in months)	11	0	9	10
Vacancy (in months)	1	12	3	2

Further all the rent were realized for the year by the assessee.

**Solution:****Calculation of Gross Annual Value of Mr. X for A.Y 2020-21**

	P	Q	R	S
Annual Rent (If let out for 12 months)	84	60	96	96
Loss due to vacancy	7	60	24	16
Unrealized rent	Nil	Nil	Nil	Nil

Actual Rent (for let out period)	77	Nil	72	88
Calculation of Gross Annual Value				
Step 1: Expected Rent	70	55	85	125
Step 2: If annual rent is more than Expected				
Rent then annual rent otherwise expected Rent	84	N.A.	96	125
Step 3: If property remain vacant then decline due to vacancy shall be considered				
Gross annual value	77	0	72	109

**Illustration 5 :**

(Vacancy and unrealized rent both exist)

Mr. X is the owner of a house property. He lets this property during the previous year 2019-20 for Rs. 7,000 p.m. The house was occupied from 1.4.2019 to 31.1.2020. From 1.2.2020, it remained vacant. Mr. X fails to realize Rs.. 10,000 from the tenant. The Expected rent of the house is Rs. 82,000 p.a.

Calculate the Gross Annual Value of the house.

**Solution**

	Rs.
Expected Rent	82,000
Annual Rent (Actual for the whole year - 7000 x 12)	84,000
Actual Rent (7,000 x 10)	70,000
Unrealized rent	10,000
Realized rent (70,000 - 10,000)	60,000
Loss Due to vacancy (7,000 x 2)	14,000
Decline due to vacancy (82,000 - 14,000) but not less than actual rent received	68,000

**Calculation of Gross Annual Value**

Step 1: Expected Rent	82,000
Step 2: If actual rent is more than expected rent than actual rent otherwise expected rent	84,000
Step 3: Decline due to vacancy in Expected Rent (i.e. Expected Rent minus Loss due to vacancy but not less than actual rent received)	14,000
Gross Annual Value	68,000

**Where property is self-occupied / unoccupied [Section 23(2)]**

Where the property consists of a house or part of a house in the occupation of the owner for his own residence, and is not actually let during any part of the previous year and no other benefit is derived therefrom by the owner, the annual value of such a house or part of the house shall be taken to be nil. The only deduction available in respect of such house is towards interest on borrowed capital in terms of Section 24(1)(vi) but subject to a ceiling of Rs. 30,000 or Rs. 2,00,000 as the case may be.. In other words, to this extent there could be a loss from such house.

**Concession for two Houses only:**

Where the assessee has occupied more than two houses for the purposes of residence for himself and family members, he has to make a choice of two houses only in respect of which he would like to claim exemption. Other self-occupied houses will be treated as if they were let out and their annual value will be determined in the same manner as we have discussed in the case of let out property.

- ✓ Annual Value would be taken as Nil
- ✓ It is imperative that the property is self-occupied OR unoccupied for the whole year
- ✓ This benefit is for two houses
- ✓ This benefit is for Individual / HUF only
- ✓ No deduction is allowed for Municipal Taxes for such property

**Illustration 6 :**

Mr. R owns a house which uses for residential purposes throughout the previous year 2019-20. Municipal Value: Rs. 2,40,000. Fair Rent: Rs. 3,00,000. Compute income from house property assuming following expenditure are incurred by him:

Municipal taxes paid: Rs. 15,000

Repairs: Rs. 12,000

Depreciation: Rs. 10,000

Interest on borrowed capital : Rs. 2,00,000 (loan taken on 1.1.2004). House was purchased on 1.5.2005.

**Solution :**

Income from House Property:

Net Annual Value	Nil
Less : Interest on borrowed capital (lower of actual interest or 2,00,000; as conditions are satisfied)	2,00,000
Loss from House Property	(2,00,000)

**Where the property is partly let out and partly self-occupied during the PY [Section 23(3)]****(a) Property let out partially:**

When a portion of the house is self-occupied for the full year and a portion is self-occupied for whole year, the annual value of the house shall be determined as under:

- (i) From the full annual value of the house the proportionate annual value for self-occupied portion for the whole year shall be deducted.
- (ii) The balance under (i) shall be the annual value for let out portion for a part of the year.

**Illustration 7 :**

Mr. R. owns a house. The Municipal value of the house is Rs. 50,000. He paid Rs. 8,000 as local taxes during the year. He uses this house for his residential purposes but lets out half of the house @ Rs. 3,000 p.m. Compute the annual value of the house.

**Solution :**

	Rs.
Gross Annual rent or Municipal valuation (higher)	72,000
Less : Local taxes paid	8,000
Net Annual value of House Property	64,000
Less : Half of annual value regarding self occupied portion for the whole year	32,000
Net Annual Value of let out portion	16,000

**(b) House let out during any part of the previous year and self occupied for the remaining part of the year:**

In this case the benefit of Section 23(2) is not available and the income will be computed as if the property is let out.

**Illustration 8 :**

M is the owner of a house. The municipal value of the house is Rs. 40,000. He paid Rs. 8,000 as local taxes during the year. He was using this house for his residential purposes but let out w.e.f. 1.1.2020 @ Rs. 4,000 p.m. Compute the annual value of the house.

**Solution**

	Rs.
Gross annual value → Actual rent or Expected Rent (whichever is higher)	48,000
Less : Local taxes	8,000
Net Annual value of the house	40,000

(No benefit shall be given for self occupied period as the house did not remain vacant during the previous year)

**Note:** If fair rent is not gives, then assume actual rent as fair rent.

**(c) Self-occupied House remaining vacant :**

If the assessee has reserved any two houses (owned by him) for his residence or he is the owner of two houses which is meant for his own residence but could not be occupied by him for residential purposes in the previous year owing to the fact that he had to live at some other place in a house not belonging to him, then he can claim non-occupation or vacancy allowance during the previous year for the period during which house remained vacant. The reason for his living at a different place might be for business or professional purposes or for a salaried employee due to transfer etc. The annual value of the house, which remained vacant in these circumstances, shall be nil.

The above mentioned concession will be granted to the assessee only if he has neither let out the said house nor has derived any benefit from it during the period for which it remained vacant. Only deduction for interest on borrowed capital upto a maximum of Rs. 2,00,000 is allowed if following conditions are satisfied:-

1. Capital is borrowed for Purchase/Construction of property;
2. Capital borrowed on or after the 1st day of April 1999 and such acquisition or construction is completed within five years( 3 years up-to assessment year 16-17) from the end of the financial year in which capital was borrowed.

If any of above conditions are not met then maximum deduction allowed shall be limited to Rs. 30,000 only.

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

- ✓ Assessee given the choice of any two houses to be construed as self-occupied and for that the Annual Value would be NIL
- ✓ For others, they would be treated as deemed to be let out
- ✓ The assessee is allowed by the Income Tax Act; the flexibility to change the option to suit his needs / benefits
- ✓ In such as case, therefore, the Expected Rent becomes the Gross Annual Value
- ✓ Municipal Taxes paid by the owner for the whole year allowed as a deduction

**Notional income from house property held as stock in trade [Section 23(5) w.e.f. AY 2018-19]**

Annual value of house property held by a person as stock in trade shall be taken as NIL if following conditions are satisfied:

- (a) The Property (consisting of buildings or land appurtenant thereto) is held as stock in trade by the owner of the property;
- (b) The property (or any part of property) is not let out during whole or any part of the previous year.

Above benefit/concession is available only for 2 years from the end of the financial year in which certificate of completion of construction of the property is obtained from the competent Authority.

**DEDUCTIONS FROM NET ANNUAL VALUE (SECTION 24)**

**Standard Deduction:** 30% of Net Annual Value

- a. This is not available when the Annual Value is NIL
- b. This is a flat deduction irrespective of the actual expenditure incurred

**Interest on Borrowed Capital**

- a. Interest on borrowed capital for purchase/construction/repair/renewal / re-construction is allowed as a deduction from gross annual value.
- b. Pre-construction period interest is also allowed as a deduction. Pre-construction period refers to the period starting from the date of taking of loan and ending with the end of financial year immediately preceding the previous year in which construction is completed (or the date of repayment of loan; whichever is earlier). This can be claimed for a period of 5 equal installments starting from the year of acquisition / completion of construction.
- c. No deduction shall be made under the second proviso unless the assessee furnishes a certificate, from the person to whom any interest is payable on the capital borrowed, specifying the amount of interest payable by the assessee for the purpose of such acquisition or construction of the property, or, conversion of the whole or any part of the capital borrowed which remains to be repaid as a new loan.

**Summary on Allowability****Let out / Deemed to be let out property**

- 1) Standard deduction of 30% of NAV is fully allowed [Section 24(a)]
- 2) Interest on borrowed capital is fully allowed [Section 24(b)]

**Self-occupied properties**

- 1) Since the Annual Value is nil, there is no Standard deduction available
- 2) In case the capital is borrowed
  - a. for repairs / renewals / reconstruction, the maximum allowable deduction on account of interest is limited to INR 30000
  - b. for acquisition / construction, the deduction would depend on whether the loan was taken prior to 1.4.99 or later
    - i. In case capital borrowed prior to 1.4.99; the maximum allowable deduction on account of interest is limited to INR 30000
    - ii. In case capital borrowed post 1.4.99; as long as the acquisition / construction was completed within 5 years from the end of the FY in which the capital was borrowed, and the assessee is in possession of a certificate on interest payable from the lender, the maximum allowable deduction on account of interest is limited to INR 200,000.

Where the assessee has opted for two houses to be treated as self occupied, the combined total deduction of the amount of interest given above shall in aggregate remain maximum to Rs. 30,000 or Rs. 2,00,000 as the case may be.

**Treatment of Unrealised Rent**

Unrealised rent can be reduced from the actual rent received / receivable, if it isn't capable of being realised, if the tenancy is bonafide, the defaulting tenant has either vacated or steps are in progress to compel him to vacate, that he isn't occupying any other property of the assessee.

**Summary of computation of income from house property****A) COMPUTATION OF INCOME IN CASE OF LET OUT PROPERTY**

GROSS ANNUAL VALUE	XXX
LESS:- DEDUCTION U/S 23(1) FOR MUNICIPAL TAXES (to the extent actually paid and borne by the owner during previous year)	XXX
NET ANNUAL VALUE	XXX
LESS:- STANDARD DEDUCTION U/S 24(a)-@ 30% OF NAV	XXX
DEDUCTION FOR INTEREST ON BORROWED CAPITAL U/S 24(b)	XXX
INCOME FROM HOUSE PROPERTY	XXX

**B) COMPUTATION OF INCOME IN CASE OF SELF OCCUPIED PROPERTY**

GROSS ANNUAL VALUE	NIL
LESS: DEDUCTION FOR MUNICIPAL TAXES (even if paid and borne by the owner during previous year)	NIL
NET ANNUAL VALUE	NIL
LESS: DEDUCTION U/S 24(a)	NIL
LESS: DEDUCTION U/S 24(b) FOR INTEREST ON BORROWED CAPITAL ACTUAL	
INCOME/LOSS FROM HOUSE PROPERTY	XXX

**Illustration 9 :**

Nikhil has a property whose Municipal Valuation is INR 500,000 pa. The Fair Rent of the property is INR 400,000 pa and the Standard Rent fixed by Rent Control Act is 450,000 pa. The property was let out for a Rent of INR 35000 pm and the tenant vacated the same on 31st Jan 2020. Unrealised Rent was INR 35000 and the conditions are fulfilled with respect to the same. He paid municipal taxes worth INR 15000 during the PY and the Interest on Loan was INR 60000. Please exhibit the computation and advise the income from house property.

<b>Computation of GAV</b>	<b>INR</b>	<b>INR</b>
<b>ER</b>		
Higher of:		
1) Fair Rent	4,00,000	
2) Municipal Value	5,00,000	
<i>Limited to Standard Rent</i>		
		4,50,000
<b>AR</b>	3,50,000	
Less: Unrealised Rent	<u>35,000</u>	
		<u>3,15,000</u>
<b>GAV (as falls Vacant)</b>		3,15,000
Less: Municipal Taxes paid by the owner during the PY		<u>15,000</u>
<b>NAV</b>		<b>3,00,000</b>
<b>Less: Deductions u/s 24</b>		
30% NAV	90,000	
Interest on borrowed capital	<u>60,000</u>	
		1,50,000
<b>Income from House Property</b>		<b>1,50,000</b>

**Illustration10 :**

Smt. Shanti Devi has a house property in Kolkata. The Municipal Valuation for the same is INR 10,00,000. The Fair Rental for the property is INR 750,000. The Standard Rent per the Rent Control Act is INR 800,000. She let out the property until 30th Nov'19 for a monthly rent of Rs. 75,000 per month. Thereafter, the tenant vacated the property and she used the house for self-occupation. Rent for the months of Oct & Nov 19 couldn't be realised despite all efforts, and all the conditions for unrealised rent were satisfied. She paid Municipal Taxes @ 12% during the year. She also paid Interest of INR 25,000 during the year for amount borrowed for repairs. Compute the Income from House Property for AY 2020-21.

**Solution :**

<b>Computation of GAV</b>	<b>INR</b>	<b>INR</b>
<b>ER</b>		
Higher of:		
1) Fair Rent	7,50,000	

2) Municipal Value	10,00,000	
<i>Limited to Standard Rent</i>		8,00,000
<b>Annual Rent</b>	6,00,000	
Less: Unrealised Rent	1,50,000	
		<u>4,50,000</u>
<b>GAV (partly let out and partly self occupied)</b>		8,00,000
Less: Municipal Taxes paid by the owner during the PY		1,20,000
<b>NAV</b>		<b>6,80,000</b>
<b>Less: Deductions u/s 24</b>		
30% NAV	2,04,000	
Interest on borrowed capital	<u>25,000</u>	2,29,000
<b>Income from House Property</b>		<b>4,51,000</b>

#### Inadmissible Deductions (Section 25)

- Interest under the Act, which is payable outside India, shall not be allowed as a deduction, if tax has not been deducted from such Interest and there is no person in India, who could be treated as an agent.

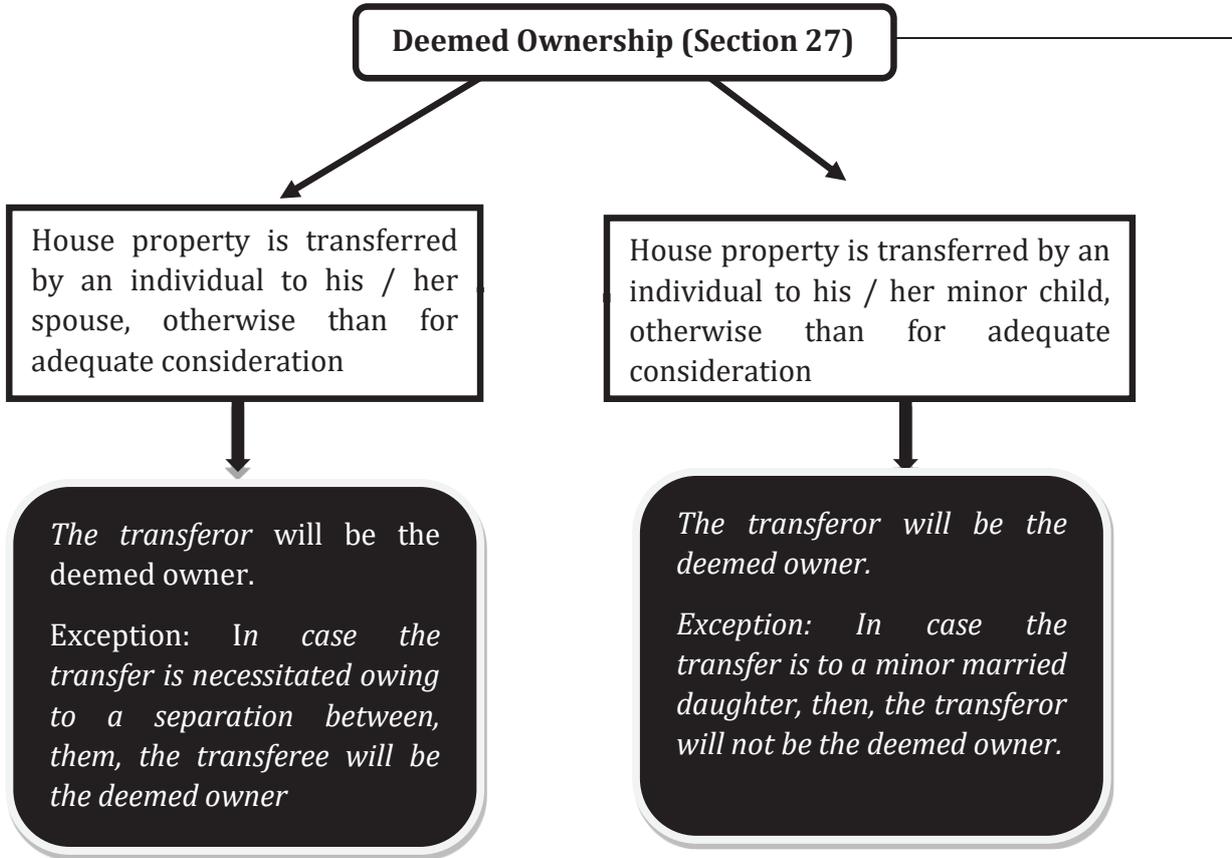
#### Treatment of Unrealized Rent / Arrear of Rent (Section 25A)

- Arrears of Rent and the unrealised rent received subsequently from a tenant by an assessee, shall be deemed to be the income from House Property in the FY in which such rental is received and shall be included in the Income from House Property of that year; irrespective of whether he is the owner of the property any more or not, in that FY.
- 30% of such arrears or unrealised rent received subsequently is allowed as a deduction.

#### Income from Co-Owned Property (Section 26)

- The share of each co-owner should be determined in accordance with Section 22 – 25 and included in the respective individual assessments
- In a scenario, where the house property owned by co-owners is self-occupied by them, the AV for each of them will be construed as NIL. Each Co-Owner shall be allowed a deduction of INR 30000 / INR 200,000 as the case may be vis-à-vis Interest on Borrowed Capital.
- In a scenario, where the house property owned by the co-owners is let out, the income from the property will be computed as if the property is owned by one owner, and thereafter such computed income would be apportioned amongst each of them as per their respective share.

**DEEMED OWNERSHIP [SECTION 27]**



- The holder of an impartible estate, i.e., one that is not legally divisible, shall be deemed to be the owner of all the properties in the estate.
- A member of a co-operative society, or any AOP, to whom a building is allotted, under a house building scheme, shall be deemed to be the owner of the portion so allotted.
- A person who acquires rights with respect to a property, by virtue of transfer vide lease of > 12 years, shall be deemed to be the owner of the property.

**HOUSE PROPERTY INCOMES – EXEMPTED FROM TAX**

There are certain cases where the income from the house property are tax-free. They are neither taxable nor included in the total income for taxation. The incomes that are exempted from tax are described below.

1. The revenue generated from the buildings in and around the agricultural land that forms a part of agricultural income is exempted from tax as per section 10(1). Eg. Renting or leasing of a farmhouse, storehouse.
2. Income from property confined to local authorities is tax-exempted as per section 10(20).

3. House property income of a political party is free from tax under section 13A.
4. Revenue earned from a property belonging to an approved scientific research association is exempted from tax under section 10(21).
5. Property income of educational organizations, medical institutions are free from tax as per section 10(23C).
6. Income from property subjected to charitable or religious purpose is tax-exempted as per section 11.
7. Property income of Certified trade union is exempted from tax under section 10(24).
8. The annual value of one palace possessed by an ex-ruler of Indian states is free from tax as per section 10(19A) where other palaces come under taxation.
9. The annual value of two self-occupied property for own residence is exempted from tax under section 23(2).
10. Income from property used for one's own business or profession is also tax-exempted under section 22.

**Illustration 11 :**

Two sisters, Seema and Rashmi, are co-owners of a house property, with 50% share each in the property. The property was constructed prior to 1st April 1999. The property has 7 equal units and is situated in Bangalore. During the FY 2019-20, each co-owner occupied one unit each and the balance were let out @ a rental of INR 20000 per unit per month. The Municipal Valuation (MV) was INR 7,00,000 and the Municipal Taxes were @ 10% of the MV. Interest payable on loan taken for construction was INR 400,000. One of the let-out units was vacant for 6 months in the year.

Compute the Income from House Property for each of the sisters.

**Solutions :**

<b>Computation of GAV</b>	<b>INR</b>	<b>INR</b>
Estimated Rent		
Higher of:		
1) Fair Rent	-	
2) Municipal Value	5,00,000	
<i>Limited to Standard Rent</i>		5,00,000
<b>Annual Rent</b>	<b>12,00,000</b>	
Less: Unrealised Rent	<u>1,20,000</u>	
		10,80,000
<b>GAV (partly let out and partly self occupied)</b>		<b>10,80,000</b>
Less: Municipal Taxes paid by the owner during the PY		<u>50,000</u>
<b>NAV</b>	<b>10,30,000</b>	
<b>Less: Deductions u/s 24</b>		
30% NAV	3,09,000	
Interest on borrowed capital	<u>2,85,714</u>	

	5,94,714
<b>Income from House Property</b>	<b>4,35,286</b>
Share of each Co-owner	2,17,643
Loss from House Property (self occupied portions)	-30,000
<b>Income from House Property (each co-owner)</b>	<b>1,87,643</b>

**Notes:**

- 1) Observe that the computation has been done for the 5 let out and 2 self-occupied portions separately and commensurately
- 2) Note that the Interest on Borrowed Capital for let out proportions is fully allowable as deduction without any cap
- 3) Note that the AV for the Self Occupied Portion is NIL and the Interest on Borrowed Capital is restricted to INR 30,000 for each co-owner

**Illustration 12:**

Mr. X is the owner of four houses. The following particulars are available:

	House 1	House 2	House 3	House 4
Municipal valuation	16,000	20,000	24,000	5,600
Rent (Actual)	—	14,000	20,000	6,800
Municipal taxes	400	1,000	1,200	300
Repairs and collection charges	200	2,500	1,040	460
Interest on mortgage	—	—	—	1,000
Ground rent	—	100	—	60
Fire premium	140	—	200	—
Annual charges	—	—	360	—

House No. 1 is self-occupied.

House No. 2 is let out for business, construction was completed on 1.3.91 and consists of two residential units.

House No. 3 is 3/4 used for own business 1/4 let out to the manager of the business.

House No. 4 is let out for residential purposes.

His other income is Rs. 30,000. Find out the income of X from house property for the assessment year 2018-19.

**Solution:**

House No. 1

	Rs.
Municipal valuation	16,000
Annual value deemed to be	NIL

House No. 2

Fair rental value	20,000
Less: Municipal taxes	1,000
Net annual value	19,000
Less: 30% of Net Annual Value	5,700
	13,300

House No. 3

Since the house is used for own business, the income from this house is not taxable under the head 'Income from house property' but will be assessed under 'Profit and gains of business or profession'. 1/4 of the house occupied by the Manager is presumed to be incidental to the business and hence not assessable under the head 'Income from house property'.

House No. 4

Rent Received	6,800
Less: Municipal taxes	300
Net annual Value	6,500
Less: 30% of Net Annual Value	1,950
	4,550

Income from House Property: Rs. NIL + Rs. 13,300 + Rs. 4,550 = Rs. 17,850. It is presumed that House No. 4 has not been mortgaged for purposes of acquiring or repairs on the house property.

**Illustration 13 :**

Mr. Lal is the owner of a house property. Its municipal valuation is Rs. 80,000. It has been let out for Rs. 1,20,000 p.a. The local taxes payable by the owner amount to Rs. 16,000 but as per agreement between the tenant and the landlord, the tenant has paid the amount direct to the municipality. The landlord, however, bears the following expenses on tenant's amenities:

	Rs.
Extension of water connection	3,000
Water charges	1,500
Lift maintenance	1,500
Salary of gardener	1,800
Lighting of stairs	1,200
Maintenance of swimming pool	750

The landlord claims the following deductions:

Repairs and Collection charges	7,500
Land revenue paid	1,500

Compute the taxable income from the house property for the assessment year 2020-21.

**Solution :**

Computation of income from house property for the assessment year 2020-21

Gross annual value: to be higher of the following:

**154 EP-TL**

(a) Municipal valuation Rs. 80,000

or

(b) De facto rent (1,20,000 less value of amenities) 1,20,000

Rent Received:

Less: Value of the amenities provided by the assessee:

(i) Extension of water connection not deductible as it is capital expenditure	–
(ii) Water charges	1500
(iii) Lift maintenance	1500
(iv) Salary of gardener	1,800
(v) Lighting of stairs	1,200
(vi) Maintenance of swimming pool	750
	(6,750)

Gross annual value 1,13,250

Less: Local tax Rs.16,000:

No deduction is permissible as the taxes have been paid by the tenant

Net annual value 1,13,250

Less: Standard deduction from net annual value:

30% of Net Annual Value 33,975

Income from house property 79,275

**Illustration 14 :**

For the assessment year 2020-21 Sonu submits the following information:

Income from business (speculative)		Rs. 40,000
Property Income	House I	House II
	Rs.	Rs.
Municipal valuation	35,000	80,000
Rent received	38,000	68,000
Municipal taxes paid by tenant	3,000	4,000
Repairs paid by tenant	500	18,000
Land revenue paid	2,000	16,000
Insurance premium paid	500	2,000
Interest on borrowed capital for payment of municipal tax of house property	200	400
Nature of occupation	Let out for residence	Let out for business

Date of completion of construction 1.4.1996 1.7.1994

Determine the taxable income of Sonu for the assessment year 2020-21.

**Solution:**

Computation of Taxable Income of Sonu for Assessment Year 2020-21

House I

Gross Annual Value	38000
Less: Municipal Taxes - not deductible since paid by tenant	NIL
Net Annual Value	38000
Less: 30% of Net Annual Value Taxable Income	11,400
	26,600

House II

Gross Annual Value	80000
Less: Taxes - not deductible, paid by tenant	NIL
Net Annual Value	80,000
Less: 30% of Net Annual Value Taxable Income	24,000
	56,000

Total Income = Rs. 26,600 + Rs. 56,000 + Rs. 40,000 = Rs. 1,22,600.

**Note:** Interest on borrowed capital for payment of municipal tax is not allowed as deduction under Section 24 of the Act.

**CASE LAW**

**1. Would income from letting out of properties by a company, whose main object as per its memorandum of association is to acquire and let out properties, be taxable as its business income, or as income from house property, considering the fact that the entire income of the company as per its return of income was only from letting out of properties?**

**Chennai Properties and Investments Ltd. v. CIT (2015) (SC)**

The Supreme Court opined that the judgment in Karanpura Development Co. Ltd.’s case squarely applied to the facts of the present case, where letting of the properties is in fact the business of the assessee. The main objective of the company as per its memorandum of association is to acquire and hold properties in Chennai and let out these properties. Therefore, holding of the properties and earning income by letting out these properties is the main objective of the company. Further, in the return of income filed by the company and accepted by the AO, the entire income of the company comprised of income from letting out of such properties. The Supreme Court, accordingly, held that the assessee had rightly disclosed the income derived from letting out of such properties under the head “Profits and gains of business or profession”.

**2. Income from letting of warehouse whether would constitute Business or Property Income**

**Nutan Warehousing Company Limited v. Dy. Commissioner of Income Tax [2010] [326 ITR 94, Mumbai]**

The question before the Bombay High Court was whether the income from warehousing activity received by the assessee was assessable as “Income from House Property” or “Income from Business”, the High

Court held that the question has to be resolved on the basis of the wellsettled decisions laid down by the Law in decided cases. The primary object of the assessee while exploiting the property is material. If the dominant intention to exploit commercial asset by carrying on a commercial activity, the income would be treated as Income from Business and whether letting out of the property constitutes a dominant aspect of the transaction or whether it was subservient to the main business of the assessee.

On the facts of the case before the Lordship it was found that the transactions of the warehousing agreements were not considered by the Tribunal. Merely styling an agreement as warehousing agreement would not be conclusive of the nature of the transaction. The question that is to be answered by the Tribunal, it was noted, whether the transaction was a bare letting out of the asset or whether the assessee was carrying on a commercial activity involving warehousing operations. The matter was remanded to consider these aspects.

What is to be noted from the aforesaid decisions is that the transactions of the leasing deed and also the dominant intention of the assessee was to exploit commercial asset by carrying out commercial activity. If the answer is in the positive, it is to be assessed as business income subject to examination of the terms of warehousing agreements.

Please also refer to the decision of the Madras High Court in C.I.T. v. Indian Warehousing Industries Ltd. and also the judgement of the Karnataka High Court in C.I.T v. Karnataka State Warehousing Corporation<sup>20</sup>.

### **3. Can benefit of self-occupation of house property under section 23(2) be denied to a HUF on the ground that it, being a fictional entity, cannot occupy a house property?**

#### **CIT v. Hariprasad Bhojnagarwala (2012) (Guj.)**

The Gujarat High Court observed that a firm, which is a fictional entity, cannot physically reside in a house property and therefore a firm cannot claim the benefit of this provision, which is available to an individual owner who can actually occupy the house. However, the HUF is a group of individuals related to each other i.e., a family comprising of a group of natural persons. The said family can reside in the house, which belongs to the HUF. Since a HUF cannot consist of artificial persons, it cannot be said to be a fictional entity.

Also, it was observed that since singular includes plural, the word “owner” would include “owners” and the words “his own” used in section 23(2) would include “their own”. Therefore, the Court held that the HUF is entitled to claim benefit of self-occupation of house property under section 23(2).

## **LESSON ROUND UP**

- **Charging Section:** Section 22 of the Act provides that the annual value of property consisting of any buildings or lands appurtenant thereto of which the assessee is the owner, other than such portions of such property as he may occupy for the purposes of any business or profession carried on by him, the profits of which are chargeable to income-tax, shall be chargeable to income-tax under the head Income from House Property”.
- **Deemed Owner:** As per section 27, the following persons though not the legal owners of a property are deemed to be the owners for the purposes of sections 22 to 26:
  - (a) Transfer to a spouse or minor child
  - (b) Holder of an impartible estate
  - (c) Member of a co-operative society
  - (d) Person in possession of a property
  - (e) Person having right in a property for a period not less than 12 years
- The measure of charging income-tax under this head is the annual value of the property, i.e., the

inherent capacity of a building to yield income. The expression 'annual value' has been defined in Section 23(1) of the Income-tax Act as, the annual value of any property shall be deemed to be:

- the sum for which the property might reasonably be expected to let from year to year; or
  - where the property or any part of the property is let and the actual rent received or receivable by the owner in respect thereof is in excess of the sum referred to in clause (a), the amount so received or receivable; or
  - where the property or any part of the property is let and was vacant during the whole or any part of the previous year and owing to such vacancy the actual rent received or receivable by the owner in respect thereof is less than the sum referred to in clause (a), the amount so received or receivable.
- Gross annual value shall be higher of
    - (a) Expected Rent
    - (b) Actual rent received or receivable.

The higher of Municipal value and fair rental value shall be Expected rent. However, expected rent shall not exceed the Standard rent.

- Net annual value shall be computed in the following manner:
  - Determine the Gross Annual Value
  - Deduct municipal tax actually paid by the owner during the previous year from the Gross Annual Value.
  - Deduction from Annual Value (Section 24): W.e.f. Assessment Year 2002-03, income chargeable under the head "Income from house property" shall be computed after making the following deductions, namely:
    - Standard deduction: a sum equal to 30% of the annual value;
    - Interest on borrowed capital: where the property has been acquired, constructed, repaired, renewed or reconstructed with borrowed capital, the amount of any interest payable on such capital. The interest on borrowed money pertaining to pre-construction period is available in 5 equal installments commencing from the previous year in which house is acquired or constructed. For this purpose the pre-construction period means the period commencing on the date of borrowing and ending on 31st March immediately prior to the date of completion of construction/date of acquisition or date of repayment of loan, whichever is earlier. Interest for current year is deductible upto Rs. 30,000/ Rs. 2,00,000 as the case may be.

## SELF-TEST QUESTIONS

### Multiple Choice Questions (MCQs)

1. The Gross Annual Value is the higher of Actual Rent and?
  - a) Municipal Valuation
  - b) Fair Rental Value
  - c) Standard Rent
  - d) Expected Rent

Answer: d

2. Expected Rent is always the higher of Fair Rental Value and Municipal Valuation?

- a) TRUE
- b) True but limited to Standard Rent
- c) True but limited to INR 250,000
- d) FALSE

Answer: b

3. Standard Rent is the rent fetched by a similar property in the neighbourhood?

- a) Yes
- b) Yes, but not limited to neighbourhood
- c) Yes, but with a Cap
- d) No

Answer: d

4. If the assessee has more than two house that is self-occupied, the choice of the houses that should be construed as self-occupied for the others to be considered as deemed to be let out lies with?

- a) Assessing Officer
- b) Assessee
- c) Either
- d) Neither

Answer: b

5. Section 24 (a) prescribes the standard deduction from NAV of a sum equal to?

- a) 33% of NAV
- b) 30% of NAV
- c) 1/3rd of NAV
- d) Actual cost of repairs

Answer: b

## SUGGESTED READINGS

### 1. Direct Taxes Law and Practice

Author : Dr. Vinod K. Singhania & Dr. Kapil Singhania

Publisher : Taxmann

Year : 2019

Edition : 2019

### 2. Direct Taxes Ready Reckoner with Tax Planning

Author : Dr. Girish Ahuja & Dr. Ravi Gupta

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# Lesson 4

## Part III – Profit and Gains from Business / Profession

### LESSON OUTLINE

- ‘Business’ or ‘Profession’
- Income Chargeable to Tax under the head Business or Profession (Section 28)
- Profits and Losses of Speculation Business
- Computation of Profits of Business or Profession
- Admissible Deductions
- Expenses Restricted/Disallowed
- Deemed Profits
- Special Provision for Deductions and Computing of Profits and Gains
- Maintenance of Accounts (Section 44AA)
- Compulsory Audit of Accounts of Certain Persons Carrying on Business or Profession
- Presumptive Basis Taxation on Business
- Presumptive Basis Taxation on Professionals
- Question and Answers
- Annexure
- Case Law
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

This lesson deals with the provisions for computation of Income from Business and Profession. The provisions for computation of Income from Business and Profession are covered under sections 28 to 44D. Section 28 defines the scope of income which can be taxed under this head. Expenses expressly allowed as deductions by the Act are listed under sections 30 to 37, whereas sections 40 and 40A enumerate those expenses which are expressly disallowed while computing taxable income.

At the end of this lesson, you will learn -

- what are the constituent of business or profession.
- which incomes are chargeable under this head.
- which are admissible/inadmissible expenses while computing the income from business and profession.
- when are certain receipts deemed to be income chargeable to tax under this head.
- which are the deductions allowable on actual payment basis.
- which assesseees are required to compulsorily maintain books of account.
- when is audit of accounts compulsory.
- who are the assesseees to whom presumptive tax provisions apply.

## BUSINESS' OR 'PROFESSION'

The meaning of the expression '**Business**, has been defined in Section 2(13) of the Income-tax Act. According to this definition, business includes any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture.

The concept of business presupposes the carrying on of any activity for profit. The definition of business given in the Act does not make it essential for any taxpayer to carry on his activities constituting business for a considerable length of time.

The definition of business given in Section 2(13) being an inclusive definition and not being exhaustive, is wide enough to cover every case of transaction entered into with the idea of earning income.

**Example:** If a person purchases a piece of land, gets it surveyed, lays down a scheme of development, divides it into a number of building plots and sells some of the plots from time to time, he would be chargeable to tax not only on the notional profits made on individual sale of plots but also on the surplus, if any, remaining after the sale of all plots and after the venture had come to an end.

The expression 'Profession' has been defined in Section 2(36) of the Act to include any vocation. In the case of a profession, the definition given in the Act is very much inadequate since it does not clearly specify what activities constitute profession and what activities do not.

According to the generally accepted principles, the meaning of the term 'profession' involves the concept of an occupation requiring either intellectual skill or manual skill controlled and directed by the intellectual skill of the operator.

For instance, an auditor carrying on his practice, the lawyer or a doctor, a painter, an actor, an architect or sculptor, would be persons carrying on a profession and not a business.

The common feature in the case of both profession as well as business is that the object of carrying them out is to derive income or to make profit. The distinction between business, profession and vocation is not however material because income from all these activities is taxable under the same head.

## INCOME CHARGEABLE TO TAX UNDER THE HEAD BUSINESS OR PROFESSION (SECTION 28)

The scope of income chargeable under this head is covered by Section 28 of the Act which lays down the following:

- (i) the profits and gains of any business or profession which was carried on by the assessee at any time during the previous year.
- (ii) any compensation received or receivable by any person, by whatever name called—
  - (a) For managing the affairs of an Indian company or any other company or in connection with the termination of his agreement or the modification of the terms and conditions relating thereto.
  - (b) For holding an agency in India for any part of the activities relating to the business of any other person or in connection with the termination of the agency or the modification of the terms and conditions relating thereto.
  - (c) For or in connection with the vesting in the Government, or in any corporation owned or controlled by the Government, of the management of any property or business.
  - (d) Any compensation received or receivable by any person at or in connection with the termination or the modification of the terms and conditions, **whether revenue or capital** of any contract relating to his business. **(inserted by the Finance Act, 2018)**

- (iii) income derived by a trade, professional or similar association from specific services performed for its members. This is an exception to the general principle of mutuality that no one can make profit out of himself. Therefore any surplus arising to the mutual associations such as Labour Welfare Association, Chamber of Commerce etc. by performing specific services to its members is deemed as income earned as carrying on business in respect of these services and accordingly chargeable to tax.
- (iv) Export incentives : Profits on sale of a Import entitlement licence granted under the Imports (Control) Order. Cash compensatory assistance against export and Duty Drawback of Customs and Central excise Duties. Profit on the transfer of the Duty Entitlement Pass Book Scheme. Profit on the transfer of the Duty Free Replenishment Certificate.
- (iv) the value of any benefit or perquisite, whether convertible into money or not arising from business or profession. For Example value of a rent free accommodation secured by an assessee from a company in consideration of his professional services to the company will be assessable in the hands of the assessee.
- (v) any interest, salary, bonus, commission or remuneration, by whatever name called, due to, or received by, a partner of a firm from such firm to the extent under section 40(b). For Example: A firm pays interest to a partner at 18% simple interest p.a. The allowable rate of interest is 12% p.a. Hence the excess 6% paid will be disallowed in the hands of the firm. Since the excess interest has suffered tax in the hands of the firm, the same will not be taxed in the hands of the partner. The interest taxable in the hands of the partner shall be 12% only.
- (vi) any sum, whether received or receivable, in cash or kind, under an agreement for –
  - (a) not carrying out any activity in relation to any business or profession, provided it is not taxable as capital gains. Example Non compete Fees.
  - (b) not sharing any know-how, patent, copyright, trade-mark, licence, franchise etc.
- (vii) any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.
- (viii) the fair market value of inventory as on the date on which it is converted into, or treated as, a capital asset determined in the prescribed manner. **(inserted by the Finance Act, 2018)**
- (ix) any sum received from transfer or destruction of any capital asset (other than land or goodwill or financial instrument) whose cost has been allowed as a deduction under section 35AD.

## SPECULATION BUSINESS

Section 43(5) defines the expression “speculative transaction” as “a transaction in which a contract for the purchase or sale of any commodity including stocks and shares is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips”. Where any part of the business of a company consists in the purchase and sale of the shares of other companies, such a company shall be deemed to be carrying on speculation business to the extent to which the business consists of the purchase and sale of such shares.

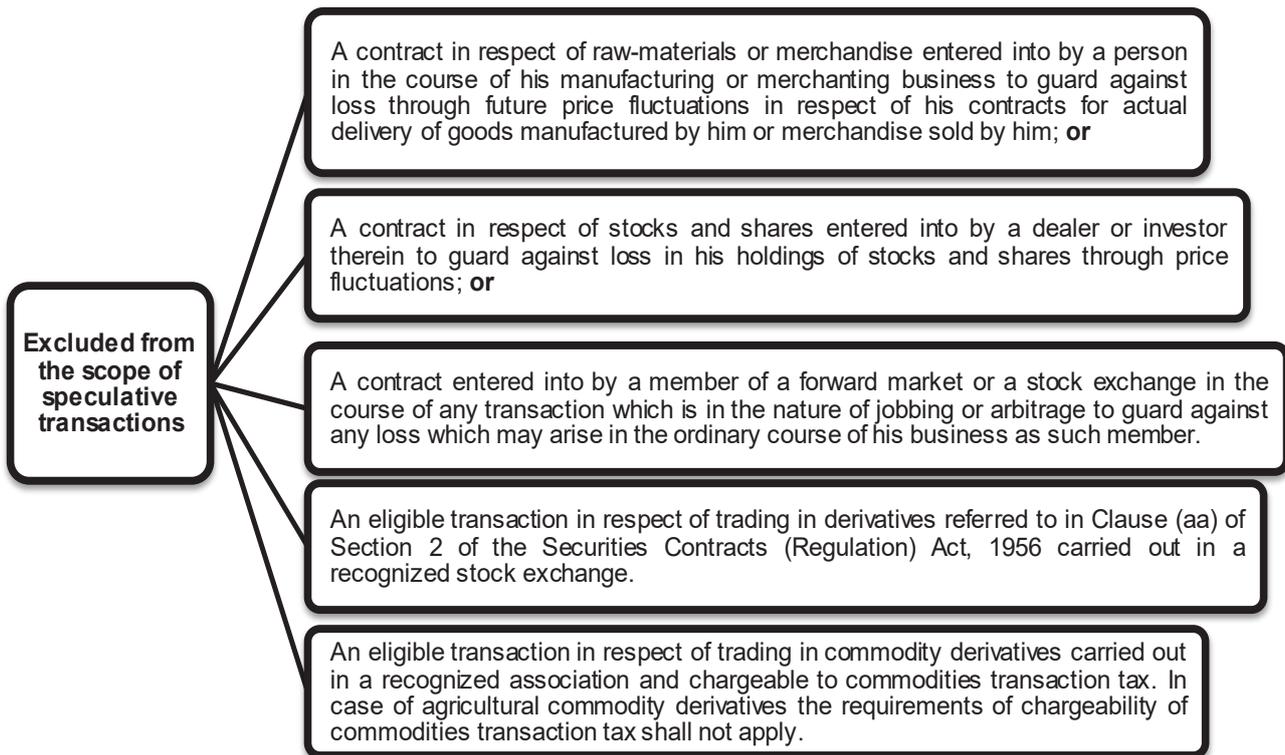
However as per the Explanation to Section 73, this deeming provision does not apply to the following companies:

- a. Where a company whose gross total income consists mainly of income which is chargeable under the heads “Interest on securities”, “Income from house property”, “Capital gains” and “Income from other sources”, or
- b. A company, the principal business of which is:

- the business of trading in shares or
- banking business or
- the granting of loans and advances

Accordingly, if these companies carry on the business of purchase and sale of shares of other companies, the income from such business is not treated as income from speculative business.

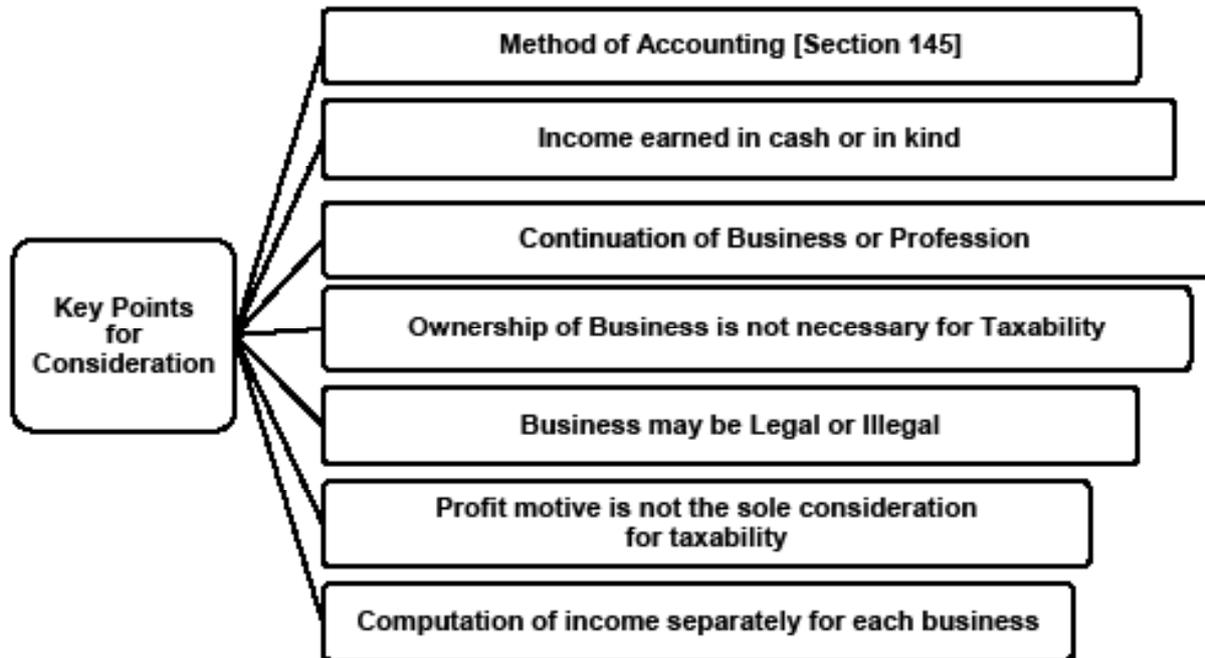
However, the following forms of transactions have been specifically excluded from the scope of speculative transactions:



*Therefore, in all cases where actual delivery or transfer of the commodity takes place, the transaction would not be a speculative transaction, however highly speculative its nature may be.*

### Key points for consideration

The provisions of the Income-tax Act contained in Sections 28 to 44D regulate the method of computing income from business. The income from business to which a person is chargeable under this head represents not the gross receipts from the business but the profits and gains derived from there.



### Method of Accounting [Section 145]

Income chargeable under the head “Profits and gains of business or profession” or “Income from other sources” shall be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee. Where the Assessing Officer is not satisfied about the correctness or completeness of the accounts of the assessee, or where the method of accounting has not been regularly followed by the assessee, or where the income has not been computed in accordance with the Income Computation and Disclosure Standards (ICDS) as notified, the Assessing Officer may make a Best Judgement assessment as provided in section 144.

The Central Government vide Notification No. 87/2016 dated 29.09.2016 has notified ten Income Computation and Disclosure Standards (ICDS) to be applicable with effect from 1st April, 2017 relating to assessment year 2017-18 for the purpose of computation of income under the head “Profits and gains of business or profession” and “Income from other sources” and not for maintaining books of accounts. Some key features of ICDS are as under :

- (i) ICDS applies to all tax payers except Individual and HUF who are not covered under the tax audit provisions under section 44AB.
- (ii) ICDS applies only to tax payers following mercantile system of accounting.
- (iii) In case of conflict between the provisions of the Income Tax Act or Income Tax Rules and the ICDS, the provisions of the Act or the Rules shall prevail to that extent.
- (iv) In case of conflict between the judicial pronouncements/ judgements and the ICDS, the provisions of the ICDS shall prevail to that extent.
- (v) ICDS shall apply irrespective of the accounting standards adopted by companies i.e., either Accounting Standards or Ind-AS.
- (vi) The provisions of ICDS shall not apply for computation of MAT. However it shall apply for computation of AMT as AMT is computed on adjusted total income which is derived by making specified adjustments to total income computed as per the regular provisions of the Act.
- (vii) ICDS shall also apply to the persons computing income under the relevant presumptive taxation

scheme. For example, for computing presumptive income of a partnership firm under section 44AD of the Act, the provisions of ICDS on Construction Contract or Revenue recognition shall apply for determining the receipts or turnover, as the case may be.

### **Method of accounting in certain cases [Section 145A]**

For the purpose of determining the income chargeable under the head “Profits and gains of business or profession” –

- (i) the valuation of inventory shall be made at lower of actual cost or net realisable value computed in accordance with ICDS.
- (ii) the valuation of purchase and sale of goods or services and of inventory shall be adjusted to include the amount of any tax, duty, cess or fee (by whatever name called) actually paid or incurred by the assessee to bring the goods or services to the place of its location and condition as on the date of valuation.
- (iii) the inventory being securities not listed on a recognised stock exchange, or listed but not quoted on a recognised stock exchange, shall be valued at actual cost as initially recognised in accordance with the ICDS.
- (iv) the inventory being securities listed and quoted on a recognised stock exchange, shall be valued at lower of actual cost or net realisable value in accordance with the ICDS.

Provided that the inventory being securities held by a scheduled bank or public financial institution shall be valued in accordance with the ICDS after taking into account the extant guidelines issued by the Reserve Bank of India in this regard.

### **Taxability of certain income [Section 145B]**

(1) Notwithstanding anything to the contrary contained in section 145, the interest received by an assessee on any compensation or on enhanced compensation, shall be deemed to be the income of the previous year in which it is received.

(2) Any claim for escalation of price in a contract or export incentives shall be deemed to be the income of the previous year in which reasonable certainty of its realisation is achieved.

(3) Subsidy or grant from Government as referred in definition of income under section 2(24) of the Act, shall be deemed to be the income of the previous year in which it is received, if not charged to income-tax in any earlier previous year.

### **Income earned in Cash or in Kind**

The income that is chargeable to tax under this head may be realised by the assessee in cash or kind. In cases where the profit is realised in any other form than cash, the market value of the commodity received as income should be taken to be the quantum of income chargeable to tax. Even in cases where an assessee is in receipt of money from his clients or other persons who are under no obligation to make such payment, the assessee would still be chargeable to tax if these monies were received by him in the ordinary course of business or profession. For instance, any amount paid to a Company Secretary by a person who has not been his client but who has been benefited by his professional service to another, would be assessable as the Company Secretary's income from profession.

The person carrying on the business or profession would be chargeable to tax under this head regardless of the fact that the profits or gains made by him ultimately go to the benefit of some other person or to the business community or public body as a whole. In other words, the subsequent application of the money derived by way of income from business is immaterial for the purpose of assessment of the businessman.

### Continuation of Business or Profession

The chargeability to tax under Section 28 is based primarily upon the condition that the assessee must have carried on a business or profession at any time during the accounting year, though not necessarily throughout the accounting year.

But there may be a few cases (e.g. deemed profits taxable under Section 41) where even if no business is carried on during the accounting year, the assessee would still be chargeable to tax.

### Ownership of Business is not Necessary for Taxability

In order to be taxable in respect of the income of a business, it is not essential that the business must be carried on by the same person who is the owner thereof. Even if the owner authorises some other person to carry on the business on his behalf or the owner is deprived by the court under certain circumstances of the right to carry on his own business, the owner will still be taxable under this head.

Similarly, it is not only the legal ownership but also the beneficial ownership that has to be considered. In this connection it has to be kept in view, as to who is the actual recipient of the income which is going to be taxed. **For example**, where a business is acquired for the benefit of a company which is going to be incorporated and the promoters carry on the business and earn profits during the period prior to the incorporation, if the company accepts the action of the promoters and receives from them the past profits made prior to its incorporation, the company shall be assessable under this section in respect of such profits although before the incorporation of the company the promoters were the legal owners of this business yet as the company was the beneficial owner (as it has actually received the profits) of the business, it will be assessable on these profits. [CIT v. Bijli Cotton Mills Ltd. (1953) 23 ITR p. 278.

### Business may be Legal or Illegal

While profit motive is indicative of the fact that the adventure of an assessee is in the nature of trade and consequently constitutes a business, it is immaterial whether the business is legal or illegal. In other words, the taxability of the income from business does not in any way depend upon or is affected by the taint of illegality in the income or the sources. Income derived from illegal activities is as much chargeable to tax as income from other operations. The fact that the person who carried on the illegal activities is punishable under the appropriate law, does not exclude him from the liability to income-tax.

Even the benefits/deductions under the act are not denied mere on the grounds of illegibility of business. As per the Supreme Court Judgement in the case of Dr. T.A. Qureshi the loss arising on account of confiscation of heroin (drugs) is a business loss even it is illegal business. Such loss can be set-off against the profits of legal business.

### Profit Motive is not the Sole Consideration for Taxability

There may be assesseees who carry on business without the primary object of making profits (e.g., a co-operative society which tries to cater to the needs of its members without the object of making maximum profits). Even in such cases, if profits arise from the business carried on by the assessee and such profits are incidental to the business, the assessee would still be taxable. Therefore, profit motive is not the only test of determining the taxability of income from any activity constituting business or profession.

### Computation of Income Separately for each Business

A taxpayer is entitled to carry on as many number of businesses as he possibly can, both in his own name and in the name of others. The profits and gains of all businesses or professions would be assessable under this head. But the profit of each business must be computed separately from one another and the deductions and allowance permissible to each business must be allowed against the income derived therefrom. The

income chargeable under this head is the aggregate of the net result of the various business or businesses or profession(s) carried on during the accounting year. Thus, the loss arising from one business would be set off against income from another business falling under the same head and the net result after such set off would alone be assessable income under this head.

### COMPUTATION OF PROFITS OF BUSINESS OR PROFESSION

The profits and gains of business or profession are computed in accordance with the provisions contained in Sections 30 to 43D. Sections 30 to 36 contain those specific deductions which are expressly allowed while Section 37(1) extends the allowance to items of business expenditure not covered by sections 30 to 36 which are otherwise allowable according to accepted commercial practices, while computing profits of business or profession. Section 40 provides those expenses which are allowed on the basis of general commercial principles while computing profits of business or profession. It is necessary to know those principles before studying the deductions expressly allowed while computing profits of business or profession.

The general commercial principles are as under:

CBDT clarified that the income from letting out of premises/developed space along with other facilities in an industrial park/SEZ is to be charged to tax under the head 'Profits and Gains of Business' and not under the head "Income from house property"

#### General Commercial Principles are as under:

- Profits should be computed according to the method of accounting regularly employed by the assessee, provided that actual profit can be ascertained by this method, whether on receipt basis or accrual basis.
- Only those expenses and losses are allowed as deductions which were incurred or sustained during the relevant previous year and related to business.
- These losses and expenses should be incidental to the operation of the business. For example, embezzlement by an employee during the course of business is a loss incidental to the business.
- If a business has been discontinued before the commencement of the previous year, its expenses cannot be allowed as deduction against the income of any other running business of the assessee.
- There are some essential expenses, though neither expressly allowed nor disallowed, but are deductible while computing the profits of business or profession on the basis of general commercial principles provided that these are not expenses or losses of a capital nature or personal nature.
- Any expenditure incurred in consideration of commercial expediency is allowed as deduction.
- Deduction can be made from the income of that business only for which the expenses were incurred. The expenses of one business cannot be charged against the income of any other business.

### COMPUTATION OF INCOME UNDER THE HEAD "PROFITS AND GAINS FROM BUSINESS OR PROFESSION"

Net Profit as per profit and loss account	xxx
Add : Inadmissible expenses debited to profit and loss account	xxx

Add : Deemed incomes not credited to profit and loss account	xxx
Less : Deductible expenses not debited to profit and loss account	(xxx)
Less : Incomes chargeable under other heads credited to Profit & Loss A/c	(xxx)

### ADMISSIBLE DEDUCTIONS

1. •Rent, rates, repairs and insurance for buildings (Section 30)
2. •Repairs and insurance for Plant & Machinery, Furniture (Section 31)
3. •Depreciation (Section 32)
4. •Investment in new plant or machinery in notified backward areas in certain States (Section 32AD)
5. •Tea/Coffee/Rubber Development Account (Section 33AB)
6. •Site restoration fund [Section 33ABA]
7. •Scientific Research (Section 35)
8. •Amortization of Spectrum fees (Section 35ABA)
9. •Expenditure on telecom licence (Section 35ABB)
10. •Expenditure of capital nature incurred in respect of specified business (Section 35AD)
11. •Expenditure by way of Payment to Associations and Institutions for carrying out Rural Development Programmes (Section 35CCA)
12. •Expenditure on Agricultural extension project (Section 35CCC)
13. •Expenditure on skill development project (Section 35CCD)
14. •Amortization of Preliminary Expenses (Section 35D)
15. •Amortisation of Expenditure in the case of Voluntary Retirement Scheme (Section 35DDA)
16. •Other Deductions [Section 36]
17. •Other Expenses [Section 37]

### Rent, rates, repairs and insurance for buildings (Section 30)

This section allows the deduction in respect of rent, rates, repairs and insurance for buildings that are used by the assessee for his business / profession.

- If the property is partly used, the deduction will be proportionate to the use.
- In case part of the property is sub-let, the differential, i.e., rent paid minus rent recovered would be allowable as deduction.
- No notional rent is allowable for owned properties.
- Repairs undertaken, whether as a owner / tenant, are allowed.
- Municipal taxes, rates, insurance incurred by the assessee for the property is also allowed.

### Deduction of expenses on the basis of usage:

Section 38 of the Act provides for the allowance of the proportionate amount of the expenses where the assessee uses the premises partly for his business or professional purposes and partly for other purposes the deduction allowable under this section is a sum proportionate to that part of the expenses which are attributable to the premises used for business or professional purposes. If the assessee is the owner of the building which is used for business or professional purposes, no deduction would be available in respect of the notional rent which would otherwise have been payable. But depreciation under Section 32 would be available in respect of such buildings. In cases where a firm carries on a business in the premises owned by one of its partners the rent payable to the partner would be an allowable deduction since the firm and the partners are separate entities.

Similarly where any building, machinery, plant or furniture is not exclusively used for the purposes of the business or profession, the deductions under Section 30, Section 31 and Section 32 shall be restricted to a fair proportionate part thereof which the Assessing Officer may determine, having regard to the user of such building, machinery, plant or furniture for the purposes of the business or profession.

### Repairs and insurance for Plant & Machinery, Furniture (Section 31)

This section allows deduction in respect of expenses on current repairs and insurance of Plant & Machinery, & furniture used for business / profession.

- Allowable in full, even if used for part of the year
- Current repairs which are of capital nature aren't allowed
- Insurance premia paid to insure the assets against risks of losses owing to damage / destruction, provided that the assets are used for business / profession are allowed, only if these premiums are paid / payable during the Previous Year.

**Note:** The assessee is entitled for deduction in respect of repairs and insurance of these assets only if these assets have been actually used for the purpose of the business of the assessee during the accounting year the profits of which are subjected to tax. Thus, if the assets are used in some business, income of which is not chargeable to tax, the assessee cannot claim deduction in respect of these expenses against the income from some other business, the profits of which are taxable.

### Depreciation (Section 32)

This section allows a deduction in respect of depreciation resulting from the diminution or exhaustion in the value of certain capital assets. The deduction on account of depreciation shall be made compulsorily, whether or not the assessee has claimed the deduction in computing his total income. The deduction towards depreciation

is very essential to arrive at the income of the assessee and also to amortise the capital cost of the amount invested in buildings, machinery, plant and furniture.

The provisions for allowing depreciation are contained in Section 32 and are regulated under Rule 5 of the Income-tax Rules. The rates of depreciation are also provided in the Income-tax Rules. Assets should have been owned and used by the assessee for the purpose of his business / profession during the Previous Year irrespective they are wholly owned by the assessee or not.

### Conditions for Allowability of Depreciation as per Rule 5 of The Income Tax Rules, 1962

In order that the depreciation is allowable, all the following conditions must be fulfilled:

**(a) Classification of Assets:**

The assets in respect of which depreciation is claimed must be buildings, machinery, plant or furniture. In addition to these tangible assets intangible assets like know how, patent rights, copy rights, trade marks, licences, franchises or any other business or commercial right of similar nature acquired on or after 1.4.1998 are eligible for depreciation. No depreciation is allowable on the cost of the land on which the building is erected because the term 'building' refers only to superstructure but not the land on which it has been erected. The term 'plant' includes ships, boats, vehicles, scientific apparatus and surgical equipments used for the purposes of the business or profession but does not include tea bushes or livestock or buildings or furniture and fittings. Similarly, the term 'buildings' includes within its scope roads, bridges, culverts, wells and tubewells.

**(b) Assets must be owned either wholly or partially:**

Depreciation is allowable to the assessee only in respect of those capital assets which are owned by him. In case of a building, the assessee must be owner of the super-structure and not necessarily of the land on which it is constructed. If the assessee is only a tenant of the building but not its owner he is not entitled for allowance in respect of depreciation thereof. Where the land on which the building is constructed has been taken on lease by the assessee, the allowance of depreciation would be admissible only if, according to the lease deed, the assessee is entitled to be the owner of the super-structure. The fact that as part of the terms of the lease deed, the building, after expiry of the lease is to be transferred to the lessor of the land would not affect the allowance for depreciation.

In the case of assets acquired on hire-purchase e.g., plant and machinery taken on hire, the assessee would not be the owner thereof and consequently would not be entitled for depreciation in respect of the same. But if the plant and machinery had been acquired on instalment basis, the assessee becomes the owner of the assets the moment the purchase or sale is concluded and consequently is entitled to depreciation although a part or whole of the price is payable in future.

**(c) Used for the purpose of Business or Profession:**

The allowance for depreciation is subject to the condition that the assets on which depreciation is claimed are actually put to use by the assessee for the purposes of his business or profession during the accounting year. The allowance for depreciation, however, is not subject to the condition that the asset in question must be used throughout the relevant accounting year in order to enable the assessee to claim depreciation. Use could also include passive use that means kept ready for use, example – fire extinguishers. In cases where the depreciable asset is used partly for business purposes and partly for other purposes, the deduction towards depreciation allowable under Section 32 would be of a sum proportionate to the depreciation allowance to which the assessee would have otherwise been entitled. It's not just use that's important, it's owned and used that's mandatory, i.e., the assets should be owned and used by the assessee in the Previous Year. If the asset is used for < 180 days, 50% of depreciation is allowable for that previous year

- (d) **No deduction on sold assets:** No depreciation is allowable in respect of the depreciable asset if the asset concerned is sold, destroyed, discarded or demolished in the same year in which it was acquired.
- (e) **Depreciation is allowed on the Written Down Value (WDV) Method:** Depreciation is computed on the written down value of the Block of the asset as on the last day of the previous year. However in case of the assessee engaged in the generation or distribution of power, depreciation may be claimed on the basis of Straight Line Method.
- (f) Where an assessee incurs any expenditure for acquisition of depreciable asset in respect of which a payment (or aggregate of payments made to a person in a day), otherwise than by an account payee cheque/draft or use of ECS through a bank account or such other electronic mode as may be prescribed, exceeds Rs. 10,000 such payment shall not be eligible for normal/ additional depreciation. Also such Payment will be ignored for the purpose of computation of Actual Cost of such asset under section 43(1).
- (g) Depreciation is allowable in the hands of the predecessor and successor, in case of succession of a firm, proprietary concern, by a company, or predecessor company and successor LLP, in case of conversion of Pvt. Ltd. Co. to LLP., in case of amalgamation or demerger, and that shall not exceed the depreciation that would have been allowed if the succession, demerger, amalgamation had not taken place and such depreciation shall be apportioned between them proportionate to use.
- (h) Rates of Depreciation
- Buildings (residential use): 5%
  - Buildings (non-residential use): 10%
  - Furniture and Fittings : 10%
  - Computers (Including Computer Software): 40%
  - Plant & Machinery: 15%
  - Motor Vehicles (personal use): 15%
  - Motor Vehicles (commercial use): 30%
  - Ships: 20%
  - Aircrafts: 40%
  - Intangible Assets: 25%

### Block of Assets

The depreciation is provided in respect of "Block of assets". As per Section 2(11) Block of assets means "a group of assets falling within a class of assets, being tangible assets such as buildings, machinery, plant or furniture and intangible assets, being know-how, patents, copyrights, trademarks, licences, Franchises or any other business or commercial rights of similar nature, in respect of which the same percentage of depreciation is prescribed".

There are four classes of the assets which are further categorized into ten Blocks of Assets according to different rates of assets prescribed as under:

S. No.	Class of Asset	Block of Asset
1.	Building	3 blocks (5%, 10% and 40%)
2.	Furniture & Fixture	1 block (10%)

3.	Plant and machinery	5 blocks (15%, 20%, 30%, 40%, 45%)
4.	Intangible Assets	1 block (25%)

### Illustration

X Ltd. has a block of assets (P&M), carrying 15% depreciation, WDV on 1st Apr 2019 is INR 75,00,000. It purchased subsequently on 1st Dec 2019, another machinery for INR 25,00,000 and put to use on the same day. X Ltd. was amalgamated with Y Ltd. effective 1st Feb 2020.

Compute the depreciation allowable for X Ltd. and Y Ltd. for the AY 2020-21.

Block	Days	Allowable	Depreciation
75,00,000	365	Full	11,25,000
25,00,000	121	Half	1,87,500
		<b>Total Depreciation</b>	<b>13,12,500</b>
Predecessor	306	On the Opening P&M	9,43,151
Successor	59		1,81,849
Predecessor	62	On the Acquired P&M	96,074
Successor	59		91,426

### Notes:

- The depreciation for the asset in existence and used for the whole year is proportionately divided basis the number of days used by the predecessor until amalgamation date and the successor post amalgamation date.
- The depreciation for the asset acquired during the year and used for the remaining part of the year is proportionately divided basis the number of days used by the predecessor until amalgamation date and the successor post amalgamation date, beginning the date of acquisition.
- In case of hire-purchase arrangements :
  - If it is an operating lease, the lease rentals would be allowable as evidenced by an agreement, in the books of the lessee, and the lessor can continue to claim depreciation
  - If it is a finance lease, the lessee can claim the depreciation and hence in this case, there is no option to avail the lease rental

### Actual Cost [Section 43(1)]

The actual cost of an asset to the assessee is normally the amount of capital expenditure incurred in respect of the acquisition, installation, etc., of the asset and also the other expenses, if any, incurred by him to make the asset ready for the purpose of its use in the business.

The expression 'actual cost' has been defined in Section 43(1) of the Act to mean that actual cost of the asset to the assessee as reduced by that portion of the cost thereof, if any, as has been met directly or indirectly by any other person or authority. For instance, if an assessee gets a subsidy from the Government for the purchase of a particular item of machinery, the actual cost of the machinery to the assessee would be total of the purchase price and the expenses in regard to installation etc. minus the subsidy received from the Government.

It is important to note that where, an assessee, in acquisition of an asset, makes payment(s) in a day otherwise than by an a/c payee cheque / demand draft / ECS / or such other electronic modes as may be prescribed, which is > INR 10000, such expenditure would not be a part of the actual cost.

The provisions of Section 43(1) of the Act clarify that the actual cost of depreciable asset should be determined in the following circumstances as indicated below:

## 174 EP-TL

- ✓ If an asset was first used for scientific research and then used for business later, the actual cost would be the initial cost incurred in acquiring the asset minus the deduction already claimed under section 3.
- ✓ If the asset is acquired as a gift / inheritance, the actual cost is the WDV of the previous owner.
- ✓ If an asset was once in use, then transferred and later re-acquired, the actual cost would be the WDV at the time of transfer OR the price of re-acquisition, whichever is lower.

**For instance**, if 'X' transfers his machinery on 1.1.2020 to 'Y' for a sum of Rs. 6.00 lakhs while the actual cost of the asset and the written down value thereof on that day to 'X' are Rs. 3.00 lakhs and Rs. 1.00 lakh respectively, it may be inferred that the transfer by 'X' to 'Y' is made with idea to enable 'Y' to claim depreciation on Rs. 6.00 Lakhs while the market value of the asset on the date of sale by 'X' to 'Y' may be Rs. 4.00 lakhs only. In such a case, the Assessing Officer would be entitled to allow depreciation to 'Y' on the basis of the cost which may be determined by him to be Rs. 4.00 lakhs instead of Rs. 6.00 lakhs as claimed by 'Y'.

- ✓ If an asset is transferred from a holding co. to a subsidiary co. or vice-versa, then subject to specified conditions, the transaction wouldn't be a transfer of a capital asset and hence, the actual cost to the transferee company shall be taken to be the same as it would have been used by the transferor company had it continued to hold it for the purposes of business / profession, and similar approach to be adopted for amalgamation / demerger.
- ✓ Any amount of interest paid / payable as interest in connection with the acquisition of an asset, and relatable to period after the asset is put to use, shall not be included in the actual cost of the asset.
- ✓ Where a portion of the cost of an asset acquired by the assessee has been met directly or indirectly by the Central Government or a State Government or any authority established under any law or by any other person, in the form of a subsidy or grant or reimbursement (by whatever name called), then, so much of the cost as is relatable to such subsidy or grant or reimbursement shall not be included in the actual cost of the asset to the assessee.
- ✓ Where an asset which was acquired outside India by an assessee, being a non-resident, is brought by him to India and used for the purposes of his business or profession, the actual cost of the asset to the assessee shall be the actual cost to the assessee, as reduced by an amount equal to the amount of depreciation calculated at the rate in force that would have been allowable had the asset been used in India for the said purposes since the date of its acquisition by the assessee.
- ✓ Where any capital asset is acquired by the assessee under a scheme for corporatisation of a recognised stock exchange in India, approved by the Securities and Exchange Board of India established under section 3 of the Securities and Exchange Board of India Act, 1992 (15 of 1992), the actual cost of the asset shall be deemed to be the amount which would have been regarded as actual cost had there been no such corporatization.
- ✓ Capital Asset on which deduction has been allowed or allowable u/s 35AD shall be treated as nil:
- ✓ Actual cost of inventory converted into capital asset, if used for business, shall be the fair Market Value.  
**[By Finance Act, 2018]**

### Written Down Value (WDV) [Section 43(6)]

- ✓ In case of acquisition of assets during the Previous Year, the actual cost becomes the WDV
- ✓ In case of assets acquired before the Previous Year, the WDV = Actual Cost to the Assessee MINUS Depreciation c/f if any.
- ✓ In case of transfer of assets from holding company to subsidiary, or vice-versa, or from a amalgamating company to an amalgamated company, then the actual cost of assets in the books of the transferee

company would be the WDV of the block of assets, as in the books of transferor company for the immediately preceding Previous Year, minus, the allowable depreciation during the Current Year.

- ✓ In case of a successor LLP, the WDV in the books of the LLP would be the WDV in the books of the predecessor company on the date of such conversion.
- ✓ The WDV of the following assets may be reduced to NIL, a) the moneys receivable by the assessee in respect of the assets sold, together with the scrap value if any is > than the current WDV of the assets, OR where the entire block of assets is sold.

### Unabsorbed Depreciation

- ✓ It's the depreciation that couldn't be consumed fully, that is, the profits were not sufficient to absorb it.
- ✓ Can be carried forward indefinitely.
- ✓ The current year depreciation and the brought forward business losses get priority in the set off over the unabsorbed depreciation, in that order.

### Depreciation on Straight line basis

In the case of Power Units [Section 2(1)(i)] (optional to power generating units) From the assessment year 1998-99, an undertaking engaged in generation or generation and distribution of power can claim depreciation on straight line basis on the actual cost of individual asset. But the aggregate depreciation can not exceed the actual cost. Alternatively, such undertaking can claim depreciation, at its option, according to written down value method like any other assessee. The option for this purpose shall be exercised before the due date of furnishing return of income. Once this option is exercised, it shall be final and shall apply to all the subsequent years.

Where an assessee incurs any expenditure for acquisition of any asset in respect of which a payment (or aggregate of payments made to a person in a day), otherwise than by an account payee cheque/draft or use of ECS through a bank account or such other electronic mode as may be prescribed, exceeds Rs. 10,000, such Payment shall be ignored for the purpose of computation of Actual Cost of such asset. **[Amendment vide Finance Act, 2017 w.e.f. AY 2018-19]**

### Terminal depreciation

If any asset, on which depreciation is claimed on basis of SLM, is sold and the amount by which money payable together with scrap value, fall short of WDV of such asset, depreciation shall be allowed equal to such deficiency in the year of sale.

### Balancing Charge [Section 41(2)]

If any asset, on which depreciation is claimed on basis of SLM, asset is sold and the amount by which moneys payable together with scrap value, exceeds WDV of such asset, then the least of the following shall be taxable under the head PGBP.

- (i) difference between the actual cost and WDV
- (ii) difference between aggregate of moneys payable and WDV

### Additional Depreciation [Section 32(1)]

The additional depreciation is available to assessee engaged in the business of manufacture or production of any article or thing or engaged in the business of generation or generation and distribution or transmission of power at the rate of 20% of actual cost of eligible new machinery or plant (other than ships and aircrafts acquired and installed in a previous year. However in case of Investment is made in New Plant and Machinery

in Notified Backward areas in state of Andhra Pradesh or Telangana on or after 1/4/15, Additional depreciation shall be allowed @ 35% of Actual cost. Additional Depreciation shall not be allowed if -

- (a) any machinery or plant which, before its installation by the assessee, was used either within or outside India by any other person; or
- (b) any machinery or plant installed in any office premises or any residential accommodation, including accommodation in the nature of a guest house; or
- (c) any office appliances or road transport vehicles; or
- (d) any machinery or plant, the whole of the actual cost of which is allowed as a deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head "Profits and gains of business or profession" of any one previous year.

**Note:** where asset is purchased in same previous year and put to use in business in same year for less than 180 days then additional depreciation is allowed at 50% of rate of additional depreciation. However in case of Plant and Machinery purchased and installed in notified Backward areas of State of Andhra Pradesh and Telangana and put to use for less than 180 days, 50% of additional depreciation will be allowed in previous year in which asset is put to use and 50% in immediately succeeding financial year.

**Note:** Where asset is purchased and put to use in business in the same previous year for less than 180 days then additional depreciation is allowed at 50% of rate of additional depreciation and balance 50% of additional depreciation in immediately succeeding financial year.

#### Calculation of Written Down Value of a block of asset [Section 43(6)]

- (a) Find out the written down value on the first day of the previous year (WDV) relevant to the assessment year, of all those depreciable assets on which the depreciation is allowed at the same rate. All such assets are known as "block assets".
- (b) The increase in the WDV by the actual cost of any asset falling within that block, acquired during the previous year;
- (c) Reduce from the above, the moneys payable in respect of any asset falling within that block, which is sold or discarded or demolished or destroyed during that previous year together with the amount of the scrap value, if any, so that the amount of such reduction does not exceed the written down value as so increased; and
- (d) In the case of a slump sale, decrease by the actual cost of the asset falling within the block as reduced by the amount of depreciation that would have been allowable to the assessee for any assessment year, so that the amount of such decrease does not exceed the written down value.

It means if the net consideration of an asset out of the block is less than the balance under (ii), there would be no capital gain. If the net consideration of an asset is more than the balance under (ii) (the value of all assets in the block) the excess shall be deemed to be short term capital gain. If all the assets of the block are sold in the previous year and the net consideration is less than the balance under (ii), the loss shall be deemed to be shortterm capital loss.

Where any capital asset is acquired by the assessee under a scheme for corporatisation of a recognised stock exchange in India, approved by the Securities and Exchange Board of India established under Section 3 of the Securities and Exchange Board of India, 1992 (15 of 1992), the actual cost of the asset shall be deemed to be the amount which would have been regarded as actual cost had there been no such corporatisation.

This may be easily followed by the following **example** :

Depreciable assets on 1.4.2018 on which the depreciation is available at the same rate of 25%.

Asset A	3,00,000
Asset B	5,00,000
Asset C	7,00,000
Total	15,00,000
Less : [Depreciation @ 25% of 15,00,000]	(3,75,000)
(i) Written down value on 1.4.2019 of block of assets	11,25,000
Add : Cost of Asset purchased during 2019-20	6,00,000
(ii) Balance	17,25,000
Asset B sold during year 2019-20	(6,75,000)
(iii) Balance	10,50,000
Less: Depreciation for 2019-20 @ 25% of Rs. 10,50,000	(2,62,500)
Written down value of all assets on 1.4.2020	7,87,500

**Illustration**

Mr. Mohan, engaged in the business of generation of power, furnishes the following details for FY 2019-20. He has opted for WDV method, you are required to compute the allowable depreciation for FY 2019-20.

The Opening Block as on 1st April, 2019 was INR 950,000 (15% block). He acquired second hand machinery for INR 250,000 on 30th Nov'19. He also acquired Power Generation Machinery on 1st Aug 2019 for INR 10,00,000. He invested in an AC for Office for INR 200,000 on 9th Sep'19 and a pollution control equipment for INR 250000 on 30th Jun' 19. He bought additional power generation machinery for INR 500,000 on 1st Feb' 20. Also, he sold assets valued INR 400,000 for INR 350,000 during the year.

	INR	Block	Date		INR	Block	Date
Opening WDV	9,50,000	15%		Air Pollution Ctrl Equipment	2,50,000	40%	30th Jun 19
Acq. Second hand	2,50,000	15%	30th Nov'19				
Power Generation Machinery	10,00,000	15%	1st Aug 19				
AC for Office	2,00,000	15%	9th Sep, 19				
Power Generation Machinery	5,00,000	15%	1st Feb, 20				
Sale Value	3,50,000						
Depreciation							
On the ones put to use for < 180 day	18,750						
	37,500						
On the Remaining Block, which comes to INR 18,00,000	2,70,000			On the Pollution Control Equipment	1,00,000		
Depreciation allowable	3,26,250						

Addl Depreciation allowable on Power Generation Machinery @ 20	2,00,000			Addl Depreciation allowable on On the Poll Control Equipment @	50,000		
Power Generation Machiner @ 20% which was used for < 180 days	50,000						
Total Depreciation Allowable	5,76,250			Total Depreciation Allowable	1,50,000		

**Notes:**

- The cells highlighted denote the ones which were put to use for < 180 days.
- Power generation equipment, pollution control equipment can enjoy additional depreciation.
- No depreciation is allowable on second hand machinery or office appliances like AC.

### Investment in New Plant or Machinery in Notified Backward Areas in Certain States (Section 32AD)

Additional investment allowance of an amount equal to 15% of the cost of new asset acquired and installed by an assessee is allowed, if

- he sets up an undertaking or enterprise for manufacture or production of any article or thing on or after 1st April, 2015 in any notified backward areas in the State of Andhra Pradesh and the State of Telangana; and
- the new assets are acquired and installed for the purposes of said undertaking or enterprise during the period beginning from the 1st April, 2015 to 31st March, 2020.

Transfer of the plant or machinery for a period of 5 years has also been restricted. However, this restriction shall not apply in a case of amalgamation or demerger but shall continue to apply to the amalgamated company or resulting company, as the case may be.

Where an assessee incurs any expenditure for acquisition of any asset in respect of which a payment (or aggregate of payments made to a person in a day), otherwise than by an account payee cheque/draft or use of ECS through a bank account, exceeds Rs. 10,000, such payment shall not be eligible for Investment Allowance u/s 32AD. **[Amendment vide Finance Act, 2017 w.e.f. AY 2018-19]**

### Tea/Coffee/Rubber Development Account (Section 33AB)

Section 33AB is applicable to an assessee carrying on the business of growing and manufacturing tea in India. For claiming the deduction u/s 33AB the assessee has to satisfy the following conditions:

- an assessee, carrying on business of growing and manufacturing tea or coffee or rubber in India
- Any amount deposited with the National Bank or in an account maintained by the assessee with the Bank in accordance with and for the purposes specified in a scheme approved in this behalf by the Tea Board of India or the Coffee Board of India or the Rubber Board;
- assessee whose accounts have been audited and the assessee furnishes along with his return of income the report of such audit in the prescribed form and duly signed and verified by such accountant. In cases where the accounts of the tax payer are required to be audited under any other law, it would be sufficient if the accounts are audited under that law and the audit report as

per that law is furnished with the return along with a further report in the form prescribed for the purposes of this provision.

**Deduction :**

- (a) a sum equal to the amount or the aggregate of the amounts so deposited; or
- (b) Forty per cent of the profits of such business (computed under the head “Profits and gains of business or profession” before making any deduction under Section 33AB), whichever is less.

**Withdrawal of Amount**

There is a restriction on the withdrawal of the amount standing in the credit of such Special account of the assessee, i.e., the withdrawal must be made either: (i) for the purposes specified in the scheme, or, in the following circumstances: (a) closure of business; (b) death of an assessee; (c) partition of a H.U.F.; (d) dissolution of a firm; (e) liquidation of a company.

**Consequences in case of closure of Business:**

Withdrawal of any amount in the event of: (a) closure of business or; (b) dissolution of a firm, the whole of such amount shall be deemed to be the profits and gains of business or profession of that previous year and chargeable to income-tax as if the business had not closed, or, the firm not dissolved and taxable in that previous year.

Conversely, where any amount standing to the credit of the assessee in the special account or in the Tea Deposit Account is utilised by the assessee for the purposes of any expenditure in connection with such business in accordance with the scheme, such expenditure shall not be allowed as a revenue deduction in computing the income chargeable under the head “Profits and gains of business or profession”.

Non-utilisation of any amount released by the National Bank, for being utilised by the assessee for the purposes of a business, in accordance with the scheme, renders the whole or part of the amount not utilised, as the case may be, deemed as profits and gains of business and, accordingly, chargeable to income-tax as income of that previous year. The exceptions to this provision are, when the amount is not utilised in the cases of: (i) death of an assessee; (ii) partition of a Hindu undivided family; (iii) liquidation of a company.

In cases where the asset acquired in accordance with the scheme or deposit scheme is sold or otherwise transferred in any previous year by the assessee to any person, at any time before the expiry of eight years from the end of the previous year in which it was acquired, such part of the cost of the asset as is relatable to the deduction already allowed is deemed to be the profits and gains of business or profession of the previous year in which the asset is sold or otherwise transferred and charged to income-tax accordingly.

**Exception to the provision :** these provisions do not apply where:

- (i) the asset is sold or otherwise transferred by the assessee to Government, local authority, corporation established by or under a Central, State or Provincial Act or a Government company as defined in Section 617 of the Companies Act, 1956; or
- (ii) Where the sale or transfer of the asset is made in connection with the succession of a firm by a company in the business or profession carried on by the firm as a result of which the firm sells or otherwise transfers to the company any asset and the scheme or the deposit scheme continues to apply to the company in the manner applicable to the firm only where,
  - (i) all the properties of the firm relating to business or profession immediately before the succession become the properties of the company;
  - (ii) all the liabilities of the firm relating to the business or profession immediately before the succession become the liabilities of the company; and

- (iii) all the shareholders of the company were partners of the firm immediately before the succession.
- (a) "Coffee Board" means the Coffee Board constituted under Section 4 of the Coffee Act, 1942 (7 of 1942);
- (aa) "National Bank" means the National Bank for Agriculture and Rural Development established under Section 3 of the National Bank for Agriculture and Rural Development Act, 1981 (61 of 1981);
- (ab) "Rubber Board" means the Rubber Board constituted under Sub-section (1) of Section 4 of the Rubber Board Act, 1947 (24 of 1947);
- (b) "Tea Board" means the Tea Board established under Section 4 of the Tea Act, 1953 (29 of 1953).

### Computation of business income in cases where income is partly agriculture and partly business

Taxability in case of composite income for manufacturing and performing other processes of Rubber; tea and Coffee is summarized as under :

S. No.	Nature of composite income	Business income (Taxable)	Agricultural Income (Exempt)
1	Income from the manufacture of rubber	35%	65%
2	Income from the manufacture of coffee		
	- sale of coffee grown and cured	25%	75%
	- sale of coffee grown, cured, roasted and grounded	40%	60%
3	Income from the manufacture of tea	40%	60%

### Site restoration fund [Section 33ABA]

- The taxpayer is engaged in the business of the prospecting for, or extraction or production of, petroleum or natural gas or both in India.
- The Central Government has entered into an agreement with the taxpayer for such business.
- The assessee deposit with SBI any amount in an account maintained by the assessee with that bank in a scheme approved by the Government of India in the Ministry of Petroleum and Natural Gas; or deposit any amount in an account opened by the assessee in accordance with, and for the purposes specified in, a scheme framed by the Ministry of Petroleum and Natural Gas.
- The aforesaid amount shall be deposited before the end of the previous year.
- The accounts of the taxpayer should be audited by an accountant as defined in the explanation below Sub-section (2) of Section 288 and the report of the auditor is filed along with the return of the relevant assessment year. Further, in case where the accounts of the taxpayer are required to be audited under any other law, e.g. under the Companies Act, it would be sufficient if the accounts are audited under that law and the audit report as per that law is furnished with the return along with a further report in the form prescribed for the purposes of the provision.

### Amount of deduction:

- (a) a sum equal to amounts deposited as mentioned above; or

- (b) 20 per cent of the profit of such business computed under the head “Profits and gains of business or profession” before making any deduction under Section 33ABA and before adjusting brought forward business loss under Section 72,

whichever is less.

**Note:**

1. Where any deduction is claimed under this section, no deduction shall be allowed in respect of such amount in any other previous year.
2. Where a deduction is claimed and allowed under this section, to a firm, association of persons or body of individuals, no deduction shall be allowed to any partner of the firm or the member of the association or body in respect of the same deposit.

The amount standing to the credit of such special account or site restoration account may be withdrawn only for the purpose specified in the scheme or deposit scheme. If the amount released by SBI or the amount withdrawn from site restoration account in a year is not utilized in the same previous year for the purpose for which it is released, the amount not so utilized will be treated as taxable profits of that year and taxed accordingly.

Where any amount standing to the credit of the assessee in the special account or in the Site Restoration Account is withdrawn on closure of the account during any previous year by the assessee, the amount so withdrawn from the account as reduced by the amount, if any, payable to the Central Government by way of profit or production share as provided in the agreement referred to in Section 42, shall be deemed to be the profits and gains of business or profession of that previous year and shall accordingly be chargeable to income-tax as the income of that previous year. Where any amount is withdrawn on closure of the account in a previous year in which the business carried on by the assessee is no longer in existence, the above provisions shall apply as if the business is in existence in that previous year.

There is an overriding condition that the deduction under this provision cannot be claimed in relation to amounts utilized for the purpose of any machinery or plant to be installed in any office premises or residential accommodation including guest house; any office appliance, other than computers; any other plant or machinery which either is installed in an undertaking producing low priority items specified in the Eleventh Schedule in the Act or is an item of plant or machinery entitled to 100 per cent write off by way of depreciation or for any other reason in any one year.

The deduction allowed under this provision will be withdrawn if the asset acquired in accordance with the scheme is sold or otherwise transferred within 8 years from the end of the previous year in which it is acquired. For this purpose, the cost of the asset relating to the deduction allowed will be treated as taxable business profits of the year in which the asset is sold or otherwise transferred.

The deduction allowed earlier will, however, not be withdrawn in cases where the asset is transferred within 8 years period to Government, local authority statutory corporation or Government company.

It will also not be withdrawn where the transfer takes place in connection with succession of a firm by a company. For this purpose it is necessary that:

- (a) the scheme continues to apply to the company in the manner applicable to the firm;
- (b) the successor company takes over all the assets and liabilities of the firm; and
- (c) all the shareholders of the company were partners of the firm before the succession.

### Scientific Research (Section 35)

The term scientific research connotes and implies activities for the extension and advancement of knowledge, in the fields of natural or applied science, including, agriculture, animal husbandries and fisheries.

The allowability of expenditure on scientific research would depend on:

In case the expenditure is made by the assessee himself, then irrespective of whether the expenditure is revenue or capital in nature, 100% of the expenditure would be allowable. However, it is prudent to note that if the expenditure is towards acquisition of land, that would not be allowable.

Key-points with respect to the deduction are as follows :

- ✓ Any revenue expenditure incurred by the assessee within 3 years immediately preceding the commencement of business, for which research is conducted, by way of salary to research personnel engaged in such research, or material inputs for such research, will be allowed as a deduction in the year in which such business is commenced. However, such expenditure would be limited to the amount certified by the prescribed authority.
- ✓ Any capital expenditure incurred by the assessee, within 3 years immediately preceding the commencement of the business would be deemed to have been incurred in the year in which the business was commenced and will therefore rank for deduction in the year of commencement of business, in full
- ✓ In case such expenditure cannot be absorbed by business profits in any year, such deficiency can be carried forward indefinitely until it is fully absorbed / consumed

In case the research is conducted by a third party, and the payment is made by the assessee for conducting the research, the allowability is as under:

- a) In case the amount is paid to a company for scientific research, 100% of such expenditure is allowable
  - ✓ This deduction is allowable only if the company is an Indian company and has as its main object, scientific research and development
- b) In case the amount is paid to a university, college or research association for social science or statistical research, 100% of such expenditure is allowable
  - ✓ The deduction is allowable only if the payment is to an approved institution and such deduction cannot be denied later, subsequent to such payments, merely on the grounds, that the approval so granted to the institution is withdrawn
- c) In case the amount is paid to a National Laboratory / IIT, 150% of the expenditure can be claimed as a deduction
  - ✓ A National Laboratory is a scientific laboratory functioning at the national level, under the ambit of Indian Council of Agricultural OR Medical OR Scientific Research, the Defence Research and Development Organisation (DRDO), the Department of Atomic Energy / Bio-technology are included
  - ✓ However, effective AY 2021-22, the deduction would be only 100%
- d) In case the amount is paid to a university, college or research association for scientific research, 150% of such expenditure is allowable
  - ✓ The payments made to such institutions would be allowable irrespective of whether such research is related to the assessee's business or not and irrespective of whether the expenditure is revenue or capital in nature
  - ✓ However, effective AY 2021-22, the deduction would be only 100%
- e) Where a company is engaged in the business of bio-technology or in the business of manufacture or production of any article / thing, not being one which is specified in the eleventh schedule, incurs any expenditure on scientific research, OR in-house research & development facility as may be approved by the prescribed authority, a weighted deduction of 150% is allowable in the Previous Year.

- ✓ No deduction is allowable in case of any expenditure that is towards acquisition of land
- ✓ Expenditure in case of drugs and pharmaceuticals shall include the expenditure of clinical drug trial, obtaining approvals from any state regulatory authority, and filing an application under the Patents Act, 1970

**Summary with Sections Sequentially**

Section	Expenditure Incurred for / Payment made	Deduction
35(1)(i)	Revenue Expenditure incurred on scientific research related to assessee's business	100%
35(1)(ii)	Research Association for Scientific Research	150%
35(1)(ia)	Paid to Company for Scientific Research	100%
35(1)(iii)	Research Association for Social Science OR Statistical Research	100%
35(1)(iv)	Capital Expenditure (except land acquisition)	100%
35(2AA)	National Laboratory / IIT for scientific research undertaken under an approved programme	150%
35(2AB)	Expenditure incurred by a company engaged in Bio-technology	150%

**Illustration**

Binod furnishes the following particulars for PY 2019-20. You are required to arrive at the deduction allowable u/s 35 for AY 2020-21, while computing the Income under the head "Profits / Gains from Business / Profession".

- 1) Amount paid to M/s ABC Ltd., a company registered in India, which has as it's main object, scientific research and development, as approved by the prescribed authority INR 600,000
- 2) Amount Paid to IIT Mumbai, for an approved scientific research programme INR 375,000
- 3) Revenue Expenditure on In-house R&D facility as approved by prescribed authority INR 450,000
- 4) Capital Expenditure on In-house R&D facility as approved by prescribed authority INR 12,00,000. This includes cost of Land INR 450,000
- 5) Amount paid to Indian Institute of Science, Bangalore, for Scientific Research INR 10,00,000

Expenditure	INR	Allowable Sec	Deduction
Amount paid to M/s ABC Ltd., a company registered in India, which has as it's main object, scientific research and development, as approved by the prescribed authority	6,00,000	100% 35(1)(ia)	6,00,000
Amount Paid to IIT Mumbai, for an approved scientific research programme	3,75,000	150% 35(2AA)	5,62,500
Revenue Expenditure on In-house R&D facility as approved by prescribed authority	4,50,000	100% 35(1)(i)	4,50,000
Capital Expenditure on In-house R&D facility as approved by prescribed authority	7,50,000	100% 35(1)(iv)	7,50,000
Amount paid to Indian Institute of Science, Bangalore for Scientific Research	10,00,000	150% 35(1)(ii)	15,00,000
<b>Totals</b>	<b>31,75,000</b>		<b>38,62,500</b>

### Amortization of Spectrum Fees for Purchase of Spectrum

New section 35ABA is inserted to provide amortization of amount paid on the acquisition of any right to use spectrum for telecommunication services by paying spectrum fees. The section provides :

- i. Any capital expenditure incurred and actually paid by the assessee on acquisition of any right of use spectrum for Telecom services by paying spectrum fee will be allowed as deduction in equal instalments. Deduction will start from the year in which payment is made (or the year of commencement of business, whichever is later) and ending with the year in which spectrum comes to an end, irrespective of the previous year in which liability for expenditure was incurred according to the method of accounting regularly followed by assessee or payable in such manner as may be prescribed.
- ii. Where the spectrum is transferred and the proceeds of transfer are less than the expenditure remaining unallowed, a deduction equal to the expenditure remaining unallowed as reduced by the proceeds of transfer, shall be allowed in the year of transfer of spectrum.
- iii. If spectrum is transferred and proceeds of transfer exceed the amount of expenditure remaining unallowed, the excess amount (to the extent it does not exceed deduction claimed u/s 35ABA) shall be chargeable to tax as profits and gains of business in the previous year in which such spectrum has been transferred.
- iv. Unallowed expenditure in a case where a part of spectrum is transferred would be amortised.
- v. Where the deduction has been claimed and granted to the assessee in accordance with the provisions of this section and, subsequently, there is failure to comply with any of the provisions of this section, then the deduction shall be deemed to have been wrongly allowed. In such case, the assessing officer can re-compute the total income of the assessee for the previous year (in which deduction was claimed) and make necessary rectification. Such rectification can be made within 4 years from the end of the previous year in which failure takes place.
- vi. Under the scheme of amalgamation, if the amalgamating company sells or transfers the spectrum to an amalgamated company, being an Indian company, then the provisions of this section shall apply the amalgamated company as they would have applied to the amalgamating company if later had not transferred the spectrum. Similar rule will be applicable in case of demerger.

Where, in a previous year, any deduction has been claimed and granted to the assessee under sub-section (1), and, subsequently, there is failure to comply with any of the provisions of this section, then, -

- (a) the deduction shall be deemed to have been wrongly allowed;
- (b) the Assessing Officer may, notwithstanding anything contained in this Act, re-compute the total income of the assessee for the said previous year and make the necessary rectification;
- (c) the provisions of section 154 shall, so far as may be, apply and the period of four years specified in subsection (7) of that section being reckoned from the end of the previous year in which the failure to comply with the provisions of this section takes place.

### Expenditure on telecom licence (Section 35ABB)

Where any capital expenditure is incurred by the assessee for acquiring any right to operate telecommunications services and for which payment has actually been made to obtain a licence, a deduction will be allowed in equal instalments over the period for which the licence remains in force, subject to the following:

- (a) If the fee is paid for acquiring any right to operate telecommunications services before the commencement of such business, the deduction shall be allowed for the previous years beginning with the previous year in which such business is commenced.

- (b) If the fee is paid for acquiring such rights after the commencement of such business the deduction shall be allowed for the previous years beginning with the previous year in which the license fee is actually paid (irrespective of the previous year in which the liability for the expenditure is incurred).

**Profit/loss on Sale -**

- Where the licence is transferred and proceeds of transfer (sale proceeds) are less than the amount of expenditure incurred remaining unallowed:
  - (i) Where whole of the licence is transferred in a previous year. Deduction as given below shall be allowed in the previous year in which the licence is transferred.  
Expenditure remaining unallowed less sale proceeds.
  - (ii) Where part of the licence is transferred in a previous year. Deduction as given below shall be allowed in the balance number of relevant previous years.  
(expenditure remaining unallowed less sale proceeds) divided by balance number of relevant previous years, i.e., the previous years not expired at the beginning of the year of transfer.
- Where the licence is transferred and the proceeds of transfer (sale proceeds) exceed the amount of expenditure incurred remaining unallowed.  
Sale proceeds less expenditure remaining unallowed subject to deductions already allowed shall be chargeable to income tax as profits and gains of the business in the previous year in which licence is transferred. Consequently, no further deduction in the previous year in which licence is transferred or in any subsequent previous years is allowed.  
Where licence is transferred in a previous year in which the business is no longer in existence, the provisions of this sub-section shall apply as if the business is in existence in that previous year.
- Where under a scheme of amalgamation a telecom licence is transferred by the amalgamating company to the amalgamated company (being an Indian company), then deduction will not be available under this section to the amalgamating company, instead the provisions of this Section (35ABB) will continue to apply to the amalgamated company as they would have applied to the amalgamating company if the latter had not transferred the licence.
- Similarly in a scheme of demerger a telecom licence is transferred by the demerged company to the resulting company, then deduction will not be available to the demerged company and will instead apply to the resulting company as they would have applied to the demerged company if the latter had not transferred the licence.

Further where a deduction for any previous year is claimed and allowed under Section 35ABB, then no deduction under Section 32(1) shall be allowed for the same or any subsequent previous year.

**Expenditure of capital nature incurred in respect of specified business (Section 35AD)**

An assessee shall be allowed a deduction of capital nature expenditure incurred for any specified business carried on by him during the previous year in which such expenditure is incurred by him. This section talks about investment linked incentives for specified businesses as under:

- A) Setting up & operating cold chain facilities for specified products
- B) Setting up & operating warehousing facilities for agricultural produce
- C) Laying and operating a cross-country natural gas or crude or petroleum oil pipeline network for storage and distribution, as a part of the network
- D) Building and operating a 2-star hotel or above, anywhere in India

- E) Building and operating a hospital with > 100 beds, anywhere in India
- F) Developing & building a housing project under a scheme for slum redevelopment / affordable housing
- G) Production of fertilizers in India
- H) Setting up and operating an Inland Container Depot OR a Container Freight Station, under Customs Act, 1962
- I) Bee-keeping and production of honey and beeswax
- J) Setting up and operating a warehousing facility for storage of sugar
- K) Laying and operating a slurry pipeline for transportation of iron-ore
- L) Setting up and operating a semi-conductor wafer fabrication manufacturing unit
- M) Developing / Maintaining & Operating / Developing & Maintaining & Operating a new infrastructure facility in India

100% of the capital expenditure incurred during the Previous Year, wholly and exclusively for the above businesses would be allowable as a deduction.

The expenditure incurred prior to the commencement of the business, would be allowed as a deduction in the year of commencement of business, and should also be capitalised in the books of the assessee on the commencement of operations.

The loss from specified businesses can be set off ONLY against profits of specified businesses but can be carried forward indefinitely for set off against one or more specified businesses.

The above deduction is allowable only if accounts of the assessee are audited by a Chartered Accountant and that any asset in respect of which the deduction is claimed, can be used ONLY for the specified businesses for a period of 8 years beginning with the PY in which the asset was acquired / constructed.

### Exceptions

- Expenditure on acquisition of land OR goodwill will not be allowed as a deduction
- Any expenditure where the aggregate of payments made to a person exceeding INR 10000 per day, otherwise than by account payee cheque / DD / ECS / or such other electronic mode as may be prescribed would not be eligible for a deduction

Any asset in respect of which a deduction is claimed and allowed under Section 35AD, shall be used only for the specified business for a period of eight years beginning with the previous year in which such asset is acquired or constructed.

If any asset on which a deduction under section 35AD has been allowed, is used for any purpose other than the specified business, the total amount of deduction so claimed and allowed in one or more previous years in respect of such asset, as reduced by the amount of depreciation allowable in accordance with the provisions of section 32 as if no deduction had been allowed under section 35AD, shall be deemed to be income of the assessee chargeable under the head "Profits and gains of business or profession" of the previous year in which the asset is so used.

**Example:** Suppose a company purchased plant and machinery for Rs 2 crores for a specified business, and claimed deduction under section 35AD. However, the very next year the plant and machinery purchased was put to use for unspecified business.

In this case, since the machinery has been used for unspecified business, the deduction claimed under section 35AD will be disallowed. However, the amount of deduction to be disallowed will be reduced by the depreciation allowable in accordance with the provisions of section 32.

Deduction claimed under section 35AD on a capital asset:	Rs. 2,00,00,000
Depreciation eligible will be @15%:	Rs. 30,00,000
Profit chargeable to tax in accordance with the sub-section (7B) of section 35AD:	Rs. 1,70,00,000

### **Expenditure by way of Payment to Associations and Institutions for carrying out Rural Development Programmes (Section 35CCA)**

Any sum paid to a rural development fund set up and notified by the Central Government and to the National Urban Poverty Eradication Fund similarly set up and notified qualifies for deduction on fulfilment of certain conditions.

### **Expenditure on Agricultural extension project (Section 35CCC)**

Where an assessee incurs any expenditure on agricultural extension project notified by the Board then, there shall be allowed a deduction of a sum equal to 150% of such expenditure. [w.e.f. AY 2021-22 deduction under section 35CCC is restricted to 100% only - Amendment vide Finance Act, 2016].

### **Expenditure on skill development project (Section 35CCD)**

Where a company incurs any expenditure (not being expenditure in the nature of cost of any land or building) on any skill development project notified by the Board then, there shall be allowed a deduction of a sum equal to 150% of such expenditure. [w.e.f. AY 2021-22 deduction under section 35CCD is restricted to 100% only - Amendment vide Finance Act, 2016].

### **Amortization of Preliminary Expenses (Section 35D)**

Under Section 35D, Indian companies and other non-corporate taxpayers resident in India would be entitled to amortisation of certain preliminary expenses incurred by them for the establishment of business concerns or the expansion of the business of existing concerns.

The expenditure which qualifies for amortisation should have been incurred by the assessee before the commencement of his business. If, however, the expenditure is incurred after the commencement of business, it is essential that the expenditure should be in connection with the extension or expansion of the undertaking of the assessee or in connection with the setting up of a new unit by the assessee.

The amount qualifying for amortisation would be allowable as a deduction in five equal instalments beginning with the previous year in which the business of the assessee actually commences or the previous year in which the extension of the present undertaking is completed or the new unit commences production or operation, as the case may be.

The following expenses incurred by the assessee, qualify for amortisation under this section as preliminary expenses:

- (i) Expenses in connection with the preparation of feasibility report or project report;
- (ii) Expenses for conducting market survey or any other survey necessary for the purpose of the business of the assessee;
- (iii) expenditure for getting engineering services related to the business of the assessee;
- (iv) expenses by way of legal charges for drafting any agreement between the assessee and any other person for any purpose relating to the setting up or conduct of the business of the assessee;
- (v) in the case of a company
  - (a) expenses by way of legal charges for drafting the Memorandum and Articles of Association of the Company;

- (b) expenses for printing the Memorandum and Articles of Association;
  - (c) expenses by way of fees for registration of the company under Companies Act, and
  - (d) expenditure incurred in connection with issue for public subscription of shares or debentures of the company, being underwriting commission, brokerage and the charges of drafting, typing, printing and advertisement of the prospectus; and
- (vi) such other items of expenses not covered by the list specified above which the Central Board of Direct Taxes may prescribe for the purpose of amortisation under this section.

### **Amount qualifying for deduction:**

The maximum aggregate amount of the qualifying expenses that can be amortised has been fixed at 5% of the cost of the project or in the case of an Indian company, or, at the option of the company, 5% of the capital employed in the business of the company, whichever is higher. The excess, if any, of the qualifying expenses shall be ignored.

For the purpose of amortisation, the expression “Cost of the Project” in relation to the expenses incurred before the commencement of the business means the actual cost of the fixed assets being land, buildings, lease holds, plant, machinery, furniture, fittings and railway sidings, including expenditure on the development of land and buildings, which are shown in the books of accounts of the assessee as on the last day of the accounting year in which the business of the assessee actually commences. Where the expenses are incurred after the commencement of business either in connection with the extension of the present undertaking or in connection with the setting up of a new unit, the cost of the project should be taken to mean the actual cost of the fixed assets, being land, buildings, lease holds, plant, machinery, furniture, fittings and railway sidings, including expenditure on the development of the land and building which are shown in the books of the assessee as on the last day of the previous year in which extension of the undertaking is completed or the new unit commences production or operations, as the case may be, to the extent to which such fixed assets have been acquired or developed in connection with the extension of the undertaking or the setting up of the new unit of the assessee.

In the case of company, the “capital employed” in the business means where preliminary expenses have been incurred before the commencement of the business, the aggregate of the issued share capital, debentures and long-term borrowings as on the last day of the accounting year in which the business of the company has actually commenced. In cases where the expenditure has been incurred after the commencement of the business, the capital employed in the business of the company should be taken to be the aggregate of the issued share capital, debentures and long-term borrowings as on the last day of the accounting year in which the extension of the undertaking is completed or, as the case may be, the new unit commences production or operation, to the extent to which the capital, debentures and long-term borrowings have been issued or obtained in connection with the extension of the undertaking or setting up of the new unit of the company.

The expression “long-term borrowings” to be included as part of the capital employed in the business of the company should be taken to mean:

- (i) any moneys borrowed by the company from the Government or the Industrial Finance Corporation of India or Industrial Credit and Investment Corporation of India or any other financial institution which is eligible for deduction under Section 36(1)(vii) of the Act or any banking institution; or
- (ii) any moneys borrowed or debt incurred by the company in a foreign country in respect of the purchases outside India of capital plant and machinery where the terms of the borrowing provide for repayment of the money borrowed or debt incurred over a period of not less than seven years.

The allowance towards amortisation of preliminary expenses is subject to the condition that the accounts of the assessee for the year or years in which the preliminary expenses are incurred have been audited by a Chartered Accountant or other accountant specified in Section 288(2) of the Act and, in addition, the assessee furnishes along with his return of income for the first year in which the deduction is claimed, the report of audit in the prescribed form, duly signed and verified by the auditor and setting out such other particulars as have been prescribed by the Board for this purpose.

In cases of amalgamation as defined in Section 2(1B) of the Act, where the undertaking of an Indian Company has been transferred before the expiry of ten years, the amalgamating company would not be entitled to the allowance towards amortisation of preliminary expenses in the year in which the amalgamation takes place. But the amalgamated company would be entitled to the allowance for the remaining period over which the allowance under this section is available. The total period over which the amortisation is allowable should not exceed ten years or five years as the case may be in the case of both the amalgamating company and the amalgamated company. The allowance under this section would not be denied, in cases of amalgamation, to the amalgamated company merely because the expenditure has not actually been incurred by the amalgamated company. Similarly, in case of demerger where an undertaking of an Indian company which is entitled to the deduction under this section is transferred before the expiry of the said period of 10 years or 5 years (as the case may be), to another company in a scheme of demerger no deduction shall be admissible to the demerged company in the year in which the demerger takes place. The resulting company would be entitled to claim deduction for the balance period under this section. In other words, the deduction for the balance period will be available to resulting company as it would have been available to demerged company, if the demerger had not taken place. In cases where preliminary expenses qualify for amortisation under Section 35D and the allowance claimed by the assessee in this regard is allowed in any assessment year, these expenses would not qualify for any allowance or deduction in respect of any other assessment year or even in the same year under any other provision of the Income-tax Act, 1961.

**Amortisation of Expenditure in the case of Voluntary Retirement Scheme (Section 35DDA)**

One-fifth of the expenditure incurred by an assessee-employer in any previous year in the form of payment to any employee in connection with his voluntary retirement in accordance with a scheme of voluntary retirement, shall be allowed as deduction in that previous year and the balance in four equal installments in the immediately four succeeding previous years.

**Other Deductions [Section 36]**

The other deductions allowable while computing the income from business/professions are as follows :

Type & Section	Deductions
Insurance Premia paid u/s 36(1)(i)	Premia paid on insurance policy to cover risk of damage / destruction to stock / stores of the business.
Premia paid by employer for health insurance of employees u/s 36 (1) (ib)	Premia paid by employer by any mode other than by cash, on health insurance of it's employees, in accordance with the scheme framed by GIC of India, or approved by the IRDA
Bonus & Commission u/s 36 (1)(ii)	Deductible in full as long as the bonus / commission shall not be payable to them as profits / dividends, if it had not been paid as bonus / commission
Interest on Borrowed Capital u/s 36(1)(iii)	Deduction allowed for any interest paid in respect of capital borrowed for business. In case the capital is borrowed for acquiring an asset, the interest is capitalised from the date of borrowing until the date when the asset is put to use. Post the "put to use" date, it cannot be capitalised anymore and then such interest becomes an allowable deduction

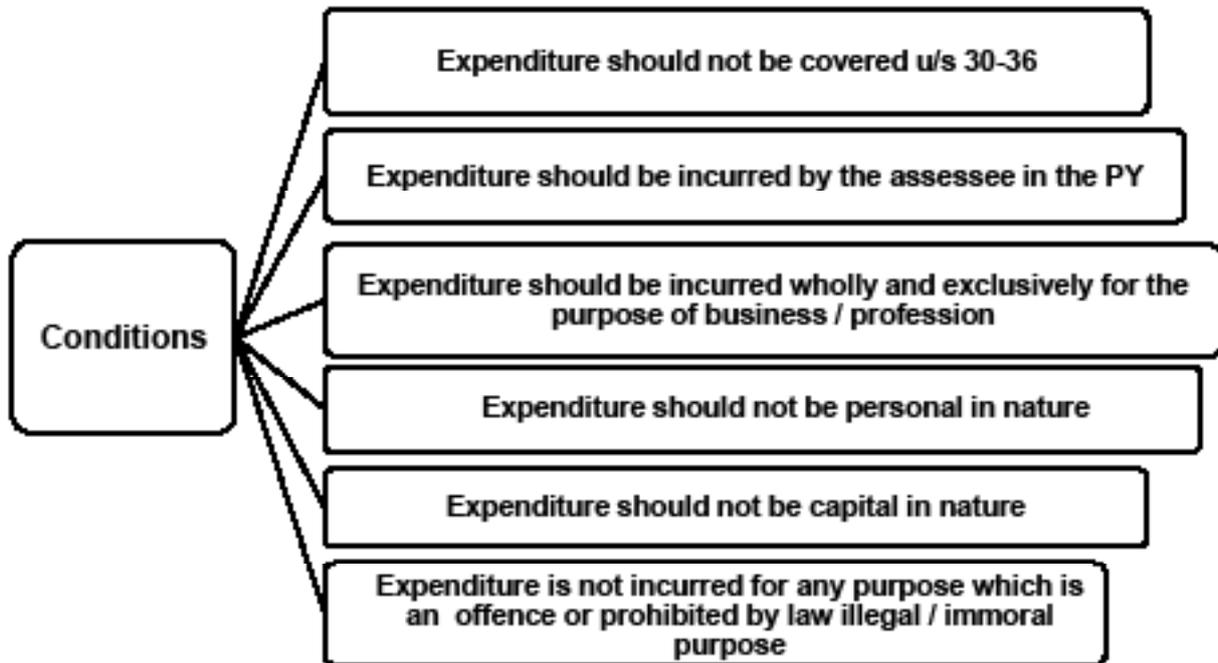
Discount on Zero Coupon Bonds u/s 36(1)(iiia)	Difference between the issue and the redemption values, as these are issued at a discount and redeemed at par. Available to Infra. Companies / funds / Scheduled Banks, starting from the date of issue of the bond, ending with the maturity / redemption.
Contribution to Provident & Other funds u/s 36(1)(iv) & (v)	Allowable if the fund is settled upon a trust, it should be recognised / approved, and the contributions should be periodic, and as long as the fund is for the benefit of the employees
Employer's contribution to the a/c of the employee under a pension scheme referred to in Section 80CCD [Section 36(1)(va)]	Deduction is restricted to 10% of salary of employee in PY. Salary, here, would include ONLY Basic & DA (if the terms of employment provide).
Employee's Contribution to Welfare Funds [Section 36(1)(va)]	Deemed as business income of the employer assessee and will be allowed as a deduction ONLY if the employee contributions have been credited to the employees' account by the assessee in the fund, on or before the due date under the respective welfare acts.
Bad Debts u/s 36(1)(vii) & 36(2)	Allowable if the debts written off as irrecoverable in the accounts of the assessee pertain to the business / profession carried on during the PY and as long as the debt was considered in the income for the PY in which it was earned. If on the final settlement, the amount recovered on any debt falls short of the total debt minus the debt allowed, the deficiency will be allowed as a deduction in the year of recovery and if the amount so recovered is more than the amount due after the allowance has been made, the excess will be chargeable to tax in the
Expenses on family planning [Section 36(1)(ix)]	If the expenditure is capital in nature, allowable in five equal instalments beginning the PY in which it was incurred and if revenue in nature, it shall be fully allowable in the PY in which it was incurred. The deduction is allowable to corporate assessees ONLY.
Securities Transaction Tax [Section 36(1)(xv)]	Allowable in respect of transactions entered in the course of business, as long as the income from the taxable securities' transactions, in respect of which it was incurred, is included under the heads "Profits / Gains from Business / Profession"
Commodities Transaction Tax [Section 36(1)(xvi)]	Allowable in respect of transactions entered in the course of business, as long as the income from the taxable commodities' transactions, in respect of which it was incurred, is included under the heads "Profits / Gains from Business / Profession"

### Other Expenses (Section 37)

Section 37(1) of the Income-tax Act provides for allowance in respect of any other item of expenditure not covered by any of the provisions contained in Sections 30 to 36 discussed above and is limited to the amount actually expended during the Previous Year.

This deduction is subject to the following conditions:

## Conditions



### Note:

- 1) Corporate Social Responsibility (CSR) expenditure is not construed to have been incurred for the purposes of business / profession and hence will be disallowed, and will be allowed aptly under the relevant Sec's 30-36
- 2) Any advertisement expenditure in souvenirs of political parties, representing contributions for political purposes, would be disallowed

### Some of the examples of allowable expenses under Section 37(1) are:

- (i) Expenditure incurred on raising loans or issuing debentures but not on issuing share capital.
- (ii) Legal expenses incurred:
  - (a) to avoid a business liability, e.g. for alleged breach of a trading contract;
  - (b) to defend the assessee's title to his assets, e.g. land, building, etc.;
  - (c) to secure the termination of a disadvantageous trading relationship, e.g. removal of an undesirable employee;
  - (d) by a director of a company in defending a suit brought to challenge the validity of his election to the directorship;
  - (e) to protect the capital asset of the business which has already been acquired;
  - (f) by a company in resisting a winding up petition by some shareholders;
  - (g) for defending monopoly rights;
  - (h) incurred in restraining another company from using assessee's trade mark.

However, the expenses incurred in criminal proceedings are not allowable. Legal expenses relating to acquisition of capital asset for a business are capital expenses and as such, not allowable.

In this connection the Supreme Court held that-where litigation expenses are incurred by the assessee for the purpose of creating, curing or completing his title to the capital, then the expenses incurred must be considered as capital expenditure. But if the litigation expenses are incurred to protect the business of the assessee, they must be considered as a revenue expenditure. [Dalmia Jain & Co. v. C.I.T. (1971) 81 ITR p. 754 (S.C.)].

Expenditure for prosecuting civil proceedings is deductible provided the expenditure was laid out for the purpose of the business wholly and exclusively i.e. to promote the interest of the business. [Sree Meenakshi Mills v. C.I.T. (1976) 63 ITR, p. 207 (S.C.)]

- (iii) Bonus to employees under an industrial award.
- (iv) Expenses for the installation of new telephone.
- (v) Sales tax is an admissible deduction but not estate duty.
- (vi) Interest on unpaid purchase price of goods or capital assets.
- (vii) Expenditure incurred to oppose nationalization or to prevent extinction of business. However, the donations given for the political parties or for political cause are not admissible deductions under Section 37.
- (viii) Subscriptions given are allowed if their payment is compulsory or commercially expedient and of benefit to the payer.
- (ix) Expenses incurred on the occasion of festival or customary days are allowed up to a reasonable amount keeping in view the size of the business and subject to the satisfaction of the Assessing Officer that the expenses are not expenses of personal, social or religions nature.
- (x) Recurring expenses incurred on imparting basic training to apprentices under the Apprentices Act, 1961 is deductible.
- (xi) Initial expenditure on the first installation of fluorescent tube lights is treated as Capital expenditure and hence not deductible but all subsequent expenditure for replacement of tubes is treated as revenue expenditure and hence deductible.
- (xii) Loss through embezzlement by an employee is deductible.
- (xiii) Professional tax paid by a person carrying on business or trade is allowed as deduction.
- (xiv) Annual listing fee paid to stock exchange is allowed as deduction.
- (xv) Expenses incurred on Civil defence measures as specified by the Board, even when there is no emergency, is deductible.
- (xvi) Brokerage paid for raising loan to finance business.
- (xvii) Stamp and registration charges for the purpose of entering into agreement for obtaining overdraft facilities.
- (xviii) Security deposited with postal authorities for telex connection deductible as business expenditure.  
However, when the amount is returned by postal authorities, when the telex connection is finally closed, the refund shall be treated as an income of the assessee of the year in which the amount is refunded.
- (xix) Compensation payable as a result of negligence in carrying on a business or termination of an employee, director or agent.
- (xx) Compensation to an employee for injury sustained or accident met with while on duty.
- (xxi) Royalty paid for mining, patents or copyrights.

- (xxii) Insurance premiums: Premium for insurance of building, plant, machinery, furniture, stock or stores are allowable under specific sections, e.g., premium paid by a businessman under a policy insuring its employees or experts against death or injury, or insuring the employer against liability for compensation in respect of accidents to its workmen or against loss of trading licence.
- (xxiii) Penalty paid by the assessee for saving from confiscation of the goods which he has purchased from a third-party without knowing that they had been illegally imported.
- (xxiv) Pension, gratuity or other voluntary payment made to the employees are deductible but a gratuity paid to a single employee when it was not the practice of the business was treated as disallowable expense. In the same way voluntary pensions and lump sum payments made by a company to its employees on its winding up were not allowed.
- (xxv) Bona fide expenditure of a revenue nature incurred for the welfare of employees on its winding up was not allowed.
- (xxvi) Excessive price paid out of extra commercial considerations shall be disallowed.
- (xxvii) Sum paid by the assessee as a surety when it is not part of his business shall be disallowed.
- (xxviii) Presents given to employees by way of gift and not as perquisites for services rendered, shall be disallowed.

### Certain Allowable Losses

Losses which are directly incidental to the business or profession of the assessee are allowable. Following are some examples of such losses:

- (1) **Robbery or Dacoity:** Loss caused by robbery or dacoity is not deductible. But, if it is incidental to business it will be allowed as a deduction and this depends upon the specific circumstances and conditions. For example, if cash is sent for disbursement at different centers by a sugar factory in rural area, it is incidental to business and is, therefore, allowed. Any loss due to robbery in a bank will be allowed as the bank is under an obligation to maintain some cash outside the storeroom for payments.
- (2) **Embezzlement, Theft, etc.:** The loss of money due to embezzlement by an employee handling the funds of the business while discharging his official duties is allowed as deduction. It is deductible when discovered. When an employee goes to bank to deposit the cash or takes cash with him for disbursement and he takes away the money for his own use, even then, the loss is allowable. Theft by a cashier, who is in charge of cash is also an allowable loss. A theft committed either by an employee or by someone else by breaking open into the business premises after office hours, is also allowable.
- (3) **Loss due to Non-recovery of advances:** If it is the practice in a business to give advance money to the suppliers and if the supplier neither supplies the order nor refunds the advance money, the loss sustained by the assessee is incidental to business and is, therefore, allowable.

### EXPENSES DISALLOWED (SECTION 40)

The following expenses shall not be deducted in computing the income chargeable under the head “profits and gains of business or profession:

- **Interest, royalty, fees for technical services payable outside India:** Under Section 40(a)(i), deduction is not allowed in respect of any interest, royalty, fees for technical services or other sum chargeable under the Income-tax Act, which is payable outside India or in India to a non-resident non-corporate or to a foreign company and on which tax has not been deducted or after deduction, has not been paid as specified in subsection (1) of section 139.

Provided that where in respect of any such sum, tax has been deducted in any subsequent year or has been deducted in the previous year but paid after the due date specified in sub-section (1) of section 139, such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.

Provided further that where an assessee fails to deduct the whole or any part of the tax in accordance with the provisions of Chapter XVII-B on any such sum but is not deemed to be an assessee in default under the first proviso to sub-section (1) of section 201, then, for the purpose of this sub-clause, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the payee referred to in the said proviso.

Since the date of furnishing the return of income by the payee is taken to be the date on which the payer has deducted tax at source and paid the same, such expenditure/payment in respect of which the payer has failed to deduct tax at source shall be disallowed under section 40(a)(i) in the year in which the said expenditure is incurred. However, such expenditure will be allowed as deduction in the subsequent year in which the return of income is furnished by the payee, since tax is deemed to have been deducted and paid by the payer in that year.

- **TDS not deducted on any sum payable to a RESIDENT: Under section 40(a)(ia)**, 30% of any sum payable to a resident on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction, has not been paid on or before the due date specified in sub-section (1) of section 139.

**Provided that where in respect of any such sum, tax has been deducted** in any subsequent year or has been deducted during the previous year but paid after the due date specified in sub-section (1) of section 139, 30% of such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.

Provided further that where an assessee fails to deduct the whole or any part of the tax in accordance with the provisions of Chapter XVII-B on any such sum but is not deemed to be an assessee in default under the first proviso to sub-section (1) of section 201, then, for the purpose of this sub-clause, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the resident payee referred to in the said proviso.

For Example: tax on rent paid to Mr. A, a resident, has been deducted during the previous year 2019-20, the same has to be paid by 31st July/ 30th September 2020, as the case may be. Otherwise, 30% of rent paid would be disallowed in computing the income for A.Y.2020-21. If in respect of such rent, tax deducted during the P.Y.2019-20 has been paid after 31st July/ 30th September, 2020, 30% of such rent would be allowed as deduction in the year of payment.

Since the date of furnishing the return of income by the payee is taken to be the date on which the payer has deducted tax at source and paid the same, 30% of such expenditure/payment in respect of which the payer has failed to deduct tax at source shall be disallowed under section 40(a)(ia) in the year in which the said expenditure is incurred. However, 30% of such expenditure will be allowed as deduction in the subsequent year in which the return of income is furnished by the payee, since tax is deemed to have been deducted and paid by the payer in that year.

- **Rate or Tax Paid on Profits:** Under Section 40(a)(ii), any sum paid by the assessee on account of any tax or rate levied on profits on the basis of or in proportion to the profits and gains of any business or profession, would be disallowed in full. For example, income-tax, foreign income-tax or a professional tax levied under the Municipal Act on persons who exercise a profession, trade or calling within the municipal limit shall be disallowed.

Explanation 1 to sub-clause (ii) of clause (a) of Section 40 clarifies that any sum paid outside India and

eligible for relief of tax under Section 90 or deduction from the Income Tax payable under Section 91 is not allowable and deemed to have never been allowable as a deduction under Section 40 of the Income Tax Act. However, the tax payers will continue to be eligible for tax credit in respect of Income Tax paid in a foreign country in accordance with the provisions of Section 90 or Section 91 as the case may be.

Explanation 2 provides that any sum paid outside India and eligible for relief of tax under new Section 90A will not be allowed as a deduction in computation of profit and gains from business or professions.

Under section 40(a)(iib), any amount paid by way of fee, charge, etc., which is levied exclusively on, or any amount appropriated, directly or indirectly, from a State Government undertaking, by the State Government, shall not be allowed as deduction for the purposes of computation of income of such undertakings under the head “Profits and gains of business or profession”.

A State Government undertaking includes –

- (a) A corporation established by or under any Act of the State Government;
- (b) A company in which more than 50% of the paid up equity share capital is held by the State Government;
- (c) A company in which more than 50% of the paid up equity share capital is held singly or jointly by (a) or (b);
- (d) A company or corporation in which the State Government has the right to appoint the majority of directors or to control the management or policy decisions

An authority, a board or an institution or a body established or constituted by or under any Act of the State Government or owned or controlled by the State Government.

- **Salaries [Section 40a(iii)]:** Any payment which is chargeable under the head “salaries” if it is payable outside India or to a non-resident and if the tax has not been paid thereon or deducted thereon under Chapter XVIIIB of the Act.
- **Payment to Provident Funds etc. [Section 40a(iv)]:** Any payment to a Provident Fund or other fund established for the benefit of employees of the assessee would be disallowed in cases where the assessee (employer) has not made effective arrangements to secure deduction of tax at source from any payment made from the fund which are chargeable to tax under the head “salaries” in the hands of the employees.

- **Payment of tax on non-monetary perquisites [Section 40a(v)]:**

In case of an employee, deriving income in the nature of perquisites (other than monetary payments), the amount of tax on such income paid by his employer is exempt from tax in the hands of that employee.

Correspondingly, such payment is not allowed as deduction from the income of the employer. Thus, the payment of tax on perquisites by an employer on behalf of employee will be exempt from tax in the hands of employee but will not be allowable as deduction in the hands of the employer.

- **Payment to Partners:** The provision of Section 40(b) in the case of a firm which is assessable as such or LLP the following **amounts shall not be deducted in computing the business income of the Firm/LLP:**
  - (a) Any payment of salary, bonus, commission or remuneration to non- working partner
  - (b) Remuneration paid to a working partner or interest paid to any partner which is not authorised by or not in accordance with the terms of the partnership deed
  - (c) any remuneration paid to a working partner or interest paid to any partner which is authorised by

or is in accordance with the terms of the partnership deed but which relates to any period falling prior to the date of such partnership deed

- (d) any interest which is paid in accordance with the terms of the partnership deed and relates to any period falling after the date of such partnership deed but which is in excess of simple interest @ 12% p.a..
- (e) any remuneration to a working partner which is authorised by and is in accordance with the terms of the partnership deed and in relation to any period falling after the date of partnership deed is an allowable deduction subject however, to the condition that the maximum amount of such payment made to all the partners during the previous year should not exceed the limits given below:

Quantum of Book Profit	Amount
(a) Up to Rs. 3,00,000 or in case of a loss	Rs. 1,50,000 or 90% of the Book profit, whichever is more
(b) on the balance	60% of book profit

For the purposes of this clause, “working partner”, means an individual who is actively engaged in conducting the affairs of the business or profession of the firm of which he is a partner; and

“Book profit” means the net profit, as shown in the profit and loss account for the relevant previous year, computed in the manner laid down in chapter IV-D (i.e. Sections 28 to 44D) as increased by the aggregate amount of remuneration paid or payable to all the partners of the firm if such amount has been deducted while computing the net profit.

For Example: A firm has paid Rs. 8 lakhs as remuneration to its partners for the P.Y.2019-20, in accordance with its partnership deed, and it has a book profit of Rs. 10 lakh. Now the allowable remuneration calculated as per the limits specified in section 40(b):

On first Rs.3 lakh of book profit [ Rs. 3,00,000 × 90%]	= Rs. 2,70,000
On balance Rs. 7 lakh of book profit [ Rs. 7,00,000 × 60%]	= Rs. 4,20,000
Total	= Rs. 6,90,000

So the excess amount of Rs. 1,10,000 (i.e., Rs.8,00,000 – Rs. 6,90,000) would be disallowed as per section 40(b)

- **Payment by AOPs / BOIs [Section 40(ba)]:** In the case of an association of persons or body of individuals (other than a company or a Co-operative Society or a society registered under the Societies Registration Act, 1860, or under any law corresponding to that Act in force in any part of India) any payment of interest, salary, bonus, commission or remuneration, by whatever name called, made by such association or body to its member shall not be allowed as a deduction in computing the income of such association or body.

As per explanation 1 to clause (ba) of Section 40 of the Income-tax Act, where interest is paid by the association or body to any member thereof, who has also paid interest to the association or body, the disallowance shall be restricted to the amount paid by the association or body to the member, after deducting therefrom the amount paid by the member to the association or body.

## EXPENSES RESTRICTED

(1) **Payment to Relatives or Associates [Section 40A(2)]:** (1) Where the assessee incurs any expenditure in respect of which payment has been or is to be made to any person specified below and the Assessing Officer is of the opinion that such expenditure is excessive or unreasonable, having due regard to the fair market value of the goods, services or facilities for which the payment is made or the legitimate needs of the business or

profession of the assessee or the benefit derived by or accruing to him therefrom, so much of the expenditure as is considered to be excessive or unreasonable must be disallowed in computing the assessee's income from business or profession. However the amount so disallowed would be taxable as income in the hands of the recipient. This section applies to expenditure only. It is not attracted when assessee makes a sale to specified person at a price lower than its Fair Market Value.

Domestic Transfer pricing provisions of arm length pricing shall not be applied to any expenditure in respect of which payment is made to a related party covered by section 40A(2) of the Income-tax Act.

The specified persons, the payments to whom may fall for disallowance under this section are the following:

Assessee	Specified Person
An Individual	a. any relative of the individual assessee b. Any person who carries on a business or profession, if individual assessee or any of his relative has a substantial interest in the business of that person
Company, firm, association of persons or H.U.F	a. any director of the company, partner of the firm, member of the association or family, or any relative of such director, partner or member b. In case of a company assessee, any individual who has substantial interest in the business or profession of the company or any relative of such individual
All Assessee	a. Any Person who has a substantial interest in the business or profession of the assessee or any relative of such Person b. Other related persons of such person, who has a substantial interest in the assessee's business like <ul style="list-style-type: none"> <li>- director of such company, partner of such firm or the member of such family or association.</li> <li>- any relative of such director, partner or member</li> <li>- Any other company carrying on business or profession in which the first mentioned company has a substantial interest</li> </ul>

Note :

- a. substantial interest in a business or profession means- (i) in cases where the business or profession is carried on by a company, if such person is the beneficial owner at any time during the relevant accounting year of equity shares carrying not less than 20% of the total voting power, and (ii) in other cases, if such person is at any time during the accounting year, beneficially entitled to not less than 20% of the profits of such business or profession.
- b. Relative in relation to an Individual means the spouse, brother or sister or any lineal ascendant or descendant of that individual.

**(2) Cash Payments exceeding Rs. 10,000 [Section 40A(3)]:**

Where the assessee incurs any expenditure in respect of which a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or account payee bank draft, or such other electronic modes as may be prescribed exceeds ten thousand rupees, no deduction shall be allowed in respect of such expenditure.

Where an allowance has been made in the assessment for any year in respect of any liability incurred by the assessee for any expenditure and subsequently during any previous year (hereinafter referred

to as subsequent year) the assessee makes payment in respect thereof, otherwise than by an account payee cheque drawn on a bank or account payee bank draft, the payment so made shall be deemed to be the profits and gains of business or profession and accordingly chargeable to income-tax as income of the subsequent year if the payment or aggregate of payments made to a person in a day, exceeds ten thousand rupees:

Provided that no disallowance shall be made and no payment shall be deemed to be the profits and gains of business or profession under sub-section (3) and this sub-section where a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or account payee bank draft or such other electronic modes as may be prescribed, exceeds ten thousand rupees, in such cases and under such circumstances as may be prescribed, having regard to the nature and extent of banking facilities available, considerations of business expediency and other relevant factors.

Provided further that in the case of payment made for plying, hiring or leasing goods carriages, the amount shall not exceed Rs. 35,000 (thirty-five thousand rupees) instead of ten thousand rupees.

Under Rule 6DD of the Income-tax Rules, the following categories of payments are exempt for the purposes of this requirement. Consequently, the provisions of Section 40A (3) do not apply to the following cases and circumstances:

- (i) Payments which are made to the Reserve Bank of India, State Bank of India or other banking institutions, including co-operative banks and land mortgage banks, primary credit societies, Life Insurance Corporation of India, Unit Trust of India and certain specified institute providing Industrial Finance.
- (ii) Payments, which under the contracts entered into prior to 1.4.1969 have to be made only in legal tender.
- (iii) Payments made to the Central or State Governments which under the Rules framed by the Government are required to be made in legal tender.
- (iv) Payments in villages and towns having no banking facility, to persons ordinarily residing or carrying on business or profession in such villages or towns.
- (v) Payments by means of book adjustment by the assessee in the account of the payee against money due to the assessee for any goods supplied or services rendered by him to the payee.
- (vi) Payments made by any Letter of Credit arrangement through bank, a mail or telegraphic transfer through bank, a book adjustment from any account in a bank to any other account in that or any other bank and a bill of exchange made payable only to a bank.
- (vii) Payments of terminal benefits made to an employee of an assessee such as gratuity, retrenchment compensation, etc. not exceeding Rs. 50,000.
- (viii) Payments made to cultivators, growers or producers for the purchase of agricultural or forest produce, animal husbandry products including hides and skins, products of dairy or poultry farming, products of horticulture or fish, products of cottage industry run without the aid of power.
- (ix) Where the payment is made to an employee temporarily but for a minimum period of fifteen days in a place other than his normal place of duty or on a ship provided tax has been deducted at source in terms of Section 192 of the Act and provided further that such employee has no bank account at such place of temporary posting or ship.
- (x) Where the payment was required to be made on a day on which the banks were closed either on account of holiday or strike.
- (xi) Where payment is made to an agent who in turn is required to make payment in cash for goods or services on behalf of the assessee.

Where an expense payable has been allowed in the assessment for any year in respect of any liability incurred by the assessee and in any subsequent year the assessee makes payment in respect thereof, otherwise than by an account payee cheque drawn on a bank or account payee bank draft or such other electronic modes as may be prescribed, the payment so made shall be deemed to be the profits and gains of business or profession and accordingly chargeable to income-tax as income of the subsequent year if the payment or aggregate of payments made to a person in a day, INR 10,000.

(3) **Provision for Gratuity [Section 40A (7)]:** No deduction shall be allowed in respect of any provision made by the assessee for the payment of gratuity to his employees on their retirement or termination of their employment for any reason. However, any provision made by the assessee for the payment of a sum by way of any contribution towards an approved gratuity fund or for the purpose of payment of any gratuity that has become payable during the previous year shall be allowed.

Where any provision made by the assessee for the payment of gratuity to his employees on their retirement or termination of their employment for any reason has been allowed as a deduction in computing the income of the assessee for any assessment year, any sum paid out of such provision by way of contribution towards an approved gratuity fund or by way of gratuity to any employee shall not be allowed as a deduction in computing the income of the assessee of the previous year in which the sum is so paid.

(4) **Restriction on contribution by employers to non-statutory funds [Sections 40A(9), (10) and (11)]:**

With a view to discouraging creation of irrevocable or discretionary trusts funds, companies, associations of persons, societies, etc. the Finance Act, 1984 has provided that no deduction shall be allowed in the computation of taxable profits in respect of any sums paid by the assessee as an employer towards the setting up or formation of or as contribution to any fund, trust, company, association of persons, body of individuals or society or any other institution for any purpose, except where such sum is paid by the assessee as an employer or contributed (within the limits laid down under the relevant provisions) to a recognised provident fund or an approved gratuity fund or an approved superannuation fund or for the purposes of and to the extent required by or under any other law.

#### **Disallowance of unpaid statutory liability (Section 43B)**

Under the income-tax law, a person carrying on a business or profession can maintain account for his income either on cash or mercantile basis. The latter, however, have to reckon with the restrictions contained in Section 43B of the Income-tax Act. This section cuts into the freedom of a business to claim certain specified expenses on due basis. The section has broadly divided the targeted expenses into two i.e., according to section 43B even if an assessee maintains books on mercantile system even then the following sums are allowed as deduction only on the basis of actual payment within the time limits specified in section 43B. In the first category are:

- (a) taxes, duties, cess or fees payable under any law;
- (b) bonus and commission to employees;
- (c) interest on any loan or borrowing from public financial institutions, state financial corporations, state industrial investment corporations, non banking financial company (deposit taking & non deposit taking NBFCs) and on any loan or advance from a scheduled bank or co-operative bank (other than primary agricultural credit society or primary co-operative agricultural and rural development bank) in accordance with the terms and conditions of the agreement governing such loan or borrowing.
- (d) leave encashment paid by employer.
- (e) any sum payable by employer by way of contribution to provident fund or super annuation fund or any other fund for welfare of employees.
- (f) Any sum payable by the assessee to the Indian Railways for use of railway assets

These expenses outstanding at the end of the previous year would be allowed as deduction only to the extent they have been actually paid on or before the due date of filing the income-tax return failing which they would be allowed in the previous year in which they have been actually paid.

The provisions of this section are applicable only to employer's contribution and are not applicable to employee's contribution for the welfare funds. Hence employer's contribution to various funds is allowed as deduction if the same is paid on or before the due date of filing return under section 139(1). However employee's contribution for the welfare funds is first deemed as income of the assessee (employer) u/s 36(1)(va) and the same is allowed deduction only when such sums are deposited by the assessee to the employee's account in the relevant fund or funds on or before the due date as per the respective welfare acts.

**Note:**

Where there is default in the payment of such interest, such interest can be converted in to a loan. Such conversion of the unpaid interest in to loan, by itself, does not constitute the payment, for purposes of Section 43B. This shall be allowed proportionately in the previous year in which the converted interest is actually paid.

Any sum payable means a sum for which the assessee incurred liability in the previous year even though such sum might not have been payable within that year under the relevant law.

### **Changes in Rate of Exchange (Section 43A)**

As per Section 43A of the Income-tax Act, where an assessee has acquired any asset in any previous year from a country outside India for the purposes of his business or profession and, in consequence of a change in the rate of exchange during any previous year after the acquisition of such asset, there is an increase or reduction in the liability of the assessee as expressed in Indian currency (as compared to the liability existing at the time of acquisition of the asset) at the time of making payment towards the whole or part of the cost of the asset or for payment of the whole or part of the moneys borrowed by him from any person directly or indirectly in any foreign currency specifically for the purpose of acquiring the capital asset. The amount by which the liability of the assessee in terms of Indian Rupees is increased or reduced as a result of change in the rate of exchange of the currency, would be added to or as the case may be deducted from the actual cost of the asset as defined in Section 43(1). Consequently, the amounts of depreciation allowable to assessee in respect of the asset would correspondingly be increased or reduced, as the case may be.

For these purposes, the expression "rate of exchange" must be taken to mean the rate of exchange determined or recognised by the Central Government for the conversion of Indian Rupee into foreign currency or vice-versa. In cases where the whole or part of the liability in respect of the payment for the cost of the asset or in respect of the money borrowed from a foreign source for acquiring the capital asset is not met by the assessee but directly or indirectly by any other person or authority, the liability so met by the other persons should not be taken into account for the purposes of any adjustment in the actual cost of the asset and consequently the depreciation allowable to the assessee arising from the change in the rate of exchange of the currency.

If, at the time of change in the rate of exchange arising on account of devaluation or otherwise the actual cost of the asset has been fully paid by the assessee and no money remains outstanding in respect of any sum borrowed specifically for the purpose, no adjustment would be permissible to the assessee. The special provision would, however, apply only in respect of capital expenditure or the value of the capital asset and would not in any way affect the value of the current assets, such as stock-in-trade or other trading assets.

The addition or deduction from the actual cost of the asset on account of change in the rate of exchange in any previous year shall be allowed to be made only on actual payment by the assessee towards the cost of the asset or repayment of the foreign loan or interest, irrespective of the method of accounting adopted by him.

## DEEMED PROFITS

Section 41 of the Income-tax Act enumerates items of notional income which are deemed to be income from business or profession chargeable to tax. The liability to tax in respect of deemed profits would arise not only during the existence of the business but also after its discontinuance. The items of deemed profits are enlisted below:

- (i) **Remission of Liability or Recoupment of Loss or Expenditure:** Where any allowance or deduction has been made in the assessment for any year in respect of losses, expenditure or trading liability incurred by the assessee and subsequently the assessee or his/its successor in business has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof during any subsequent accounting year, the amount so obtained or the value of the benefit so accruing to the assessee or his/its successor in business as the case may be, must be deemed to be the profits and gains of business or profession and must be charged to tax as the income of the assessee or his/its successor in business as the case may be for the year in which the remission or cessation takes place. This tax liability would arise irrespective of the fact whether the business or profession in respect of which the allowance or deduction has been made is being continued to be carried on by the assessee in the year of remission of liability or not. For instance, if sales tax is paid by the assessee in the year 1998-99 and the assessee gets a refund of sales-tax previously paid in the year 1999-2000, the refund would be taxable as the assessee's income of 1999-2000. But the taxability of any deemed profit on account of remission of liability or recoupment of loss would arise only if the liability in question or the amount of the loss was previously allowed as a deduction in computing the business income of the assessee. For instance, if the income-tax assessment for the year in which the expenditure or loss was claimed was made *ex parte* or was a best judgement assessment and the income was estimated, it cannot be said that the expenditure was actually allowed as a deduction in the assessment. Consequently, if there is a remission of the liability subsequently, the assessee cannot be brought to charge in respect of the same. Unilateral write off of any liability would be taxable as deemed income.
- (ii) Where any building, machinery plant or furniture owned by the assessee and used for the purpose of business for which depreciation under Section 32(1)(i) is claimed, is sold, discarded, demolished or destroyed and the money payable together with scrap value in respect of such assets exceeds the written down value, the excess to the extent of difference between the actual cost and the written down value shall be taxable as business income in the previous year in which the moneys payable become due.

Even if in the year the moneys payable becomes due, the business for which these assets were used is no longer in existence, the provisions of this section shall apply as if the business is in existence in that previous year.

- (iii) **Capital expenditure on Scientific Research:** Where an assessee incurs capital expenditure on scientific research, the entire amount of such expenditure is allowable as a deduction in computing the business income of the assessee in the same year in which the expenditure is incurred. If subsequent to the incurring of the expenditure, the asset representing the capital expenditure is sold, without having been used for other purposes, the assessee would be liable to pay tax on the excess of sale proceeds together with the deduction allowed earlier over the amount of capital expenditure or the amount of deduction allowed earlier whichever is less.

Further, the assessee is liable to pay tax on the balancing charge even if the assessee's business is not in existence during the previous year in which the money payable in respect of any asset becomes due.

**Explanation:** For the purpose of Sub-section (3) -

(1) “moneys payable in respect of any building, machinery, plant or furniture” includes -

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

so however, that where the actual cost of a motor car is, in accordance with the proviso to clause (1) of Section 43, taken to be twenty-five thousand rupees, the moneys payable in respect of such motor car shall be taken to be a sum which bears to the amount for which the motor car is sold or, as the case may be, the amount of any insurance, salvage or compensation moneys payable in respect thereof (including the amount of scrap value, if any) the same proportion as the amount of twenty-five thousand rupees bears to the actual cost of the motor car to the assessee as it would have been computed before applying the said proviso;

(2) “sold” includes a transfer by way of exchange or a compulsory acquisition under any law for the time being in force but does not include a transfer, in a scheme of amalgamation, of any asset by the amalgamating company to the amalgamated company where the amalgamated company is an Indian Company.

- (iv) **Recovery of Bad Debts:** Where the assessee claims a deduction in any year in respect of a debt which has become bad or irrecoverable and the Assessing Officer allows a deduction to the extent of the bad debts, if subsequently the assessee recovers either the full amount of the debt which was previously written off as bad or part thereof, the amount so recovered would be chargeable to tax as the business income of the assessee in the year of recovery. But if the amount claimed by the assessee as bad debt was previously disallowed by the Assessing Officer on the ground that it had not actually become bad or it was not written off by the assessee, when the money is recovered, there would be no liability to tax in respect thereof. In cases where the Assessing Officer had allowed only a part thereof as bad, in the subsequent year of recovery, the tax liability under this section must be on the amount of difference between the amount recovered and the bad debt disallowed by the Assessing Officer.
- (v) **Withdrawal of any amount from special reserve:** Where a deduction has been allowed in respect of any special reserve created and maintained under clauses (viii) of Sub-section (1) of Section 36 any amount subsequently withdrawn from such special reserve shall be deemed to be the profits and gains of business or profession and accordingly be chargeable to income tax as the income of the previous year in which such amount is withdrawn.

Where any amount is withdrawn from the special reserve in a previous year in which the business is no longer in existence, the provisions of this sub-section shall apply as if the business is in existence in that previous year.

- (vi) **Set off of Losses of a Defunct Business against Deemed Profit:** Where the business or profession referred to in this section is no longer in existence and there is income chargeable to tax under points (i),(iv) and (v) given above in respect of that business or profession, any loss, not being a loss sustained in speculation business, which arose in that business or profession during the previous year in which it ceased to exist and which could not be set off against any other income of that previous year shall as far as may be, be set off against the income chargeable to tax under the sub-section aforesaid.

### Transfer of Immovable Property [Section 43CA]

Currently, when a capital asset, being immovable property, is transferred for a consideration which is less than the value adopted, assessed or assessable by any authority of a State Government for the purpose of payment of stamp duty in respect of such transfer, then such value (stamp duty value) is taken as full value of consideration under section 50C of the Income-tax Act.

It has been pointed out this variation between the stamp duty value and the value of sale consideration can occur in respect of similar properties in the same area because of a variety of factors such as shape of plot or location. **(Amended by the Finance Act, 2018)**

Hence in order to minimise the hardship to the assessee in case of genuine transactions it is provided that where the stamp duty value does not exceed 105% of the consideration received or accruing as a result of the transfer, the consideration so received or accruing as a result of the transfer shall, for the purposes of computing profits and gains from transfer of such asset, be deemed to be the full value of the consideration.

These provisions do not apply to transfer of immovable property, held by the transferor as stock-in-trade. Hence, this section has been inserted with effect from assessment year 2014-15 where the consideration for the transfer of an asset (other than capital asset), being land or building or both, is less than the stamp duty value, the value so adopted or assessed or assessable by any authority of state government for the purpose of payment of stamp duty in respect of such transfer the value so adopted or assessed or assessable shall for the purpose of computing income under the head “Profits and gains of business of profession” shall be deemed to be the full value of the consideration received or accruing as a result of such transfer.

Where the date of an agreement fixing the value of consideration for the transfer of the asset and the date of registration of the transfer of the asset are not same, the stamp duty value may be taken as on the date of the agreement for transfer and not as on the date of registration for such transfer. However, this exception shall apply only in those cases where amount of consideration or a part thereof for the transfer has been received by way of account payee cheque/bank draft or by use of electronic clearing system through a bank account on or before the date of the agreement.

#### **SPECIAL PROVISION IN CASE OF INCOME OF PUBLIC FINANCIAL INSTITUTIONS, ETC. (SECTION 43D)**

Section 43D has been inserted by Finance (No. 2) Act, 1991 w.e.f. 1.4.1991. This section provides that in the case of a public financial institution or a scheduled bank or a state financial corporation or a state industrial investment corporation, the income by way of interest on such categories of bad and doubtful debts as may be prescribed having regard to the guidelines issued by the Reserve Bank of India in relation to such debts shall be chargeable to tax in the previous year in which it is credited to profit and loss account by such institution referred above for that year or in the previous year in which it is actually received by them whichever is earlier.

With a view to improve the viability of leasing finance companies, the section has been amended to provide that in case of a public company, the income by way of interest in relation to such categories of bad and doubtful debts as may be prescribed having regard to the guidelines issued by the National Housing Bank established under the National Housing Bank Act, 1987 in relation to such debt shall be chargeable to tax in the previous year in which it is credited to the profit and loss account by the said public company for that year or in the previous year in which it is actually received by it, whichever is earlier.

The benefit of Section 43D shall also be extended to co-operative banks (other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank).

#### **SPECIAL PROVISIONS RELATED TO INSURANCE BUSINESS (SECTION 44)**

The profits and gains of any business of insurance must, according to Section 44, be computed in accordance with the rules contained in the First Schedule to the Income-tax Act. For the purpose of the computation, it is immaterial whether the insurance business is carried on by mutual insurance company or by a co-operative society or by any other person. The rules contained in the Schedule would apply notwithstanding anything to the contrary contained in the provisions of the Income-tax Act relating to the computation of income chargeable

under the head 'Interest on Securities', 'income from house property', 'capital gains', or 'income from other sources' or under the head 'income from business or profession'.

### **COMPULSORY MAINTENANCE OF BOOKS OF ACCOUNT (SECTION 44AA)**

1) Every person carrying on the legal / medical / engineering / architectural profession / accountancy / technical consultancy / interior decoration, or any other profession as notified by the Central Board of Direct Taxes (CBDT), in the Official Gazette, must statutorily maintain such books of account and other documents as may enable the Assessing Officer to compute his total income under the Act, if total gross receipts exceeds Rs. 1,50,000 in any one of three immediately preceding years.

2) An individual or HUF carrying on any business / profession other than those specified above, must maintain the books of accounts necessary for computation and assessment, if the income from business / profession exceeds INR 250,000 OR the total turnover / gross receipts as the case may be, exceeds INR 25,00,000 in any 1 of the 3 years immediately preceding the accounting year and if the business / profession is newly set up, if the income / sales turnover is likely to exceed the thresholds mentioned, in the Previous Year.

3) Every person other than an Individual / HUF carrying on any business / profession other than those specified above, must maintain the books of accounts necessary for computation and assessment, if the income from business / profession exceeds INR 120,000 OR the total turnover / gross receipts as the case may be, exceeds INR 10,00,000 in any 1 of the 3 years immediately preceding the accounting year and if the business / profession is newly set up, if the income / sales turnover is likely to exceed the thresholds mentioned, in the Previous Year.

4) Where profits and gains from business are deemed to be profits and gains under section 44AE or Section 44BB or Section 44BBB and assessee has claimed his income to be lower than the profits and gains then such profits and gains shall be deemed to be profits and gains of his business during the previous year or

5) where the provisions of section 44AD(4) or section 44ADA are applicable to him and his total income exceeds the maximum amount which is not chargeable to income tax.

Under presumptive assessment under sections mentioned above, if assessee claims that his income is lower than that specified under these sections, assessee is required to get his accounts audited by a Chartered Accountant and copy of that report needs to be attached alongwith his return of income. Therefore to get his accounts audited he needs to maintain such books to substantiate his claim and also to enable Chartered Accountant to issue Audit Report to this effect.

The CBDT has the authority under the act to prescribe the books of accounts necessarily to be maintained having regard to the nature of business / profession, including their format and the details to be mentioned therein, and the place where these need to be maintained.

The books of accounts and other documents shall be kept and maintained for a period of 6 years from the end of relevant assessment year.

For details students may refer to Rule 6F also for specified books to be maintained.

### **COMPULSORY AUDIT OF BOOKS OF ACCOUNT (SECTION 44AB)**

Section 44AB makes it obligatory for a person to get his accounts audited before the "specified date" by a "Chartered Accountant"; if the total sales, turnover or gross receipts in business for the previous year exceeds INR 1 crore or if his gross receipts in profession for the previous year exceeds INR 50 lakhs. This includes professionals who are covered under the provisions of presumptive taxation and claim that their profits and gains from business / profession is lower than what computed under presumptive basis.

The provision also casts an obligation on such persons to furnish by the "specified date", a report of the audit in

the prescribed form duly signed and verified by the Chartered Accountant setting forth such particulars as may be prescribed by rules made in this behalf by the Central Board of Direct Taxes.(Form 3CA/3CB/3CD).

The requirement of audit u/s 44AB, doesn't apply to a person who declares profits / gains on a presumptive basis, u/s 44AD, and his total sales / turnover / gross receipts doesn't exceed INR 2 Cr.

Specified Date is the due date for filing Annual Return of Income u/s 139(1).

### **SPECIAL PROVISION FOR COMPUTING PROFITS AND GAINS OF BUSINESS ON PRESUMPTIVE BASIS (SECTION 44AD)**

The provisions of this section shall be applicable to resident Individual, HUF, Firm (excluding LLP) carrying on any business except the business of plying, hiring or leasing goods carriages referred to in section 44AE and whose total turnover or gross receipts in the previous year does not exceed an amount of 2 Crores. This section aims at providing relief to all the small businesses from maintaining the books of accounts and to reduce the compliance and administrative burden.

- A sum equal to 8% of the total turnover or gross receipts of the assessee in the previous year shall be deemed to be the profits and gains of such business chargeable to tax under the head “Profits and gains of business or profession”

Presumptive income u/s 44AD shall be calculated @ 6% instead of 8% in respect of those portions of turnover/ sales/gross receipts if following conditions are satisfied:

- a) Turnover / sales / gross receipts is received by an account payee cheque / draft / ECS through a bank account or such other modes as may be prescribed.
  - b) The above payment is received during the previous year or before the due date of submission of return u/s 139(1) in the assessment year.
- No deduction shall be allowed to the assessee under sections 30 to 38 and the salary and interest paid to the partners shall not be allowed for deduction subject to the conditions and limits specified in section 40(b).
  - The written down value of any asset of an eligible business shall be deemed to have been calculated as if the eligible assessee had claimed and had been actually allowed the deduction in respect of the depreciation for each of the relevant assessment years.
  - The intent of this section is to reduce administrative and compliance burden on small businesses, and relieve them from the requirement of maintenance of books of accounts. Therefore, people opting for taxation on presumptive basis are not required to maintain books of account u/s 44AA or get them audited u/s 44AB. Assessee to maintain accounts and get them audited, if he claims the profits to be less than 6% or 8% (as applicable) of the gross receipts.
  - An assessee opting for section 44AD is required to pay advance tax by 15th March, every FY.

**Persons not eligible for presumptive taxation scheme:** The following persons are specifically excluded from the applicability of the presumptive provisions of section 44AD -

- (a) a person carrying on profession as referred to in section 44AA(1) i.e., legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or any other profession as is notified by the Board (namely, authorized representatives, film artists, company secretaries and profession of information technology have been notified by the Board for this purpose);
- (b) a person earning income in the nature of commission or brokerage; or

- (c) a person carrying on any agency business.

### Illustration

In the example below, the assessee has opted for presumptive taxation in AY 2018-19 and 2019-20 but in AY 2020-21, since his computed gains from business were lower than the presumptive, he didn't opt for it. Hence for 5 AY's subsequent to that year, i.e. from AY 2021-22 to AY 25-26, he will not be able to opt for presumptive basis u/s 44AD.

	ASSESSMENT YEAR		
	2018-19	2019-20	2020-21
Gross Receipts	1,80,00,000	1,90,00,000	2,00,00,000
Presumptive Opted	Y	Y	N
Tax Rate	8%	8%	Not Applicable
Deemed Income for Taxation	14,40,000	15,20,000	10,00,000
Books of Accounts & Audit	N	N	Y

### **PRESUMPTIVE TAXATION FOR PROFESSIONALS [Section 44ADA]**

This section allows presumptive basis, for a resident assessee who is engaged in the following professions: legal / medical / engineering / architectural / accountancy / technical consultancy / interior decoration, or any other profession as notified by the Central Board of Direct Taxes (CBDT), in the Official Gazette and whose gross receipts does not exceed INR 50,00,000 in the PY.

50% of the total gross receipts or such higher sum as may be declared by the assessee shall be deemed as income under the head Profit and Gains of Business and Profession (PGBP).

No deduction shall be allowed to the assessee under sections 30 to 38 and the salary and interest paid to the partners shall not be allowed for deduction subject to the conditions and limits specified in section 40(b).

The written down value of any asset of an eligible business shall be deemed to have been calculated as if the eligible assessee had claimed and had been actually allowed the deduction in respect of the depreciation for each of the relevant assessment years.

The intent of this section is to reduce administrative and compliance burden on small businesses, and relieve them from the requirement of maintenance of books of accounts. Therefore, people opting for taxation on presumptive basis are not required to maintain books of account u/s 44AA or get them audited u/s 44AB.

Assessee to maintain accounts and get them audited if he claims profits to be less than 50% of the Gross Receipts.

An assessee opting for section 44ADA is required to pay advance tax by 15th March, every FY.

### **SPECIAL PROVISIONS FOR COMPUTING PROFITS AND GAINS OF BUSINESS OF PLYING, HIRING OR LEASING GOODS CARRIAGES [Section 44AE]**

This section provides a presumptive basis of taxation for estimating business income from plying, hiring or leasing goods carriages, so long as the assessee doesn't own > 10 vehicles at any time in the PY.

The current presumptive income scheme is applicable to all classes of goods carriages being less than 10 in number, irrespective of their tonnage capacity. Hence with amendment by Finance Act, 2018 the presumptive income shall be as under:

- (i) In case of heavy goods vehicle (the gross vehicle weight of which exceeds 12,000 kilograms), the presumptive income would be deemed to be an amount equal to Rs. 1,000 per ton of gross vehicle weight or unladen weight, as the case may be, for every month or part of a month during which the heavy

goods vehicle is owned by the assessee in the previous year or an amount claimed to have been actually earned from such vehicle, whichever is higher.

- (ii) The vehicles other than heavy goods vehicle will continue to be taxed at as per the existing rates of Rs. 7,500 for every month or part of a month during which the goods carriage is owned by the assessee in the previous year or an amount claimed to have been actually earned from such goods carriage, whichever is higher.

An assessee may claim lower income than the presumptive income as specified under this section, if he keeps and maintains such books of account under section 44AA and gets his accounts audited and furnishes a report of such audit as required under section 44AB.

An assessee, who is in possession of a goods carriage, whether taken on hire purchase or on instalments and for which the whole or part of the amount payable is still due, shall be deemed to be the owner of such goods carriage.

No deduction shall be allowed to the assessee under sections 30 to 38 and the salary and interest paid to the partners shall not be allowed for deduction subject to the conditions and limits specified in section 40(b).

The written down value of any asset of an eligible business shall be deemed to have been calculated as if the eligible assessee had claimed and had been actually allowed the deduction in respect of the depreciation for each of the relevant assessment years.

The intent of this section is to reduce administrative and compliance burden on small businesses, and relieve them from the requirement of maintenance of books of accounts. Therefore, people opting for taxation on presumptive basis are not required to maintain books of account u/s 44AA or get them audited u/s 44AB.

## QUESTIONS AND ANSWERS

### Case 1

Ms. Priya is engaged in the business of generation and distribution of power and opts the WDV method for claiming Depreciation. She has an opening block of INR 50,00,000. She acquired new machinery for INR 25,00,000 on 15th Nov 2019. She also imported a new machinery from Zurich for INR 10,00,000 on 14th Apr 2019. This machine was used there earlier and she is the first user in India. Additionally, she bought computers for INR 500,000 on 9th Sep 2019.

You are required to compute the allowable depreciation under Income Tax Act, 1961 for AY 2020-21.

### Answer

Items	Date	INR	Category	Rate	Depreciation
Opening WDV	1st Apr 2019	50,00,000	Full	15%	7,50,000
New Machinery	15th Nov 2019	25,00,000	Half	15%	1,87,500
Imported Machinery	14th Apr 2019	10,00,000	Full	15%	1,50,000
Computers	9th Sep 2019	5,00,000	Full	40%	2,00,000
<b>Total Depreciation</b>					<b>12,87,500</b>
Addl Depreciation					
New Machinery		25,00,000	Half	20%	2,50,000
Computers		5,00,000	Full	20%	1,00,000

Additional Depreciation					3,50,000
Annual Depreciation					16,37,500

*Note:* The machinery that was imported was first used therein at Zurich, earlier before being imported in to India and hence no depreciation will be allowable on the same.

### Case 2

Examine whether the following expenses incurred by Ms. Priyanka, a dealer in Securities, will be allowable?

- Expenses on CSR Activities INR 750,000
- Setting up a cold chain facility for specified products, INR 10,00,000
- Interest on loan paid to Mr. Shyam, INR 100,000 on which no TDS was affected. Her sales for the PY was INR 5 Crores
- Securities Transaction Tax paid INR 50,000

### Answer

- Expenses on CSR activities are not allowable as a deduction u/s 37 and hence the entire INR 750,000 would be disallowed
- This is a specified business for which she can claim 100% deduction u/s 35AD, hence entire INR 10,00,000 will be allowable
- The turnover of Ms. Priyanka exceeds the threshold of INR 100,00,000 and hence she was required to deduct tax at source. Since she didn't, 30% of the interest, i.e., 30% of INR 100,000, that is INR 30,000 would be disallowed u/s 40(a)(ia) and the balance INR 70,000 would be allowable for the assessee u/s 36(1)(iii)
- Securities Transaction Tax of INR 50,000 would be an allowable expense, assuming that income from such source, has been included under the head "Profits / Gains from Business / Profession".

### Case 3

Mr. Kundan Lal, a trader at Kolkata, submits the P&L as under, for FY 2019-20:

Profit & Loss Account for Year Ended 31st March, 2020			
Particulars	INR	Particulars	INR
To Opening Stock	1,00,000	By Sales	1,25,00,000
To Purchases	1,20,00,000	By Closing Stock	2,00,000
To Gross Profit	6,00,000		
Total	1,27,00,000	Total	1,27,00,000
To Rent, Rates, Taxes	1,08,000	By Gross Profit	6,00,000
To Salaries	1,25,000	By Interest Income	5,000
To Interest on loan	25,000		
To Depreciation	2,25,000		
To Printing & Stationery	25,000		

To Postage & Telegram	1,750		
To Loss on Sale of Shares (Short Term)	12,190		
To General Expenses	17,060		
To Net Profit	66,000		
Total	6,05,000	Total	6,05,000

**Additional Information:**

- a) Closing Stock & Opening Stock was under-valued by 10%
- b) Salary includes INR 20,000 paid to a relative which was considered unreasonable
- c) The whole amount of Printing & Stationery was paid in Cash at one go
- d) WDV of the Plant & Machinery on 1st Apr was INR 12,00,000. Additions of INR 5,00,000 were made on 1st June 2019 and on 1st Oct 2019, Machinery was sold for INR 12,57,993
- e) Rent & Rates included outstanding GST Liability for Mar' 20, of INR 27,000, duly paid within 7th April 2020
- f) A donation of INR 12,000 was made to a public charitable trust during the year

**You are required to:**

- a) Calculate the Profits / Gains from Business Profession
- b) Advise whether he should opt for the Presumptive scheme u/s 44AD

You can assume that the entire amount of turnover was received by account payee cheque.

**Answer:**

	Particulars	INR
	Net Profit	66,000
Add:	UV Closing Stock	2,22,222
	Salary (Relative)	20,000
	Printing & Stationery (Cash > 20000)	25,000
	Depreciation	2,25,000
	Donation	12,000
	Loss on Sale of Shares	12,190
		<b>5,82,412</b>
Less:	UV Opening Stock	1,11,111
	Allowable Depreciation	66,301
	Interest Income	<b>5,000</b>
	Profits / Gains from Business / Profession	4,00,000
	Under Presumptive Taxation	7,50,000

Since the tax liability on presumptive basis, i.e. 6% of Gross Receipts (INR 125,00,000 \*6%) = INR 750,000 is higher than the computed Profits / Gains from Business Profession, he shouldn't adopt for presumptive basis. However, since his turnover is > INR 1 Crore, audit u/s 44AB would be mandatory, if he doesn't adopt presumptive basis.

**Notes:**

- a) Under-valued closing stock added to Profits (100/90\*200,000)
- b) Under-valued opening stock reduced (100/90\*100,000)
- c) Salary to relative, to the extent considered reasonable, added back
- d) Since the cash payment was > INR 10,000, entire amount disallowed u/s 40 A (3)
- e) Depreciation added back and allowed as under:

Particulars	INR
Opening WDV	12,00,000
Additions	5,00,000
Disposals	12,57,993
Closing WDV	4,42,007
Depreciation @ 15%	66,301

- f) Since the unpaid GST Liability was paid before the due date and before the date of filing return of income u/s 139(1), it is allowable

**Illustration :**

Net profit as per profit and loss account of X is Rs. 6,86,000 for the year ending 31st March, 2020. The following information is noted from his accounts:

- (a) Advertisement expenditure debited to profit and loss account include the following:
  - (i) Expenditure incurred outside India: Rs. 46,000 (permitted by RBI);
  - (ii) Articles presented by way of advertisement (60 articles cost of each being Rs. 900; and 36 articles cost of each being Rs. 1,700);
  - (iii) Rs 16,000 being cost of advertisement which appeared in a newspaper owned by a political party;
  - (iv) Rs. 11,400 being capital expenditure on advertisement;
  - (v) Rs. 12,000 paid in cash; and
  - (vi) Rs. 7,000 paid to a concern in which X has substantial interest (amount is excessive to the extent of Rs. 1,400).
- (b) Out of salary to employees of Rs. 8,70,000 debited to the profit and loss account:
  - (i) Rs. 40,000 is employees' contribution to recognised provident fund, Rs. 37,500 of which is credited in the employees' account in the relevant fund before the 'due date';
  - (ii) Rs. 46,000 is bonus which is paid on 13th November, 2020;
  - (iii) Rs. 36,000 is commission which is paid on 1st December, 2020;
  - (iv) Rs. 20,000 is incentive to workers which is paid on 10th December, 2020;
  - (v) Rs. 40,000 is paid outside India in respect of which tax is not deducted at source;
  - (vi) Rs. 6,000 being capital expenditure for promoting family planning amongst employees; and
  - (vii) Rs. 40,000 being entertainment allowance given to employees.
- (c) Entertainment expenditure debited to profit and loss account is Rs. 9,000.

Determine the net income of X for the assessment year 2020-21.

**Solution:**

Calculation of Net Income of X for assessment year 2020-21

Net Profit as per Profit and Loss Account	6,86,000
Add: Inadmissible items:	
Cash paid for advertisement expenses (Note 3)	12000
Cost of advertisement which appeared in a newspaper owned by a political party	16000
Excessive amount paid to a concern in which X has substantial interest	1400
Employee contribution to recognised provident fund (to the extent not credited in the employees' account in the relevant fund before the 'due date')	2500
Bonus being paid to employees after the 'due date' of filing the return	46000
Commission being paid to employees after the 'due date' of filing the return	36000
Salary paid outside India in respect of which tax is not deducted at source	40000
Capital expenditure for promoting family planning amongst employees (allowed only to a corporate assessee)	6000
Capital expenditure on Advertisements	11400
Net Income	8,57,300

**Notes:**

1. Restrictions on advertisement and entertainment abolished.
2. With the abolition of Section 37(3), which inter alia governed the deductibility of advertising expenses, advertising too has come within the fold of the omnibus Section 37(1) which specifically frowns on capital expenditure. The Himachal Pradesh High Court verdict in Mohan Meakin Breweries Ltd. v. CIT (1979) 118 ITR 101 allowing capital expenditure on advertising therefore has ceased to have the force of law as it was rendered in the context of Section 37(3).
3. Advertisement expenses of Rs. 12,000 (i.e. exceeding the limit of Rs. 10,000) is paid in cash, hence disallowed under section 40A(3).
4. The 'due date' for filing return where the assessee is a person (other than a company) who is required to get his accounts audited under the Income-tax Act or any other law is September 30; and where the assessee is a person deriving income from business and who is not required to get his accounts audited, the 'due date' is July, 31. Under the provisions of Section 43B of the Act - Bonus Rs. 46,000 paid on 13th Nov., 2020 and Commission Rs. 36,000 paid on 1st Dec., 2020 are not admissible since the payments are made after the above mentioned 'due date'.
5. Incentive to workers which is paid on 10th December, 2020 is admissible on 'due basis'

## ANNEXURE

Rates at which Depreciation shall be allowable from Assessment Year 2006-2007 Onwards

### APPENDIX I

[See rule 5]

**Table of Rates at which Depreciation is Admissible**

Block of assets	Depreciation allowance as percentage of written down value
1	2
<b>PART A</b>	
<b>TANGIBLE ASSETS</b>	
I. BUILDING [See Notes 1 to 4 below the Table]	
(1) Buildings which are used mainly for residential purposes except hotels and boarding houses	5
(2) Buildings other than those used mainly for residential purposes and not covered by sub-items (1) above and (3) below	10
(3) Buildings acquired on or after the 1st day of September, 2002 for installing machinery and plant forming part of water supply project or water treatment system and which is put to use for the purpose of business of providing infrastructure facilities under clause (1) of sub-section (4) of section 80-IA	40
(4) Purely temporary erections such as wooden structures	40
II. FURNITURE AND FITTINGS	
Furniture and fittings including electrical fittings [See Note 5 below the Table]	10
III. MACHINERY AND PLANT	
(1) Machinery and plant other than those covered by sub-items (2), (3) and (8) below	15
(2) Motor cars, other than those used in a business of running them on hire, acquired or put to use on or after the 1st day of April, 1990	15
(3) (i) Aeroplanes - Aeroengines	40
(ii) Motor buses, motor lorries and motor taxis used in a business of running them on hire	30
(iii) Commercial vehicle which is acquired by the assessee on or after the 1st day of October, 1998, but before the 1st day of April, 1999 and is put to use for any period before the 1st day of April, 1999 for the purposes of business or profession in accordance with the third proviso to clause (ii) of sub-section (1) of section 32 [see Note 6 below the Table]	40

(iv) New commercial vehicle which is acquired on or after the 1st day of October, 1998, but before the 1st day of April, 1999 in replacement of condemned vehicle of over 15 years of age and is put to use for any period before the 1st day of April, 1999 for the purposes of business or profession in accordance with the third proviso to clause (ii) of sub-section (1) of section 32 [see Note 6 below the Table]	40
(v) New commercial vehicle which is acquired on or after the 1st day of April, 1999 but before the 1st day of April, 2000 in replacement of condemned vehicle of over 15 years of age and is put to use before the 1st day of April, 2000 for the purpose of business or profession in accordance with the second proviso to clause (ii) of sub-section (1) of section 32 [see Note 6 below the Table]	40
(vi) New commercial vehicle which is acquired on or after the 1st day of April, 2001 but before the 1st day of April, 2002 and is put to use before the 1st day of April, 2002 for the purposes of business or profession [see Note 6 below the Table]	40
(vii) Moulds used in rubber and plastic goods factories	30
(viii) Air pollution control equipment, being	40
(a) Electrostatic precipitation systems	
(b) Felt-filter systems	
(c) Dust collector systems	
(d) Scrubber-counter current/venturi/packed-bed/ cyclonic scrubbers	
(e) Ash handling system and evacuation system	
(ix) Water pollution control equipment, being—	40
(a) Mechanical screen systems.	
(b) Aerated detritus chambers (including air compressor)	
(c) Mechanically skimmed oil and grease removal systems	
(d) Chemical feed systems and flash mixing equipment	
(e) Mechanical flocculators and mechanical reactors	
(f) Diffused air/mechanically aerated activated sludge systems	
(g) Aerated lagoon systems	
(h) Biofilters	
(i) Methane-recovery anaerobic digester systems	
(j) Air floatation systems	
(k) Air/steam stripping systems	
(l) Urea Hydrolysis systems	
(m) Marine outfall systems	

(n) Centrifuge for dewatering sludge	
(o) Rotating biological contractor or bio-disc	
(p) Ion exchange resin column	
(q) Activated carbon column	
(x) (a) Solidwaste, control equipments being, caustic/ lime/chrome/ mineral/cryolite recovery system	40
(b) Solidwaste recycling and resource recovery systems	
(xi) Machinery and plant, used in semi-conductor industry covering all integrated circuits (ICs) (excluding hybrid integrated circuits) ranging from small scale integration (SSI) to large scale integration/very large scale integration (LSI/VSLI) as also discrete semi-conductor devices such as diodes, transistors, thyristors, triacs, etc., other than those covered by entries (viii), (ix) and (x) of this sub-item and sub-item (8) below.	30
(xia) Life saving medical equipment, being	40
(a) D.C. Defibrillators for internal use and pace makers	
(b) Haemodialysors	
(c) Heart Lung Machine	
(d) Cobalt Therapy Unit	
(e) Colour Doppler	
(f) SPECT Gamma Camera	
(g) Vascular Angiography System including Digital subtraction Angiography	
(h) Ventilator used with anaesthesia apparatus	
(i) Magnetic Resonance Imaging System	
(j) Surgical Laser	
(k) Ventilators other than those used with anaesthesia	
(l) Gamma knife	
(m) Bone Marrow Transplant Equipment including silastic long standing intravenous catheters for chemotherapy	
(n) Fibre optic endoscopes including, Paediatric resectoscope/audit resectoscope, Peritoneo-scopes, Arthroscope, Microlaryngoscopi Fibreoptic Flexible Nasal Pharyngo Bronchoscope, Fibreoptic Flexible Laryngo Brochoscope, Video Laryngo Brochoscope and Video Oesophago Gastroscope, Stroboscope, Fibreoptic Flexible Oesophago Gastroscope	,
(o) Laparoscope (single incision)	
(4) Containers made of glass or plastic used as re-fills	40
(5) Computers including computer software [see Note 7 below the Table]	40

(6) Machinery and plant, used in weaving, processing and garment sector of textile industry, which is purchased under TUFS on or after the 1st day of April, 2001 but before the 1st day of April, 2004 and is put to use before the 1st day of April, 2004 [see Note 8 below the Table]	40
(7) Machinery and plant, acquired and installed on or after the 1st day of September, 2002 in a water supply project or a water treatment system and which is put to use for the purpose of business of providing infrastructure facility under clause (i) of sub-section (4) of section 80-IA [see Notes 4 and 9 below the Table]	40
(8) (i) Wooden parts used in artificial silk manufacturing machinery	40
(ii) Cinematograph films - bulbs of studio lights	40
(iii) Match factories - wooden match frames	40
(iv) Mines and quarries:	40
(a) Tubs, winding ropes, haulage ropes and sand stowing pipes	
(b) Safety lamps	
(v) Salt works - Salt pans, reservoirs and condensers, etc., made of earthy sandy or clayey material or any other similar material	40
(vi) Flour mills - Rollers	40
(vii) Iron and steel industry - Rolling mill rolls	40
(vi) Sugar works - Rollers	40
(ix) Energy saving devices, being	–
A. Specialised boilers and furnaces:	
(a) Ignifluid/fluidized bed boilers	
(b) Flameless furnaces and continuous pusher type furnaces	
(c) Fluidized bed type heat treatment furnaces	40
(d) High efficiency boilers (thermal efficiency higher than 75 per cent in case of coal fired and 80 per cent in case of oil/ gas fired boilers)	
B. Instrumentation and monitoring system for monitoring energy flows:	
(a) Automatic electrical load monitoring systems	
(b) Digital heat loss meters	
(c) Micro-processor based control systems	
(d) Infra-red thermography	40
(e) Meters for measuring heat losses, furnace oil flow, steam flow, electric energy and power factor meters	

(f) Maximum demand indicator and clamp on power meters	
(g) Exhaust gases analyser	
(h) Fuel oil pump test bench	
C. Waste heat recovery equipment	
(a) Economizers and feeds water heaters	
(b) Recuperates and air pre-heaters	40
(c) Heat pumps	
(d) Thermal energy wheel for high and low temperature waste heat recovery	
D. Co-generation systems:	
(a) Back pressure pass out, controlled extraction, extraction-cum- condensing turbines for co-generation along with pressure boilers	
(b) Vapour absorption refrigeration systems	40
(c) Organic rankine cycle power systems	
(d) Low inlet pressure small steam turbines	
E. Electrical equipment:	
(a) Shunt capacitors and synchronous condenser systems	
(b) Automatic power cut off devices (relays) mounted on individual motors	
(c) Automatic voltage controller	
(d) Power factor controller for AC motors	
(e) Solid state devices for controlling motor speeds	40
(f) Thermally energy-efficient stenters (which require 800 or less kilocalories of heat to evaporate one kilogram of water)	
(g) Series compensation equipment	
(h) Flexible AC Transmission (FACT) devices - Thyristor controlled series compensation equipment	
(i) Time of Day (TOD) energy meters	
(j) Equipment to establish transmission highways for National Power Grid to facilitate transfer of surplus power of one region to the deficient region	
(k) Remote terminal units/intelligent electronic devices, computer hardware/software, router/bridges, other required equipment and associated communication systems for supervisory control and data acquisition systems, energy management systems and distribution management systems for power transmission systems	
(l) Special energy meters for Availability Based Tariff (ABT)	

F. Burners:	
(a) 0 to 10 per cent excess air burners	
(b) Emulsion burners	40
(c) Burners using air with high pre-heat temperature (above 300oC)	
G. Other equipment:	40
(a) Wet air oxidation equipment for recovery of chemicals and heat	
(b) Mechanical vapour recompressors	
(c) Thin film evaporators	
(d) Automatic micro-processor based load demand controllers	
(e) Coal based producer gas plants	
(f) Fluid drives and fluid couplings	
(g) Turbo charges/super-charges	
(h) Sealed radiation sources for radiation processing plants	
(x) Gas cylinders including valves and regulators	40
(xi) Glass manufacturing concerns - Direct fire glass melting furnaces	40
(xii) Mineral oil concerns:	40
(a) Plant used in field operations (above ground) distribution - Returnable packages	
(b) Plant used in field operations (below ground), but not including kerbside pumps including under ground tanks and fittings used in field operations (distribution) by mineral oil concerns	
(xiii) Renewable energy devices being:	40
(a) Flat plate solar collectors	
(b) Concentrating and pipe type solar collectors	
(c) Solar cookers	
(d) Solar water heaters and systems	
(e) Air/gas/fluid heating systems	
(f) Solar crop drivers and systems	
(g) Solar refrigeration, cold storages and air conditioning systems	
(h) Solar steels and desalination systems	
(i) Solar power generating systems	

(j) Solar pumps based on solar-thermal and solar-photovoltaic conversion	
(k) Solar-photovoltaic modules and panels for water pumping and other applications	
(l) Wind mills and any specially designed devices which run on wind mills	
(m) Any special devices including electric generators and pumps running on wind energy	
(n) Biogas-plant and biogas-engines	
(o) Electrically operated vehicles including battery powered or fuel-cell powered vehicles	
(p) Agricultural and municipal waste conversion devices producing energy	
(q) Equipment for utilising ocean waste and thermal energy	
(r) Machinery and plant used in the manufacture of any of the above sub-items	
(9) (i) Books owned by assessee carrying on a profession:	
(a) Books, being annual publications	40
(b) Books, other than those covered by entry (a) above	40
(ii) Books owned by assessee carrying on business in running lending libraries	40
IV. SHIPS	
(1) Ocean-going ships including dredgers, lugs, barges, survey launches and other similar ships used mainly for dredging purposes and fishing vessels with wooden hull	20
(2) Vessels ordinarily operating on inland waters, not covered by sub-item (3) below	20
(3) Vessels ordinarily operating on inland waters being speed boats [see Note 10 below the Table]	20
PART B INTANGIBLE ASSETS	
Know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature	25

**Notes:**

1. "Buildings" include roads, bridges, culverts, wells and tubewells.
2. A building shall be deemed to be a building used mainly for residential purposes, if the built-up floor area thereof used for residential purposes is not less than sixty-six and two-third per cent of its total built-up floor area and shall include any such building in the factory premises.
3. In respect of any structure or work by way of renovation or improvement in or in relation to a building referred to in Explanation 1 of clause (ii) of sub-section (1) of section 32, the percentage to be applied will be the percentage specified against sub-item (1) or (2) of item I percentage to be applied will be the percentage specified against sub-item (1) or (2) of item I as may be appropriate to the class of building in or in relation to which the renovation or improvement is effected. Where the structure is constructed or the work is done by way of extension of any such building, the percentage to be applied would be such percentage as would be appropriate, as if the structure or work constituted a separate building.
4. Water treatment system includes system for desalinisation, demineralisation and purification of water.

5. “Electrical fittings” include electrical wiring, switches, sockets, other fittings and fans, etc.
6. “Commercial vehicle” means “heavy goods vehicle”, “heavy passenger motor vehicle”, “light motor vehicle”, “medium goods vehicle” and “medium passenger motor vehicle” but does not include “maxi-cab”, “motor-cab”, “tractor” and “road-roller”. The expressions “heavy goods vehicle”, “heavy passenger motor vehicle”, “light motor vehicle”, “medium goods vehicle”, “medium passenger motor vehicle”, “maxicab”, “motor-cab”, “tractor” and “road-roller” shall have the meanings respectively as assigned to them in section 2 of the Motor Vehicles Act, 1988 (59 of 1988).
7. “Computer software” means any computer programme recorded on any disc, tape, perforated media or other information storage device.
8. “TUFS” means Technology Upgradation Fund Scheme announced by the Government of India in the form of a Resolution of the Ministry of Textiles vide No. 28/1/99-CTI of 31.3.1999.
9. Machinery and plant includes pipes needed for delivery from the source of supply of raw water to the plant and from the plant to the storage facility.
10. “Speed boat” means a motor boat driven by a high speed internal combustion engine capable of propelling the boat at a speed exceeding 24 kilometers per hour in still water and so designed that when running at a speed, it will plane, i.e., its bow will rise from the water.

#### CASE LAW

##### **1. “Actual write off” of individual debtor’s account is not necessary under 36(1)(vii) Bad Debt, of the Income-tax Act, 1961**

##### **Vijaya Bank v. Commissioner of Income Tax [2010] [323 ITR 166]**

On a question before the Hon’ble Supreme Court whether it is imperative for assessee-bank to close individual account of each of its debtors in its books for claiming deduction under section 36(1)(vii) of the Income-tax Act, the Supreme Court referring to its judgement in Southern Technologies Limited v. Joint CIT9 held that in order to understand the term “write-off” one has to see how the write off has been effected. If an assessee debits an amount of doubtful debtors to profit and loss account and credits the asset account (i.e., sundry debtors) it would constitute an actual write off of a debt.

On the contrary, if the amount is credited to “current liabilities and provisions”, then it would be a provision. In the latter case the assessee would not be entitled to the deduction after 1-4-1989. It was also held that the assessing officer was empowered to tax the subsequent repayment, if any, under section 41(1) of the Income-tax Act.

Reference may also be made to the Supreme Court decision in TRF Limited vs CIT10 wherein it was held that bad debts need not be proven to be irrecoverable under section 36(1)(vii). It is sufficient if they are written off.

##### **2. Remission of a liability under section 41(1) of the Income Tax Act**

##### **Commissioner of Income-tax v. Smt. Sita Devi Juneja [2010] [325 ITR 593, Punjab and Haryana High Court]**

The High Court held that merely because liability was outstanding for the last six years, it could not be presumed that the said liability had ceased to exist. It was also conceded that there was no bilateral act between the assessee and the creditors, which indicated that the said liability had ceased to exist. In absence of any bilateral act, the said liability could not have been treated as ceased. In view of these facts, the Commissioner (Appeals) as well as the Tribunal had rightly come to the conclusion that the Assessing

Officer had wrongly invoked the Explanation I to section 41(1) and made the aforesaid addition on the basis of presumptions, conjectures and surmises. It had been further found that the Assessing Officer had failed to show that in any earlier year allowance of deduction had been in respect of any trading liability incurred by the assessee. It was also not proved that any benefit was obtained by the assessee concerning such a trading liability by way of remission or cessation thereof during the concerned year. Thus, there did not accrue any benefit to the assessee which could be deemed to be the profit or gain of the assessee's business, which would otherwise not be the assessee's income. It had been further found as a fact that the assessee had filed the copies of accounts of sundry creditors signed by the concerned creditors.

**3. Is interest income on margin money deposited with bank for obtaining bank guarantee to carry on business, taxable as business income?**

**CIT v. K and Co. (2014) (Del)**

The High Court held that the interest income received on funds kept as margin money for obtaining the bank guarantee would be taxable under the head "Profits and gains of business or profession".

**4. Is expenditure incurred for construction of transmission lines by the assessee for supply of power to UPPCL by the assessee deductible as revenue expenditure?**

**Addtl. CIT v. Dharmpur Sugar Mill (P) Ltd (2015 Allahabad HC)**

Following the principle of law laid down by the Supreme Court in Empire Jute Mills' case, the Allahabad High Court, in this case, held that the expenditure which was incurred by the assessee in the laying of transmission lines was clearly on the revenue account. The transmission lines, upon erection, vested absolutely in UPPCL. The expenditure which was incurred by the assessee was for aiding efficient conduct of its business since the assessee had to supply electricity to its sole consumer UPPCL. This was not an advantage of a capital nature.

**5. What is the nature of expenditure incurred on glow-sign boards displayed at dealer outlets - capital or revenue?**

**CIT v. Orient Ceramics and Industries Ltd. (2013) (Delhi)**

The Delhi High Court held that such expenditure on glow sign boards displayed at dealer outlets was revenue in nature.

**6. Would the expenditure incurred on issue and collection of convertible debentures be treated as revenue expenditure or capital expenditure?**

**CIT v. ITC Hotels Ltd. (2011) (Kar.)**

The Karnataka High Court held that the expenditure incurred on the issue and collection of debentures shall be treated as revenue expenditure even in case of convertible debentures, i.e., the debentures which had to be converted into shares at a later date.

**7. Can the commission paid to doctors by a diagnostic centre for referring patients for diagnosis be allowed as a business expenditure under section 37 or would it be treated as illegal and against public policy to attract disallowance?**

**CIT v. Kap Scan and Diagnostic Centre P. Ltd. (2012) (P&H)**

The demanding as well as paying of such commission is bad in law. It is not a fair practice and is opposed to public policy and should be discouraged. Thus, the High Court held that commission paid to doctors for referring patients for diagnosis is not allowable as a business expenditure.

**8. Where the lump sum amount paid as One Time Settlement (OTS), without bifurcation of interest**

**and principal, has been offered to tax under section 41(1), can the assessee claim benefit of deduction of interest (interest paid plus interest waived) under section 43B?**

**CIT v. KLN Agrotechs (P) Ltd (2015 Kar. HC)**

The High Court concurred with the Tribunal's view that if out of the total sum of INR 256.54 lakhs which has been offered and subjected to tax by the assessee in its return, the amount of unpaid interest of INR 193.96 lakhs is deducted then the waived principal sum would come to 62.58 lakhs (i.e., INR 441.30 lakhs minus 378.72 lakhs), which is the amount which ought to have been taxed under section 41(1). Based on the above reasoning, the HC held that either the interest amount has to be allowed as deduction under section 43B or the sum offered for tax (as waived by the bank) has to be reduced by the amount of interest. In either case, the effective amount which is subjected to tax, would come to the same.

**9. In a case where payment of bonus due to employees is paid to a trust and such amount is subsequently paid to the employees before the stipulated due date, would the same be allowable under section 36(1)(ii) while computing business income?**

**Shasun Chemicals & Drugs Ltd v. CIT (2016 - SC)**

The Apex Court held that section 36(1) contains various kinds of expenses which are allowable as deduction while computing the business income. The amount paid by way of bonus is one such expenditure which is allowable as deduction under section 36(1)(ii).

It also held that the embargo contained in section 43B(b) or section 40A(9) does not come in the way of the assessee's claim, since the bonus was ultimately paid to the employees before the due date as per the statutory requirement. Therefore, the payment in respect of bonus is allowable as deduction, as there is no dispute that the amount was paid by the assessee to its employees before the due date by which such payment is supposed to be made in order to claim deduction under section 36(1)(ii).

**Note:** In this case, the Supreme Court has held that the bonus was allowable as deduction under section 36(1)(ii), even though it was initially remitted to the trust created for this purpose, from which the payment was ultimately made to the employees before the due date. The Supreme Court has applied the concept of "substance over form" in allowing the deduction of bonus paid under section 36(1)(ii) by considering that the payment of bonus was ultimately made to employees before the stipulated due date. Applying the same concept, the intermittent process of creation of trust for remittance of bonus and subsequent payment therefrom to the employees, which formed the basis of disallowance of bonus by the Assessing Officer on the basis of the provisions of section 40A(9) has been ignored. However, had the payment to employees not been made before the stipulated due date, deduction under section 36(1)(ii) would not be allowable merely because the amount was remitted to the trust before the stipulated due date. It may be noted that as date of filing of return of income under section 139(1) is a pre-requisite for claiming deduction under section 36(1)(ii).

**10. Income from Rent out Business is 'Profits & gains of business' not 'Income from House property.**

**M/s. Rayala Corporation Pvt. Ltd vs. Assistant Commissioner of Income Tax**

In a recent case between M/s. Rayala Corporation Pvt. Ltd vs. Assistant Commissioner of Income Tax, the Supreme Court of India has declared that, Income which arises from Rent out business should be taxed under the Head "Profits and gains of business or profession" not 'Income from House property'.

The appellant-assessee, a private limited company, is having house property, which has been rented and the assessee is receiving income from the said property by way of rent.

The division bench comprising of Justice Anil R Dave and Justice L Nageshwar Rao has relied the case Chennai Properties and Investments Ltd. v. Commissioner of Income Tax [2015] 373 ITR 673 (SC) that if an assessee is having his house property and by way of business he is giving the property on rent and if he is

receiving rent from the said property as his business income, the said income, even if in the nature of rent, should be treated as “Business Income” because the assessee is having a business of renting his property and the rent which he receives is in the nature of his business income.

While setting aside the Madras High Court Judgment, the division bench of Supreme Court observed that, “the rent should be the main source of income or the purpose for which the company is incorporated should be to earn income from rent, so as to make the rental income to be the income taxable under the head “Profits and Gains of Business or Profession”. It is an admitted fact in the instant case that the assessee company has only one business and that is of leasing its property and earning rent there from. Thus, even on the factual aspect, we do not find any substance in what has been submitted by the learned counsel appearing for the Revenue”.

“The judgment relied upon by the learned counsel appearing for the assessee squarely covers the facts of the case involved in the appeals. The business of the company is to lease its property and to earn rent and therefore, the income so earned should be treated as its business income”.

**11. Where the waiver is in respect of loan taken for purchase of plant and machinery and tooling equipment, would the same be subject to tax in the hands of the recipient by virtue of the provisions contained in either section 28(iv) or section 41(1)?**

**CIT v. Mahindra and Mahindra Ltd. [2018] 404 ITR 1 (SC)**

The assessee, Mahindra and Mahindra is advanced with a loan for procurement of capital assets, namely, plant, machinery and tooling equipment from a foreign Company K. Later on, AMC took over K and agreed to waive the principal amount of loan advanced by K to the assessee-company. This was communicated to the assessee-company which filed its return showing Rs.57,74,064 as cessation of its liability towards AMC. The Income-tax Officer concluded that the waiver of the loan amount represented income and held that the sum of Rs. 57,74,064 was taxable under section 28(iv) as a perquisite. The alternate argument of the revenue authorities was that the sum would be taxable under section 41(1) as a waiver of a trading liability.

The Supreme Court observed that for applicability of section 28(iv), income must arise from business or profession and the benefit received has to be in non-monetary form. The amount of Rs. 57,74,064, being a cash receipt, therefore, does not fall under section 28(iv).

For being covered under section 41(1), the assessee-company should have claimed an allowance or deduction in any assessment for any year in respect of a trading liability incurred by the assessee. In this case, the loan was taken for procurement of capital assets, namely, plant, machinery and tooling equipment. The purchase amount had not been debited to the trading account or to the profit and loss account in any of the assessment years. Hence, waiver of such loan would not tantamount to cessation of a trading liability

## LESSON ROUND UP

- Sections 28 to 44D contain the provisions for computation of Income from Business and Profession.
- Section 28 defines the scope of income which can be taxed under this head.
- Section 29 specify the method of computation of income under the business or profession.
- Expenses/allowances expressly allowed by the Act are listed under sections 28 to 37, whereas sections 40 and 40A enumerate those expenses which are expressly disallowed and 43B expenses to be made on actual payment basis, while computing taxable income under this head.
- Section 44AA provides for maintenance of accounts by the assessee carrying on business or profession.

- Mandatory tax audit of accounts of the persons carrying on business or profession is prescribed in section 44AB.
- Computation of profit from business and profession on presumptive basis are covered under sections 44AD, 44ADA and 44AE.
- Section 44B laid down special provisions for computing profits and gains of shipping business in case of non-residents.

### SELF TEST QUESTIONS

*These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.*

#### Multiple Choice Questions “MCQs”

1. Preliminary Expenses u/s 35D, qualifying so would be deductible in ----- equal installments
  - a) Five
  - b) Seven
  - c) Ten
  - d) One

Answer: (a)

2. The rate of depreciation specified for intangible assets is?
  - a) 25%
  - b) 30%
  - c) 40%
  - d) 15%

Answer: (a)

3. Salary, Bonus etc. under section 40(b) is allowed to:
  - a) Working partner
  - b) Non-working partner
  - c) All the partners
  - d) None of the partners

Answer: (a)

### SUGGESTED READINGS

1. **Direct Taxes Law and Practice**  
Author : Dr. Vinod K. Singhania & Dr. Kapil Singhania  
Publisher : Taxmann  
Year : 2019  
Edition : 2019
2. **Direct Taxes Ready Reckoner with Tax Planning**  
Author : Dr. Girish Ahuja & Dr. Ravi Gupta



# Lesson 4

## Part IV – Income from Capital Gains

### LESSON OUTLINE

- Capital Gains
- Capital Asset [Section 2(14)]
- Short Term & Long Term Assets
- Transfer [Section 2(47)]
- Mode of Computation
- Ascertainment of Cost in Specified Circumstances [Section 49]
- Advanced Money Received [Section 51]
- Exemption from Capital Gain Tax
- Tax Rates
- Case Law
- LESSON ROUND UP
- SELF TEST QUESTION

### LEARNING OBJECTIVES

The provisions for computation of Income from capital gains are covered under sections 45 to 55 of the Income Tax Act, 1961. Section 2(14) defines the term capital gain and section 45, the charging section lays down basis of charge for taxability of capital gain/loss arises on transfer of capital asset.

Taxability of capital gain depends upon the nature of capital gain i.e., short term capital gain or long term capital gain. The type of capital gain depends upon the period for which the capital asset is held. The taxability of capital gain shall satisfy the conditions like there should be capital asset, the asset is transferred by the assessee, such transfer takes place during the previous year, etc. To give relief to the assessee, the concept of exemption introduced under section 54, 54B, 54D, 54EC, 54EE, 54F, 54G, 54GA, 54GB and 54H.

At the end of this lesson, you will learn

- the conditions to be satisfied for income to be chargeable under this head,
- which assets are classified as capital asset,
- the year in which the capital gains are chargeable to tax,
- classification of capital gain into long term and short term,
- which transactions are not regarded as transfer,
- what are the exemptions available in respect of capital gains,
- when can the assessing officer make a reference to the valuation officer.

## CAPITAL GAINS

### Proforma for Computation of Income under the head “Capital Gains”

Particulars	Short Term Capital Gain		Long Term Capital Gain	
	Amt. (Rs.)	Amt. (Rs.)	Amt. (Rs.)	Amt. (Rs.)
Full value of consideration received or accruing as a result of transfer	Xxxx		xxx	
Less: Expenditure incurred wholly and exclusively in connection with such transfer (for e.g., brokerage on sale)				
(Note: Deduction on account of STT paid will not be allowed)	Xxxx		xxx	
Net Sale Consideration		Xxx		xxx
Less:	Cost of acquisition	Xxx	Indexed Cost of acquisition	xxx
Less:	Cost of improvement	xxx	Indexed Cost of improvement	xxx
	Short Term Capital Gain	Xxx	Long Term Capital Gain	xxx
	Exemption under sections 54B/54D	Xxx	Exemption under sections 54/ 54B/ 54D/ 54EC/ 54EE/54F	xxx
Short-term Capital Gain (STCG)		xxx	Long-term Capital Gains (LTCG)	xxx

Sections 45 to 55A of the Income-tax Act, 1961 deal with capital gains.

Section 45 of the Act, provides that any profits or gains arising from the transfer of a capital asset effected in the previous year shall, save as otherwise provided in various sections of Sec. 54, be chargeable to income-tax under the head “Capital Gains” and shall be deemed to be the income of the previous year in which the transfer took place.

Doubts may arise as to whether “Capital Gains” being a capital receipt can be brought to tax as income. It may be noted that the ordinary accounting canons of distinctions between a capital receipt and a revenue receipt are not always followed under the Income-tax Act. Section 2(24)(vi) of the Income-tax Act specifically provides that “Income” includes “any capital gains chargeable under Section 45(1)”. It may not be out of place to mention here that in the absence of a specific provision in Section 2(24) capital gains have no logic to be taxed as income. The constitutional validity of the provisions of the Act relating to capital gains was challenged in *Navin Chandra Mafatlal v. C.I.T. (1955) 27 ITR 245*. The Supreme Court while upholding

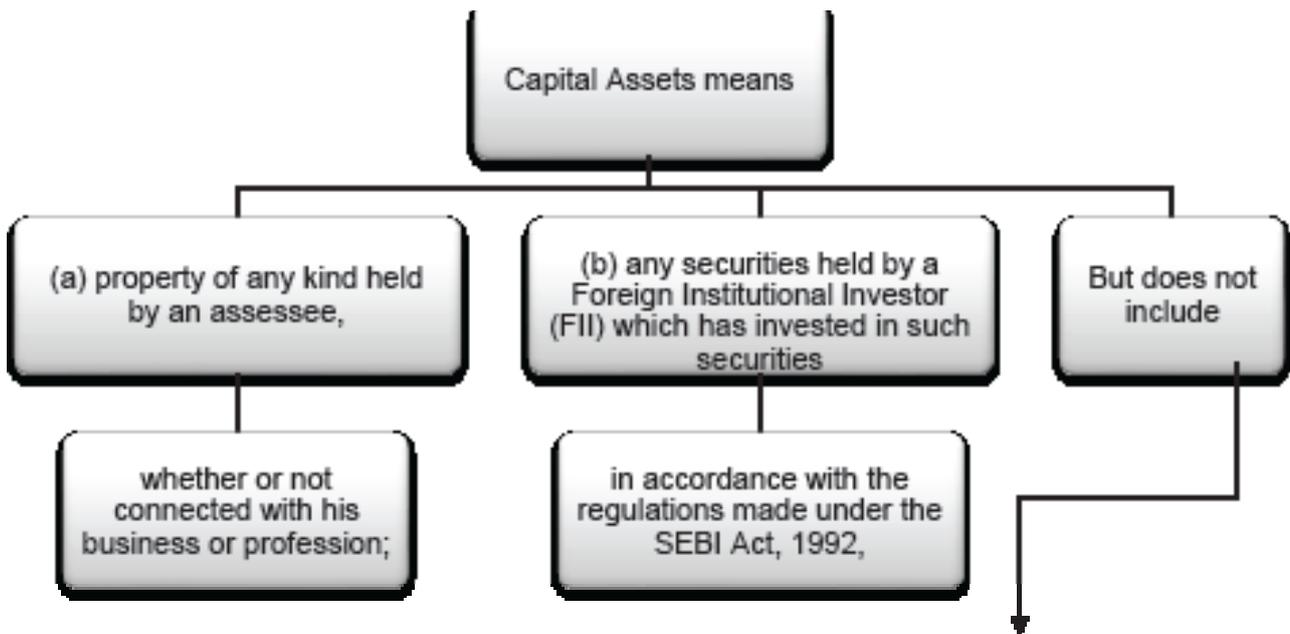
the competence of parliament in legislating with regard to capital gains as part of income, observed that the term income should be given the widest connotation so as to include capital gains within its scope. However, all capital profits do not necessarily constitute capital gains. For instance, profits on re-issue of forfeited shares, profits on redemption of debentures, premium on issue of shares, are capital profits and not capital gains, hence, not liable to tax.

The requisites of a charge to income-tax, of capital gains under Section 45(1) are:

- (i) There must be a capital asset.
- (ii) The capital asset must have been transferred.
- (iii) The transfer must have been effected in the previous year.
- (iv) There must be a gain arising on such transfer of a capital asset.
- (vi) Such capital gain should not be exempt under Sections 54, 54B, 54D, 54EC, 54EE, 54ED, 54F, 54G, or 54GA

These requisites are briefly analysed below.

**CAPITAL ASSET [Section 2(14)]**





- (i) any stock-in-trade (other than securities held by FII mentioned in clause (b) above), consumable stores or raw-materials held for the purposes of his business or profession;  
The exclusion of stock-in-trade from the definition of capital asset is only in respect of sub-clause (a) above and not sub-clause (b). This implies that even if the nature of such security in the hands of the Foreign Portfolio Investor is stock in trade, the same would be treated as a capital asset and the profit on transfer would be taxable as capital gains.
- (ii) personal effects that is to say, movable property (including wearing apparel and furniture ) held for personal use by the assessee or any member of his family dependent on him but excludes
- a) jewellery;
  - b) archaeological collections;
  - c) drawings;
  - d) paintings;
  - e) sculptures; or
  - f) any work of art
- For this purpose, the expression 'jewellery' includes the following:
- (1) Ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals, whether or not containing any precious or semi-precious stones and whether or not worked or sewn into any wearing apparel;
  - (2) Precious or semi-precious stones, whether or not set in any furniture, utensil or other article or worked or sewn into any wearing apparel.
- (iii) Rural agriculture land excludes :
- a) any area within the jurisdiction of a municipality or a cantonment board and which has a population of not less than ten thousand; or
  - b) any area within the distance, measured aerially from the jurisdiction of a municipality or a cantonment board –
    - I. not being more than two kilometres, from the local limits of any municipality or cantonment board and which has a population of more than ten thousand but not exceeding one lakh
    - II. not being more than six kilometres, from the local limits of any municipality or cantonment board and which has a population of more than one lakh but not exceeding ten lakh
    - III. not being more than eight kilometres, from the local limits of any municipality or cantonment board and which has a population of more than ten lakh.
  - (iv) 6 per cent Gold Bonds, 1977 or 7 per cent Gold Bonds, 1980 or National Defence Gold Bonds, 1980 issued by the Central Government;
  - (v) Special Bearer Bonds 1991 issued by the Central Govt.
  - (vi) Gold Deposit Bonds issued under the Gold Deposit Scheme, 1999 or deposit certificates issued under the Gold Monetisation Scheme, 2015 notified by the Central Government.

The Supreme Court in the case of Vodafone International Holdings B.V vs. Union of India [2012] 204 Taxman 408 held that influence/persuasion of a parent company over its subsidiary could not be construed as a right in the legal sense.

To supersede this ruling with retrospective effect from 1st April 1962, an Explanation has been inserted to clarify that "property" includes and shall be deemed to have always included any rights in or in relation to an Indian company, including rights of management or control or any other rights whatsoever.

## SHORT-TERM & LONG-TERM ASSETS

- Section 2(42A) defines short term capital asset as a capital asset held by the assessee for not more

than 36 months immediately preceding the date of transfer. Therefore, an asset which is held by the assessee for period of > 36 months immediately preceding the date of transfer is a long-term capital asset.

- However, a security (other than a unit) listed in a recognised stock exchange or a unit of an equity oriented fund, or of UTI or a Zero-Coupon Bond, will be considered as a long-term asset if it is held for period of > 12 months immediately preceding the date of transfer.
- A share of a company not being a share which is listed on a recognised stock exchange in India or an immovable property, being land or building or both, would be treated as a short-term capital asset if it was held by an assessee for not more than 24 months immediately preceding the date of its transfer. Thus, the period of holding of unlisted shares or an immovable property, being land or building or both, for being treated as a long-term capital asset would be “more than 24 months” instead of “more than 36 months”.
- Assets other than short-term capital assets are known as ‘long-term capital assets’ and the gains arising therefrom are known as ‘long-term capital gains’. In the case of other long-term capital assets, the period of holding is determinable subject to any rules made by CBDT. An asset should be held for more than 36 months immediately prior to the date of its transfer to become a long term capital asset. However, where a capital asset, being Immoveable property (land or building or both) is transferred on or after April 1, 2017, then it will be treated as Long Term Capital Asset if it is held for more than 24 months immediately prior to the date of its transfer.

**Period of Holding**

STCA, if held for ≤ 12 month LTCA, if held for > 12 months	<ul style="list-style-type: none"> <li>• Security (other than unit) listed in a recognized stock exchange</li> <li>• Unit of equity oriented fund/ unit of UTI</li> <li>• Zero Coupon bond</li> </ul>
STCA, if held for ≤ 24 month LTCA, if held for > 24 months	<ul style="list-style-type: none"> <li>• Unlisted shares</li> <li>• Land or building or both</li> </ul>
STCA, if held for ≤ 36 month LTCA, if held for > 36 months	<ul style="list-style-type: none"> <li>• Unit of debt oriented fund</li> <li>• Unlisted securities other than shares</li> <li>• Other capital assets</li> </ul>

In determining the period for which a capital asset is held by an assessee, the following must be noted:

- In the case of **shares held in a company in liquidation**, the period subsequent to the date on which the company goes into liquidation shall be excluded;
- In case the **asset becomes the property of the assessee** under the circumstances mentioned in Section 49(1) - discussed later in this lesson - the period for which the asset was held by the previous owner shall be included;
- In the case of the shares in an Indian Company which become the property of the assessee in a **scheme of amalgamation**, the period for which the shares in the amalgamating company were held by the assessee shall be included;
- In the case of a capital asset, being **a share or any other security subscribed to by the assessee**

**on the basis of his right to subscribe to such financial asset or subscribed to by the person in whose favour the assessee has renounced his right to subscribe to such financial asset**, the period shall be reckoned from the date of allotment of such financial asset;

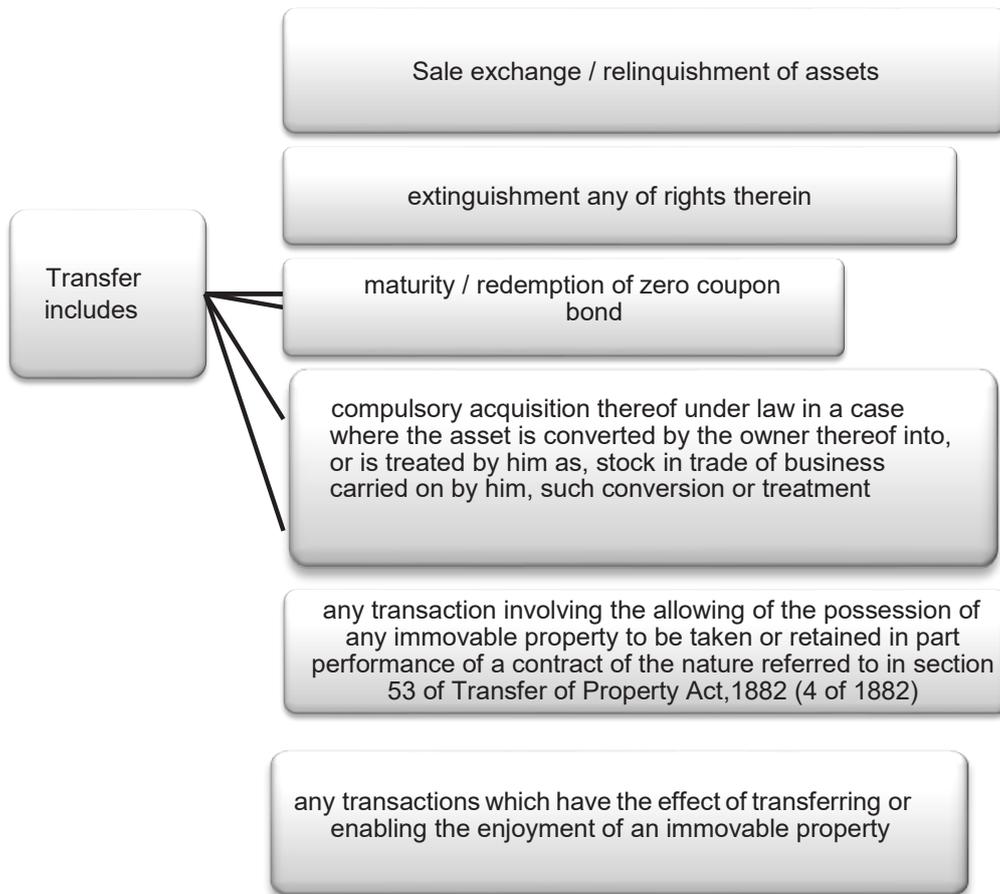
- (v) In the case of a capital assets, being the **right to subscribe to any financial asset**, which is renounced in favour of any other person, the period shall be reckoned from the date of the offer of such right by the company or institution, as the case may be, making such offer;
- (vi) In the case of a **capital asset, being a financial asset, allotted without any payment and on the basis of holding of any other financial asset**, the period shall be reckoned from the date of the allotment of such financial asset;
- (vii) In the case of a **capital asset, being a share or shares in an Indian company, which becomes the property of the assessee in consideration of a demerger**, there shall be included the period for which the share or shares held in the demerged company were held by the assessee;
- (viii) In the case of a **capital asset, being trading or clearing rights of a recognized stock exchange in India acquired by a person pursuant to demutualisation or corporatisation of the recognized stock exchange in India as referred to in Clause (xiii) of Section 47**, there shall be included the period for which the person was a member of the recognized stock exchange in India immediately prior to such demutualisation or corporatisation;
- (viiiia) In the case of a **capital asset, being equity share or shares in a company allotted pursuant to demutualisation or corporatisation of a recognised stock exchange in India as referred to in Clause (xiii) of Section 47**, there shall be included the period for which the person was a member of the recognized stock exchange in India immediately prior to such demutualisation or corporatisation;

Where preference shares are converted into equity shares, the period of holding shall be considered from the date of acquisition of preference shares. Cost of acquisition of preference shares shall be taken as cost of acquisition of equity shares in the hands of assessee.

Where units are held by an assessee in the consolidating plan of a mutual fund scheme, made in consideration of the allotment to him of units, in the consolidated plan of that scheme of mutual fund, then the period of holding shall also include the period for which the units in consolidating plan of mutual fund scheme were held by him. Cost of acquisition of units in the consolidated plan of mutual fund scheme referred u/s 47(xix) shall be the cost of acquisition of units in the consolidating plan of mutual fund scheme.

## **TRANSFER [SECTION 2(47)]**

The essential requirement for the incidence of tax on capital gains is the transfer of a “capital asset”. The Act contains an inclusive definition of “transfer”, and hence, it includes:



The Supreme court in the case of Vodafone International Holdings B.V. vs. Union of India [2012] 204 Taxman 408 gave the following ruling -

- (a) the transfer of shares in the foreign holding company does not result in an extinguishment of the foreign company's control of the Indian company.
- (b) It does not constitute an extinguishment and transfer of an asset situated in India.
- (c) Transfer of foreign holding company shares offshore, cannot result in an extinguishment of the holding companies right of control of the Indian company and the same does not constitute extinguishment and transfer of an asset/management and control of property situated in India.

To supersede this ruling with retrospective effect from 1st April 1962, Explanation 2 to section 2(47) has been inserted which defines transfer as follows:

“Transfer” includes and shall be deemed to have always included disposing of or parting with an asset or any interest therein, or creating any interest in any asset in any manner whatsoever, directly or indirectly, absolutely or conditionally, voluntarily or involuntarily by way of an agreement (whether entered into in India or outside India) or otherwise, notwithstanding that such transfer of rights has been characterized as being effected or dependent upon or flowing from the transfer of a share or shares of a company registered or incorporated outside India.

The above transactions would be deemed as a transfer notwithstanding that such transfer of rights has been characterized as being effected or dependent upon or flowing from the transfer of a share or shares of a company registered or incorporated outside India.

The distribution of capital assets on the dissolution of a firm, body of individuals or other association of persons,

is also regarded as transfer liable to capital gains tax. For the purposes of computing capital gain in such cases, the fair-market value of the capital asset on the date of such distribution will be deemed to be the full value of consideration received or accruing as a result of transfer of the capital asset.

### What doesn't constitute Transfer?

Section 47 specifies certain transactions which will not be regarded as a transfer, as below:

- ✓ Any distribution of capital assets on **total / partial partition of HUF**
- ✓ Any transfer of a capital asset under a **gift / irrevocable trust** (doesn't include ESOP's)
- ✓ Transfer of asset from **Holding Company to its wholly owned Indian Subsidiary and vice-versa**
- ✓ Transfer of capital asset from **amalgamating company to amalgamated company**, in a scheme of amalgamation, as long as the resultant company is an Indian Company
- ✓ Transfer of capital asset from **demerged company to resulting company**, in a scheme of demerger, as long as the resultant company is an Indian Company
- ✓ **Transfer / issue of shares by the resulting company to the shareholders of the demerged company**, if such transfer was made in consideration of such demerger
- ✓ Transfer of shares by a shareholder, held in the amalgamating company, in a scheme of amalgamation, if such transfer is made as a consideration, by way of **allotment of shares in the amalgamated Indian company**
- ✓ Transfer of **rupee denominated bonds / any government security**, outside India, by a non-resident to another non-resident
- ✓ **Redemption of sovereign gold bonds**, issued by RBI, by an individual
- ✓ **Transfer of any capital asset to the Government / University / National Museum / National Art Gallery**, any work of art, book, manuscript, drawing, painting, print
- ✓ **Transfer made outside India of Rupee Denominated Bond (RDB's) of an Indian Company**, issued outside India by a non-resident to another non-resident.
- ✓ **Transfer by way of conversion of bonds / debentures / preference shares into equity shares of that Company**
- ✓ Transfer of capital asset under **reverse mortgage**
- ✓ Transfer by a unit holder under **consolidation plans / schemes of Mutual Fund**

### Year of Chargeability as "Capital Gains"

Capital gains shall be Chargeable in the Previous Year in which the transfer takes place. Some exceptions to this Rule are :

#### (i) Insurance Receipts [Section 45(1A)]

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

- flood, typhoon, hurricane, cyclone, earthquake or other convulsion of nature; or
- riot or civil disturbance; or
- accidental fire or explosion; or

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

any profits or gains arising from receipt of such money or other assets shall be chargeable to income-tax under the head “Capital gains” and shall be deemed to be the income of the such person for the previous year in which such money or other asset was received and for the purpose of section 48, value of any money or the FMV of other assets on the date of such receipt shall be deemed to be the full value of consideration received or accruing as a result of the transfer of such capital asset.

### **(ii) Conversion or treatment of a capital asset as stock-in-trade [Section 45(2)]**

A person who is the owner of a capital asset may convert the same or treat it as stock-in-trade of the business carried on by him. As noted above, the above transaction is a transfer.

As per section 45(2), notwithstanding anything contained in section 45(1), being the charging section, the profits or gains arising from the above conversion or treatment will be chargeable to income-tax as his income of the previous year in which such stock-in-trade is sold or otherwise transferred by him and for the purpose of section 48, the fair market value of the asset on the date of such conversion or treatment shall be deemed to be the full value of the consideration received as a result of the transfer of the capital asset.

Income arising on account of Stock in trade:

1. Business Income = Sale price of stock in trade (-) FMV on the date of conversion
2. Capital Gain= FMV on the date of conversion (-) Cost/Indexed cost of acquisition / improvement [Indexation benefit would be considered in relation to the year of conversion of capital asset into stock in trade.
3. Both Capital Gains and Business income are chargeable to tax in the year in which stock-in-trade is sold or otherwise transferred.

### **(iii) Transfer of beneficial interest in any securities [Section 45(2A)]**

As per section 45(2A), where any person has had at any time during the previous year any beneficial interest in any securities, then, any profits or gains arising from the transfer made by the Depository or participant of such beneficial interest in respect of securities shall be chargeable to tax as the income of the beneficial owner of the previous year in which such transfer took place and shall not be regarded as income of the depository who is deemed to be the registered owner of the securities by virtue of section 10(1) of the Depositories Act, 1996 and For the purposes of section 48 and proviso to section 2(42A), the cost of acquisition and the period of holding of securities shall be determined on the basis of the first-in-first-out (FIFO) method.

### **(iv) Introduction of capital asset as capital contribution [Section 45(3)]**

Where a person transfers a capital asset to a firm, AOP or BOI in which he is already a partner/ member or is to become a partner/ member by way of capital contribution or otherwise, the profits or gains arising from such transfer will be chargeable to tax as income of the previous year in which such transfer takes place and For the purpose of section 48, the value of the consideration will be the amount recorded in the books of account of the firm, AOP or BOI as the value of the capital asset.

### **(v) Distribution of capital assets on dissolution of firm/ AOP or BOI [Section 45(4)]**

The profits or gains arising from the transfer of capital assets by way of

- distribution of capital assets on the dissolution of a firm or AOP or BOI or
- otherwise

shall be chargeable to tax as the income of the firm etc. of the previous year in which such transfer takes place and For the purpose of section 48, the fair market value of the asset on the date of such transfer shall be the full value of consideration.

Since the tax treatment accorded to a LLP and a general partnership is the same, the conversion from a general partnership firm to an LLP will have no tax implications if the rights and obligations of the partners remain the same after conversion and if there is no transfer of any asset or liability after conversion. However, if there is a change in rights and obligations of partners or there is a transfer of asset or liability after conversion, then the provisions of section 45 would get attracted.

#### **(vi) Compensation on compulsory acquisition [Section 45(5)]**

Sometimes, a building or some other capital asset belonging to a person is taken over by the Central Government by way of compulsory acquisition. In that case, the consideration for the transfer is determined or approved by the Central Government or RBI. Such capital gains are chargeable as income of the previous year in which such compensation or part thereof is received.

**Enhanced Compensation** - Many times, persons whose capital assets have been taken over by the Central Government and who get compensation from the Government go to the Court of law for enhancement of compensation. If the court awards a compensation which is higher than the original compensation, the difference thereof will be chargeable to capital gains in the year in which the same is received from the government.

**Cost of acquisition/improvement in case of enhanced compensation** - For this purpose, the cost of acquisition and cost of improvement shall be taken to be nil.

**Compensation received in pursuance of an interim order deemed as income chargeable to tax in the year of final order** - In order to remove the uncertainty regarding the year in which the amount of compensation received in pursuance of an interim order of the Court, Tribunal or other authority is to be charged to tax, a proviso has been inserted after clause (b) to provide that such compensation shall be deemed to be income chargeable under the head 'Capital gains' in the previous year in which the final order of such Court, Tribunal or other authority is made.

**Reduction of enhanced compensation** - Where capital gain has been charged on the compensation received by the assessee for the compulsory acquisition of any capital asset or enhanced compensation received by the assessee and subsequently such compensation is reduced by any Court, Tribunal or any authority, the assessed capital gain of that year shall be recomputed by taking into consideration the reduced amount. This re-computation shall be done by way of rectification.

**Death of the transferor**- It is possible that the transferor may die before he receives the enhanced compensation. In that case, the enhanced compensation or consideration will be chargeable to tax in the hands of the person who received the same.

#### **Taxability of capital gains in case of Specified Agreement [Section 45(5A)]**

- in case of an assessee being individual or Hindu undivided family,
- who enters into a specified agreement for development of a project,
- the capital gain arising from such transfer shall be chargeable to income-tax as income of the previous year in which the certificate of completion for the whole or part of the project is issued by the competent authority.

**Full value of consideration:** For this purpose, the stamp duty value of his share, being land or building or both, in the project on the date of issuing of said certificate of completion as increased by any consideration received in cash, if any, shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of the capital asset.

**Non-applicability of the beneficial provision:** It may, however, be noted these beneficial provisions would not apply, where the assessee transfers his share in the project on or before the date of issue of said completion certificate and the capital gain tax liability would be deemed to arise in the previous year in which such transfer took place. In such a case, full value of consideration received or accruing shall be determined by the general provisions of the Act.

**Meaning of certain terms:**

**Competent authority:** The authority empowered to approve the building plan by or under any law for the time being in force

**Meaning of Specified Agreement:** Specified agreement means the registered agreement in which a person owning land or building or both, agrees to allow another person to develop a real estate project on such land or building or both, in consideration of a share, being land or building or both in such project, whether with or without payment of part of the consideration in cash.

**Stamp duty value:** The value adopted or assessed or reassessable by any authority of Government for the purpose of payment of stamp duty in respect of an immovable property being land or building or both.

### **CAPITAL GAINS ON DISTRIBUTION OF ASSETS BY COMPANIES IN LIQUIDATION [SECTION 46]**

- (1) **In the hands of liquidated company:** Where the assets of a company are distributed to its shareholders on its liquidation, such distribution shall be regarded as a transfer by the company for the purposes of section 45 [Section 46(1)].
- (2) **In the hands of shareholders:** Shareholders receive money or other assets from the company on its liquidation. They will be chargeable to income-tax under the head 'capital gains' in respect of the market value of the assets received on the date of distribution, or the moneys so received by them. The portion of the distribution which is attributable to the accumulated profits of the company is to be treated as dividend income of the shareholder under section 2(22)(c), which is subject to dividend distribution tax in the hands of the company. The same will be deducted from the amount received/ fair market value for the purpose of determining the consideration for computation of capital gains.

Capital gains tax on subsequent sale by the shareholders: If the shareholder, after receipt of any such asset on liquidation of the company, transfers it, then Fair Market value on the date of distribution would be treated as cost of acquisition of such asset.

### **CAPITAL GAINS ON BUYBACK OF SHARES OR SPECIFIED SECURITIES [SECTION 46A]**

- (1) **In case of specified securities other than shares:** Any consideration received by a holder of specified securities (other than shares) from any company on purchase of its specified securities is chargeable to tax in the hands of the holder of specified securities. The difference between the cost of acquisition and the value of consideration received by the holder of securities is chargeable to tax as capital gains in his hands. The computation of capital gains shall be made in accordance with the provisions of section 48.

Such capital gains shall be chargeable in the year in which such securities were purchased by the company. For this purpose, "specified securities" shall have the same meaning as given in Section 68 of the Companies Act, 2013, "specified securities" includes employees' stock option or other securities as may be notified by the Central Government from time to time.

**Note** – With effect from 5.7.2019, as far as shares are concerned, this provision would be attracted in

the hands of the shareholder only if the shares are bought back by a company, other than a domestic company. Prior to that date, this provision was attracted even in the hands of shareholders of domestic company, where listed shares were bought back.

- (2) **In case of shares (whether listed or unlisted):** With effect from 5.7.2019, in case of buyback of shares (whether listed or unlisted) by domestic companies, additional income-tax @ 20% (plus surcharge @ 12% and cess @ 4%) is leviable in the hands of the company.

Consequently, the income arising to the shareholders in respect of such buyback of shares by the domestic company would be exempt under section 10(34A), since the domestic company is liable to pay additional income-tax on the buyback of shares.

### MODE OF COMPUTATION

Section 48 of the Act provides that the income chargeable under the head “capital gains” shall be computed by deducting from the full value of consideration received or accruing as a result of the transfer of the capital asset the following amounts –

- (i) the expenditure [No deduction will be allowed in respect of Securities Transaction Tax (STT paid)] incurred wholly and exclusively in connection with such transfer;
- (ii) the cost of acquisition of the capital asset and the cost of any improvement thereto

However, in the case of an assessee who is a non-resident, capital gains arising from the transfer of a capital asset, being shares in, or debentures of, an Indian company shall be computed by converting the cost of acquisition, expenditure incurred wholly and exclusively in connection with such transfer and the full value of the consideration received or accruing as a result of the transfer of the capital asset into the same foreign currency as was initially utilised in the purchase of the shares or debentures, and the capital gains so computed in such foreign currency shall be reconverted into Indian currency.

The Finance Act, 1997 has with effect from 1.4.1998 denied the benefit of indexation of cost of bonds and debentures other than indexed bonds issued by the government.

Provided also that where shares, debentures or warrants referred to in the proviso to Clause (iii) of Section 47 are transferred under a gift or an irrevocable trust, the market value on the date of such transfer shall be deemed to be the full value of consideration received or accruing as a result of transfer for the purposes of this section.

The RBI has recently permitted Indian corporate to issue rupee denominated bonds outside India as a measure to enable Indian corporate to raise funds from outside India. For providing relief to non-residents who bear risk of currency fluctuation, w.e.f. AY 2017-18, section 48 has been amended to provide that capital gain, arising in case of appreciation of rupee between the date of issue and the date of redemption against the foreign currency in which investment is made, shall be exempt from tax on capital gains.

Benefit of Indexation shall be available in the case of long term capital gain arising on transfer of sovereign Gold Bonds.

For this purpose:

- (i) “**foreign currency**” and “**Indian currency**” have the meanings respectively assigned thereto in Section 2 of the Foreign Exchange Management Act, 1999, and
- (ii) the conversion of Indian currency into foreign currency and the re-conversion of foreign currency into Indian currency shall be at the rate of exchange prescribed in that behalf;
- (iii) “**indexed cost of acquisition**” means an amount which bears to the cost of acquisition the same proportion as Cost Inflation Index for the year in which the asset is transferred bears to the Cost Inflation Index for the first year in which the asset was held by the assessee or for the year beginning on the 1st day of April 2001 whichever is later;

- (iv) “**indexed cost of improvement**” means an amount which bears to the cost of improvement the same proportion as Cost Inflation Index for the year in which the asset is transferred bears to the Cost Inflation Index for the year in which the improvement to the asset took place; and
- (v) “**cost inflation index**”, in relation to a previous year, means such Index as the Central Government may, having regard to seventy-five per cent of average rise in the Consumer Price Index (urban) the immediately preceding previous year to such previous year, by notification in the Official Gazette, specify in this behalf. (Refer to CII Table below)

FY	CII
2001-02	100
2002-03	105
2003-04	109
2004-05	113
2005-06	117
2006-07	122
2007-08	129
2008-09	137
2009-10	148
2010-11	167
2011-12	184
2012-13	200
2013-14	220
2014-15	240
2015-16	254
2016-17	264
2017-18	272
2018-19	280
2019-20	289

Cost of acquisition shall have to be adjusted by the Cost Inflation Index to arrive at the indexed cost of acquisition.

**Note:** Base year for the purpose for calculation of Indexed cost of acquisition or improvement has been shifted from 1981-82 to 2001-2002. Accordingly if any assessee/previous owner has acquired capital asset prior to 1-4-2001 then he will have option to choose actual cost of acquisition or FMV as on 1-4-2001 as his cost of acquisition. Cost of improvement incurred by assessee or previous owner prior to 1-4-2001 shall taken as NIL. In case of goodwill, trademark or other intangible assets, the option to take cost of acquisition or market price which ever is higher is not available (as on 01.04.2001), irrespective its purchased or self generated.

#### Cost of Acquisition of certain assets

Asset	Cost of Acquisition
Goodwill, if self-generated	NIL
Goodwill, if acquired	Purchase Price
On Gift / inheritance / distribution of assets of HUF on partition	Cost to the previous owner
Bonus Shares allotted prior to 1st Apr'01	FMV (1st Apr'01)
Bonus Shares allotted post 1st Apr'01	NIL

Rights Shares	Amount paid to acquire the shares
Rights shares which are purchased by person in whose favour the assessee has renounced the rights entitlement	Purchase price paid to the renouncer + Price paid for acquiring rights shares

Cost of acquisition for stock in trade converted into capital asset, shall be the Fair Market Value.

### Illustration 1 :

Mr Nagendra Kumar converts his capital asset acquired for an amount of INR 125000 in 2005-06, into stock in trade in the FY 2016-17. He thereafter sells this asset for INR 10,00,000 in 2019-20.

Please advise on the taxability.

### Solution

It is to be noted that when the owner of a capital asset, converts it in to stock in trade, the “capital gains” arises in the year of such conversion, that is regarded as transfer, i.e., in the year in which the transfer (conversion) was effected. Therefore, in this case the Capital Gains arises in FY 2016-17. However, the same will be taxable only in the year the asset was sold, and along with it shall be chargeable to tax, the relevant income under the head “Profits / Gains from Business / Profession”.

Particulars	INR
FMV of asset on date of conversion	7,50,000
Indexed Cost of acquisition[See Note 1]	2,82,051
<b>Capital Gain arises in FY 2016-17</b>	<b>4,67,949</b>
Finally sold for	10,00,000
Cost of Acquisition	7,50,000
Business Income arises in FY 2019-20	2,50,000

### Note:

- 1) Indexed Cost of Acquisition is INR 125000/117\*264 (refer to the CII table for the indices of respective years)
- 2) The Capital Gain arises in FY 2016-17
- 3) The Capital Gain is taxable only in FY 2019-20 when the asset is sold, along with the Business Income

### Illustration 2 :

Mr Srinivasan, purchases 2000 equity shares in ABC Ltd., for INR 50 per share (Brokerage 1%), in Feb 1997. He gets 200 Bonus shares in Sep 2000. He again gets 2200 bonus shares in Sep 2007. FMV of the Shares on 1st Apr'01 was INR 125.

In Jan'20, he sells all the shares for INR 500 per share (Brokerage 2%).

Compute the Capital Gains Tax in the hands of Srinivasan in FY 2019-20.

### Solution

Cost of Acquisition	Nos.	Per Share	Total INR
Original	2,000	50.50	1,01,000
Bonus Shares prior to 1st Apr'01	200	-	25,000
Bonus Share post 1st Apr'01	2,200	-	-

Full value of Consideration	4,400	490.00	21,56,000
Indexed Cost of Acquisition			
Original (2000 x 125 x 289/100)		7,22,500	
Bonus (200 x 125 x 289/100)		72,250	7,94,750
<b>Capital Gains (Long Term)</b>			<b>13,61,250</b>

**Note:**

- The brokerage is netted against the costs and sales vales
- The Cost of Acquisition of Bonus Shares acquired prior to 1st Apr'01 is the FMV on 1st Apr'01 and for the ones acquired post 1st Apr'01 is NIL
- For the Original Shares, since the acquisition cost (INR 50) is less than the FMV (INR 125) as on 1st Apr'01, the FMV as on 1st Apr'01 is considered for computing the indexed cost of acquisition
- Refer to the tables for the Indices used in the computation

**Cost of Improvement**

Section 55 mentions that in relation to a capital asset, being goodwill, or a right, the cost of improvement will be taken as NIL.

For any other capital asset:

- a) Cost of improvement, prior to 1st Apr' 01 shall be Nil
- b) Cost of improvement shall be all expenditure of a capital nature, incurred in making additions / alterations on or after 01.04.2001.

**Illustration 3 :**

M & sons, HUF, had purchased a land for INR 150,000 in 2002-03. In the PY 2006-07, a partition takes place and the Coparcener, Mr. B, gets this plot, valued at INR 200,000. In PY 2007-08, he incurs expenses of INR 250,000 on the plot towards fencing of the plot of land. Mr. B then sells this plot at INR 15,00,000 in PY 2019-20. You are required to compute the capital gains for AY 2020-21.

**Solution :**

Cost of acquisition	1,50,000
Cost of Improvement	2,50,000
Full Value of Consideration	15,00,000
Indexed Cost	
Acquisition [See Note (b)]	4,12,857
Improvement [See Note (c)]	5,60,077
<b>Capital Gains</b>	<b>5,27,066</b>

**Note:**

- a) Although the cost of acquisition for the land, in case of partition of HUF would be the cost to the previous owner, the year would be the year in which he gets the asset upon partition, that is FY 2006-07
- b) Indexed Cost of Acquisition therefore is INR  $(150,000/105) * 289 = 412857$
- c) Indexed Cost of Improvement therefore is INR  $(250,000/129) * 289 = 560077$

**Illustration 4 :**

Mr. X purchases a property for INR 50000 on 3rd May 1975. The following expenses were incurred by him:

- o Improvement of property in 1998-99 INR 250,000
- o Construction of two floors in 2002-03 INR 800,000
- o Reconstruction and refurbishment of property in 2012-13 INR 15,00,000

FMV of property on 1st Apr'01 is 10,00,000. He sells the house on 9th Sep'19 for INR 80,00,000 and incurs INR 250,000 on transfer. Compute the Capital Gains taxable in his hands in AY 2020-21.

**Solution :**

		<b>INR</b>
	<b>Net Sale of Consideration</b>	<b>77,50,000</b>
Less	Indexed Cost of Acquisition[(FMV as on 01.04.2001 or cost of acquisition whichever is higher i.e. $10,00,000 \times 289/100$ )]	28,90,000
	Indexed Cost of Improvement [ $800000 \times 289/105$ ]	22,01,905
	Indexed Cost of Improvement [ $1500000 \times 289/200$ ]	21,67,500
	<b>Long Term Capital Gains</b>	<b>4,90,595</b>

**Note:**

The improvement to the property only after 1st Apr'01 are considered. The costs are indexed using the indices from the CII table.

**ASCERTAINMENT OF COST IN SPECIFIED CIRCUMSTANCES [SECTION 49]**

A person becomes the owner of a capital asset not only by purchase but also by several other methods. Section 49 gives guidelines as to how to compute the cost under different circumstances.

**(1) Cost to previous owner deemed as cost of acquisition of asset:** In the following cases, the cost of acquisition of the asset shall be deemed to be cost for which the previous owner of the property acquired it. To this cost, the cost of improvement to the asset incurred by the previous owner or the assessee must be added:

Where the capital asset became the property of the assessee:

- (i) on any distribution of assets on the total or partition of a HUF;
- (ii) under a gift or will;
- (iii) by succession, inheritance or devolution;
- (iv) on any distribution of assets on the liquidation of a company;
- (v) under a transfer to revocable or an irrevocable trust;
- (vi) under any transfer of capital asset by a holding company to its wholly owned subsidiary Indian company or by a subsidiary company to its 100% holding Indian company, referred to in section 47(iv) and 47(v) respectively;
- (vii) under any transfer referred to in section 47(vi) of a capital asset by amalgamating company to the amalgamated Indian company, in a scheme of amalgamation;

- (viii) under any transfer referred to in section 47(vib), of a capital asset by the demerged company to the resulting Indian company, in a scheme of demerger;
- (ix) by conversion by an individual of his separate property into a HUF property, by the mode referred to in section 64(2).

Accordingly, section 2(42A) provides that in all such cases, for determining the period for which the capital asset is held by the transferee, the period of holding of the asset by the previous owner shall also be considered.

### Indexation benefit from which year

The issue as to whether indexation benefit in respect of a gifted asset shall apply from the year in which the asset was first held by the assessee or from the year in which the same was first acquired by the previous owner was taken up by the Bombay High Court in *CIT v. Manjula J. Shah 16 Taxman 42 (Bom.)*.

As per *Explanation 1* to section 2(42A), in case the capital asset becomes the property of the assessee in the circumstances mentioned in section 49(1), *inter alia*, by way of gift by the previous owner, then for determining the nature of the capital asset, the aggregate period for which the capital asset is held by the assessee and the previous owner shall be considered.

As per the provisions of section 48, the profit and gains arising on transfer of a long-term capital asset shall be computed by reducing the indexed cost of acquisition from the net sale consideration.

The indexed cost of acquisition means the amount which bears to the cost of acquisition the same proportion as Cost Inflation Index (CII) for the year in which the asset is transferred bears to the CII for the year in which the asset was first held by the assessee transferring it i.e., the year in which the asset was gifted to the assessee in case of transfer by the previous owner by way of gift.

The issue under consideration was whether, in a case where the assessee had acquired a capital asset by way of gift from the previous owner, the said asset can be treated as a long-term capital asset considering the period of holding by the assessee as well as the previous owner.

The Bombay High Court held that the indexed cost of acquisition in case of gifted asset has to be computed with reference to the year in which the previous owner first held the asset and not the year in which the assessee became the owner of the asset.

As per the plain reading of the provisions of section 48, however, the indexed cost of acquisition would be determined by taking CII for the year in which in which asset is first held by the assessee.

**Cost of acquisition of shares received under the scheme of Amalgamation:** Where shares in an amalgamated company which is an Indian company become the property of the assessee in consideration of the transfer of shares referred to in section 47(vii) held by him in the amalgamating company under a scheme of amalgamation, the cost of acquisition to him of the shares in the amalgamated company shall be taken as the cost of acquisition of the shares in the amalgamating company [Section 49(2)]

**(2) Cost of acquisition of shares received during the process of conversion of bonds or debentures, debenture stock or deposit certificates:** It is possible that a person might have become the owner of shares or debentures in a company during the process of conversion of bonds or debentures, debenture stock or deposit certificates referred under section 47(x).

In such a case, the cost of acquisition to the person shall be deemed to be that part of the cost of debentures, debenture stock, bond or deposit certificate in relation to which such asset is acquired by that person [Section 49(2A)].

**(3) Cost of acquisition of specified security or sweat equity shares:** Where the capital gain arises from the transfer of specified security or sweat equity shares referred to in section 17(2)(vi), the cost of acquisition of

such security or shares shall be the fair market value which has been taken into account for perquisite valuation [Section 49(2AA)].

**(4) Cost of acquisition of units acquired under consolidated scheme of Mutual Fund:** The cost of acquisition of the units acquired by the assessee in consolidated scheme of mutual fund in consideration of transfer referred in section 47(xviii) shall be deemed to be the cost of acquisition to him of the units in the consolidating scheme of mutual fund [Section 49(2AD)].

**(5) Cost of acquisition of equity shares received at the time of conversion of preference shares:** Cost of acquisition of the equity share of a company, which became the property of the assessee in consideration of transfer referred to in section 47(xb), shall be deemed to be that part of the cost of the preference share in relation to which such asset is acquired by the assessee [Section 49(2AE)].

**(6) Cost of acquisition of units acquired under consolidated plan of Mutual Fund scheme:** Cost of acquisition of the unit or units in the consolidated plan of the scheme of the mutual fund in consideration of a transfer referred to in section 47(xix) shall be deemed to be the cost of acquisition to him of the unit or units in consolidating plan of the scheme of the mutual fund [Section 49(2AF)].

**Cost of acquisition of shares received in the resulting company, in the scheme of demerger:** In the case of a demerger, the cost of acquisition of the shares in the resulting company shall be the amount which bears to the cost of acquisition of shares held by the assessee in the demerged company the same proportion as the net book value of the assets transferred in a demerger bears to the net worth of the demerged company immediately before such demerger [Section 49(2C)].

$$\text{Cost of acquisition of shares in the resulting company} = A \times \frac{B}{C}$$

A = Cost of acquisition of shares held in the demerged company B = Net book value of the assets transferred in a demerger

C = Net worth of the demerged company i.e. the aggregate of the paid up share capital and general reserves as appearing in the books of account of the demerged company immediately before the demerger.

**(7) Cost of acquisition of the shares held in the demerged company:** The cost of acquisition of the original shares held by the shareholder in the demerged company shall be deemed to have been reduced by the amount as so arrived under the sub-section (2C) [Section 49(2D)].

**(8) Cost of acquisition of property subject to tax under section 56(2)(x):** Where the capital gain arises from the transfer of such property which has been subject to tax under section 56(2)(x), the cost of acquisition of the property shall be deemed to be the value taken into account for the purposes of section 56(2)(x) [Section 49(4)].

[For illustration, see Unit 5 of Chapter 4 "Income from Other Sources" under section 56(2)(x)]

**(9) Cost of acquisition of capital asset, being share in the project referred under section 45(5A):** Where the capital gain arises from the transfer of a capital asset, being share in the project, in the form of land or building or both, referred to in section 45(5A) which is chargeable to tax in the previous year in which the completion of certificate for the whole or part of the project is issued by the competent authority), the cost of acquisition of such asset, shall be the amount which is deemed as full value of consideration in that sub-section i.e., stamp duty value on the date of issue of certificate of completion plus cash consideration.

**(10)** However, this does not apply to a capital asset, being share in the project which is transferred on or before the date of issue of said completion certificate [Section 49(7)].

**(11) Cost of acquisition of a capital asset which was used by the assessee as an inventory:** Where the capital gain arises from the transfer of a capital asset which was used by the assessee as inventory earlier before its conversion into capital asset, the cost of acquisition of such capital asset shall be deemed to be the

fair market value of the inventory as on the date on such conversion determined in the prescribed manner [Section 49(9)]

### Capital Gains for Depreciable Assets (Section 50)

Where the capital asset is an asset forming part of a block of assets in respect of which depreciation has been allowed, the provisions of sections 48 and 49 shall be subject to the following modification:

- Where the full value of consideration received or accruing for the transfer of the asset plus the full value of such consideration for the transfer of any other capital asset falling with the block of assets during previous year exceeds the aggregate of the following amounts namely:
  - expenditure incurred wholly and exclusively in connection with such transfer;
  - WDV of the block of assets at the beginning of the previous year;
  - the actual cost of any asset falling within the block of assets acquired during the previous year such excess shall be deemed to be the capital gains arising from the transfer of short-term capital assets.
  - Where all assets in a block are transferred during the previous year, the block itself will cease to exist. In such a situation, the difference between the sale value of the assets and the WDV of the block of assets at the beginning of the previous year together with the actual cost of any asset falling within that block of assets acquired by the assessee during the previous year will be deemed to be the capital gains arising from the transfer of short-term capital assets.

**Cost of acquisition in case of power sector assets [Section 50A]:** With respect to the power sector, in case of depreciable assets referred to in section 32(1)(i), the provisions of sections 48 and 49 shall apply subject to the modification that the WDV of the asset (as defined in section 43(6)), as adjusted, shall be taken to be the cost of acquisition.

### Capital Gains in respect of Slump Sale (Section 50B)

#### Meaning of slump sale [Section 2(42C)]

**Slump sale' means** the transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the individual assets and liabilities in such sales. In other words it is a sale where the assessee transfers one or more undertaking as a whole including all the assets and liabilities as a going concern. The consideration is fixed for the whole undertaking and received by the transferor it is not fixed for each of the asset of the undertaking as a whole by way of such sale. Thus it may be noted that the undertaking as a whole or the division transferred shall be a capital asset.

- Any gains arising from the slump sale of one / more undertakings held for more than 36 months, shall be chargeable to tax as Long-Term Capital Gains in the Previous Year in which the slump sale was effected
- Any gains arising from the slump sale of one / more undertakings held for less than 36 months, shall be chargeable to tax as Short-Term Capital Gains in the Previous Year in which the slump sale was effected
- The Net Worth of the undertaking or the division, as the case may be, shall be deemed to be the Cost of Acquisition / Improvement of the Unit(s) for the purposes of sections 48 and 49 in relation to capital assets of such undertaking or division transferred by way of such sale and the provisions contained in the second proviso to section 48 shall be ignored [Sub-section (2)]. It means no indexation benefit would be available.

**Meaning of certain terms:**

**Net Worth:** Aggregate value of total assets of the undertaking or division **as reduced by** the value of liabilities of such undertaking or division as appearing in the books of account. **However, any change in the value of assets on account of revaluation of assets shall not be considered for this purpose:**

Aggregate value of total assets of undertaking or division:

**In the case of depreciable assets:** The written down value of block of assets determined in accordance with the provisions contained in sub-item (C) of item (i) of section 43(6)(c);

**Capital asset in respect of which 100% deduction is claimed:** In case of capital assets in respect of which the whole of the expenditure has been allowed or is allowable as a deduction under section 35AD: **Nil**;

**For all other assets:** Book value

**Illustration 5 :**

Mohan is the proprietor of Photo Film Agencies which has 2 units, one for printing and the other for binding. He transferred, by way of slump sale, one of the units (Unit 2) on 1st Apr'19, for a total consideration of INR 50,00,000. Expenses on sale were 0.5%. This unit was started in the year 2012-13.

Appended below is the Balance Sheet:

Particulars	Unit 1	Unit 2
Building	7,50,000	15,00,000
Machinery	5,00,000	10,00,000
Debtors	2,50,000	5,00,000
Other Assets	1,00,000	2,00,000
	<b>16,00,000</b>	<b>32,00,000</b>
Capital		40,00,000
Revaluation Reserve		2,50,000
Bank Loan		3,50,000
Creditors		2,00,000
		<b>48,00,000</b>

The Revaluation Reserve was created by upward revaluation of Buildings in Unit 2. Other Assets of Unit 2 include, INR 100,000 of Patents acquired on 1st Jul'15, on which no depreciation has been charged. 75% of Creditors and 25% of Bank Loan is for Unit 2.

Compute the Capital Gains on the slump sale for AY 2020-21.

**Solution :**

The Capital Gains from Slump Sale are as under:

Full Value of Consideration	50,00,000
Expenses on Sale	25,000
Net Sale Consideration	49,75,000
Net Worth	26,44,141
Long Term Capital Gains	23,30,859

## Working Notes

1. The first note details the computation of net worth for Unit 2

	Net Worth		
	Buildings	15,00,000	
Less :	Reval Reserve	<u>2,50,000</u>	
	Net for Buildings		12,50,000
	Machinery		10,00,000
	Debtors		5,00,000
	Other Assets		1,00,000
	Patents		31,641
	Total Assets		28,81,641
Less:	Creditors	1,50,000	
	Bank Loan	87,500	
	Total Liabilities		2,37,500
	Net Worth		26,44,141

2. The second note details the valuation of WDV of Patents

Patents	
Op Block	1,00,000
Dep Y1	25,000
WDV EOY1	75,000
Dep Y2	18,750
WDV EOY2	56,250
Dep Y3	14,063
WDV EOY3	42,188
Dep Y4	10,547
WDV EOY4	31,641

### Computation of Capital Gain in Real Estate Transaction [Section 50C]

Section 50C makes a special provision for determining the full value of consideration in cases of transfer of immovable property. It provides that where the consideration declared to be received or accruing as a result of the transfer of land or building or both, is less than the value adopted or assessed by any authority of a State Government (i.e. “stamp valuation authority”) for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed shall be deemed to be the full value of the consideration, and capital gains shall be computed on the basis of such consideration under Section 48 of the Income-tax Act. Provided that where the stamp duty value does not exceed 105% of the consideration received or accruing as a result of the transfer, the consideration so received or accruing as a result of the transfer shall, for the purposes of computing profits and gains from transfer of such asset, be deemed to be the full value of the consideration. **(Amended by the Finance Act, 2018)**

Rationalization of section 50C in case sale consideration is fixed under agreement executed prior to the date of registration of immovable property (w.e.f. AY 2017-18)

- Section 50C of the Act has been amended in line with section 43CA to provide that where the date of the agreement fixing the amount of consideration and the date of registration for the transfer of the capital asset are not the same, the value adopted or assessed or assessable by the stamp valuation authority on the date of agreement may be taken for the purposes of computing full value of consideration for such transfer.
- It is further provided that this provision shall apply only in a case where the amount of consideration referred to therein, or a part thereof, has been received by way of an account payee cheque or account payee bank draft or by use of electronic clearing system through a bank account or through such other prescribed electronic mode as may be prescribed on or before the date of the agreement of transfer of such immovable property.

**Reference to Valuation Officer:** Where

- the assessee claims before an Assessing Officer that the value so adopted or assessed or assessable by the authority for payment of stamp duty exceeds the fair market value of the property as on the date of transfer and
- the value so adopted or assessed or assessable by such authority has not been disputed in any appeal or revision or no reference has been made before any other authority, court or High Court, the Assessing Officer may refer the valuation of the capital asset to a Valuation Officer as defined in section 2(r) of the Wealth-tax Act, 1957 [Section 50C(2)].
- **Where the value ascertained by such Valuation Officer exceeds the value adopted or assessed or assessable by the Stamp authority:** The value adopted or assessed or assessable shall be taken as the full value of the consideration received or accruing as a result of the transfer [Section 50C(3)].

### Practical Questions (MCQs)

1. Section 50C makes special provision for determining the full value of consideration in cases of transfer of —
- (a) Plant and machinery
  - (b) Land or building
  - (c) All movable property other than plant & machinery and computers.
  - (d) Computers.

Answer: (b) Land or building

2. X entered into an agreement for sale of his house located at Jaipur to Y on 1st April, 2018 for a total sale consideration of Rs. 90 lakh. Y paid an amount of Rs. 20 lakh by account payee cheque to X on the date of agreement and balance was to be paid at the time of registration of deed. However, the conveyance deed could not be executed till 1st Sept., 2019. The Stamp Valuation Authority determined the value of the property on the date of registration of conveyance deed at Rs. 120 lakh and the value determined by the Stamp Valuation Authority on the date of agreement was Rs. 100 lakh. The value for the purpose of capital gain u/s 50C shall be taken:

- (a) Rs. 90 lakh      (b) Rs. 120 lakh
- (c) Rs. 20 lakh      (d) Rs. 100 lakh

Ans: (d)

### Capital Gain on Transfer of Unlisted Shares in a Company [Section 50CA]

This Section is applicable if an assessee transfers shares in a company (other than quoted shares) at less

than the fair market value of such share determined in accordance with prescribed manner. In such case, the FMV of such shares shall be deemed to be the full value of consideration for the purpose of computation of capital gain. Provided that the provisions of this section shall not apply to such transactions undertaken by certain class of persons and subject to such conditions as may be prescribed by CBDT.

**Fair Market Value to be Full Value of Consideration in Certain Cases (Section 50D)**

Capital gains are calculated on transfer of a capital asset, as sale consideration minus cost of acquisition. In some recent rulings, it has been held that where the consideration in respect of transfer of an asset is not determinable under the existing provisions of the Income-tax Act, then, as the machinery provision fails, the gains arising from the transfer of such assets is not taxable.

Section 50D has been inserted to provide that fair market value of the asset on the date of transfer shall be deemed to be the full value of consideration if actual consideration is not attributable or determinable.

**REFERENCE TO VALUATION OFFICER (SECTION 55A)**

With a view to ascertaining the fair market value of a capital asset, the concerned Assessing Officer may refer the valuation of the capital asset to a Valuation Officer appointed by the Income-tax Department in the following cases:

- (a) Where the value of the asset as claimed by the assessee is in accordance with the estimate made by a registered valuer (who works in a private capacity under a licence issued by the Board and his valuation is not binding on the Assessing Officer), but the Assessing Officer is of the opinion that the value so claimed is less than its fair market value (upto june 30, 2012) w.e.f 1st july 2012, the Assessing Officer is enabled to make a reference to the Valuation Officer where in his opinion the value declared by the assessee is at variance from the fair market value [Section 55A(a)].
- (b) Where the Assessing Officer is of the opinion that the fair market value of the asset exceeds the value of the asset by more than ₹ 25,000 or 15 per cent of the value claimed by the assessee whichever is less [Section 55A(b)(i) read with Rule 111AA].
- (c) Where the Assessing Officer is of the opinion that, having regard to the nature of an asset and relevant circumstances, it is necessary so to make a reference to the Valuation Officer [Section 55A(b)(ii)].

It may be noted that in a case where the assessee has opted for substitution of the cost of acquisition of an asset by its fair market value as on 1.4.1981, the fair market value as claimed by him may be higher than its actual fair market value. The provisions of Section 55A(a) and (b)(i) are, therefore, not applicable to such a case. It is, however, open to the Assessing Officer to make a reference to the Valuation Officer under Section 55A(b) (ii).

Note that in cases covered by Section 55A(a) and (b)(i) above it is the duty of the Assessing Officer to refer the valuation of the capital asset in question to the Valuation Officer attached to the department and not to decide the question of the valuation on his own.

**Illustration 6 :**

A has the following incomes for the previous year 2019-20:

	Rs.	
Business income	(--)	30,000 (viz. business loss of 30,000)
Short-term capital gains	6,000	
Long-term capital gains	1,90,000	

A deposits Rs. 9,000 in public provident fund account. You are required to find out his tax liability for the assessment year 2020-21.

**Solution:**

Computation of net Income of Mr. A for the assessment year 2020-21

	Rs.	Rs.
Business Income		(-) 30,000
Capital gain		
– Short-term	6,000	
– Long-term	1,90,000	1,96,000
		1,66,000

Computation of Tax Liability for the assessment year 2020-21

Tax on Total income	Nil
---------------------	-----

**Notes :**

1. If the net income (other than long-term capital gain) is below the amount of first slab which is not taxable (i.e. Rs. 2,50,000), then the long-term capital gain is to be reduced by the amount by which the total income (other than long-term capital gain) falls short of the maximum amount which is not chargeable tax.
2. In this case, net income (other than long-term capital gain) is (-) Rs. 24,000 which will be allowed for carried forward i.e. not to be deducted from Rs. 2,50,000. Therefore, long-term capital gain shall be reduced by Rs. 2,50,000. Thus, no tax shall be leviable on long-term capital gain.

### ADVANCE MONEY RECEIVED [SECTION 51]

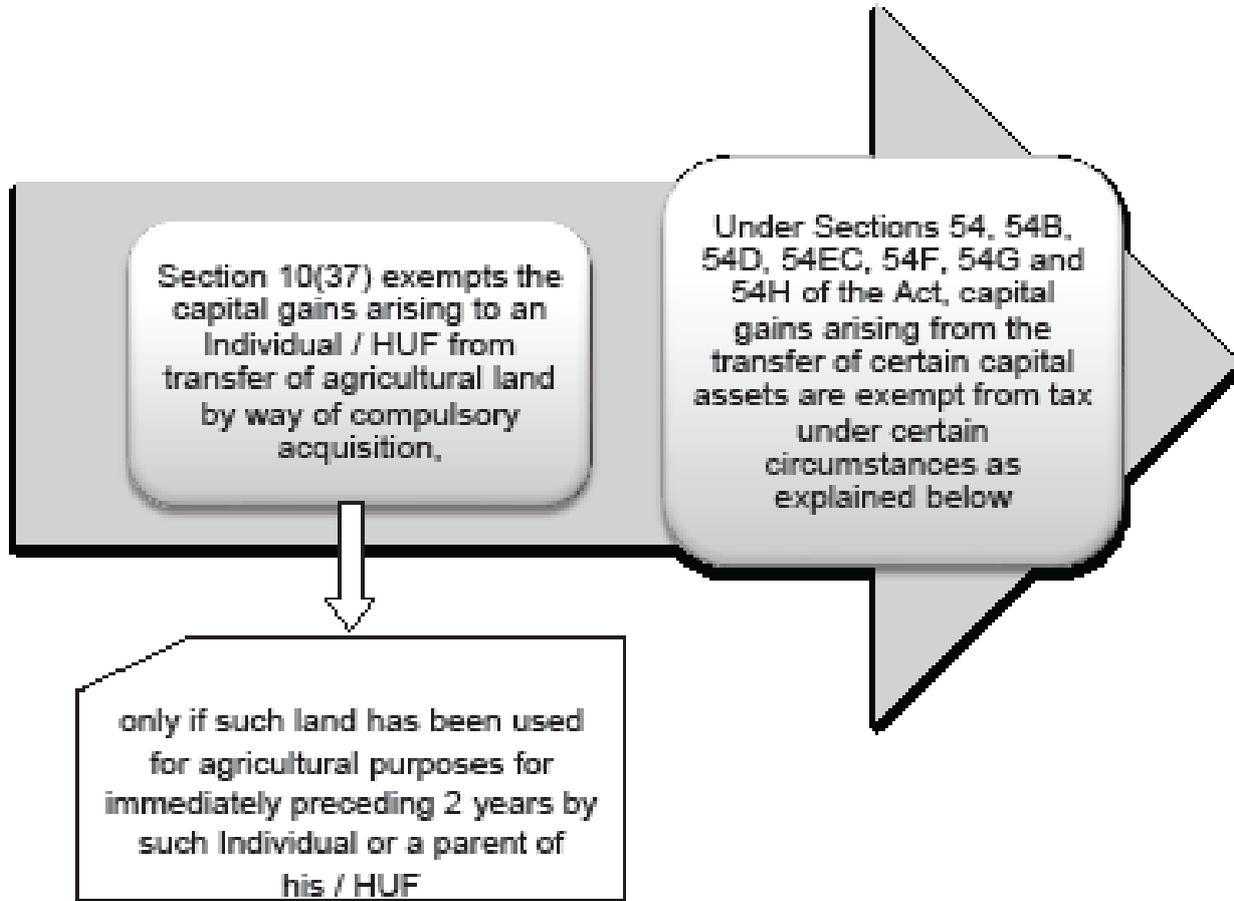
Section 51 provides that while calculating capital gains, the above advance retained by the assessee must go to reduce the cost of acquisition. However, if advance has been received and retained by the previous owner and not the assessee himself, then the same will not go to reduce the cost of acquisition of the assessee.

Section 56(2)(ix) provides for the taxability of any sum of money, received as an advance or otherwise in the course of negotiations for transfer of a capital asset. Consequently, such sum shall be chargeable to income-tax under the head 'Income from other sources', if such sum is forfeited on or after 1st April, 2014 and the negotiations do not result in transfer of such capital asset.

In order to avoid double taxation of the advance received and retained, section 51 provides that where any sum of money received as an advance or otherwise in the course of negotiations for transfer of a capital asset has been included in the total income of the assessee for any previous year in accordance with section 56(2)(ix), then, such amount shall not be deducted from the cost for which the asset was acquired or the written down value or the fair market value, as the case may be, in computing the cost of acquisition.

However, any such sum of money forfeited before 1st April, 2014, will be deducted from the cost of acquisition for computing capital gains.

**EXEMPTION OF CAPITAL GAINS**



**Profit on sale of property used for residence [Section 54]**

**Conditions for claiming exemption:**

- Assessee: Individual or HUF
- Which asset to transfer: Residential house (buildings or lands appurtenant thereto)
- It must be a long-term capital asset
- Income from such house should be chargeable to tax under the head “Income from House Property”

S.No.	Situation	Investment
1.	Where the amount of capital gains exceeds Rs. 2 crore	one residential house in India should be – <ul style="list-style-type: none"> <li>● purchased within 1 year before or 2 years after the date of transfer (or)</li> <li>● constructed within a period of 3 years after the date of transfer.</li> </ul>
2.	Where the amount of capital gains does not exceed Rs. 2 crore	<ul style="list-style-type: none"> <li>● purchase two residential houses in India within 1 year before or 2 years after the date of transfer (or)</li> <li>● construct two residential houses in India within a period of 3 years after the date of transfer.</li> </ul>

Where during any assessment year, the assessee has exercised the option to purchase or construct two residential houses in India, he shall not be subsequently entitled to exercise the option for the same or any other assessment year.

This implies that if an assessee has availed the option of claiming benefit of section 54 in respect of purchase of two residential houses in Jaipur and Jodhpur, say, in respect of capital gains of Rs. 1.50 crores arising from transfer of residential house at Bombay in the P.Y.2019-20 then, he will not be entitled to avail the benefit of section 54 again in respect of purchase of two residential houses in, say, Pune and Baroda, in respect of capital gains of Rs. 1.20 crores arising from transfer of residential house in Jaipur in the P.Y.2023-24, even though the capital gains arising on transfer of the residential house at Jaipur does not exceed Rs. 2 crore.

**Amount of Exemption under section 54 will be lower of:**

- Long term capital gains arising on transfer of residential house; or
- Amount invested in purchase/construction of new residential house or houses. (including the amount deposited in CGAS before due date of filing of return)

If till the date of filing the return of income, the LTCG on such transfer of the house is not utilised (in whole or in part) to purchase or construct another house, then the benefit of exemption can be availed by depositing the unutilised amount into Capital Gains Deposit Account Scheme (CGAS) with any scheduled bank.

If the amount deposited in the Capital Gains Account Scheme in respect of which the assessee has claimed exemption under section 54 is not utilised within the specified period for purchase/construction of the residential house, then the unutilised amount (for which exemption is claimed) will be taxed as income by way of long-term capital gains of the year in which the specified period of 2 years/3 years gets over.

If the new house is also transferred within 3 years from date of acquisition or construction, the cost of new house would be reduced by the capital gains exempted earlier under section 54.

**Illustration 7:**

Mr. Khan purchased a residential house in the previous year 2005-06 for Rs. 2 crores. The house property is sold for Rs. 10 crores in the previous year 2019-20 and the capital gain is invested in two residential house properties worth Rs. 4 crores each. Can he claim the benefit of section 54 in respect of both houses ?

**Solution :**

Exemption under section 54 can be claimed in respect of capital gains arising on transfer of capital asset, being long-term residential house property. With effect from Assessment Year 2020-21, an assessee has an option to make investment in two residential house properties in India to claim section 54 exemption. This option can be exercised by the assessee only once in his lifetime provided the amount of long-term capital gain does not exceed Rs. 2 crores. Since, the gain arising in hands of Mr. Khan is Rs. 5.06 crores which is more than Rs. 2 crore, he cannot claim the benefit of section 54 by making investment in both the house properties. However he can claim the benefit only in respect of one residential property invested.

**Computation of Long Term Capital Gains (LTCG)**

	Sale Consideration	10 Crores
Less	Indexed Cost of Acquisition ( $2 \times 289/117$ )	4.94 Crores
	Long Term Capital Gains (LTCG)	5.06 Crores
Less	Deduction U/s 54	4 Crores
	Taxable LTCG	1.06 Crores

**Transfer of land used for agricultural purposes [Section 54B]**

Conditions for claiming exemption:

- Assessee: Individual or HUF
- There should be a transfer of an urban agricultural land
- Asset must be either short term or long term capital asset.
- Such land has been used for agricultural purposes for immediately preceding 2 years by such Individual or his parent or HUF
- He should purchase another agricultural land (urban or rural) within 2 years from date of transfer
- If such investment is not made before the date of filing of return of income, then the capital gain has to be deposited under the CGAS
- Amount utilized by the assessee for purchase of new asset and the amount so deposited shall be deemed to be the cost of new asset.

Amount of Exemption:

- If cost of new agricultural land  $\geq$  capital gains, entire capital gains is exempt.
- If cost of new agricultural land  $<$  capital gains, capital gains to the extent of cost of new agricultural land is exempt.

If the new agricultural land is also transferred within 3 years from date of acquisition, the cost of land would be reduced by the capital gains exempted earlier (not applicable if the new land was rural)

**Compulsory acquisition of lands and buildings [Section 54D]**

Conditions for claiming exemption:

- Assessee: Any assessee
- There must be a compulsory acquisition of land & building or any right in land or building forming part of an industrial undertaking
- Such land & building should have been used for business purposes of the industrial undertaking for 2 years immediately preceding the date of transfer.
- The assessee must purchase any another land / building / construct any building (for shifting or re-establishing the existing undertaking or setting up a new industrial undertaking) within 3 years from date of transfer
- If such investment is not made before the date of filing of return of income, then the capital gain has to be deposited under the CGAS. Amount utilized by the assessee for purchase of new asset and the amount so deposited shall be deemed to be the cost of new asset.

In such a case, if the cost of the new land & building is  $>$  the Capital Gains, the entire LTCG will be exempt, and if less, then the LTCG will be exempt only to the extent of the cost of new land & building.

If the new land & building is also transferred within 3 years from date of acquisition, the cost of such land & building would be reduced by the capital gains exempted earlier

**No tax on long-term capital gains if investments made in specified bonds [Section 54EC]**

Conditions for claiming exemption:

- Assessee: Any assessee
- There should be a transfer of a long-term capital asset being land or building or both.
- Such asset can also be a depreciable asset held for more than 36 months
- The capital gains arising from transfer of such asset should be invested in a long-term specified asset within 6 months from date of transfer.
- Long-term specified assets would imply, bonds redeemable after 5 years issued on or after 1.4.2018 by National Highways Authority of India (NHAI), or Rural Electrification Corporation Limited or, Power Finance Corporation Ltd., Indian Railway Finance Corporation Limited or any other bond notified by central government in this behalf.
- The assessee should neither transfer nor convert / avail loan or advance with this bond as security for a period of 5 years from date of acquisition of such bonds, and in case that does happen before 5 years, the capital gain exempted earlier shall be taxed as long-term capital gain in that year.

In this case, the entire LTCG or amount invested in the specified bonds, whichever is lower, is exempt.

The maximum investment which can be made in notified bonds or bonds of NHAI and RECL, out of capital gains arising from transfer of one or more assets, during the previous year in which the original asset is transferred and in the subsequent financial year cannot exceed Rs. 50 Lacs.

### Practical Questions (MCQs)

State with reason whether the following statements are true or false with regard to the provisions of the Income-tax Act, 1961 for the Assessment year 2020-21 :

1. Capital gain of Rs. 75 lakh arising from transfer of long term capital assets will be exempt from tax if such capital gain is invested in the bonds redeemable after three years, issued by NHAI u/s 54 EC of the Act.

Answer : False : Because the maximum limit of investment in bond of NHAI u/s 54 EC, is just Rs. 50 lakhs.

2. In order to enjoy exemption under section 54EC, the resultant long-term capital gains should be invested in specified bonds within a period of from the date of transfer.

- (a) 36 Months                      (b) 4 Months  
(c) 6 Months                        (d) 12 Months.

Answer: (c) 6 Months

3. Long-term capital gains on sale of a long-term capital asset in October, 2019 is Rs. 105 lakh. The assessee invested Rs. 50 lakh in REC bonds in March, 2020 and Rs. 55 lakh in NHAI bonds in May, 2020. The amount of exemption eligible under section 54EC is —

- (a) Nil                                      (b) Rs. 50 lakh  
(c) Rs. 55 lakh                        (d) Rs. 105 lakh.

Answer: (b) Rs. 50 lakh

4. Mr. Madan sold a vacant land for Rs. 120 lakhs on 10-10- 2019. The indexed cost of acquisition amounts to Rs. 18 lakhs. He deposited Rs. 50 lakhs in REC bonds in January 2020 and another Rs. 50 lakhs in March, 2020. The amount of capital gain liable to tax after deduction under section 54EC is :

- (a) Rs. 2 lakhs                        (b) Rs. 18 lakhs

(c) Rs. 102 lakhs      (d) Rs. 52 lakhs

Answer: (d) Rs. 52 lakhs

### Tax incentives for start-ups [Section 54EE]

Conditions for claiming exemption:

- Assessee: Any assessee
- Which asset to transfer: One or more original Assets
- Investment of Long-term Capital Gains in units of a specified fund (to finance start-ups in India) issued before 1st April, 2019 of such fund, as may be notified by the Central Government in this behalf
- Within 6 months from date of transfer
- Maximum Investment Allowed in any financial year or years is INR 50,00,000

In such case, the entire LTCG or amount invested in the bonds, whichever is lower, is exempt.

Units so acquired should not be transferred for a period of 3 years, and if that does happen before 3 years, the capital gain exempted earlier shall be taxed as long-term capital gain in that year.

Further, if the assessee takes any loan or advance on the security of such units, he shall be deemed to have transferred such units on the date on which such loan or advance is taken.

### Capital gain on the transfer of certain capital assets not to be charged in case of investment in residential house [Section 54F]

Conditions for claiming exemption:

- Assessee: Individual or HUF
- There must be a transfer of a long-term capital asset other than a residential house
- The assessee should purchase 1 residential house situated in India within 1 year before OR 2 years after the date of transfer OR construct one residential house in India within 3 years from date of transfer
- If such investment is not made before the date of filing of return of income, then the net sale consideration has to be deposited under the CGAS. Amount utilized by the assessee for purchase or construction of new asset and the amount so deposited shall be deemed to be the cost of new asset.

If the cost of the investment in a new residential house is > the Net Sale Consideration, the entire LTCG is exempt, and if less than Net Sale Consideration, then, LTCG is exempt proportionately (that is:  $\text{LTCG} \times \frac{\text{Investment in New House}}{\text{Net Sale Consideration}}$ ).

There is also a condition, that the assessee should not own more than one residential house on the date of transfer and should not purchase any other residential house within 2 years OR construct any other residential house within 3 years from date of transfer of original asset, and if that does happen then, the entire LTCG exempted earlier will be chargeable to tax as LTCG in that year.

Additionally, if the new house is transferred within 3 years of purchase, capital gains would arise on transfer and the LTCG exempt earlier would be taxable as LTCG in that year.

1. Under which section, the assessee has to reinvest the entire net consideration to claim full exemption for the long-term capital gains earned during a previous year —

- (a) Section 54EC      (b) Section 54F  
 (c) Section 54GA      (d) Section 54D.

Answer: Section 54F

**Exemption of capital gain on transfer of assets of shifting of industrial undertaking from urban area to a Special Economic Zone [Section 54GA]**

Conditions for claiming exemption:

Assessee: Any Assessee

The exemption is available to all categories of assesses in respect of capital gain arising on the transfer of fixed assets other than furniture and fittings of industrial undertaking effected in the course of shifting of such industrial undertaking to any Special Economic Zone.

The conditions for claiming exemptions are as under:

- (i) The transfer is effected in the course of or in consequence of shifting the undertaking from an urban area to any Special Economic Zone. The special Economic Zone may be developed in any urban area or any other area.
  - 1. Any other area means an area not declared as an urban area.
  - 2. 'Urban Area' means any such area within the limits of a municipal corporation of municipality, as the Central Government may, having regard to the population, concentration of industries, need for proper planning of the area and other relevant factors, by general or special order, declare to be an urban area for the purposes of this sub-section.
  - 3. "Special Economic Zone" means each Special Economic Zone notified under the proviso to Sub-section (4) of Section 3 and Sub-section (1) of Section 4 of the Special Economic Zone Act, 2005 (including Free Trade and Warehousing Zone) and includes an existing Special Economic Zone. [Section 2(za) of the Special Economic Act, 2005].
- (ii) Asset transferred is machinery, plant, building, land or any right in building or land used for the business of industrial undertaking in an urban area;
- (iii) The capital gain arising on the asset transferred may be short-term or long-term capital gain. Normally, it will be short-term capital gain because most of the assets of the industrial undertaking will be depreciable assets;
- (iv) The capital gain is utilized within 1 year before or 3 years after the date of transfer for the specified purpose.

Specified purpose includes the following:

- (a) for purchase of new machinery or plant for the purpose of business of the Industrial Undertaking in the Special Economic Zone to which the said undertaking is shifted;
- (b) acquisition of building or land or construction of building for the purposes of the assessee's business in the Special Economic Zone;
- (c) expenses on shifting of the old undertaking and its establishment to the Special Economic Zone; and
- (d) incurring of expenditure on such other purposes as specified by the Central Government for this purpose.

**Capital Gain on Transfer of Residential Property (a house or a plot of land) [Section 54GB]**

Who can claim exemption	An Individual or a Hindu undivided family.
Which specified asset is eligible	On transfer of a long term residential property (a house or a plot of land) if transfer takes place during April 1, 2012 and March 31, 2017. (in case of eligible start up, residential property can be transferred up to March 31, 2021).

Which asset the taxpayer should acquire to get benefit of exemption	Equity shares of 25% of share capital or voting rights in an “eligible company
What is the time-limit for acquiring the new asst.	Equity shares in an “eligible company” should be acquired on or before the due date of furnishing of return of income under section 139(1). The “eligible company” should utilize this amount for the purchase of a “new asset” within one year from the date of subscription in equity shares.
How much is exempt	Investment in “new asset” by the eligible company net sale consideration x capital gain. Exemption cannot exceed capital gain.
It is possible to revoke the exemption	In the following cases, exemption will be taken back and the amount of exemption (or proportionate exemption) given earlier under section 54 GB will become long-term capital gain of the assessee (i.e. transferor of residential property). It shall be taxable in the year in which the assessee or the eligible company commits the following defaults-
	<ol style="list-style-type: none"> <li>1. If the equity shares in the eligible company are sold or otherwise transferred by the assessee within 5 years from the date of acquisition.</li> <li>2. If the “new asset” is sold or otherwise transferred by the eligible company within 5 years from the date of acquisition.</li> <li>3. If the deposit account is not utilized fully or partly by the eligible company for purchasing the new asset within 1 year from the date of subscription in equity shares (by the assessee).</li> </ol>

#### **Extension of Time for Acquiring New Asset or Depositing or Investing Amount of Capital Gain (Section 54H)**

This section states that where the transfer of the original asset is by way of compulsory acquisition under any law and the amount of compensation awarded for such acquisition is not received by the assessee on the date of such transfer, the period of acquiring the new asset by the assessee referred to in Sections 54, 54B, 54D, 54EC and 54F or for depositing or investing the amount of capital gain shall be extended. This extended period shall be reckoned from the date of receipt of such compensation.

#### **Tax on long-term capital gains in case of specified securities [Section - 112A New section Inserted by Finance Act of 2018]**

Applicable on sale of equity share listed on a recognised Stock exchange or unit of equity oriented fund or unit of business trust, where such sale transaction is chargeable to securities transaction tax (STT).

Prior to 01.04.2018 any LTCG on sale of such specified securities was exempt under Section 10(38). This exemption has been withdrawn by the Finance Act, 2018 w.e.f. Assessment Year 2019-20 and a new section 112A is introduced in the Income-tax Act.

As per this new section, where the total income of an assessee, includes any LTCG income [which was earlier exempt under section 10(38) upto 31.03.2018] shall now be taxed at the rate of 10% on such capital gains exceeding Rs. 1,00,000 [excess will be taxable]. The benefit of indexation shall not be allowed on such LTCG. Deductions under Chapter VIA (section 80C to 80U) not to be allowed from such LTCG. Rebate of tax under section 87A not to be allowed from the tax payable on such LTCG.

The cost of acquisitions for computing LTCG in respect of a listed equity share acquired by the assessee before February 1, 2018, shall be deemed to be the higher of following:

- a) The actual cost of acquisition of such asset; or

- b) Lower of following :
- (i) Fair market value of such shares as on January 31, 2018; or
  - (ii) Actual sales consideration accruing on its transfer

**Note:** The Fair market value of listed equity share shall mean its highest price quoted on the stock exchange as on January 31, 2018.

**Illustration 7 :** Mr. Raman is a salaried employee. In the month of January, 2014 he purchased 100 shares of X Ltd. @ Rs. 1,400 per share from Bombay Stock Exchange. These shares were sold through BSE in April, 2018 @ Rs. 2,600 per share. The highest price of X Ltd. share quoted on the stock exchange on January 31, 2018 was Rs. 1,800 per share. What will be the nature of capital gain in this case?

**Solution :** Shares were purchased in January, 2014 and were sold in April, 2018, i.e., sold after holding them for a period of more than 12 months and, hence, the gain will be long-term capital gain (LTCG). In the given case, shares are sold after holding them for a period of more than 12 months, shares are sold through recognised stock exchange and the transaction is liable to STT. Therefore, section 112A is applicable in this case.

The cost of acquisition of X Ltd. shares shall be higher of:

- a) Cost of acquisition i.e., 1,40,000 (1,400 × 100)
- b) Lower of:
  - i). Highest price quoted as on 31-1-218 i.e., 1,80,000 (1,800 × 100);
  - ii). Sales consideration i.e., 2,00,000 (2,000 × 100)

Thus, the cost of acquisition of shares shall be Rs. 1,80,000. Accordingly, Long-term capital gains in hands of Mr. Raman would be Rs. 80,000 (i.e., 2,60,000 – 1,80,000). Since long-term capital gains doesn't exceed Rs. 1,00,000, nothing is taxable in hands of Mr. Raman.

## TAX RATES

### **Short-term Capital Gains (STCG)**

- STCG is clubbed with Total Income and therefore charged to tax at normal rates
- However, STCG on transfer of listed equity shares / unit of an equity-oriented fund / unit of a business trust, where STT has been paid, STCG is taxable @ 15% under section 111A.
- However, short-term capital gains arising from transactions undertaken in foreign currency on a recognized stock exchange located in an International Financial Services Centre (IFSC) would be taxable at a concessional rate of 15% even though STT is not leviable in respect of such transaction.
- Deductions under Chapter VI-A cannot be availed in respect of such short-term capital gains on equity shares of a company or units of an equity oriented mutual fund or unit of a business trust included in the total income of the assessee.

**Long-term Capital Gains (LTCG)**

	Person	Rate of tax	Particulars	
1.	Resident persons, Other than Companies Resident Individuals and HUF Resident AOPs and BOIs Resident Firms and LLPs	20% 20% 20%	Unexhausted basic exemption limit can be exhausted against LTCG taxable u/s 112 Unexhausted basic exemption limit cannot be adjusted against LTCG taxable u/s 112	In case of transfer of listed securities (other than units) and Zero Coupon Bonds, LTCG would be taxable at the lower of the following rates – (1) 10% without indexation benefit; and (2) 20% with indexation benefit.
2.	Domestic Companies	20%		
3.	Non-corporate non-Residents and foreign companies	20%  10%	Capital assets, other than unlisted securities or shares of closely held companies  Unlisted securities or shares of closely held companies (without benefit of indexation or foreign currency fluctuation)	

**Note:** STT is not allowed as a deduction in the computation of Capital Gains. Also note, that the unexhausted basic exemption limit can be exhausted under LTCG only for individuals / HUF's

**Illustration**

1. Long-term capital gains on zero coupon bonds are chargeable to tax —

- @ 20% computed after indexation of such bonds
- @ 10% computed without indexation of such bonds
- Higher of (a) or (b)
- Lower of (a) or (b).

Answer: (d) Lower of (a) or (b).

2. Short-term capital gains arising from the transfer of equity shares in a company or units of an equity oriented fund or units of a business trust charged with security transaction tax are subject to income-tax at the rate of —

- 10%      (b) 15%
- 20%      (d) Normal rate.

Answer: (b) 15%

**Case Study 1**

Mr. Kapoor (age 67 years and resident) is a retired person earning total pension of Rs. 1,00,000. He purchased gold in December, 2010 and sold the same in April, 2019. Taxable LTCG amounted to Rs. 2,80,000. What will be his tax liability for the A.Yr. 2020- 21?

**Solution :** Computation of tax liability for the A.Yr. 2020- 21 is as under :

**258 EP-TL**

Gross Salary (pension income)	Rs. 1,00,000
Less: Standard deduction U/s 16 (ia)	<u>Rs. 50,000</u>
Income under the head Salary	Rs. 50,000
LTCCG on sale gold	Rs. 2,80,000
Total income	Rs. 3,30,000
Tax on LTCCG U/s 112 on Rs. 30,000 @ 20%*	Rs. 6,000
Less : Rebate as per section 87A	Rs. 6,000
Tax after Rebate	NIL

\* Resident individual above 60 years but below 80 years of age has basic exemption limit of Rs. 3,00,000. Which can be adjusted against LTCCG of Rs. 2,80,000 but after the adjustment of salary income of Rs. 50,000. Hence, the balance LTCCG taxable will come to Rs. 30,000 @ 20%.

**Case Study 2**

Mr. Gagan (age 69 years and non-resident) is a retired person earning total pension of Rs. 1,00,000 from Indian employer. He purchased a piece of land in Delhi in December, 2010 and sold the same in April, 2019. Taxable LTCCG amounted to Rs. 2,30,000. What will be his tax liability for the year 2019-20?

Solution : Computation of tax liability for the A.Yr. 2020-21 is as under :

Gross Salary (pension income)	Rs. 1,00,000
Less: Standard deduction U/s 16 (ia)	<u>Rs. 50,000</u>
Income under the head Salary	Rs. 50,000
LTCCG on sale gold	Rs. 2,30,000
Total income	Rs. 2,80,000
Tax on LTCCG U/s 112 on Rs. 2,20,000 @ 20%*	Rs. 44,000
Less : Rebate as per section 87A (Not available to non resident)	NIL
Tax after Rebate	Rs. 44,000
Add : Health & education cess @ 4%	Rs. 1,760
Net tax payable	Rs. 45,760

\*Non-Resident individual (of any age) has basic exemption limit of Rs. 2,50,000. Which cannot be adjusted against LTCCG of Rs. 2,20,000 but the same can be adjusted against salary income of Rs. 60,000. Hence, the whole amount of LTCCG is taxable @ 20%.

**Case Study 3**

Priyanka furnishes the following data for the PY ended 31st Mar' 20.

- She had unlisted shares of XYZ Ltd., 100,000 in number, which she sold on 30th Jun'19 for INR 750 per share.
- The above shares were acquired as under:
  - Gift from father: 50000 shares on 3rd May' 99 (FMV on 1st Apr'01 is INR 300)
  - Bonus Shares on 21st Jun' 09: 20000 shares

- Purchased 30000 shares on 1st Jan'11 @ INR 525 per share

Thereafter, she invested the proceeds to buy a residential house at INR 4,00,00,000 on 3rd May'20 and she was already owing a residential house prior to the purchase of this one.

You are required to compute the taxable capital gains.

**Solution :**

	Particulars	Number	Rate per Share	Amount	Date
	Full Value of Consideration	1,00,000	750	7,50,00,000	30th Jun'19
Less:	Indexed COA				
	Gift from father	50,000	300	4,33,50,000	3rd May'99
	Bonus	20,000	0	-	21st Jun'09
	Purchased	30,000	525	2,72,55,988	1st Jan'11
	Total Indexed COA			7,06,05,988	
	LTCG			43,94,012	
	New Residential House			4,00,00,000	
	LTCG exempt			23,43,473	
	Taxable LTCG			20,50,539	

**Note:**

- The bonus shares were granted after 1st Apr'01 and hence the cost of acquisition is NIL
- For the shares gifted by her father prior to 1st Apr'01, the FMV as on 1st Apr'01 would be considered as the Cost of Acquisition
- Indexed COA for the gifted shares therefore is  $50000 \times 300 / 100 \times 289$
- Indexed COA for the acquired shares therefore is  $30000 \times 525 / 167 \times 289$
- In the case above the necessary conditions u/s 54F have been fulfilled and therefore she is entitled to a proportionate exemption from LTCG (i.e. INR 4 Crores/INR 7.50 Crores \* 43,94,012)

#### Case Study 4

Mrs. Shanti Devi, a resident individual, sold her residential property on 18th Jul'19 for INR 75,00,000. She had purchased the same for INR 25,00,000 on 3rd May 2006. She paid INR 1,00,000 towards brokerage for the sale. The stamp duty valuation was INR 100,00,000.

She bought another property for INR 20,00,000 on 14th Dec'19 and deposited another INR 5,00,000 on 21st Jun'20 in the capital gain deposit scheme with SBI for construction of an additional floor in the property.

She also deposited INR 13,50,000 on 30th Nov'19 in the NHAI Bonds.

Compute the Capital Gains and Tax Liability.

**Solution :**

Particulars	INR
Full Value of Consideration	1,00,00,000

Brokerage	1,00,000
Net Sale Consideration	99,00,000
Less: Indexed COA	59,22,131
LTCG	39,77,869
Exemption u/s 54	25,00,000
Exemption u/s 54EC	13,50,000
<b>Taxable LTCG (Total Income)</b>	<b>1,27,869</b>
Tax Payable	–
Rebate u/s 87A	–
Tax Payable	–
Cess	–
<b>Total Tax Liability</b>	<b>–</b>

**Notes:**

As Per Section 50C, in case the actual sale consideration is less than the stamp duty value, the stamp duty valuation would be the full value of the consideration. B) Indexed COA = 25,00,000 / 122\*289. C) Exemptions u/s 54 are towards purchase of another house within 2 years of date of transfer and Deposit in Capital Gains Accounts Scheme (CGAS) on or before the due date of filing return of Income. D) Exemption u/s 54EC is towards investment in specified bonds (NHAI) within 6 months from date of transfer. E) Since the Taxable LTCG, which is less than basic exemption limit of Rs. 2,50,000, therefore no tax will be payable.

**CASE LAW**

**1. Whether, for the purpose of computing the period of holding of the property, the date of allotment letter issued by the builder of the flat or the date of registration of the property has to be considered for determining the nature of capital asset – long-term or short-term?**

**CIT v. S.R. Jeyashankar (2015 Madras HC)**

In effect, the P&H HC (in a similar case) held that the allottee gets the title to the property on issuance of allotment letter and payment in installments is only a consequential act upon which delivery of possession to the property flows. The Madras HC also noted that the Punjab & Haryana HC had taken a similar view in Vinod Kumar Jain's case Accordingly, the Madras HC held that the assessee had rightly claimed the benefit of long-term capital gain, since the holding period exceeded 36 months (i.e., from 22.02.2005, being the date of agreement, to 10.04.2008, being the date of sale of property).

**2. What would be the period of holding to determine whether the capital gains on renunciation of right to subscribe for additional shares is short-term or long-term?**

**Navin Jindal v. ACIT (2010) (SC)**

For determining whether the capital gains on renunciation of right to subscribe for additional shares is short term or long-term, the period of holding would be from the date on which such right to subscribe for additional shares comes into existence upto the date of renunciation of such right.

**3. Whether indexation benefit in respect of the gifted asset shall apply from the year in which the asset was first held by the assessee or from the year in which the same was first acquired by the previous owner?**

**CIT v. Manjula J. Shah (2013) (Bom.)**

The indexed cost of acquisition in case of gifted asset has to be computed with reference to the year in which the previous owner first held the asset and not the year in which the assessee became the owner of the asset.

**4. Would an assessee be entitled to exemption under section 54 in respect of purchase of two flats, adjacent to each other and having a common meeting point?****CIT v. Syed Ali Adil (2013) (A.P.)**

The Andhra Pradesh High Court, on the basis of the above rulings of the Karnataka High Court, held that in this case, the assessee was entitled to investment in both the flats purchased by him, since they were adjacent to each other and had a common meeting point, thus, making it a single residential unit.

**5. Can exemption under section 54EC be denied on account of the bonds being issued after six months of the date of transfer even though the payment for the bonds was made by the assessee within the six month period?****Hindustan Unilever Ltd. v. DCIT (2010) (Bom.)**

For the purpose of the provisions of section 54EC, the date of investment by the assessee must be regarded as the date on which payment is made. The High Court, therefore, held that if such payment is within a period of six months from the date of transfer, the assessee would be eligible to claim exemption under section 54EC.

**6. Sale of a Running Business with all Assets and Liabilities is a Slump Sale, would not attract Sec 50(2) of Income Tax Act****CIT v. Equinox Solution Pvt. Ltd**

In CIT v. Equinox Solution Pvt. Ltd, the two-judge bench of the Supreme Court held that the sale of a running business with all its assets and liabilities would not be covered by section 50(2) of the Income Tax Act since such transactions are slump sale of a “long term capital asset” within the ambit of section 48(2) of the Income Tax Act.

The factual settings of the case are that the assessee-Company sold its entire business- a running concern to another Company. For the year under consideration, the assessee filed return claiming deduction under section 48 of the IT Act stating that the sale is in the nature of “slump sale” of the going concern being in the nature of long term capital gain in the hands of the assessee.

The assessing officer rejected the contention of the assessee and denied the claim by invoking section 50(2). He was of the view that the transaction was in the nature of short term capital gain as specified in Section 50 (2) of the Act.

Assessee successfully appealed the impugned order before the first appellate authority. Though the order was challenged before the ITAT and High Court, the Revenue couldn't secure any relief. Dissatisfied by the orders of the appellate authorities and the High Court, the Revenue carried the matter before the Apex Court.

Concurring with the orders of the lower authorities, the bench comprising Justice R.K agarwal and Justice Ajay Manohar Sapre held that the transaction was rightly treated as slump sale under section 48. “Section 50 (2) applies to a case where any block of assets are transferred by the assessee but where the entire running business with assets and liabilities is sold by the assessee in one go, such sale, in our view, cannot be considered as “short-term capital assets”. In other words, the provisions of Section 50 (2) of the Income Tax Act would apply to a case where the assessee transfers one or more block of assets, which he was using in running of his business. Such is not the case here because in this case, the assessee sold the entire business as a running concern.”

## LESSON ROUND UP

- Sections 45 to 55A of the Income-tax Act, 1961 deal with capital gains. Section 45 of the Act, provides that any profits or gains arising from the transfer of a capital asset effected in the previous year shall, save as otherwise provided in Sections 54, 54B, 54D, 54EC, 54EE, 54ED, 54F, 54G, 54GA and 54H 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.
- Section 2(14) of the Income-tax Act defines the term “capital asset” to mean Property of any kind held by an assessee whether or not connected with his business or profession but does not include any stock-in-trade, personal effects, agricultural land in India, 6<sup>th</sup> per cent Gold Bonds, Special Bearer Bonds, Gold Deposit Bonds.
- The essential requirement for the incidence of tax on capital gains is the transfer of a ‘capital asset’.- Any capital gain arising as a result of transfer of a short-term capital asset is known as short-term capital gain. “Short term” capital asset means a capital asset held by an assessee for not more than thirty-six months immediately preceding the date of its transfer. In the case of capital assets (being equity or preference share in a company) held by an assessee for not more than 12 months immediately prior to its transfer.
- Assets other than short-term capital assets are known as ‘long-term capital assets’ and the gains arising therefrom are known as ‘long-term capital gains’. Section 48 of the Act provides that the income chargeable under the head ‘capital gains’ shall be computed by deducting from the full value of consideration received or accruing as a result of the transfer of the capital asset the full amount of expenditure incurred wholly and exclusively in connection with such transfer and the cost of acquisition of the capital asset and the cost of any improvement thereto.
- ‘Cost of acquisition’ of goodwill of a business or a right to manufacture, produce or process any article or thing, tenancy rights, stage carriage permits or lorry hours is in the case of acquisition of such asset by the assessee by purchase from a previous owner, cost of acquisition means the amount of the purchase price; and in any other case cost of acquisition shall be Nil.
- Cost of improvement means all capital expenditure in making any additions or alterations by the assessee after it became his property and where the capital asset became the property of the assessee by any of the modes specified in Section 49(1) by the previous owner as the case may be.
- Under Sections 54, 54B, 54D, 54EC, 54EE, 54F, 54G and 54H of the Act, capital gains arising from the transfer of certain capital assets are exempt from tax under certain circumstances.

## SELF TEST QUESTIONS

These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.

### Practical Questions (MCQs)

1. Capital asset excludes all except-

- (a) Stock-in-trade      (b) Personal effects  
(c) Jewellery      (d) Agricultural land in India.

Answer: (c) Jewellery

2. In terms of section 2(42A), listed securities are treated as long-term capital asset, if they are held for a period of more than —

- (a) 12 Months (b) 36 Months

(c) 24 Months (d) 48 Months.

Answer: (a) 12 Months

3. Which of the following is not a requisite for charging income-tax on capital gains —

- (a) The transfer must have been effected in the relevant assessment year
- (b) There must be a gain arising on transfer of capital asset
- (c) Capital gains should not be exempt under section 54
- (d) Capital gains should not be exempt under section 54EC.

Answer: (a) The transfer must have been effected in the relevant assessment year

4. Rajat purchased a car for his personal use for Rs. 5,00,000 in April, 2018 and sold the same for Rs. 5,50,000 in July, 2018. The taxable capital gains is —

- (a) Nil
- (b) Rs. 5,50,000
- (c) Rs. 50,000
- (d) Rs. 4,00,000

Answer: (a) Nil [Car for personal use is not capital asset. Therefore, no capital gain shall arise.]

5. Which of the following is not a capital asset for Mr. Rao who is employed in a public sector bank?

- (a) Urban land
- (b) Agricultural land within 2 kms from local limits of municipality
- (c) Deposit certificate issued under Gold Monetisation Scheme, 2015
- (d) Jewellery

Answer: (c) Deposit certificate issued under Gold Monetisation Scheme, 2015

6. Land or building, or both, if transferred on or after 1st April, 2018 shall be treated as a long term capital asset, if it is being held immediately prior to the date of its transfer for more than :

- (a) 36 months
- (b) 12 months
- (c) 24 months
- (d) None of the above

Ans: (c)

## SUGGESTED READINGS

### 1. Direct Taxes Law and Practice

Author : Dr. Vinod K. Singhania & Dr. Kapil Singhania

Publisher : Taxmann

Year : 2019

Edition : 2019

### 2. Direct Taxes Ready Reckoner with Tax Planning

Author : Dr. Girish Ahuja & Dr. Ravi Gupta

Publisher : Wolters Kluwer

Year : 2019

Edition : 20th Edition



# Lesson 4

## Part V – Income from Other Sources

### LESSON OUTLINE

- Income chargeable under the head 'Income from other Sources'
- Taxation of Casual Income
- Income from family pension
- Taxation of Dividends
- Deductions allowable in computing income from other sources
- Deemed Income [Section 59]
- Computation of Income under the head "Other sources"
- Amounts not Deductible [Section 58]
- Case Law
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

Income chargeable under Income-tax Act, which does not specifically fall for assessment under any of the heads discussed earlier, must be charged to tax as "income from other sources". This head is thus a residuary head of income under which income can be computed only after deciding whether the particular item of income is otherwise assessable under any of the first four heads. In addition to the taxation of income not covered by the other heads, Section 56(2) specifically provides certain items of incomes as being chargeable to tax under the head in every case. The provisions for computation of income from other sources are covered under sections 56 to 59. While section 56 defines the scope of income chargeable under this head, sections 57 and 58 specify the basis of computation of such income.

At the end of this lesson, you will learn (i) which are the income chargeable under the head income from other sources, (ii) which are the incomes specifically taxable under this head (iii) what are admissible deductions, (iv) which are the inadmissible deductions and (v) what are the provisions of taxability of gift in kind or in cash from relative or unrelated persons.

***The incomes which are neither covered under the head salary, house property, business income or capital gains shall be taxable under head Income from other sources. This head of income is a residual head because it covers all other incomes which are uncovered and which are not exempt from tax.***

## BASIS OF CHARGE OF INCOME FROM OTHER SOURCES [SECTION-56]

Income chargeable under Income-tax Act, which does not specifically fall for assessment under any of the heads discussed earlier, must be charged to tax as “income from other sources”. This head is thus a residuary head of income under which income can be computed only after deciding whether the particular item of income is otherwise assessable under any of the first four heads. Section 56(2) covers certain specific incomes which are chargeable under the head “Income From Other Sources”. Section 56(1) covers all the residual incomes which are not covered by first Four Heads of Income and Section 56(2).

In other words any income is taxable under this head if following conditions are satisfied:

1. There is an Income.
2. Such income is not exempt under any provisions of the Income Tax Act.
3. Such income is not taxable under First four heads of Income.

The following specific incomes are chargeable to Income Tax under the head “Income from other sources” under Section 56(2): -

- (a) **Dividends [Section 56(2)(i)]** : Dividend income other than dividend referred under section 10(34) not exceeding Rs. 10 lakh shall be included under income from other sources.
- (b) **Keyman Insurance policy** : Amount received under a Keyman insurance Policy, including bonus on such Policy, if it is not taxable under any other head of income shall be chargeable under Income from other sources.
- (c) **Winnings from lotteries [Section 56(2)(ib)]** : Any winnings from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature shall be chargeable to tax under Income from other sources.

The entire income of winnings, without any expenditure or allowance or deductions under Sections 80C to 80U, will be taxable. However, expenses relating to the activity of owning and maintaining race horses are allowable.

Further, such income is taxable at a special rate of income-tax i.e., 30% + surcharge + cess @ 4% [Section 115BB]

- (d) **Contribution to Provident fund** : Income of the nature referred to in Section 2(24)(x) (relating to certain contributions to any provident fund or superannuation fund or any fund set up under the provisions of the ESI Act or any other fund for the welfare of such employees received by the assessee from his employees in his capacity as an employer) will be chargeable to income-tax under the head “income from other sources” if such income is not chargeable to income-tax under the head “profits and gains of business or profession”. But if the employer deposits such amount on or before due date of deposit applicable for such contribution, he will be allowed a deduction on account of the same. [Section 56(2)(ic)].
- (e) **Income by way of interest on securities** : if the income by way of interest on securities is not chargeable to income-tax under the head, “Profits and gains of business or profession”, then such income shall be taxable under Income from other sources. It is chargeable on “receipt” basis if books of accounts are maintained on “Cash Basis”, however if books are maintained on “Mercantile System” then interest is taxable on “accrual” basis. It is worthwhile to mention here, that many interest incomes are exempt u/s 10(15).
- (f) **Income from hiring of machinery, etc. [Section 56(2)(ii)]** : Income from machinery, plant or furniture belonging to the assessee and let on hire; if the income is not chargeable to income-tax under

the head “profits and gains of business or profession” shall be taxable under Income from other sources.

**(g) Hiring out of building with machinery etc. [Section 56(2)(iii)] :** Where an assessee lets on hire machinery, plant or furniture belonging to him and also building and the letting of the building is inseparable from the letting of the said machinery, plant or furniture, the income from such letting, if it is not chargeable to income-tax under the head “Profits and gains of business or profession” shall be taxable under Income from other sources.

**(h) Share premiums in excess of the fair market value to be treated as income [Section 56(2) (viib)]**

Where a company, not being a company in which the public are substantially interested, receives, in any previous year, from any person being a resident, any consideration for issue of shares that exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds the fair market value of the shares shall be taxable under Income from other sources.

However, that this clause shall not apply where the consideration for issue of shares is received:

- (i) by a venture capital undertaking from a venture capital company or a venture capital fund [or a specified fund having Category I or Category II Alternative Investment Fund Certificate ( w.e.f. Assessment Year 20-21)] or
- (ii) by a company from a class or classes of persons as may be notified by the Central Government in this behalf (for this purpose Govt. has notified that provisions of this section are not applicable in case consideration is received by a company for issue of shares of a “startup” company)

Provided where the class of companies notified by Central Government does not comply on account of fulfilment of conditions specified in the notification issued under clause (ii), then, any consideration received for issue of share that exceeds the face value of such share shall be deemed to be the income of that company chargeable to income-tax for the previous year in which such failure has taken place.

**Explanation** - For the purposes of this clause,

- (a) the fair market value of the shares shall be the value
  - (i) as may be determined in accordance with such method as may be prescribed (value is to be determined as per method given in rule 11UA); or
  - (ii) as may be substantiated by the company to the satisfaction of the Assessing Officer, based on the value, on the date of issue of shares, of its assets, including intangible assets being goodwill, know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature,

whichever is higher;

- (i) income by way of interest received on compensation or on enhanced compensation referred to in clause (b) of section 145A shall be chargeable to tax under Income from other sources. [Section 56(2) (viii)].
- (j) Advance money received- any sum of money, received as an advance or otherwise in the course of negotiations for transfer of a capital asset is chargeable to income-tax under the head “Income from other sources”, if such sum is forfeited and the negotiations do not result in transfer of such capital asset. [Section 56(2)(ix)].
- (k) Receipt of Money or Property without consideration or without adequate consideration by any person [Section 56(2)(x)]

**The following shall be taxable under the head ‘Income from other sources’ :**

Where any person receives, in any previous year, from any person or persons on or after the 1st day of April, 2017,—

- (a) Any sum of money, without consideration, the aggregate value of which exceeds INR 50,000, the whole of the aggregate value of such sum.
- (b) Any immovable property,—
  - i. without consideration, the stamp duty value of which exceeds INR 50,000, the stamp duty value of such property is chargeable to tax;
  - ii. for a consideration, the stamp duty value of such property as exceeds such consideration, if the amount of such excess is more than the higher of the following amounts, namely:—
    - the amount of INR 50,000; or
    - the amount equal to five per cent of the consideration
    - then the difference between stamp duty value of such property and consideration is chargeable to tax.

Provided that where the date of agreement fixing the amount of consideration for the transfer of immovable property and the date of registration are not the same, the stamp duty value on the date of agreement may be taken for the purposes of this sub-clause.

Provided further that the provisions of the first proviso shall apply only in a case where the amount of consideration referred to therein, or a part thereof, has been paid by way of an account payee cheque or an account payee bank draft or by use of electronic clearing system through a bank account, on or before the date of agreement for transfer of such immovable property.

Provided also that where the stamp duty value of immovable property is disputed by the assessee on grounds mentioned in sub-section (2) of section 50C, the Assessing Officer may refer the valuation of such property to a Valuation Officer, and the provisions of section 50C and sub-section (15) of section 155 shall, as far as may be, apply in relation to the stamp duty value of such property for the purpose of this sub-clause as they apply for valuation of capital asset under those sections.

- (c) any property, other than immovable property, –
  - (A) without consideration, the aggregate fair market value of which exceeds INR 50,000, then the whole of the aggregate fair market value of such property.
  - (B) for a consideration which is less than the aggregate fair market value of the property by an amount exceeding INR 50,000, the aggregate fair market value of such property as exceeds such consideration.

Provided that this clause shall not apply to any sum of money or any property received—

- (i) from any relative; or
- (ii) on the occasion of the marriage of the individual; or
- (iii) under a will or by way of inheritance; or
- (iv) in contemplation of death of the payer or donor, as the case may be; or
- (v) from any local authority as defined in section 10(2); or
- (vi) from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in section 10(23C); or

- (vii) from or by any trust or institution registered under section 12A; or
- (viii) by any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in section 10(23C); or
- (ix) by way of transaction not regarded as transfer under certain clauses of section 47; or
- (x) from an individual by a trust created or established solely for the benefit of relative of the individual.
- (xi) From such class of persons and subject to such conditions, as may be prescribed. (w.e.f. AY 20-21)

Explanation—For the purposes of this clause:

- a) “fair market value” of a property, other than an immovable property, means the value determined in accordance with the method as may be prescribed;
- b) “property” means the following capital asset of the assessee, namely:—
  - (i) immovable property being land or building or both;
  - (ii) shares and securities;
  - (iii) jewellery;
  - (iv) archaeological collections;
  - (v) drawings;
  - (vi) paintings;
  - (vii) sculptures;
  - (viii) any work of art; or
  - (ix) bullion;
- (c) “relative” means,—
  - (i) in case of an individual—
    - (A) spouse of the individual;
    - (B) brother or sister of the individual;
    - (C) brother or sister of the spouse of the individual;
    - (D) brother or sister of either of the parents of the individual;
    - (E) any lineal ascendant or descendant of the individual;
    - (F) any lineal ascendant or descendant of the spouse of the individual;
    - (G) spouse of the person referred to in items (B) to (F); and
  - (ii) in case of a Hindu undivided family, any member thereof;
- (l) Any compensation or other payment, due to or received by any person, by whatever name called, in connection with the termination of his employment or the modification of the terms and conditions relating thereto. If the same is not taxable under the head Salary. [Section 56(2)(xi)]

If any income is neither covered by first Four Heads of Income nor it falls under Section 56(2) then it is taxable under Section 56(1). For example:

- (1) Any fees or commission received by an employee from a person other than his employer.

## 270 EP-TL

- (2) Any annuity received under a Will. It does not include an annuity received by an employee from his employer.
- (3) All interest other than interest on securities, e.g. interest on bank deposits, interest on loan, etc.
- (4) Income of a tenant from sub-letting the whole or a part of the house property.
- (5) Remuneration received by a teacher or a lawyer for doing examination work.
- (6) Income of Royalty.
- (7) Director's fees.
- (8) Rent of land not appurtenant to any building.
- (9) Agricultural Income from land situated outside India.
- (10) Income from markets, ferries and fisheries, etc.
- (11) Income from leasehold property.
- (12) Remuneration received for writing articles in Journals.
- (13) Income from undisclosed sources.
- (14) Interest received by an employee on his own contributions to an unrecognised provident fund.
- (15) Casual income
- (16) Salary of a Member of Parliament, Member of Legislative Assembly or Council.
- (17) Interest received on securities of co-operative society.
- (18) Gratuity received by a director who is not an employee of the company.
- (19) Director's commission for giving guarantee to bank.
- (20) Director's commission for underwriting shares of a new company.

Further, under the provisions of Section 60 to 65 an assessee may be chargeable to tax in respect of income arising to other persons, e.g. spouse or minor children. In such cases, the income in question will be first computed under the appropriate head after allowing various deductions and includible in the total income of the assessee under the head "income from other sources". In other words, wherever the assessee is taxable in respect of income of somebody else, the income must be charged to tax in the hands of the assessee only under this head; even if the income is of a character which would otherwise fall for assessment under any other head of income.

### **CASUAL INCOME [SECTION 56(2)(IB)]**

Casual income includes income by way of winnings from lotteries; crossword puzzles; races including horse races; gambling and betting of any nature or form; card games, game show or entertainment program on television or electronic mode and any other game of any sort. All these incomes are chargeable to tax under the head income from other sources. However, following income are not chargeable under the head "income from other sources":

- (a) **Lottery held as stock in trade:** Winning from lottery to an agent or trader out of its unsold stock of lottery tickets shall be treated as incidental to business and taxed under the head "profit and gains of business or profession".
- (b) **Income of jockey:** Income of jockey from such profession is not treated as winning from the horse races.

- (c) **Winning from a motor car rally:** Winning from a motor car rally is a return for skill and effort and cannot be created as casual income, these are taxable as normal income.
- No deduction or exemption is provided in respect of the casual income. [Section 58 (4)].
  - No deduction can be claimed from such income even if such expenditure is incurred exclusively and wholly for earning such income.
  - Further, deduction under section 80C to 80U is also not available from such income.

**Taxation of Casual Income:** Casual income is liable to TDS. The casual income is taxed at a flat rate of 30% plus surcharge (if any), plus health and education cess.

When the TDS has already been deducted from the income, then in order to calculate the tax liability on such income, the income is to be grossed up. [Section 115BB]

However, the following incomes are not liable to TDS:

- (1) Winning from lottery upto amount Rs.10,000
- (2) Winning from racing other than horse race
- (3) Winning from horse race upto Rs. 10,000

### INCOME FROM FAMILY PENSION

Family pension is a regular amount payable by the employer to a family member of a deceased employee. It is taxable under the head income from other sources. The income by way of family pension is eligible for a standard deduction under section 57(iia) which is either 1/3rd of such pension or Rs. 15000 whichever is lower.

Family pension received by the widow or children or nominated heirs, as the case may be, of a member of the armed forces (including paramilitary forces) of the Union, where the death of such member has occurred in the course of operational duties, in such circumstances and subject to such conditions, as may be prescribed, shall be exempt from tax. Further, income by way of family pension received as family pension of an individual who has been in the service of Central/State Government and has been awarded Param Vir Chakra or Maha Vir Chakra or Vir Chakra or such other gallantry award as may be notified is also exempt from tax.

### TAXATION OF DIVIDENDS

Section 10(34) exempts dividend as defined in Section 115-O from tax in the hands of recipients thereof. Section 115-O, the main operative provision in the Chapter XII-D, however, calls upon a company declaring/distributing dividend to pay 15% plus surcharge plus Health and Education Cess by way of Dividend Distribution Tax (DDT) on distributed profits in addition to what it is liable by way of tax on its income in the normal course. This tax on distribution paid by a company is not available for deduction under any provision of the Act. Grossing up the dividend for computing the tax liability on account of dividend distribution tax. With the grossing up, the effective tax rate will be 20.555% as under:

Grossed Up	117.647
DDT @ 15%	17.647
Div	1,00,000
DDT	17,647
SC @ 12%	2,117
Agg	19,764
Cess @ 4%	791
Total	20,555

Under the existing provisions of clause (34) of section 10 of the Act, dividend which suffer dividend distribution tax (DDT) under section 115-O is exempt in the hands of the shareholder. Under section 115-O dividends are taxed only at the rate of fifteen percent at the time of distribution in the hands of company declaring dividends.

This creates vertical inequity amongst the tax payers as those who have high dividend income are subjected to tax only at the rate of 15% whereas such income in their hands would have been chargeable to tax at the rate of 30%.

With a view to rationalise the tax treatment provided to income by way of dividend, it is provided by amending the section of the Income-tax Act that any income by way of dividend in aggregate exceeding INR 10 lakh shall be chargeable to tax in the case of an individual, Hindu undivided family (HUF) or a firm who is resident in India, at the rate of 10% (+SC+EC+SHEC). The taxation of dividend income in aggregate exceeding ten lakh rupees shall be on gross basis. However, this rule is not applicable in case of deemed dividend under section 2(22)(e).

Scope of section 115BBDA has been increased: Earlier this section was applicable to an Individual/HUF/ Firm. However, from AY 2018-19 this section is applicable to individual/HUF/firm or any person (not being a domestic company, or a fund/institution/trust/university/educational institution/hospital/medical institution referred to in section 10(23C) (iv)(v)(vi) (via), or a trust/institution registered under section 12A/12AA).

### Illustration

ABC Ltd. declared a dividend of INR 200,00,000 for the FY 2017-18 and distributed the same on 15th Jul'18. Mr. A holds 10% shares and therefore receives INR 20,00,000 as dividend. Mr B hold 4% shares and therefore receives INR 8,00,000 as dividend.

The tax treatment would be as under:

- ✓ Mr A would be taxed on the amount exceeding INR 10,00,000, that is, on INR 10,00,000 he would be taxed at 10% + SC (if any) + Cess
- ✓ Mr B has received dividends < INR 10,00,000 and therefore this would entirely be exempt from tax under section 10(34)
- ✓ The company however would have to pay DDT on the dividend so distributed u/s 115O

**Meaning of the term “Dividend” [Section 2(22)]** :The term “dividend” is ordinarily used to refer to any distribution made by a company to its shareholders out of its profits in proportion to the number of shares held by the shareholder concerned in the company.

Apart from that dividend paid by a company to its shareholders, the definition of dividend includes deemed dividend as laid down under section 2(22) of the Act, which is inclusive but not exhaustive. Accordingly the following payments or distribution made by a company to its shareholders are deemed as dividends to the extent of accumulated profits of the company whether capitalised or not (i.e. bonus shares issued is the capitalisation of profit). It may be noted that these payments may not be covered as dividend under Companies Act, 2013.:

- (a) Any distribution if such distribution entails the release of all or any part of the assets of the company. Such accumulated profits are distributed in cash or in kind. For in kind distribution, the market value of assets shall be the deemed dividend in hands of share holders.
- (b) Any distribution of debentures, debenture-stock, or deposit certificates in any form, whether with or without interest to Equity or Preference shareholders. Any distribution of bonus shares to its preference shareholders. However bonus shares allotted to equity shareholders does not amount to deemed dividend.
- (c) Any distribution made on liquidation of a company

(d) any distribution on the reduction of capital of a company

Deemed dividend under clause (c) and clause (d) does not include :

- i. Any distribution by to shareholders on liquidation or reduction of capital of the company in respect of full cash consideration, where the shareholder is not entitled to participate in the surplus asset in the event of liquidation.
  - ii. Any payment made by a company on purchase of its own shares from a shareholder in accordance with the provisions of section 77A of the Companies Act.
  - iii. Any distribution of shares made in accordance with the scheme of demerger by the resulting company to the shareholders of the demerged company (whether or not there is a reduction of capital in the demerged company).
- (e) Any payments in the form of loans or advances to the extent of accumulated profits (excluding capitalised profit) made by a closely-held company (i.e. a company in which public are not substantially interested) to:
- i. its shareholder who is the beneficial owner of shares holding not less than 10% of voting power in such company.
  - ii. to any concern (HUF, Firm, AOP, BOI or Company) in which such shareholder is a member or a partner and which he has a substantial interest (20% of voting power or share of profit)
  - iii. any person on behalf of such shareholder for his/her individual benefit.

Deemed dividend under clause (e) does not includes:

- Any dividend paid by a company which is set off by the company against the whole or any part of any sum previously paid by it and treated as a dividend within the meaning of sub-clause (e), to the extent to which it is so set off.
- Vide CBDT circular No. 19/2017, any trade advance in the nature of commercial transactions would not fall within the ambit of advance.

**With amendments by the Finance Act, 2018**

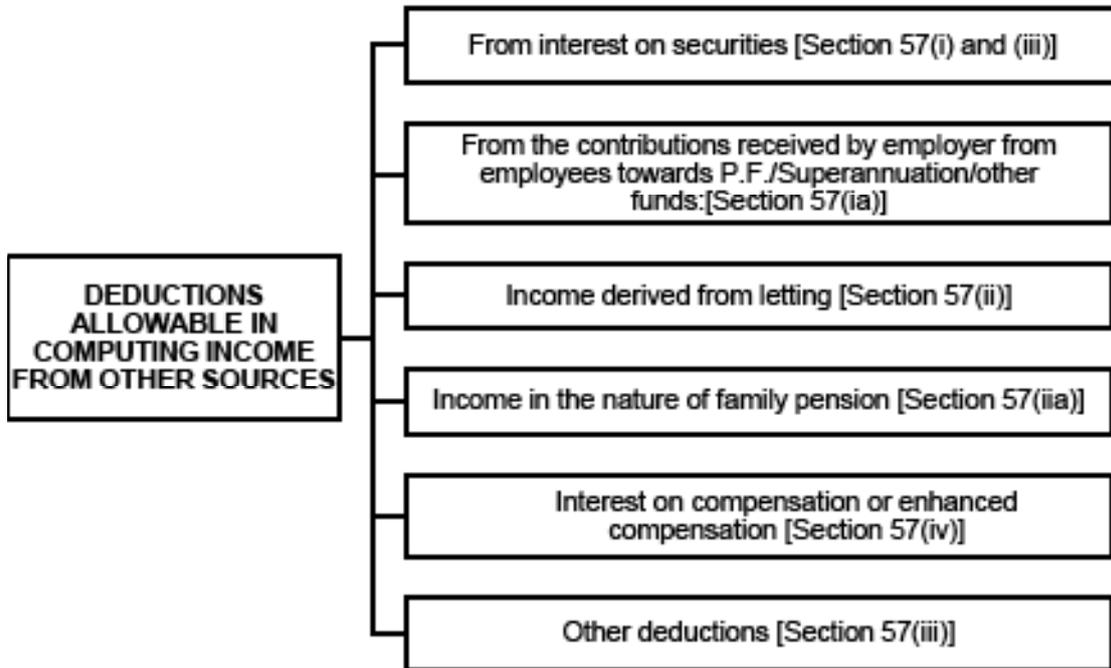
- All dividends under section 2(22) are exempt in the hands of shareholders and company is liable to pay Dividend Distribution Tax (DDT) u/s 115-O @ 15% (gross) on Dividend under section 2(22) (a) to (d) and @ 30%(Gross) on Dividend under section 2(22)(e) .
- In case of an amalgamated company, accumulated profit or loss shall be increased by the accumulated profit of amalgamating company (whether capitalized or not) on the date of amalgamation.

**Illustration**

Suppose, X is holding 29% shares in a company and he took a loan of INR 10,00,000 from the Company and on the date, the loan was granted, the accumulated profits stood at INR 800,000. The tax treatment would be as under:

- In case the company is one, where the public is substantially interested, the loan would not be taxable as deemed dividend in hands of X
- However, in case the company is a private limited company, since X holds > 10% stake, this loan would be taxable in the hands of X as deemed dividend, but only to the extent of accumulated profits on the date of grant of loan, i.e., INR 800,000.

## DEDUCTIONS ALLOWABLE IN COMPUTING INCOME FROM OTHER SOURCES



The income chargeable under the head “Income from other sources” is the income after making the following deductions:

1. **From interest on securities [Section 57(i) and (iii)]:** any reasonable sum paid by way of commission or remuneration to a banker or any other person for the purpose of realising such interest on behalf of the assessee. Interest on money borrowed for investment in securities can be claimed as a deduction.
2. **From the contributions received by employer from employees towards P.F./Superannuation/ other funds [Section 57(ia)]:** In the case of income of the nature referred to in Section 2(24)(x), which is chargeable to income-tax under the head “Income from other sources” deduction shall be allowable in accordance with the provisions of Section 36(1) (va), i.e., if the employer has credited the employee’s accounts in the respective funds with the amounts of contributions received, the employer shall be allowed credit thereof.
3. **Income derived from letting [Section 57(ii)]:** Where income is derived from letting out of machinery, plant or furniture on hire and also buildings where the letting of building is inseparable from the letting of such machinery, plant or furniture and the income from such letting is not chargeable to Income-tax under the head “Profits and Gains of Business or profession”, the following expenses incurred in respect of those assets:
  - (a) Current repairs of buildings.
  - (b) Insurance premium against risk of damage or destruction of the premises.
  - (c) Current Repairs and insurance of machinery, plant or furniture.
  - (d) Depreciation.

Where the expenses referred to at (a) to (d) hereinabove are incurred on property used partly for the business of the assessee, a proportionate deduction shall be allowed.

4. **Income in the nature of family pension [Section 57(iaa)]:** Where a regular monthly amount is payable by an employer to a person belonging to the family of an employee in the event of his death, i.e., “family

pension”, a sum equal to 33-1/3% of the income or Rs. 15,000, whichever is less, is allowable as a deduction.

All these expenses will be allowed only when the prescribed particulars are furnished by the assessee.

5. **Interest on compensation or enhanced compensation [Section 57(iv)]:** a deduction of a sum equal to 50% of such income and no deduction shall be allowed under any other clause of this section.
6. **Other deductions [Section 57(iii)]:** Any other expenditure (not being in the nature of capital expenditure) laid out or expended wholly and exclusively for the purpose of making or earning such income. [Smt. Virmati Ramkrishna v. C.I.T. (1981) 131 ITR 659(Guj)]

### AMOUNTS NOT DEDUCTIBLE [SECTION 58]

The following amounts shall not be deducted in computing income chargeable under the head “Income from other Sources”.

In the case of any assessee:

- (i) Any personal expenses of the assessee.
- (ii) Any interest chargeable under the Income-tax Act which is payable outside India and from which income-tax has not been paid or deducted at source.
- (iii) Any payment which is chargeable under the head “Salaries” if it is payable outside India unless tax has been paid thereon or deducted therefrom at source.

**Note:** The disallowance provisions pertaining to TDS defaults covered by section 40(a)(ia) will be applicable for computing the Income chargeable under the head Income from Other Sources.

- (iv) Any expenditure referred to in Section 40A of Income-tax Act.

No deduction is allowed in respect of any expenditure or allowance in computing the income by way of winnings from lotteries crossword puzzles races (including horse races) card games and other games of any sort or from gambling or betting of any form or nature whatsoever. The prohibition however will not apply in respect of income of an assessee who is owner of horses maintained for running in horse races [Section 58(4)]. The winnings are now taxed at the rate of 30%. The amount is taxable at source and it does not matter whether amount goes to one or more recipients. Similarly, the amount spent in buying of in fructuous tickets is not deductible as the gross amount will be taxed.

### DEEMED INCOME [SECTION 59]

Where any allowance or deduction has been provided in the assessment of Income under the head “Income From Other Sources” in any Assessment Year in respect of loss or expenditure or trading liability incurred by the assessee and later on during any previous year any amount or any remission or any benefit is obtained by assessee (whether in cash or otherwise) then such amount or remission or benefit shall be taxable under the head “Income From Other Sources” in the previous year in which it is so obtained.

### SUMMARY OF COMPUTATION OF INCOME UNDER THE HEAD “INCOME FROM OTHER SOURCES”

As per section 145 income taxable under this head is to be computed in accordance with the method of accounting regularly followed by assessee. In other words; if books of accounts are regularly maintained on “Cash system” then income shall be computed on “receipt basis” and If books are regularly maintained on “Mercantile system” then Income shall be computed on “accrual basis”.

**COMPUTATION OF INCOME**

Income taxable under Section 56 & 59	XXXX
Less:- Expenditure allowed as deduction under Section 57	XXXX
Income taxable under the head "Income From Other Sources"	XXXX

**Case Study 1**

Nikhil, a dealer in shares received from his friend Anshul, the following without any consideration:

- ✓ Cash Gift INR 100,000 on his birthday (14th April)
- ✓ Bullion, FMV INR 75,000 on his anniversary (22nd April)
- ✓ Plot of land at Gurgaon on 1st Jun'17, stamp duty value INR 750,000 on that date.

Advise on tax treatment.

**Answer**

- a) Cash Gift is > INR 50000, therefore, the entire amount of INR 100,000 is chargeable to tax as Income from Other Sources
- b) Bullion received without consideration is taxable too in full as it is received without consideration, therefore, the entire amount of INR 75000 is chargeable to tax as Income from Other Sources
- c) Plot of land received without consideration is taxable too in full as it is received without consideration, therefore, the entire amount of INR 750,000 is chargeable to tax as Income from Other Sources

**Case Study 2**

Nisha, on 1st Dec'19 took possession of a flat booked by her 2 years back, at INR 25,00,000. The Stamp Duty of the flat on the date of possession was INR 40,00,000 and on the date of booking was INR 29,00,000. She had paid INR 200,000 by account payee cheque, on date of booking.

Advise tax treatment.

**Answer**

It is to be noted that where the date of the agreement fixing the amount of consideration for the transfer of immovable property and the date of registration are not the same, the stamp duty value on the date of the agreement (in this case booking) may be taken. However, this exception shall apply only in a case where the amount of consideration referred to therein, or a part thereof, has been paid by any mode other than cash on or before the date of the agreement for the transfer of such immovable property.

Therefore, the difference between the Stamp Duty Value on date of booking (INR 29,00,000) and the actual consideration (INR 25,00,000); i.e. INR 400,000 would be taxable under the head "Income from Other Sources".

**Case Study 3**

Discuss the taxability of the following transactions in the hands of the recipient.

1. An HUF received from the Karta's niece, INR 80,000 in cash
2. Shruti, a member of her father's HUF, transferred to the HUF a property without any consideration. The Stamp Duty valuation was INR 12,00,000
3. Robin received from his friend 100 shares of INR 200 each and jewellery worth INR 55,000 (FMV) from

his nephew on the same day

4. An HUF gifted a Car to the Karta's son, for brilliant performance in the board exams. The FMV of Car was 10,00,000

**Answer**

1. **Taxable:** Sum of money received exceeding INR 50,000 without consideration from a non-relative is taxable. Therefore INR 80000 is taxable as his niece, not being a member of the HUF is not a relative of the HUF
2. **Non-Taxable:** Immovable property received without consideration from a relative is non-taxable. Since Shruti is a member of the HUF, she is a relative of the HUF and hence the same is not taxable
3. **Taxable:** In this case, the aggregate FMV of the property other than immovable property, received without consideration exceeds INR 50000 (INR 75,000 actually for the shares & jewellery together). Hence, the entire amount would be taxable
4. **Non-taxable:** Car is not a property for the purposes of Sec. 56 and hence the transaction is non-taxable

**CASE LAW**

**1. Income from other sources – Deduction of interest under section 57(iii)**

**Commissioner of Income Tax v. Smt. Swapna Roy [2010] [233 CTR 10, Allahabad High Court]**

On a question whether the amount invested by the assessee in sister concerns running in loss since several years may be treated as investment or expenditure made exclusively for the purpose of making or earning such income, the Allahabad High Court held that the expenditure towards interest on loan cannot be said to have been laid out wholly and exclusively for the purpose of making earning income but was a colourable device, to utilize the funds of one company in the other sister concern and therefore, the interest on loan is not allowable deduction under section 57(iii).

Further on the principle of consistency, the High Court held that in case an assessee changes his or her stand repeatedly and does not come with a clean hand, then it shall be sufficient to depart from earlier practice and the principle of consistency shall not come in the way to assess the income on the basis of the material on record.

**2. Dividend distributed by a company earning agricultural income is liable to be taxed u/s 115-O**

**Union of India vs Tata Tea- [2017] (SC)**

Tata Tea Company is engaged in cultivation of tea which is an agricultural process contends that when company distributes dividend it is not liable to dividend distribution tax u/s 115-O as tax on this dividend is nothing but tax on agriculture Income.

Supreme Court decided that when dividend is distributed to company's shareholders it is not impressed with the character of its source of income. Dividend is not revenue derived from land and hence cannot be termed as agriculture income in the hands of the shareholders. Therefore dividend distribution tax u/s 115-O is to be levied in respect of entire dividend declared and distributed by the Tata Tea Company.

### LESSON ROUND UP

- Income chargeable under Income-tax Act, which does not specifically fall for assessment under any of the heads discussed earlier, must be charged to tax as “income from other sources”.
- Section 56(2) specifically provides for the certain items of incomes as being chargeable to tax under the head such as Dividend, Keyman Insurance policy, Winnings from lotteries, Contribution to Provident fund, Income by way of interest on securities, Income from hiring machinery etc, Hiring out of building with machinery, Money Gifts, Share premiums in excess of the fair market value to be treated as income, income by way of interest received on compensation.
- The entire income of winnings, without any expenditure or allowance or deductions under Sections 80C to 80U, will be taxable. However, expenses relating to the activity of owning and maintaining race horses are allowable. Further, such income is taxable at a special rate of income-tax i.e., 30% + surcharge + cess @ 4%.
- Admissible Deductions : The income chargeable under the head “Income from other sources” is the income after making the deductions such as
  - sum paid by way of commission or remuneration to a banker or any other person for the purpose of realising such interest;
  - deduction shall be allowable in accordance with the provisions of Section 36(1)(va), i.e., if the employer has credited the employee’s accounts in the respective funds;
  - a sum equal to 33-1/3% of the income or Rs. 15,000, whichever is less, is allowable as a deduction from family pension;
  - a deduction of a sum equal to 50% of from Interest on compensation or enhanced compensation, and
  - any other expenditure (not being in the nature of capital expenditure) laid out or expended wholly and exclusively for the purpose of making or earning such income.
- Inadmissible deductions: The following amounts shall not be deducted in computing income chargeable under the head ‘Income from other sources’:
  - Any personal expenses of the assessee.
  - Any interest chargeable under the Income-tax Act which is payable outside India and from which income-tax has not been paid or deducted at source.
  - 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.
  - Any expenditure referred to in Section 40A of Income-tax Act.

### SELF TEST QUESTIONS

*These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation.*

#### Multiple Choice Questions “MCQs”

1. Mr. Dev has earned interest of Rs. 12,000 under Post Office Savings Bank Account. The income taxable as other sources is ?
  - a) Rs. 12000
  - b) Fully Exempt
  - c) Rs. 8,500
  - d) Rs. 6,000

Answer: c

2. Mr. Raj received Rs. 80,000 from his friends on the occasion of his Marriage anniversary. Taxable income from other sources is?
- Entire Rs. 80,000 is exempt
  - Entire Rs. 80,000 is taxable
  - only Rs. 30,000 is taxable
  - Only 50% , i.e. Rs. 40,000

Answer: b

3. Ram received INR 80,000 from his best friend on his birthday?
- INR 80000 is taxable
  - INR 30000 is taxable
  - Entire amount is exempt
  - None of the above

Answer: a

4. Mr. C aged 72 years, received INR 15,00,000 as dividend, in FY 2017-18. The tax chargeable @ 10% is on
- INR 15,00,000
  - INR 5,00,000
  - Nil
  - INR 750000

Answer: b

## SUGGESTED READINGS

### 1. Direct Taxes Law and Practice

Author : Dr. Vinod K. Singhanian & Dr. Kapil Singhanian

Publisher : Taxmann

Year : 2019

Edition : 2019

### 2. Direct Taxes Ready Reckoner with Tax Planning

Author : Dr. Girish Ahuja & Dr. Ravi Gupta

Publisher : Wolters Kluwer

Year : 2019

Edition : 20th Edition



# Lesson 5

## Clubbing provisions and Set Off and / or Carry Forward of Losses

### LESSON OUTLINE

- Clubbing of Income
- Transfer of Income (Section 60)
- Revocable Transfer of Assets (Section 61)
- Transfer irrevocable for a specified period (Section 62)
- Income of Spouse
- Income to son's wife [Section 64(1)(vi)]
- Transfer for immediate or deferred benefit of Son's Wife [Section 64(1)(viii)]
- Income to Spouse through a Third Person [Section 64(1)(vii)]
- Clubbing of income of minor child [Section 64(1A)]
- Income from the converted property [Section 64(2)]
- Recovery of Tax
- Set-off and Carry-forward of Losses
- Carry forward of losses
- Treatment of carry-forward of losses of certain assessees
- Submission of Section of Loss
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

In addition to the general provisions which are applicable for computation of total income, there are special provisions in Sections 60 to 65 of the Income-tax Act which provide for inclusion of income of other persons in the total income of assessee. The special provisions contained in these sections are designed to counteract the various attempts of an individual for avoiding or reducing his liability to tax by transferring his assets or income to other person(s) while, at the same time, retaining certain powers or interest over the property or its income. These provisions may also be termed as clubbing provisions.

In the second part of this lesson provisions for set-off and carry forward of losses are discussed. Sometimes the assessee incurs a loss from a source of income and unless such loss is set-off against any income, the net result of the assessee's activities during the particular accounting year cannot be ascertained and consequently the tax payable would also be incapable of determination. For this purpose, the Income-tax Act contains specific provisions (Sections 70 to 80) for the set-off and carry-forward of losses.

At the end of this lesson, you will learn

- When are clubbing provisions applicable
- What are the provisions of set off/carry forward and set off of losses
- How can losses be set off inter-head and intra-head.
- The conditions to be satisfied for carry forward and set off of loss from house property, business loss and unabsorbed depreciation.
- Up to what period can the loss be carried forward and set-off.

**CLUBBING OF INCOME**

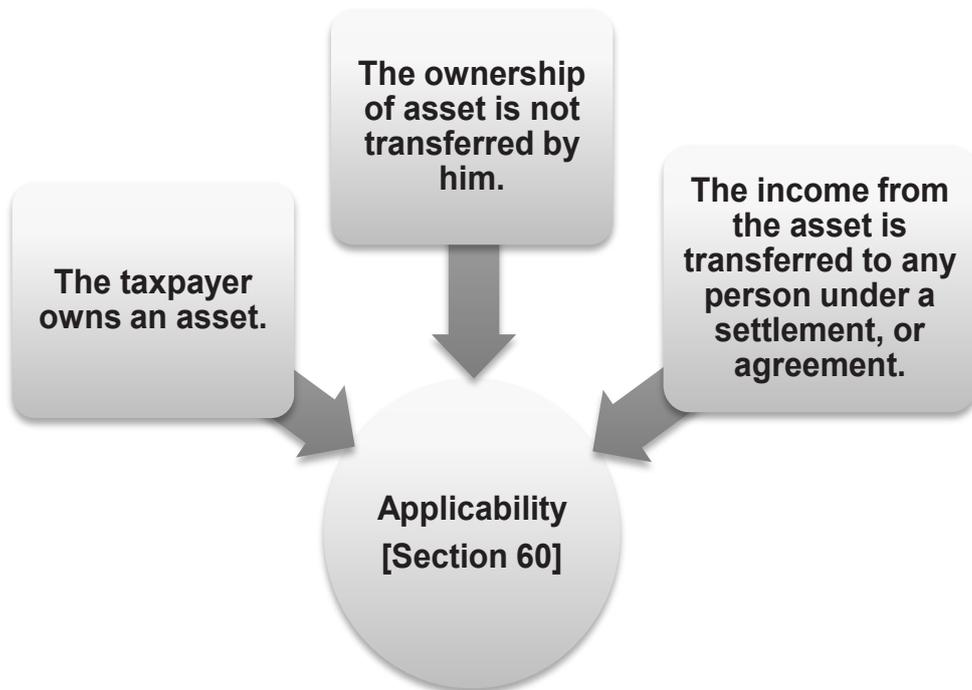
Normally, a person is taxed in respect of income earned by him only. However, in certain special cases income of other person is included (i.e. clubbed) in the taxable income of the taxpayer and in such a case he will be liable to pay tax in respect of his income (if any) as well as income of other person too. The situation in which income of other person is included in the income of the taxpayer is called as clubbing of income. E.g., Income of minor child is clubbed with the income of his/her parent. Section 60 to 64 of the Income-tax Act, contains various provisions relating to clubbing of income.

The special provisions contained in these sections are designed to counteract the various attempts which an individual may make for avoiding or reducing his liability to tax by transferring his assets or income to other person(s) while, at the same time, retaining certain powers or interest over the property or it's income. These provisions are explained below.

**TRANSFER OF INCOME [SECTION 60]**

Section 60 of Income Tax Act, 1961 provides the provisions relating to clubbing of income where transfer of income is done without transferring the assets. Where a person transfers to any other person, income (whether revocable or not) from an asset without transferring that asset, the income shall be included in the total income of the transferor. "Transfer" includes any settlement, trust, covenant, agreement or arrangement. The transfer also includes a lease for inadequate consideration and the income derived by the lessee from the leased property is included in the income of the lessor.

These are applicable if the following conditions are satisfied:



If the above conditions are satisfied, the income from the asset would be taxable in the hands of the transferor.

If the transferor transfers the asset and keeps the income for himself, the income shall be included in the income of transferor.

Section 60 of the Act has no application where assets producing income are transferred along with the income

C.I.T. v. Ram Prasad Mehta (1975) 100 ITR 468 (Bombay). There may be a field of operation of Sections 61 to 64 but certainly not of Section 60.

**Illustration 1:** A owns Debentures worth Rs 1,000,000 of ABC Ltd., (annual) interest being Rs. 100,000. On April 1, 2019, he transfers interest income to B, his friend without transferring the ownership of these debentures.

In this particular case during 2018-19, interest of Rs. 100,000 is received by B; it will be taxable in the hands of A as per Section 60.

**Illustration 2 :** Mr. X owns Debentures worth Rs 1,000,000 of ABC Ltd., (annual) interest being Rs. 100,000. On April 1, 2019, he transfers interest income to Mr. Y, his friend without transferring the ownership of these debentures. Although during 2019-20, interest of Rs. 100,000 is received by Mr. Y, it is taxable in the hands of Mr. X as per Section 60.

### REVOCABLE TRANSFER OF ASSETS [SECTION 61]

'Revocable transfer' means the transferor of asset assumes a right to re-acquire asset or income from such an asset, either whole or in parts at any time in future, during the lifetime of transferee. It also includes a transfer which gives a right to re-assume power of the income from asset or asset during the lifetime of transferee.

Where a person transfers any asset to any person with a right to revoke the transfer, all income accruing to the transferee from the asset shall be included in the total income of the transferor.

The income under revocable transfer of asset shall be included in the income of transferor even when only a part of income from transferred asset has been applied for the transferor.

For this purpose assets include movable or immovable property whether situated in India or abroad.

As per Section 63, a transfer shall be deemed to be revocable if:

- (i) it contains any provision for the re-transfer directly or indirectly of the whole or any part of the income or assets to the transferor; or
- (ii) it, in any way, gives the transferor a right to reassume power directly, or indirectly over the whole or any part of the income or assets.

#### Examples of revocable transfers

Some of the examples of revocable transfers are as follows:

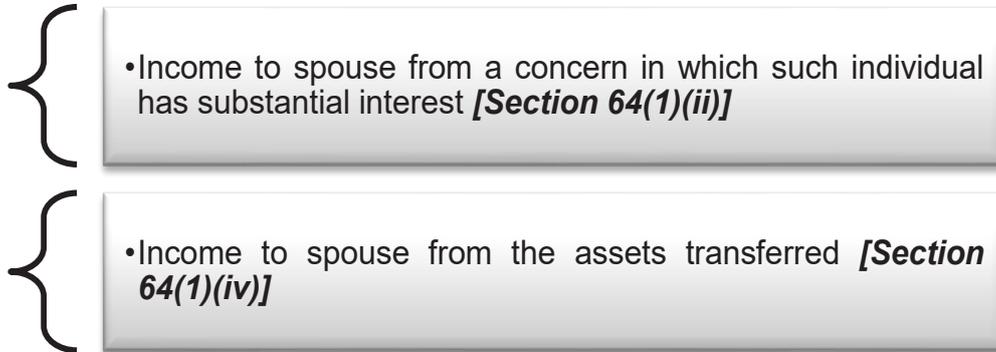
- (i) If there is an express clause of revocation in the instrument of transfer; or
- (ii) If there is a sale with a condition of re-purchase; or
- (iii) If the transfer is to a trust and if the transfer can be revoked with the consent of two or more beneficiaries; or
- (iv) If the trustees are empowered in sole discretion to revoke the transfer; or
- (v) If the transferor has power to change beneficiary or trustees.

"Transfer" includes any settlement, trust, covenant, agreement or arrangement.

**Note:** Re-transfer to the transferor must be in the same capacity in which he made the transfer or settlement. If a settlement is made by a Hindu undivided family and there is a re-transfer to one member of the family in his capacity as an individual and not in his capacity as a member of the family this cannot be termed a re-transfer for this purpose.

## INCOME OF SPOUSE

The following incomes of the spouse of an individual shall be included in the total income of the individual:



### (a) Income to spouse from a concern in which such individual has substantial interest [Section 64(1)(ii)]

All such income as arises directly or indirectly, to the spouse of an individual by way of salary, commission, fees or any other remuneration, whether in cash or kind from a concern in which such individual has a substantial interest, shall be included in the income of the individual.

**Exception:** However, where the spouse possesses technical or professional qualifications and the income is solely attributable to the application of his/her technical or professional knowledge and experience, the income shall not be included in the income of (other spouse) the assessee.

**Substantial Interest :** An individual shall be deemed to have a substantial interest in a concern -

- (i) In a case where the concern is a company, if its shares (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in profits) carrying not less than 20% of the voting power are, at any time during the previous year, owned beneficially by such person or partly by such person and partly by one or more of his relatives;
- (ii) In any other case, if such person is entitled, or such person and one or more of his relatives are entitled in the aggregate, at any time during the previous year, to not less than 20% of the profits of such concern.

### Illustration

X has a substantial interest in A Ltd. and Mrs. X is employed by A Ltd. without any technical or professional qualification to justify the remuneration. In this case, salary income of Mrs. X shall be taxable in the hands of X.

### When both husband and wife have substantial interest

Where both husband and wife have a substantial interest in the concern and both are in receipt of the remuneration in such concern, the remuneration from such concern is to be included in the total income of the husband or, as the case may be, the wife whose total income excluding the income referred to in that clause i.e. 64(1)(ii) is greater; and where any such income is once included in the total income of either spouse, any such income arising in any succeeding year shall not be included in the total income of the other spouse unless the Assessing Officer is satisfied, after giving that spouse an opportunity of being heard, that it is necessary so to do.

**Illustration**

Mr. P is employed as Public Relation Officer in a company where Mrs. P holds 21 per cent equity shares. She has been holding the share before marriage with Mr. P., Mr. P gets a salary of Rs. 1,500 per month.

The whole salary of Rs. 18,000 will be included in the income of Mrs. P provided Mr. P has no technical or professional qualification. It is immaterial that the remuneration so paid is genuine and not excessive and that Mrs. P had substantial interest in the company even before her marriage.

**(b) Income to spouse from the assets transferred [Section 64(1)(iv)]**

Where any individual transfers directly or indirectly any asset (other than a house property) to the spouse, the income from such asset shall be included in the income of the transferor.

In order to attract the provisions of this section, it is not necessary that the asset must have been transferred by the assessee to his spouse in the same form in which it stands at the time the income arises. Conversion of assets from one form to another would be totally immaterial and it is also not essential that the transfer must have taken place directly between the spouses.

**Exception:** However, there are exceptions to this rule:

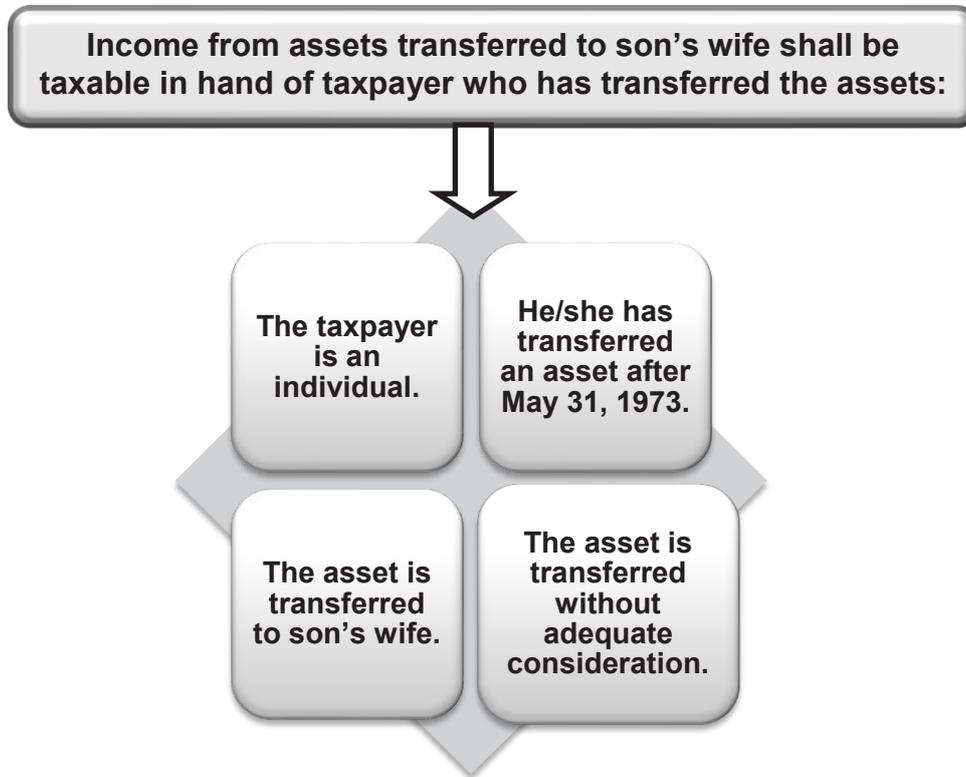
- (i) The transferor has received adequate consideration in money or money's worth. If the consideration was inadequate, proportionate income shall be included in the income of the transferor.
- (ii) The transfer has been made in connection with an agreement to live apart. This separation can be either judicial or voluntary under circumstances in which a judicial separation can be granted.
- (iii) The income from the assets transferred shall not be included in the income of transferor after the death of spouse, either transferor or transferee.
- (iv) The income from assets transferred shall be included in the income of the transferor, only if the relationship as spouse exists on the two dates, i.e., the date of transfer and the date on which the income accrues or arises to the transferee. If any asset has been transferred before marriage, the income from such asset cannot be included in the income of the transferor.
- (v) Only the direct income (including capital gains) earned with the help of the transferred assets shall be included in the income of the transferor. Any indirect income to the transferee from the transferred assets shall not be included in the income of the transferor.

Suppose, A transfers certain shares to his wife B. Dividends received on such shares are taxable in the hands of A. If B sells the shares and makes some capital gains, such gains are also taxable in A's hands. Now from the dividend money, B purchases some more shares and receives dividends on these new shares, such dividends are not taxable to A. In the same way, if B receives certain bonus shares on the shares transferred by her husband and later on she receives dividend on such bonus shares, the dividend shall not be included in the income of the transferor because the bonus shares were never transferred by her husband.

If some pin-money is given to wife by her husband neither the savings out of pin-money nor the income earned with the help of savings out of pin-money can be included in the income of husband.

**Illustration** - X transfers 500 debentures of IFCI to his wife without adequate consideration. Interest income on these debentures will be included in the income of X.

### INCOME FROM ASSETS TRANSFERRED TO SON'S WIFE [SECTION 64(1)(vi)]



### TRANSFER FOR IMMEDIATE OR DEFERRED BENEFIT OF SON'S WIFE [SECTION 64(1)(viii)]

Any income arising, directly or indirectly, to any person or association of persons from assets transferred directly or indirectly after June 1, 1973, otherwise than for adequate consideration to the person or association of persons by such individual shall, to the extent to which the income from such assets is for the immediate or deferred benefit of his son's wife be included in computing the total income of such individual.

*Explanation:* For the purpose of clauses (iv) and (vi), where the assets transferred directly or indirectly by an individual to his spouse or son's wife (hereafter in this Explanation referred to as "the transferee") are invested by the transferee -

- (i) in any business, such investment being not in the nature of contribution of capital as a partner in a firm or, as the case may be, for being admitted to the benefits of partnership in a firm, that part of the income arising out of the business to the transferee in any previous year, which bears the same proportion to the income of the transferee from the business as the value of the assets aforesaid as on the first day of the previous year bears to the total investment in the business by the transferee as on the said day;
- (ii) in the nature of contribution of capital as a partner in a firm, that part of the interest receivable by the transferee from the firm in any previous year, which bears the same proportion to the interest receivable by the transferee from the firm as the value of investment aforesaid as on the first day of the previous year bears to the total investment by way of capital contribution as a partner in the firm as on the said day,

shall be included in the total income of the individual in that previous year.

**INCOME TO SPOUSE THROUGH A THIRD PERSON [SECTION 64(1)(vii)]**

Where a person transfers some assets directly or indirectly to a person or association of persons (trustee or body of trustees or juristic person) without adequate consideration for the immediate or deferred benefit of his or her spouse, all such income as arises directly or indirectly from assets transferred shall be included in the income of the transferor. If only a portion is reserved for the benefit of spouse and a portion is utilised for the benefit of others, only the portion reserved for the spouse shall be included in the income of the transferor.

The share of income of the spouse can be included in the income of the transferor provided the spouse has either received the income or the income has accrued to spouse or the spouse has a beneficial interest in the income. If an individual creates a life-interest in a property in favour of a third person and grants the remainder to his spouse, and so long as the third person is alive, she should not be getting any benefit out of transferred asset, such income cannot be included in the income of the transferor. If however, the benefit from the assets transferred is to be derived by the transferor himself, the transfer would be treated as revocable and would consequently fall within the purview of Section 61 which provides that the entire income arising from the assets so transferred shall be included in the total income of the transferor.

Where a trust was created by assessee's mother for the benefit of the assessee, his wife and the trustees were authorised to carry on business, the income from the business was held to be income of the trust and the share of wife could not be added to the income of the spouse because neither the trust was created by the assessee nor the business done in the partnership. [*K.T Doctor v. C.I.T (1980) 124 ITR 501 (Guj.)*].

**CLUBBING OF INCOME OF MINOR CHILD [SECTION 64(1A)]**

All income which arises or accrues to the minor child (not being a minor child suffering from any disability of the nature specified in Section 80U) shall be clubbed in the income of his parent. However, any income which is derived by the minor from manual work or from any activity involving application of his skill, talent or specialised knowledge and experience will not be included in the income of his parent. Further, the income of the minor shall be included in the income of that parent whose total income excluding income includible under this sub-section is greater, where the marriage of minor's parents subsists, otherwise the income of the minor will be includible in the income of that parent who maintains the minor child in the relevant previous year.

Once the income of the minor is included in the total income of any one parent, clubbing of income of the minor with the same parent will continue in subsequent years also, unless the Assessing Officer is satisfied, after giving that parent an opportunity of being heard that it is necessary so to do.

In case the income of an individual includes any income of his minor child in terms of this section [i.e. Section 64(1A)], such individual shall be entitled to exemption of the amount of such income or Rs. 1,500 whichever is less.

**INCOME FROM THE CONVERTED PROPERTY [SECTION 64(2)]**

Where an individual, being a member of Hindu Undivided Family, transfers his self-acquired property after 31st December, 1969 to the family for the common benefit of the family, or throwing it into the common stock of the family, or transfers it directly or indirectly to the family otherwise than for adequate consideration, such property is known as converted property. The income derived from the converted property or any part thereof, shall be included in the income of the transferor.

For this section "property" includes any interest in property, movable or immovable the proceeds of sale thereof and any money or investment for the time being representing the proceeds of sale thereof and where the property is converted into any other property by any method, such other property.

**Income from converted property to spouse after partition**

Where the converted property has been the subject matter of total or partial partition amongst the members of

the family, the income derived from such converted property as is received by the spouse of the transferor on partition shall be included in the income of the individual.

The income so included in the total income of the individual shall be excluded from the total income of the family or spouse, as the case may be.

The income from the above mentioned items shall first be computed under the appropriate heads in the hands of the transferee and after that it shall be included in the total income of the transferor under the head, "Income from other sources". However, the income from house property transferred to spouse shall be computed under the head 'Income from house property' in the hands of transferor and not in the hands of the transferee.

Explanation to the term 'income' used in Section 64 includes 'loss'. This amendment nullifies the decision in *Dayalbai Madhavji Vadera v. C.I.T. (1966) 60 ITR 551* of the Gujarat High Court that the term 'income' used in Sub-section (1) of Section 64 does not include a loss.

#### SUMMARY OF THE CLUBBING PROVISION

Nature of Transaction	Clubbed in the Hands of	Conditions/Exceptions	Relevant Reference
<b>Transfer of Income without transfer of Assets (Section 60)</b>	Transferor who transfers the income	Irrespective of: 1. Whether such transfer is revocable or not. 2. Whether the transfer is effected before or after the commencement of IT Act.	1. Income for the purpose of Section 64 includes losses. [P. Doriswamy Chetty 183 ITR 559 (SC)] [also see Expl. (2) to Section 64] 2. Section 60 does not apply if corpus itself is transferred. [Grandhi Narayana Rao 173 ITR 593 (AP)]
<b>Revocable transfer of Assets (Section 61)</b>	Transferor who transfers the Assets	Clubbing not applicable if: 1. Trust/transfer irrevocable during the lifetime of beneficiaries/transferee or 2. Transfer made prior to 1-4-1961 and not revocable for a period of 6 years. Provided the transferor derives no direct or indirect benefit from such income in either case.	Transfer held as revocable 1. If there is provision to re transfer directly or indirectly whole/part of income/asset to transferor; 2. If there is a right to reassume power, directly or indirectly, the transfer is held revocable and actual exercise is not necessary. [S. Raghbir Singh 57 ITR 408 (SC)] 3. Where no absolute right is given to transferee and asset can revert to transferor in prescribed circumstances, transfer is held revocable. [Jyotendrasinhji vs. S. I. Tripathi 201 ITR 611 (SC)]

Nature of Transaction	Clubbed in the Hands of	Conditions/Exceptions	Relevant Reference
<b>Salary, Commission, Fees or remuneration paid to spouse from a concern in which an individual has a substantial* interest. [Section 64 (1)(ii)]</b>	Spouse whose total income (excluding income to be clubbed) is greater.	Clubbing not applicable if: Spouse possesses technical or professional qualification and remuneration is solely attributable to application of that knowledge/qualification.	1. The relationship of husband and wife must subsist at the time of accrual of the income. [Philip John Plasket Thomas 49 ITR 97 (SC)] 2. Income other than salary, commission, fees or remuneration is not clubbed under this clause
<b>Income from assets transferred directly or indirectly to the spouse without adequate consideration [Section 64 (1)(iv)]</b>	Individual transferring the asset.	Clubbing not applicable if: The assets are transferred; 1. With an agreement to live apart. 2. Before marriage. 3. Income earned when relation does not exist. 4. By Karta of HUF gifting co-parcenary property to his wife. L. Hirday Narain vs. ITO 78 ITR 26 (SC) 5. Property acquired out of pin money. R.B.N.J. Naidu vs. CIT 29 ITR 194 (Nag.)	1. Income earned out of Income arising from transferred assets not liable for clubbed. [M.S.S. Rajan 252 ITR 126 (Mad)] 2. Cash gifted to spouse and he/she invests to earn interest. [Mohini Thaper vs. CIT 83 ITR 208 (SC)] 3. Capital gain on sale of property which was received without consideration from spouse [Sevential M. Sheth vs. CIT 68 ITR 503 (SC)] 4. Transaction must be real. [O.N. Mohindroo 99 ITR 583 (Delhi)]
<b>Income from the assets transferred to son's wife [Section 64 (1)(vi)]</b>	Individual transferring the Asset.	Condition: The transfer should be without adequate consideration.	Cross transfers are also covered [C.M.Kothari 49 ITR 107 (SC)]
<b>Transfer of assets by an individual to a person or AOP for the immediate or deferred benefit of his: (vii) - Spouse (viii) - Son's wife [Section 64(1)(vii)&amp;(viii)]</b>	Individual transferring the Asset.	Condition: 1. The transfer should be without adequate consideration.	1. Transferor need not necessarily have taxable income of his own. [P. Murugesan 245 ITR 301 (Mad)] 2. Wife means legally wedded wife. [Executors of the will of T.V. Krishna Iyer 38 ITR 144 (Ker)]

Nature of Transaction	Clubbed in the Hands of	Conditions/Exceptions	Relevant Reference
<b>Income of a minor child [Child includes step child, adopted child and minor married daughter] [Section 64 (1A)]</b>	1. If the marriage subsists, in the hands of the parent whose total income is greater; or; 2. If the marriage does not subsist, in the hands of the person who maintains the minor child. 3. Income once included in the total income of either of parents, it shall continue to be included in the hands of same parent in the subsequent year unless AO is satisfied that it is necessary to do so (after giving that parent opportunity of being heard)	Clubbing not applicable for: – 1. Income of a minor child suffering any disability specified u/s. 80U. 2. Income on account of manual work done by the minor child. 3. Income on account of any activity involving application of skills, talent or specialized knowledge and experience.	1. Income out of property transferred for no consideration to a minor married daughter, shall not be clubbed in the parents' hands. [Section 27] 2. The parent in whose hands the minor's income is clubbed is entitled to an exemption up to Rs. 1,500 per child. [Section 10(32)]
<b>Income of HUF from property converted by the individual into HUF property [Section 64 (2)]</b>	Income is included in the hands of individual & not in the hands of HUF.	Clubbing applicable even if: The converted property is subsequently partitioned; income derived by the spouse from such converted property will be taxable in the hands of individual.	Fiction under this section must be extended to computation of income also. [M.K. Kuppuraj 127 ITR 447 (Mad)]

## RECOVERY OF TAX

**Dual Liability for Tax :** The tax on the income of the other person which has been included in the income of the assessee can either be recovered from the assessee or from the other person. The liability of other person is limited to the portion of the tax levied on the assessee which is attributable to the income so included. His liability arises after the service of a notice of demand by the Assessing Officer in this behalf.

Where any such asset (the income from which has been included in that of the assessee) is held jointly by more

than one person, they shall be jointly and severally liable to pay the tax which is attributable to the income from the assets so included.

**Illustration 1 :**

Mr Sharma invests Rs 10 lakh in a fixed deposit (FD) at a bank, in his wife's name. Interest of Rs. 1 lakhs arises on this income. Mrs Sharma invests the interest on periodic basis and interest for an amount of Rs. 5,000 arises on the interest deposited by her in bank. Analyze the clubbing provisions and find out the taxability of interest accrued.

**Solution**

Rs. 1 lakhs in the Now Interest income on FD will be clubbed with his (Mr. Sharma) income. Interest of Rs. 5,000 aroused out of Investment made by Mrs. Sharma will be taxed as her own income.

**Illustration 2 :**

Red holds 40% of shares in a Company. Mrs. Red (a CS) is employed in the company as a Company Secretary and is getting salary of Rs. 15,000 per month. Compute total income and tax payable by Red and Mrs. Red for the Assessment Year 2020-21 assuming other income of Red is Rs. 2,00,000 from a business and dividend income from company is Rs. 3,00,000.

**Solution**

In the present case, Mrs. Red's salary income will be taxable in her hands only as she is earning the same through her professional qualification.

**Computation of Total Income and Tax Liability for Assessment Year 2020-21**

Particulars	Mr. Red (Rs.)	Mrs. Red (Rs.)
Income from Salary	Nil	1,80,000
Income from Business	2,00,000	Nil
Income from other sources: Dividend Income [Exempt u/s 10(34)]	Nil	Nil
<b>Gross Total Income (or Total Income)</b>	<b>2,00,000</b>	<b>1,80,000</b>
Tax Liability (as total income does not exceed ₹ 2,50,000):	<b>Nil</b>	<b>Nil</b>

**Illustration 3:**

Mr. Amit is beneficially holding 21% equity shares of Essem Minerals Pvt. Ltd. Mrs. Amit is employed as Manager (in accounts department) in Essem Minerals Pvt. Ltd. at a monthly salary of Rs. 84,000. Mrs. Amit is not having any knowledge, experience or qualification in the field of accountancy. Will the remuneration (i.e., salary) received by Mrs. Amit be clubbed with the income of Mr. Amit?

**Solution**

In this situation, Mr. Amit is having substantial interest in Essem Minerals Pvt. Ltd. and remuneration of Mrs. Amit is not justifiable (i.e., she is employed without any technical or professional knowledge or experience) and, hence, salary received by Mrs. Amit from Essem Minerals Pvt. Ltd. will be clubbed with the income of Mr. Amit and will be taxed in the hands of Mr. Amit.

**Illustration 4:**

Mr. Kapoor gifted Rs. 8,40,000 to his wife. The said amount is invested by his wife in debenture of a company. Will the income from the debenture purchased by Mrs. Kapoor from gifted money be clubbed with the income of Mr. Kapoor?

**Solution**

Rs. 8,40,000 is transferred to spouse. Fund is transferred via gift (i.e., without adequate consideration) and, hence, the provisions of section 64(1)(iv) will be attracted. The provisions of clubbing will apply even if the form of asset is changed by the transferee-spouse.

In this case asset transferred is money and, subsequently, the form of asset is changed to debentures, hence, income from debentures acquired from money gifted by her husband will be clubbed with the income of her husband. Thus, interest on debenture received by Mrs. Kapoor will be clubbed with the income of Mr. Kapoor.

**SET-OFF AND CARRY-FORWARD OF LOSSES**

While one endeavors to derive income, the possibility of incurring losses cannot be ruled out. Based on the principles of natural justice, a set-off should be available for loss incurred. The income tax laws in India recognize this and provide for adjustment and utilization of the losses. For this purpose, the Income-tax Act, 1961 contains specific provisions (Sections 70 to 80) for the set-off and carry-forward of losses.

Income-tax is levied on the total income of the previous year of an assessee and it is necessary to ascertain the total income. Further, loss incurred by the assessee is to be set-off against any income, the net result of the assessee’s activities during the particular accounting year cannot be ascertained and consequently the tax payable would also be incapable of determination.

**Set-Off of Losses from One Source Against Income from Another Source under the Same Head of Income [Section 70]**

The process of adjustment of loss from a source under a particular head of income against income from other source under the same head of income is called intra-head adjustment, e.g. Adjustment of loss from business A against profit from business B.

Income of a person is computed under five heads. ‘Sources’ of income derived by an individual may be many but yet they could be classified under the same head. Consider a situation where Harish has two properties - one, occupied by him and the other, let out. Harish pays interest on loan of Rs 1.50 lakh on the property occupied and derives net rental income of Rs 1.50 lakh from the let-out property. In case of a self-occupied property, income is computed as nil and interest expenditure results in loss. The loss of Rs 1.50 lakh can be set off against rent income of Rs 1.50 lakh; the income chargeable under the head ‘House property’ will be ‘Nil’.

Thus, in general, if the net result for any assessment year in respect of any source falling under any head of income is a loss, the assessee is entitled to set off the amount of such loss against his income from any other source under the same head.

However, the following are the **exceptions to general rule**:



1. **Speculative Business Losses:** Loss from speculation business cannot be set off against profit from a non-speculation business however loss from non-speculative business can be set-off against speculation income.)
2. **Long-term capital Loss:** Long Term Capital Loss (LTCL) can only be set off against Long Term Capital Gain (LTCG) and cannot be set off against Short term Capital Gain (STCG) however STCL can be set off against LTCG)
3. **Casual Income:** No loss can be set-off against casual income i.e. Income from lotteries, crossword puzzles, race including horse race, card game, and any other game of any sort or from gambling or betting of any form or nature. No expenses can be claimed against casual income.
4. **Losses from the activity of owning and maintaining race horses:** Loss from the business of owning and maintaining race horses cannot be set off against any income other than income from the business of owning and maintaining race horses.
5. **Loss from an exempted source cannot be set off against taxable Income:** If income from a particular source is exempt from tax, then loss from such source cannot be set off against any other income which is chargeable to tax, e.g., Agricultural income is exempt from tax, hence, if the taxpayer incurs loss from agricultural activity, then such loss cannot be adjusted against any other taxable income.
6. **Income Losses of specified Business:** Loss from business specified under section 35AD cannot be set off against any other income except income from specified business (section 35AD is applicable in respect of certain specified businesses like setting up a cold chain facility, setting up and operating warehousing facility for storage of agricultural produce, developing and building a housing projects, etc.)

### Income losses Intra-head Set off

#### (A) Loss from business or profession

Any loss from business or profession (other than speculation business or loss from the activity of owning and maintaining race horses) can be set off against the income from any other business or profession including the income from speculation business or income from the activity of owning and maintaining race horses.

If any business has been discontinued during the year, the loss from such business can also be set-off from the income of other business or profession.

The loss suffered by a wholly owned subsidiary company cannot be set-off by the parent company, since both are separate assesseees. Similarly, where loss incurred by a wholly owned subsidiary company is reimbursed by the holding company, the subsidiary company does not use the right to carry forward and set-off the loss. [*C.I.T v. Handicraft Handloom Export Corporation (1982) 133 ITR 590 (Delhi)*].

#### (B) Loss from speculation business

Such loss can be set-off only against the income from speculation business. It is not essential that the nature of the other speculation transaction must be the same. Speculative transactions in different commodities and in different markets are to be treated as one business. However, a loss from an illegal speculation business cannot be set-off against income from any lawful speculation. [*C.I.T. v. K.J. Kotecha 107 ITR 101 (SC)*]. Similarly, where the assessee earns commission on speculative transactions, he is not entitled to set-off speculative loss against such commission because there is no element of speculation in the commission [*C.I.T. v. Pangal Vittal Nayak & Co. Pvt. Ltd. (1969) 74 I.T.R. 754 (S.C.)*]. By virtue of an explanation to Section 73 where any part of the business of a company (other than a company whose gross total income consists mainly of income which is chargeable under the heads: "Interest on securities", "Income from House Property", "Capital gains", "Income

from other sources”, or a company the principal business of which is the business of banking or granting of loans and advances) consists of the purchase and sale of shares of other companies, such company shall for the purpose of this section (Section 73), be deemed to be carrying on a speculation business to the extent to which the business consists of the purchase and sale of such shares.

### **Set-Off of Loss from One Head Against Income from Another Head [Section 71]**

After making intra-head adjustment (if any) the next step is to make inter-head adjustment. If in any year, the taxpayer has incurred loss under one head of income and is having income under other head of income, then he can adjust the loss from one head against income from other head, E.g., Loss under the head of house property to be adjusted against salary income.

A person may have various sources of income computed under different heads of income. Loss under one head of income is generally allowed to be set off against income under another head.

For instance, X has only one property, which is occupied by him and the loss is Rs 1.50 lakh. He derives salary of Rs 10 lakh during the year. Here, he can set off the loss of Rs 1.50 lakh against his salary income by making appropriate declarations to his employer, thereby making his net taxable income Rs 8.50 lakh.

The provision of Section 71 reads as under:

- (a) loss under the head “capital gains” cannot be set off against income under any other head. It must be set off only against income from “capital gains”.
- (b) Loss under the head “Profits and gains of business or profession” cannot be set off against the head “income from Salaries”.
- (c) Where the assessee incurs any loss under the head income from house property it can be set off against the assessee’s any other income under other head during the previous years where such loss is not fully adjusted under other heads of income in the same assessment year, then the balance loss shall be allowed to be carried forward and set off in subsequent years subject to a limit of eight assessment years against income from house property.

Section 71(3A) Inter head adjustment of loss under the head House Property (i.e. adjustment of loss under the head House Property against Income under any other head in the same year) cannot exceed Rs 2,00,000 for any assessment year. Remaining loss can be carried forward to be set off in future as per provisions of Section 71B. (There is no restriction of Rs. 2,00,000 in section 71B).

- (d) Loss incurred by an assessee from a source, income from which is exempt, cannot be set-off against income from a taxable source.

There are certain exceptions to the general rule that Loss under one head of income is allowed to be set off against income under another head.

- a) Loss from speculative business cannot be set off against any other income. However, non-speculative business loss can be set off against income from speculative business. For Example: House property loss can be set-off against Speculative Incomes but speculation loss cannot be set off against House property)
- b) Business loss cannot be set-off against salary income. (It can be set-off against other incomes)
- c) Loss under the head Capital Gains (LTCL or STCL) cannot be set-off against any other head however Loss from other heads can be set-off against Capital Gains. For an instance, House Property loss can be set-off against CG but LTCL or STCL cannot be set off against HP, i.e., house property Income.

- d) No loss can be set off against Casual income such as winnings from lotteries, crossword puzzles, race including horse race, card game, and any other game of any sort or from gambling or betting of any form or nature.
- e) No expenses can be claimed against casual income.
- f) Loss from the business of owning and maintaining race horses cannot be set off against any other income.
- g) Loss from an exempted source cannot be set off (e.g. Share of loss of firm, agricultural income, cultivation expenses)
- h) Loss from business specified under section 35AD cannot be set off against any other income (section 35AD is applicable in respect of certain specified businesses like setting up a cold chain facility, setting up and operating warehousing facility for storage of agricultural produce, developing and building housing projects, etc.)

It may be noted that Before making inter-head adjustment, the taxpayer has to first make intra-head adjustment.

### **CARRY-FORWARD OF LOSSES**

Many times it may happen that after making intra-head and inter-head adjustments, still the loss remains unadjusted. Such unadjusted loss can be carried forward to next year for adjustment against subsequent year(s) income. Separate provisions have been framed under the Income-tax Law for carry forward of loss under different heads of income. Losses can be set-off against the income of following years provided that they have been suffered by assessee and determined in pursuance of a return filed by the assessee. Further, carry forward of losses (other than loss from house property and unabsorbed depreciation) is permissible if the return of income for the year, in which loss is incurred, is filed in time. The late filing of return should not impact the status of carry forward of loss of previous years.

The following losses could be carried forward :

- (i) Loss in non-speculation business or profession.
- (ii) Loss in speculation business.
- (iii) Loss in transfer of capital assets [whether short-term or long-term].
- (iv) Loss from activity of owning and maintaining of race horses.
- (v) Loss under the head 'Income from House Property'.

However, losses suffered under the following heads are not allowed to be carried forward and set off:

- (1) Losses under the head 'salaries'.
- (2) Losses under the head 'Income from other sources' (excepting loss suffered from the activity of owning and maintaining race horses).

### **(A) Loss in Non-Speculation Business [Section 72]**

It shall be set-off against the profits and gains, if any, of any business or profession carried on by him and assessable for that assessment year.

From this it follows that the loss from non-speculation business or profession can be set-off against the income of the business in which it was suffered or any other business or profession either old or new including speculation business income or from any other head, such as house property, or other sources, if the income under this

head forms part of the trading activities of the assessee. [*Western States Trading Co. (P) Ltd. v. C.I.T. (1971) 80 ITR 21 (SC)*].

The loss can be set-off against the business profits of the year provided such profits are assessable to tax. If the profits are exempt from tax for any reason, no set-off can be made by the income-tax officer against such profits.

#### Conditions for carry forward and set-off of business loss

- (i) The right of carry-forward and set-off is available to the same assessee who has sustained the loss. A holding company however, cannot claim to carry forward the losses, if any, incurred by its wholly owned subsidiary company. Exceptions to this rule are (a) cases of succession by inheritance [a loss incurred by the father in the course of carrying on his business can be carried forward and set-off by his son, if the son succeeds to the business of his father on account of the father's death but not otherwise] (b) accumulated business loss of an amalgamating company under Section 72A (c) the share of loss of partnership taken over by one of its partners can also be set-off by the partner [*Dwarkadass Leeladhar v. CIT (1963) 47 ITR 619 (Ker.)*]

However, loss incurred by HUF cannot be carried forward and set-off after its partition against income of firm formed thereafter by certain coparceners [*KeshrichandBhanabhai v. CIT(1951) 20ITR 201 (Bom.)*].

- (ii) The loss can be carried forward to a maximum of eight consecutive assessment years immediately succeeding the assessment year for which the loss was first computed.

In case of a business on which rehabilitation allowance has been allowed, the previous losses are allowed to be carried forward to the assessment year relevant to the previous year in which the business was so revived or re-established and are allowed to be set-off against the profits of that assessment year. Any balance of loss can be carried forward to the succeeding seven assessment years.

- (iii) Where any unabsorbed depreciation or capital expenditure on scientific research has been brought forward alongwith business loss, the business loss shall first be set-off.

#### Order of Set-off of losses

In case where profits are insufficient to absorb brought forward losses, current depreciation and current business losses, the same should be deducted in the following order:

- (a) Current scientific research expenditure [under Section 35(1)].
- (b) Current Depreciation [under Section 32(1)].
- (c) Brought forward business losses [under Section 72(1)].
- (d) Unabsorbed family planning promotion capital expenditure [under Section 36(1)(ix)].
- (e) Unabsorbed Depreciation [under Section 32(2)].
- (f) Unabsorbed scientific research expenditure [under Section 35(4)].

#### **(B) Loss in Speculation Business [Section 73]**

Where, for any assessment year, any loss computed in respect of a speculation business has not been wholly set-off against the profits of another speculation business, it shall be carried forward to the following assessment year and shall be set-off against the profits of any speculation business carried on by him and assessable for the assessment year.

### Speculative Business

Explanation to section 73 provides that where any part of the business of a company (other than a company whose gross total income consists mainly of income which is chargeable under the heads “Interest on securities”, “Income from house property”, “Capital gains” and “Income from other sources”, or a company the principal business of which is the business of trading in shares or banking or the granting of loans and advances) consists in the purchase and sale of shares of other companies, such company shall, for the purposes of this section, be deemed to be carrying on a speculation business to the extent to which the business consists of the purchase and sale of such shares.

Sub-section (5) of section 43 defines the term speculative transaction as a transaction in which a contract for purchase or sale of any commodity, including stocks and shares, is settled otherwise than by way of actual delivery. However, the proviso to sub-section (5) of section 43 exempts, inter alia, transaction in respect of trading in derivatives on a recognised stock exchange and commodity derivative which are chargeable to commodity transaction tax, from its ambit.

### Carry forward of losses in speculative business

In case of speculation loss even if the particular speculation business in which there is loss is discontinued, this loss can be carried forward to be set-off in the succeeding year against the profits of any other speculation business.

This loss can be carried forward to a maximum of **four consecutive assessment years** immediately succeeding the assessment year for which the loss was first computed.

However, the loss from an illegal speculation business or loss incurred in speculation business in banned items can be neither set-off against income from any lawful speculation business nor can it be carried forward for being set-off in the subsequent year against income even from an illegal speculation business because the law assumes that any illegal business dies with all its losses in the same year [*CIT v. Kurji Jinabhai Kotecha (1977) 107 ITR 101 (SC)*].

Where any unabsorbed depreciation or capital expenditure on scientific research has been brought forward along with speculation loss, the speculation loss shall first be set-off.

Sometimes there may be brought-forward speculation loss and current year’s non-speculation business loss. Now the problem arises whether the brought forward speculation loss should be adjusted first against the current year’s speculation income or current year’s non-speculative business loss should be set-off first against the current year’s speculative income. Accordingly to the administrative instructions the Assessing Officer may allow the assessee:

- (i) either to first set-off the speculation loss carried forward from an earlier year against the speculation profits of the current year and then to set-off the current year’s losses against other sources and against the remaining part, if any, of the current year’s speculation profits; or
- (ii) to first set-off the current year’s losses from non-speculation business and other sources against the current year’s speculation profits and then to set-off the carried forward speculation losses of the earlier year against the remaining part, if any, of the current year’s speculation profits, whichever is advantageous to the assessee.

Where an assessee has brought forward speculative loss from his individual business and during the current year he receives some speculative gains from a firm in which he is a partner, the brought forward loss can be set-off against the speculative profits received from the firm. Similarly, where a speculation business is carried on by sole proprietor and after his death the business is continued by legal heirs forming partnership, the firm is entitled to carry forward and set-off such loss. [*C.I.T. v. Madhukant M. Mehta (1981) 132 ITR 159 (Guj.)*].

**(C) Carry Forward and Set Off of Losses by Specified Business [Section 73A]**

- (1) Any loss of any specified business in section 35AD shall not be set off except against profits and gains of any other specified business.
- (2) Where for any assessment year any loss computed of the specified business has not been wholly set off, the loss not set off shall be carried forward to the following assessment year, and
  - (i) it shall be set off against the profits and gains of any specified business carried on by him and
  - (ii) if the loss can not be wholly set off, the amount of loss not set off shall be carried forward to the following assessment year and so on.

**(D) Set-Off and Carry Forward of Capital Losses [Section 74]**

Where, in respect of any assessment year, the net result of the computation under the head "Capital gains" is a loss to the assessee, it can be carried forward to the following assessment year. The short-term and long-term losses shall be separately carried forward. In case of short-term capital loss it can be set off against income, if any, under the head "Capital gains" (whether short-term or long-term) assessable for that assessment year in respect of any other capital asset. But in case of long-term capital loss, it can be set off only against long-term capital gain.

While losses on transfer of capital assets, whether short-term or long-term cannot be set off against any other income of the assessee under other heads of income i.e. heads other than 'capital gains' in the previous year in which such loss was incurred, it can be carried forward to be set off against capital gains if any during the next eight assessment years.

**(E) Loss on Maintenance of Race Horses [Section 74A]**

Where an assessee who is the owner of race horses sustains a loss in the activity of owning and maintaining race horses, he can carry-forward and set-off such loss against his income (Prize money received on a race horse or race horses) from the activity of owning and maintaining race horses in subsequent years. This loss can be carried forward to a maximum of four assessment years immediately succeeding the assessment year for which the loss was first computed.

**(F) Loss Under the Head "Income From Other Sources"**

Except the loss from the activity of owning and maintaining of race horses, the unabsorbed loss from no other activity under the above head is permitted to be carried forward and set off against income of subsequent years.

**CARRY FORWARD AND SET-OFF OF ACCUMULATED BUSINESS LOSS AND UNABSORBED DEPRECIATION IN CERTAIN CASES OF AMALGAMATION OR DEMERGER ETC. [SECTION 72A]**

Section 72A provides for carry forward and set off of accumulated loss and unabsorbed depreciation allowance in case of:

- (i) amalgamation [Section 72A(1), (2) and (3)], or
- (ii) demerger [Section 72A(4) and (5)], or
- (iii) reorganisation of business [Section 72A(6)].

**(i) Carry forward and set off of accumulated loss and unabsorbed depreciation in case of amalgamation [Section 72A(1), (2) and (3)]**

- (1) Where there has been an amalgamation of a company owning an industrial undertaking or a ship or a hotel with another company or an amalgamation of a banking company referred to in Clause (c) of Section 5 of the Banking Regulation Act, 1949 (10 of 1949) with a specified bank, then, notwithstanding anything contained in any other provision of this Act, the accumulated loss and the unabsorbed depreciation of the amalgamating company shall be deemed to be the loss or, as the case may be, allowance for depreciation of the amalgamated company for the previous year in which the amalgamation was effected, and other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly.
- (2) Notwithstanding anything contained in Sub-section (1), the accumulated loss shall not be set off or carried forward and the unabsorbed depreciation shall not be allowed in the assessment of the amalgamated company unless -
  - (a) the amalgamating company -
    - (i) has been engaged in the business, in which the accumulated loss occurred or depreciation remains unabsorbed, for three or more years;
    - (ii) has held continuously as on the date of the amalgamation at least three-fourths of the book value of fixed assets held by it two years prior to the date of amalgamation;
  - (b) the amalgamated company -
    - (i) holds continuously for a minimum period of five years from the date of amalgamation at least three-fourths of the book value of fixed assets of the amalgamating company acquired in a scheme of amalgamation;
    - (ii) continues the business of the amalgamating company for a minimum period of five years from the date of amalgamation;
    - (iii) fulfils such other conditions as may be prescribed to ensure the revival of the business of the amalgamating company or to ensure that the amalgamation is for genuine business purpose.

**Consequences if the above conditions are not satisfied [Section 72A(3)]:** In a case where the conditions laid down under Clause (b) above are not complied with, the set off of loss or allowance of depreciation made in any previous year in the hands of the amalgamated company shall be deemed to be in the income of the amalgamated company chargeable to tax for the year in which such conditions are not complied with.

**[Note:** The carry forward and set off of loss and unabsorbed depreciation as per the above provisions shall be allowed only when amalgamation is as per the provisions of Section 2(1B) of the Income-tax Act, 1961].

**(ii) Carry forward and set off of accumulated losses and unabsorbed depreciation in case of demerger [Sections 72A(4) and (5)]**

Notwithstanding anything contained in any other provisions of this Act in the case of a demerger, the accumulated loss and the allowance for absorbed depreciation of the demerged company shall -

- (a) where such loss or unabsorbed depreciation is directly relatable to the undertakings transferred to the resulting company, be allowed to be carried forward and set off in the hands of the resulting company;
- (b) where such loss or unabsorbed depreciation is not directly relatable to the undertakings transferred to the resulting company, be apportioned between the demerged company and the resulting company in the same proportion in which the assets of the undertakings have been retained by the demerged company and transferred to the resulting company, and be allowed to be carried forward and set off transferred to the resulting company, and be allowed to be carried forward and set off in the hands of the demerged company or the resulting company, as the case may be.

The Central Government may, for the purposes of this Act, by notification in the Official Gazette, specify such conditions as it considers necessary to ensure that the demerger is for genuine business purposes.

[**Note:** The carry forward and set off of accumulated loss and unabsorbed depreciation as per the above provisions shall be allowed only when demerger is as per the provisions of Section 2(19AA) of the Income-tax Act.]

**(iii) Carry forward and set off of accumulated losses and unabsorbed depreciation in case of reorganisation of business [Section 72A(6)]**

Where there has been reorganisation of business, whereby, a firm is succeeded by a company fulfilling the conditions laid down in Clause (xiii) of Section 47 or a proprietary concern is succeeded by a company fulfilling the conditions laid down in Clause (xiv) of Section 47, then, notwithstanding anything contained in any other provisions of this Act, the accumulated loss and the unabsorbed depreciation of the predecessor firm or the proprietary concern, as the case may be, shall be deemed to be the loss or allowance for depreciation of the successor company for the purpose of previous year in which business reorganisation was effected and other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly.

Section 72(6A): Where there has been reorganisation of business whereby a private company or unlisted public company is succeeded by a limited liability partnership fulfilling the conditions laid down in the proviso to clause (xiiib) of section 47, then, notwithstanding anything contained in any other provision of this Act, the accumulated loss and the unabsorbed depreciation of the predecessor company, shall be deemed to be the loss or allowance for depreciation of the successor limited liability partnership for the purpose of the previous year in which business reorganisation was effected and other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly.

***Consequences if the conditions laid down under Section 47(xiii), (xiv) and 47(xiiib) are not complied with [Proviso to Section 72A(6) & (6A)]***

If any of the conditions laid down under Section 47(xiii) and (xiv) are not complied with, the set off of loss or allowance of depreciation made in any previous year in the hands of the successor company, shall be deemed to be the income of the company chargeable to tax in the year in which such conditions are not complied with.

If any of the conditions laid down in the proviso to clause (xiiib) of section 47 are not complied with, the set off of loss or allowance of depreciation made in any previous year in the hands of the successor limited liability partnership, shall be deemed to be the income of the limited liability partnership chargeable to tax in the year in which such conditions are not complied with.

**Note: “Accumulated loss”** means so much of the loss of the predecessor firm or the proprietary concern or the private company or unlisted public company before conversion into limited liability partnership or the amalgamating company or the demerged company, as the case may be, under the head “Profits and gains of business or profession” (not being a loss sustained in a speculation business) which such predecessor firm or the proprietary concern or the company or amalgamating company or demerged company, would have been entitled to carry forward and set off under the provisions of section 72 if the reorganisation of business or conversion or amalgamation or demerger had not taken place;

**“Unabsorbed depreciation”** means so much of the allowance for depreciation of the predecessor firm or the proprietary concern or the private company or unlisted public company before conversion into limited liability partnership or the amalgamating company or the demerged company, as the case may be, which remains to be allowed and which would have been allowed to the predecessor firm or the proprietary concern or the company or amalgamating company or demerged company, as the case may be, under the provisions of this Act, if the reorganisation of business or conversion or amalgamation or demerger had not taken place.

## **CARRY FORWARD AND SET OFF OF ACCUMULATED LOSS AND UNABSORBED DEPRECIATION ALLOWANCE IN SCHEME OF AMALGAMATION OF BANKING COMPANY IN CERTAIN CASES [SECTION 72AA]**

Section 72AA inserted by the Finance Act, 2005 provides for carry forward and set off of accumulated loss and unabsorbed depreciation allowance in scheme of amalgamation of banking companies.

Where there has been an amalgamation of a banking company with any other banking institution under a scheme sanctioned and brought into force by the Central Government under Sub-section (7) of Section 45 of the Banking Regulation Act, 1949, the accumulated loss and the unabsorbed depreciation of such banking company shall be deemed to be the loss or, as the case may be, allowance for depreciation of such banking institution for the previous year in which the scheme of amalgamation was brought into force and other provisions of this Act relating to set-off and carry forward of loss and allowance for depreciation shall apply accordingly.

The terms, “accumulated loss”, “banking company”, “banking institution” and “unabsorbed depreciation” for the purposes of this Section are defined as under:

- (i) **“accumulated loss”** means so much of the loss of the amalgamating banking company under the head “Profits and gains of business or profession” (not being a loss sustained in a speculation business) which such amalgamating banking company, would have been entitled to carry forward and set-off under the provisions of Section 72, if the amalgamation had not taken place.
- (ii) **“banking company”** shall have the same meaning assigned to it in Clause (c) of Section 5 of the Banking Regulation Act, 1949 (10 of 1949);
- (iii) **“banking institution”** shall have the same meaning assigned to it in Sub-section (15) of Section 45 of the Banking Regulation Act, 1949 (10 of 1949);
- (iv) **“unabsorbed depreciation”** means so much of the allowance for depreciation of the amalgamating banking company which remains to be allowed and which would have been allowed to such banking company if amalgamation had not taken place.

## **TREATMENT OF CARRY-FORWARD OF LOSSES OF CERTAIN ASSESSEES**

### **(1) Carry-forward and set-off of losses in case of change in constitution of firm [Section 78]**

Where a change has occurred in the constitution of a firm, the firm is not entitled to carry forward and set off so much of the loss proportionate to the share of a retired or deceased partner as exceeds his share of profits, if any, in the firm in respect of the previous year.

### **(2) Carry-forward and set-off of losses in case of succession of business or profession**

When a business or profession is succeeded by another person, the brought forward losses by the predecessor can be set-off against the income earned by the predecessor before the succession. The successor is not entitled to carry forward the losses sustained by the predecessor and set them off against the income earned by him. However, there is exception. If the succession is by inheritance, the heir-at-law is entitled to carry-forward and set-off the losses sustained by the predecessor provided the business in question continues to be carried on by the successor.

### **(3) Carry-forward and set-off of losses of companies in which the public are not substantially interested [Section 79]**

The losses of companies in which the public are not substantially interested can be carried forward and set-off only if the following condition is satisfied:

- (a) The shares of the company carrying not less than 51 per cent of the voting power were beneficially held

by the same persons on the last day of the year or years in which the loss was incurred and also on the last day of the previous year in which the brought forward loss is to be adjusted. Where a change in voting power of more than 51 per cent of share holding has occurred between the two dates mentioned above (i.e. last day of the year of occurrence of loss and the last day of the previous year in which the brought forward loss is to be adjusted), the assessee will not be entitled to the benefit of set-off.

However, the benefit of set-off will not be denied if the change in voting power is due to the death of a shareholder or on account of transfer of shares by way of gift to any relative of the shareholder making such gift.

The effect of this provision is that if the majority of the voting power is not in the same hands both on the last day of the previous year in which the loss was sustained by the closely-held company and on the last day of the previous year in which the set off is claimed, set off will not be allowed under Section 72. This is obviously to frustrate attempts at trafficking in losses.

It has been further provided by Finance Act, 1999 w.e.f. 1.4.2000 that benefit of set off will also not be denied in the case where any change in the shareholding of an Indian company which is a subsidiary of a foreign company as a result of amalgamation or demerger of a foreign company subject to the condition that fifty one per cent shareholders of the amalgamating or demerged foreign company continue.

It has further been provided by Finance Act, 2018 that benefit of carry forward and set off of losses shall not be denied to a closely held company seeking insolvency resolution, where a change in the shareholding takes place in a previous year pursuant to a resolution plan approved under the Insolvency and Bankruptcy Code, 2016, after affording a reasonable opportunity of being heard to the jurisdictional Principal Commissioner or Commissioner.

#### **(4) Carry forward and set of losses in case of eligible start-up [Section 79(b)]**

This section is applicable if following conditions are satisfied:

- a) The assessee is a company in which public are not substantially interested.
- b) It is an eligible start up referred u/s 80-IAC.
- c) Loss is incurred by the assessee company during the period of 7 years (starting from the year in which the company is incorporated).

If the above conditions are satisfied then brought forward loss can be set off against current year's income only if all the shareholders of the company (who held shares carrying voting power) on the last day of the previous year in which the loss was incurred, continue to hold shares on the last day of the current year.

**Exceptions :** The above mentioned restriction shall not be applicable in following cases:

- a) Where the change in the shareholding takes place due to death of a shareholder or any shareholder gifting his shares to his/her relative.
- b) Carry forward of unabsorbed Depreciation, unabsorbed capital expenditure on Scientific Research, unabsorbed capital expenditure by a company on promotion of family planning among its employees.
- c) If the assessee is a subsidiary of foreign company and the foreign holding company is amalgamated / merged with another foreign company (and the persons holding 51% or more shares in the amalgamating/ demerged company become the shareholders of the amalgamated/resulting foreign company).

### **SUBMISSION OF RETURN FOR LOSS [SECTION 80]**

An assessee is not entitled to carry-forward a loss unless he has filed a return of loss to the Department in time and in the prescribed form. It is obligatory on the part of the assessee to file such return, otherwise he will be deprived of the benefit of carry-forward of losses. In fact, only that amount of loss is allowed to be carried-forward which has been computed by the Assessing Officer and not by the assessee.

However losses under the head 'Income from House Property' and 'Unabsorbed depreciation' shall be carried forward even if the return of income is furnished after the due date as specified under section 139(1).

Section 80 of the Act provides that a loss which has not been determined in pursuance of return filed u/s 139(3) shall not be carried forward and set-off u/s 72(1), 73(2), 74(1), 74(3), 74A. Previously, it does not include Section 73A which provides that any loss, computed in respect of any specified business referred to in section 35AD.

Section 80 of the Act has been amended by Finance Act, 2016 to provide that the loss determined u/s 73A shall not be allowed to be carried forward and set off unless it is determined in pursuance of a return filed u/s 139(3).

These amendments effective retrospectively from 1st April, 2016 and accordingly apply in relation to the assessment year 2016-17 and subsequent years.

### SUMMARY OF PROVISIONS REGARDING CARRY FORWARD AND SET-OFF OF LOSSES

#### SET-OFF OF LOSSES [SECTIONS 70, 71]

Loss	Set-Off
1. Loss from house property.	(a) Income from any other house property (b) Any other head of income upto maximum of Rs. 2,00,000
2. Loss from business or profession	(a) Income from any other business or Profession. (b) Any other head of income except under the head "Salaries"
3. Loss from speculation	(a) Income from speculation
4. Short-term capital loss	(a) Short-term capital gain (b) Long-term capital gain
5. Long-term capital loss	(a) Long-term capital gain
6. Loss from activity of owning and maintaining race horses	(a) Income from activity of owing and maintaining race horses.

#### CARRY FORWARD AND SET-OFF OF LOSSES [SECTION 72]

Loss	Set-Off
1. Loss from house property.	In following eight years, income from house property.
2. Loss from business or profession	In following eight years, income from business or profession.
3. Loss from speculation	In following four years (w.e.f. A.Y. 2006-07), income from speculation.
4. Short-term capital loss	In following eight years : (a) Short-term capital gain (b) Long-term capital gain
5. Long-term capital loss	In following eight years, Long-term capital gain.
6. Loss from activity of owning and maintaining race horses	In following four years, Income from activity of owing and maintaining race horses

### LESSON ROUND UP

- Sections 60 to 65 of the Income-tax Act provide that in computing the total income of an individual for purposes of assessment, there shall be included all the items of income specified in these sections.
- **Transfer of Income (section 60)** : Where a person transfers to any other person income (whether revocable or not) from an asset without transferring that asset, the income shall be included in the total income of the transferor. “Transfer” includes any settlement, trust, covenant, agreement or arrangement.
- **Revocable transfer**: Where a person transfers any asset to any other person with a right to revoke the transfer, all income accruing to the transferee from the asset shall be included in the total income of the transferor.
- The income under revocable transfer of asset shall be included in the income of transferor even when only a part of income from transferred asset has been applied for the transferor.
- **Irrevocable Transfer**: In case of an irrevocable transfer of assets for a specified period, the income from such assets shall not be included in the income of transferor.
- **Income to spouse from a concern in which such individual has substantial interest [Section 64(1)(ii)]**: All such income as arises directly or indirectly, to the spouse of an individual by way of salary, commission, fees or any other remuneration, whether in cash or kind from a concern in which such individual has a substantial interest, shall be included in the income of the individual.
- **Income to spouse from the assets transferred [Section 64(1)(iv)]**: Where any individual transfers directly or indirectly any asset (other than a house property) to the spouse, the income from such asset shall be included in the income of the transferor.
- **Income to Son’s Wife [Section 64(1)(vi)]**: Where any individual transfers, directly or indirectly, any asset to his/her son’s wife without adequate consideration, the income from such asset shall be included in the income of the transferor.
- **Transfer for Immediate or Deferred Benefit of Son’s Wife [Section 64(1)(viii)]**: Any income arising, directly or indirectly, to any person or association of persons from assets transferred directly or indirectly after June 1, 1973, otherwise than for adequate consideration to the person or association of persons by such individual shall, to the extent to which the income from such assets is for the immediate or deferred benefit of his son’s wife be included in computing the total income of such individual.
- **Income to spouse through a third person [Section 64(1)(vii)]**: Where a person transfers some assets directly or indirectly to a person or association of persons (trustee or body of trustees or juristic person) without adequate consideration for the immediate or deferred benefit of his or her spouse, all such income as arises directly or indirectly from assets transferred shall be included in the income of the transferor.
- **Clubbing of Income of Minor Child [Section 64(1A)]**: All income which arises or accrues to the minor child (not being a minor child suffering from any disability of the nature specified in Section 80U) shall be clubbed in the income of his parent. However, any income which is derived by the minor from manual work or from any activity involving application of his skill, talent or specialised knowledge and experience will not be included in the income of his parent.

In case the income of an individual includes any income of his minor child in terms of this section [i.e. Section 64(1A)], such individual shall be entitled to exemption of the amount of such income or Rs. 1,500 whichever is less.

- **Income From The Converted Property [Section 64(2)]:** Where an individual, being a member of Hindu Undivided Family, transfers his self-acquired property after 31st December, 1969 to the family for the common benefit of the family, or throwing it into the common stock of the family, or transfers it directly or indirectly to the family otherwise than for adequate consideration, such property is known as converted property.
- **Dual Liability for Tax:** The tax on the income of the other person which has been included in the income of the assessee can either be recovered from the assessee or from the other person. The liability of other person is limited to the portion of the tax levied on the assessee which is attributable to the income so included.
- **Set Off - carry Forward of losses:** Sometimes the assessee incurs a loss from a source of income and unless such loss is set-off against any income, the net result of the assessee's activities during the particular accounting year cannot be ascertained and consequently the tax payable would also be incapable of determination. For this purpose, the Income-tax Act contains specific provisions (Sections 70 to 80) for the set-off and carry-forward of losses.
- **Set-Off of Losses from one source against Income from another source under the same Head of Income [Section 70]:** If the net result for any assessment year in respect of any source falling under any head of income is a loss, the assessee is entitled to set off the amount of such loss against his income from any other source under the same head. However, Loss from Speculation Business, Loss from the activity of owning and maintaining race horses, long-term capital loss can be set-off from any other source of income.
- Where any individual transfers directly or indirectly any asset (other than a house property) to the spouse, the income from such asset shall be included in the income of the transferor.
- **Carry-Forward and Set-Off of Losses** If it is not possible to set-off the losses during the same assessment year in which these occurred, so much of the loss as has not been so set-off out of the following losses, can be carried forward to the following assessment year and so on to be set-off against the income of those years provided the losses have been determined in pursuance of a return filed by the assessee and it is the same assessee who sustained the loss.

However, losses suffered under the following heads are not allowed to be carried forward and set off:

- (1) Losses under the head 'salaries'.
  - (2) Losses under the head 'Income from other sources' (excepting loss suffered from the activity of owning and maintaining race horses).
- W.e.f. assessment year 2000-2001, Section 72A has been substituted by new section to provide for carry forward and set off of accumulated loss and unabsorbed depreciation allowance in case of:
    - (i) amalgamation [Section 72A(1), (2) and (3)], or
    - (ii) demerger [Section 72A(4) and (5)], or
    - (iii) reorganisation of business [Section 72A(6)].
  - **Submission of Return for Loss (Section 80):** An assessee is not entitled to carry-forward a loss unless he has filed a return of loss to the Department in time and in the prescribed form. It is obligatory on the part of the assessee to file such return; otherwise he will be deprived of the benefit of carry-forward of losses. In fact, only that amount of loss is allowed to be carried-forward which has been computed by the Assessing Officer and not by the assessee.

### SELF TEST QUESTIONS

*These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation.*

#### Multiple Choice Questions "MCQs"

1. Income of a minor child from a Fixed Deposit with a bank, made out of income earned from scholarship, is to be?
  - a) Assessed in the hands of the minor child
  - b) Clubbed with the income of the parent whose total income before such clubbing is higher
  - c) Exempted from tax
  - d) Clubbed with father's income

Answer: (b)

2. Carried forward losses of normal business can be set-off against other income in subsequent assessment year except:
  - a) Income from speculation business
  - b) Income under the head house property
  - c) Income under the head other sources
  - d) Income under the head salaries

Answer: (d)

3. Transfer of income without transfer of asset would be taxable in the hands of:
  - a) Transferor only
  - b) Transferee only
  - c) Either transferor or transferee
  - d) Both transferor and transferee

Answer: (a)

4. The maximum period for which losses from speculative business can be carried forward:
  - a) 4 years
  - b) 8 years
  - c) Indefinitely
  - d) None of the above

Answer: (a)

5. Income of Minor Child, includible in the income of his/her parents income, deductible to the extent of such income does not exceeds \_\_\_\_\_ for each minor child:
  - a) Rs. 500
  - b) Rs. 1000
  - c) Rs. 1500
  - d) Rs. 2000

Answer: (c)





# Lesson 6

## Deductions from Gross Total Income, Rebate and Relief

### LESSON OUTLINE

- Introduction
- Deductions [Sections 80C to 80U]
- Relief and Rebate in respect of Income-tax
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

At the end of this lesson, you will learn

- The type of deductions allowable from gross total income
- What are the permissible deductions in respect of payments
- What are the permissible deductions in respect of incomes
- What are the deductions allowable in the case of a person with disability.
- Provision related to Rebate & Relief

*The aggregate of income computed under each head, after giving effect to the provisions for clubbing of income and set off of losses, is known as "Gross Total Income". Sections 80C to 80U of the Income-tax Act lay down the provisions relating to the deductions allowable to assesseees from their gross total income.*

## INTRODUCTION

The Income-tax Act provides various tax exemptions and deductions. The incomes which are exempt from tax, i.e. which are not included in total income are provided under Sections 10 to 13A. Chapter VI A contains deductions from gross total income under section 80C to 80U in respect of certain payments, investments, incomes and other deductions. Deduction helps in reducing the taxable income. It decreases the overall tax liabilities and helps to save tax. However, depending on the type of tax deduction claim, the amount of deduction varies.

The deductions are available only to the assessee where the gross total income is positive. If however, the gross total income is nil or negative, the question of any deduction from the gross total income does not arise. For this purpose, the expression 'gross total income' means the total income of the assessee computed in accordance with the provisions of the Income-Tax Act, before making any deduction under Chapter VI A, i.e., the aggregate income computed under each head, after giving effect to the provisions for clubbing of income and set off of losses, is known as "Gross Total Income". Sections 80C to 80U of the Income-tax Act lay down the provisions relating to the deductions allowable to assessee from their gross total income. The income arising after deduction under section 80C to 80U is called Total Income.

### Summary of Deductions under Chapter VI-A

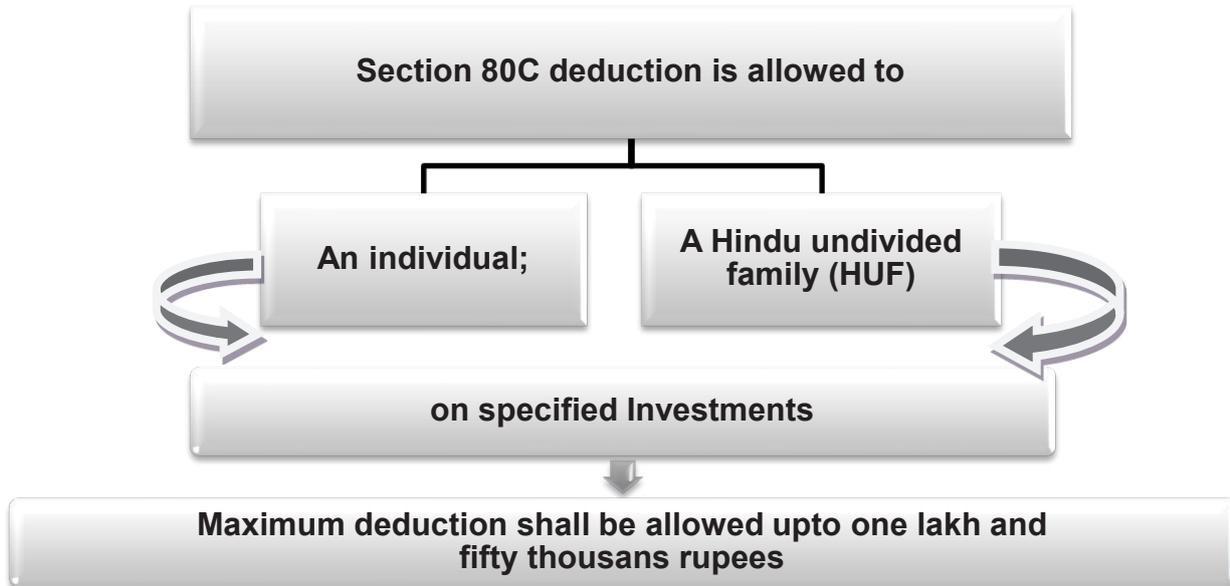
Section	Nature of deduction	Who can claim
(1)	(2)	(3)
<b>80C</b>	<ul style="list-style-type: none"> <li>● Life insurance premium</li> <li>● Sum paid towards notified annuity plan of LIC or other insurer, a contract for a deferred annuity</li> <li>● Contributions towards Employees' Provident Fund Scheme, Public Provident Fund Account, a recognised provident fund, an approved superannuation fund, notified unit-linked insurance plan of LIC Mutual Fund, participation in unit-linked Insurance Plan of UTI, any pension fund set up by any mutual fund which is referred to in section 10(23D) or by the UTI</li> <li>● Subscription to any notified security, notified deposit scheme of the Central Government, notified savings certificates, notified pension fund set up by National Housing Bank</li> <li>● Tuition fees paid by an individual to any university, college, school or other educational institution situated in India, for full time education of any 2 of his/her children</li> <li>● Certain payments for purchase/construction of residential house property</li> <li>● Subscription to notified schemes of (a) public sector companies engaged in providing long-term finance for purchase/construction of houses in India for residential purposes/(b) authority constituted under any law for satisfying need for housing accommodation or for planning, development or improvement of cities, towns and villages, or for both</li> <li>● Subscription to equity shares or debentures forming part of any approved eligible issue of capital made by a public company or public financial institutions, any units of any approved mutual fund referred to in section 10(23D), notified bonds issued by the NABARD.</li> <li>● Term deposits for a fixed period of not less than 5 years with a scheduled bank or post office</li> <li>● Deposit in an account under the Senior Citizen Savings Scheme Rules, 2004</li> </ul>	Individual/HUF
<b>80CCC</b>	<ul style="list-style-type: none"> <li>● Contributions to certain pension funds of LIC or any other insurer (up to Rs. 1,50,000)</li> </ul>	Individual

<b>80CCD</b>	<ul style="list-style-type: none"> <li>● Contribution to pension scheme notified by Central Government up to 10% of salary.</li> <li>● Contribution made by employer shall also be allowed as deduction under section 80CCD(2) while computing total income of the employee. However, amount of deduction could not exceed 10% of salary of the employee</li> </ul> <p><i>Note:</i> The maximum limit of Rs. 1,50,000 is the aggregate of the deduction that may be claimed under sections 80C, 80CCC and 80CCD. However, additional deduction of maximum Rs. 50,000 be allowed under section 80CCD(1b) over and above the limit of Rs. 1,50,000.</p>	
<b>80CCG</b>	50 per cent of amount invested by specified resident individuals in notified equity savings scheme (subject to certain conditions and limits) (maximum deduction : Rs. 25,000)	Specified resident individuals (new retail investors)
<b>80D</b>	<p>Amount paid (in any mode other than cash) by an individual or HUF to LIC or other insurer to effect or keep in force an insurance on the health of specified person.</p> <p>Payment towards health scheme and/or on account of preventive health check-up</p>	Individual/HUF
<b>80DD</b>	Deduction of Rs. 75,000 (Rs. 1,25,000 in case of severe disability) to a resident individual/HUF where (a) any expenditure has been incurred for the medical treatment (including nursing), training and rehabilitation of a dependant, being a person with disability, or (b) any amount is paid or deposited under an approved scheme framed in this behalf by the LIC or any other insurer or the Administrator or the specified company for the maintenance of a dependent, being a person with disability	Resident Individual/HUF
<b>80DDB</b>	Expenses actually paid for medical treatment of specified diseases and ailments subject to certain conditions	Resident Individual/HUF
<b>80E</b>	Interest on loan taken from financial institution/approved charitable institution for pursuing higher education	Individual
<b>80EE</b>	Interest payable on loan taken from any financial institution for the purpose of acquisition of a residential house property	Individual
<b>80EEA</b>	Tax incentives for affordable housing	All assessees
<b>80EEB</b>	Tax incentives for electric vehicles	All assessees
<b>80G</b>	Donations to certain approved funds, trusts, charitable institutions/ donations for renovation or repairs of notified temples, etc.	All assessees
<b>80GG</b>	Rent paid in excess of 10% of total income for furnished/unfurnished residential accommodation (subject to maximum of Rs. 5,000 p.m. or 25% of total income, whichever is less)	Individuals not receiving any house rent allowance
<b>80GGA</b>	Certain donations for scientific, social or statistical research or rural development programme or for carrying out an eligible project or scheme or National Urban Poverty Eradication Fund	All assessees not having any income chargeable under the head 'Profits and gains of business or profession'
<b>80GGB</b>	Sum contributed to any political party/electoral trust	Indian company
<b>80GGC</b>	Sum contributed to any political party/electoral trust	All assessees, other than local authority and artificial juridical person wholly or partly funded by Government
<b>For certain incomes</b>		
<b>80-IA</b>	Profits and gains from industrial undertakings engaged in infrastructure facility, telecommunication services, industrial park, development of Special Economic Zone, power undertakings, etc.	All assessees

<b>80-IAB</b>	Profits and gains derived by undertaking/enterprise from business of developing a Special Economic Zone notified on or after 1-4-2005	Assessee being Developer of SEZ
<b>80-IB</b>	Profits and gains from industrial undertakings, cold storage plant, hotel, scientific research & development, mineral oil concern, housing projects, cold chain facility, multiplex theatres, convention centres, ships, etc.	All assesses
<b>80-IC</b>	Profits and gains derived by an undertaking or an enterprise in special category States (Himachal Pradesh, Uttaranchal, Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland and Tripura)	All assesses
<b>80IAC</b>	Deduction in respect of eligible Start-Up	All assesses
<b>80IBA</b>	Deductions in respect of profits and gains from Housing Projects	All assesses
<b>80IC</b>	Special provisions in respect of certain undertakings or enterprises in certain special category States	All assesses
<b>80-ID</b>	Profits and gains from business of hotels and convention centres in specified areas	All assesses
<b>80-IE</b>	Deduction in respect of certain undertakings in North Eastern States.	All assesses
<b>80JJA</b>	Entire income from business of collecting and processing or treating of bio-degradable waste for generating power, or producing bio-fertilizers, bio-pesticides or other biological agents or for producing bio-gas, making pellets or briquettes for fuel or organic manure	All assesses
<b>80JJAA</b>	Additional wages paid to new regular workmen employed in the previous year for 3 assessment years	Indian company having profits and gains derived from manufacture of goods in a factory
<b>80LA</b>	Certain incomes of Scheduled banks/banks incorporated outside India	Scheduled banks/banks incorporated outside India having Offshore Banking Units in a Special Economic Zone/ Units of International Financial Services Centre
<b>80P</b>	Specified incomes	Co-operative societies
<b>80PA</b>	Specified incomes	Producer Company
<b>80QQB</b>	Royalty income of author of certain specified category of books (up to Rs. 3,00,000)	Resident Individual - Author
<b>80RRB</b>	Royalty on patents up to Rs. 3,00,000	Resident individuals who is a patentee and is in receipt of income by way of royalty in respect of a patent registered on or after 1-4-2003
<b>80TTA</b>	Interest on deposits in savings bank accounts (up to Rs. 10,000 per year)	Individuals/HUFs
<b>80TTB</b>	Interest on deposits in case of senior citizens upto Rs. 50,000	Senior Citizen Individuals
<b>80U</b>	Deduction of Rs. 75,000, in the case of a person with severe disability, allowable deduction is Rs. 1,25,000	Resident individuals who, at any time during the previous year, is certified by the medical authority to be a person with disability
<b>Rebates</b>		
<b>87A</b>	Rebate of Rs. 12,500 or the income tax whichever is less	Resident individual whose total income does not exceed five lakh rupees

**DEDUCTIONS****Deduction in respect of investments [Section 80C]**

Section 80C provides deduction to (a) an individual; (b) a Hindu undivided family for investments made in specified assets subject to a maximum amount of one lakh and fifty thousand rupees.



The specified Investments include:

- a) Premium paid on life Insurance policy taken on the life of an individual assessee or spouse and any child of such individual, and any member of the Hindu Undivided Family subject to a maximum of 10% of the actual sum assured, if insurance policy is taken on or after 1.04.2012. But if, insurance policy is taken on or before 31.03.2012, then maximum limit is 20% of actual sum assured. Further, if insurance policy is taken on or after 01.04.2013 and the policy is on the life of a person with disability or severe disability mentioned in Section 80U or a person suffering from a disease or ailment mentioned in Section 80DDB, then 15% of actual sum assured.

*“actual sum assured” in relation to a life insurance policy shall mean the minimum amount assured under the policy on happening of the insured event at any time during the term of the policy, not taking into account –*

1. the value of any premium agreed to be returned; or
  2. any benefit by way of bonus or otherwise over and above the sum actually assured, which is to be or may be received under the policy by any person.
- b) Amounts paid to effect or to keep in force a contract for a non-cumulative deferred annuity not being an annuity plan referred to in clause (j) below on the life of: (i) in the case of an individual, the individual, spouse or any child of such individual and

However, such contract should not contain a provision for exercise of an option by the insured to receive cash payment in lieu of the payment of the annuity.

- c) Deduction from the salary payable by or on behalf of the Government to any individual, in accordance with the conditions of his service, for securing to him a deferred annuity or making provision for his wife or children, to the extent of one-fifth of salary.

314 EP-TL

- d) Contribution made by an individual to a Recognised provident fund; an approved superannuation fund; public provident fund; a ten-year account or a fifteen-year account under the Post Office Savings Bank (Cumulative Time Deposits) Rules, 1959
- e) Purchase of notified securities or deposit scheme of the Central Government. Sukanya Samridhi Account Scheme has been notified.
- f) Subscription to other notified savings certificates defined in Section 2(c) of the Government Savings Certificates Act, 1959 [For this clause, National Savings Certificates (VIII & IX) issue has been notified] and interest accrued deemed to be reinvested also qualifies.
- g) Contributions made by an individual or HUF, for participation in the Unit-Linked Insurance Plan, 1971, deemed to have been made under Section 19(8)(a) of the Unit Trust of India Act, 1963. [For this clause, Dhanaraksha-1989 plan of LIC Mutual Fund has been notified].
- h) Contributions made in the name of an individual or HUF for participation in any notified Unit-Linked Insurance Plan of the LIC Mutual Fund.
- i) Any contribution to effect or keep in force any notified annuity plan of the LIC or any other insurer.
- j) Any subscription, to any units of any Mutual Fund or the Unit Trust of India under any notified plan formulated by the Central Government.
- k) Any contribution to any pension fund set up by any Mutual Fund as notified by the Central Government.
- l) Subscription to the notified deposit scheme of or contribution to any such pension fund set up by the National Housing Bank established under Section 3 of the National Housing Bank Act, 1987. [For this clause, Home Loan Account Scheme of National Housing Bank has been notified].
- m) Subscription paid towards scheme of :-
  - 1) Public sector company engaged in providing long term finance for purchase or construction of houses in India (public deposit scheme of HUDCO)
  - 2) Housing board constituted in India for planning, development or improvement of cities or towns
- n) Only tuition fees (excluding any payment towards any development fees or donation or payment of similar nature), whether at the time of admission or thereafter, - (for full time education of any 2 children) to any university, college, school or other educational institution situated within India;
- o) For purchase or construction of a residential house property, the income of which is chargeable to tax under the head "Income from House Property", where such payments are made towards or by way of:
  - i. any installment or part payment of the amount due towards the cost of the house property allotted or construction and sale of house property on ownership basis; or
  - ii. E-payment of any loan taken for the purpose of purchase or construction of residential house property subject to some conditions.
- p) Subscription to equity shares or debentures or units forming part of any eligible issue of capital i.e. issue made by a company registered in India or a public financial institution or an approved mutual fund for the purpose of developing, maintaining and operating an infrastructure facility as defined in the explanation to Sub-section (4) of Section 80-IA or for generation, or for generation and distribution of power or for providing telecommunication services whether basic or cellular.
- q) Fixed deposits for a minimum period of 5 years in any Scheduled Banks

- r) As subscription to such bonds issued by the National Bank for Agriculture and Rural Development, as the Central Government may, by notification in the Official Gazette specify in this behalf.
- s) Amount deposited in an account under the Senior Citizens Savings Scheme Rules, 2004.
- t) As five year time deposit in an account under the Post Office Time Deposit Rules, 1981.
- u) Contribution made by a Central Govt. employee to his Tier-II NPS account for a fixed period not less than 3 years. (w.e.f. Assessment Year 20-21)

#### **Deduction for Contribution to Pension Fund [Section 80CCC]**

Section 80CCC provides deduction with respect to amount deposited by an individual out of his taxable income to any annuity plan of the Life Insurance Corporation of India or any insurer approved by the IRDAI for receiving pension subject to a maximum of Rs. 1,50,000.

No deduction for this contribution will be available u/s 80C. The pension received by the assessee or his nominee is taxable in the year of receipt.

If the assessee or his nominee surrenders the annuity before its maturity, then surrender value including bonus/interest is taxable in the year of receipt.

#### **Deduction in respect of Contribution to Pension Scheme of Central Government [Section 80CCD]**

Section 80CCD provides deduction with respect to employers and employees contribution to pension scheme which is applicable to new employees of the Central Government employed on or after 01.01.2004 or being an individual employed by any other employer. It is mandatory for such employee to contribute 10% of salary every month towards the pension scheme. A 10% contribution is required to be made by the employer also. [ 14% in case where employer is Central Govt. as approved by Union cabinet meeting on 6/12/2018 ]

As per section 80CCD (1), employees contribution towards the notified pension scheme is deductible, but upto maximum of 10% of the salary of employee. As per section 80CCD (1B), an additional deduction of maximum Rs. 50,000 can also be availed. This deduction is out of the focus of section 80CCE. As per section 80CCD(2) if the employer contributes towards the notified pension scheme, then deduction can be claimed but upto maximum of 10 % of the salary of employee (14% in case where employer is Central Govt. w.e.f. Assessment Year 20-21). This deduction is out of the focus of section 80CCE.

Salary here means basic salary plus dearness allowance (forming part) plus commission at a fixed percentage of turnover achieved by the employee. Self-employed individuals can also contribute to NPS and in such a case, maximum limit of deduction is 20% of his gross total income. Any amount received from pension fund, shall be taxable as income of the recipient (assessee or his nominee) in the year in which such amount is received.

#### **Limit on Deductions under sections 80C, 80CCC and 80CCD [Section 80CCE]**

The aggregate amount of deductions under Sections 80C, 80CCC and 80CCD (1) shall not in any case, exceed Rs. 1,50,000. As per section 80CCD (1B), an additional deduction of maximum Rs. 50,000 can also be availed. This deduction is out of the focus of section 80CCE.

#### **Deduction in respect of Medical Insurance Premia [Section 80D]**

Section 80D provides deduction to an individual or a Hindu undivided family towards medical insurance premium and preventive health check-up or contribution to Central Government Health Scheme (CGHS) or any scheme notified by the Central Government on the health of the assessee, his family, parents or members of the HUF.

Where the assessee is an individual, the deduction under this section shall be the aggregate of the following:

- (a) the whole of the amount paid to effect or to keep in force an insurance on the health of the assessee or his family or "any contribution made to the Central Government Health Scheme" or such other scheme as may be notified by the Central Government in this behalf or any payment made on account of preventive health check-up of the assessee or his family and the sum does not exceed in the aggregate Rs. 25,000; and
- (b) the whole of the amount paid to effect or to keep in force an insurance on the health of the parent or parents of the assessee or any payment made on account of preventive health check-up of the assessee or his family as does not exceed in the aggregate Rs. 25,000.
- (c) the whole of the amount paid on account of medical expenditure incurred on the health of the assessee or any member of his family as does not exceed in the aggregate Rs. 50,000.
- (d) the whole of the amount paid on account of medical expenditure incurred on the health of any parent of the assessee, as does not exceed in the aggregate Rs. 50,000.

Provided that amount referred in (c) and (d) is paid in respect of a senior citizen and no amount has been paid to effect or to keep in force an Insurance on the health of such person;

Provided further that aggregate of amount specified under (a) and (c) or aggregate of sum specified under (b) and (d) shall not exceed Rs. 50,000.

**Explanation :** family means the spouse and dependent children of the assessee.

*Payment shall be made by any mode, including cash, in respect of any sum paid on account of preventive health check-up and by any mode other than cash in all cases other than preventive health check up.*

Where the assessee is a Hindu undivided family, the deduction under this section, shall be aggregate of the following namely:

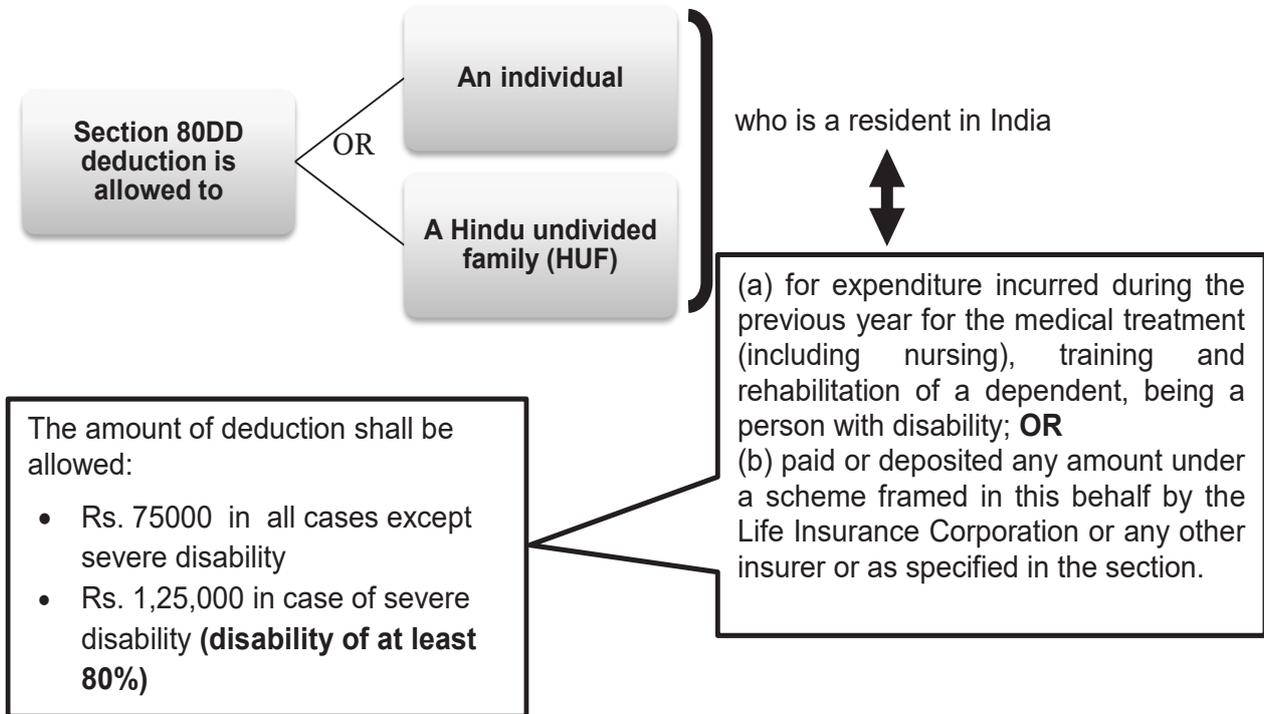
- (a) whole of the amount paid to effect or to keep in force an insurance on the health of any member of that Hindu undivided Family as does not exceed in the aggregate Rs. 25,000
- (b) whole of the amount paid on account of medical expenditure incurred on the health of any senior citizen member of the Hindu undivided family as does not exceed in the aggregate Rs. 50,000 and no amount has been paid to effect or to keep in force and insurance on the health of such a person:

Provided that the aggregate of the sum specified under the clause (a) and clause (b) shall not exceed Rs. 50,000

**Explanation:** For the purposes of this section,

1. Senior citizen means an individual resident in India who is of the age of sixty years or more at any time during the relevant previous year.
2. Where the amount of health insurance premium in above cases has been paid in lump sum for more than one previous year then deduction shall be allowed for each relevant previous year. Amount of deduction for each previous year shall be calculated by dividing lump sum premium amount by number of relevant previous years.

### Deduction in respect of maintenance including medical treatment of a dependent who is a person with disability [Section 80DD]



The deduction under clause (b) shall be allowed only if the following conditions are fulfilled, namely: -

- the scheme provides for payment of annuity or lump sum amount for the benefit of a dependent, being a person with disability, in the event of the death of the individual or the member of the Hindu undivided family in whose name subscription to the scheme has been made;
- the assessee nominates either the dependent, being a person with disability, or any other person or a trust to receive the payment on his behalf, for the benefit of the dependent, being a person with disability.

If the dependent, being a person with disability, predeceases the individual or the member of the Hindu undivided family, an amount equal to the amount paid or deposited under Clause (b) shall be deemed to be the income of the assessee of the previous year in which such amount is received by the assessee and shall accordingly be chargeable to tax as the income of that previous year.

The assessee, claiming a deduction under this section, shall furnish a copy of the certificate issued by the medical authority in the prescribed form and manner, along with the return of income under Section 139, in respect of the assessment year for which the deduction is claimed:

*For the purpose of this section*

- “dependent”** means -
  - in the case of an individual, the spouse, children, parents, brothers and sisters of the individual or any of them;
  - in the case of a Hindu undivided family, a member of the Hindu undivided family, dependent wholly or mainly on such individual or Hindu undivided family for his support and maintenance,

and who has not claimed any deduction under Section 80U in computing his total income for the assessment year relating to the previous year;

- (b) “**disability**” shall have the meaning assigned to it in clause (i) of Section 2 of the Persons with Disabilities (Equal Opportunities, Protection of Rights and Full Participation) Act, 1995 (1 of 1996);

### **Deduction in respect of medical treatment of certain specified disease or ailment [Section 80DDB]**

Section 80DDB provides deduction to an individual or a Hindu undivided family, who is a resident in India for amount actually paid during the previous year, for the medical treatment of such disease or ailment as may be specified in the rules made in this behalf by the Board -

- (a) for himself or a dependent, in case the assessee is an individual; or  
 (b) for any member of a Hindu undivided family, in case the assessee is a Hindu undivided family,

subject to a maximum of Rs. 40,000 (in case of senior citizen Rs. 1,00,000)

*Deduction is allowed only when a certificate in Form No. 10-I (issued by neurologist, oncologist, urologist, hematologist, immunologist or any such specialist as may be specified working in a Government Hospital) is furnished. Concept of very super senior citizen abolished by Finance Act, 2018.*

Provided further that the deduction under this section shall be reduced by the amount received, if any, under an insurance from an insurer, or reimbursed by an employer, for the medical treatment of the person referred to in Clause (a) or Clause (b).

For the purposes of this section, “**dependent**” means –

- (a) in the case of an individual, the spouse, children, parents, brothers and sisters of the individual, dependant wholly or mainly on such individual for support and maintenance;  
 (b) in the case of a Hindu undivided family, any member of the Hindu undivided family, dependant wholly or mainly on Hindu undivided family for support and maintenance;

#### **Illustration 1:**

X a resident individual incurs Rs. 30,000 expenditure on his own treatment of a specified disease and Rs. 15,000 on medical treatment of his wife in a Government hospital. Rs. 2,000 is reimbursed by insurance company for his wife and Rs. 5,000 are reimbursed by his employer for him. Compute the amount of deduction under section 80DDB?

**Solution :** The amount of deduction under section 80DDB shall be lower of 1 and 2 below less amount recovered from insurance company and employer.

$$1. \quad 30,000 + 15,000 = 45,000$$

$$2. \quad 40,000$$

$$\text{Rs. } 40,000 \text{ less } (2,000+5,000) = 33,000$$

Hence, Rs. 33, 000 is the amount of deduction under section 80 DDB.

#### **Illustration 2:**

1. If X, an individual incurs Rs. 1,80,000 expenditure on medical treatment of a specified disease for his mother (65 years) in a hospital recognised by Chief Commissioner and Rs. 8,000 are reimbursed by insurance company, what will be the amount of deduction available to him under section 80DDB?

- (a) **Rs. 92,000**
- (b) Rs. 72,000
- (c) Rs. 1,80,000
- (d) Any amount

2. If X, an individual incurs Rs. 1,80,000 expenditure on medical treatment of a specified disease for his grand mother (85 years) in a hospital recognised by Chief Commissioner and Rs. 8,000 are reimbursed by insurance company, what will be the amount of deduction available to him under section 80DDB?

- (a) Rs. 60,000
- (b) Rs. 1,80,000
- (c) **Rs. 92,000**
- (d) NIL

### Deduction in respect of repayment of loan taken for Higher Education [Section 80E]

Section 80E provides deduction to an individual for amount actually paid during the previous year out of his income chargeable to tax by way of an interest on loan, taken by him from any financial institution or any approved charitable institution for the purpose of pursuing higher education of self or any of the relative (i.e. spouse, children of the assessee or student for whom the individual is the legal guardian). The deduction will be available in computing the total income in respect of initial assessment year and the seven assessment years immediately succeeding the initial assessment year or until the interest thereon is paid by such individual in full, whichever is earlier. The expression "initial assessment year" means the assessment year relevant to the previous year, in which the assessee starts paying the interest on the loan.

For the purposes of this section, the expression "higher education" is being defined to mean any course of study pursued after passing the Senior Secondary Examination or its equivalent from any school, board or university recognised by the Central Government or State Government or local authority or by any other authority authorised by the Central Government or State Government or local authority to do so. Higher education should be in India only.

The expression "financial institution" is being defined to mean a banking company to which the "Banking Regulation Act, 1949 applies (including any bank or banking institution referred to in Section 51 of the Act) or any other financial institution which the Central Government may, by notification in the Official Gazette, specify in this behalf.

The expression "approved charitable institution" is being defined to mean an institution specified in, or as the case may be, an institution established for charitable purposes and notified by the Central Government under Section 10(23C) or an institution referred to in Section 80G(2)(a).

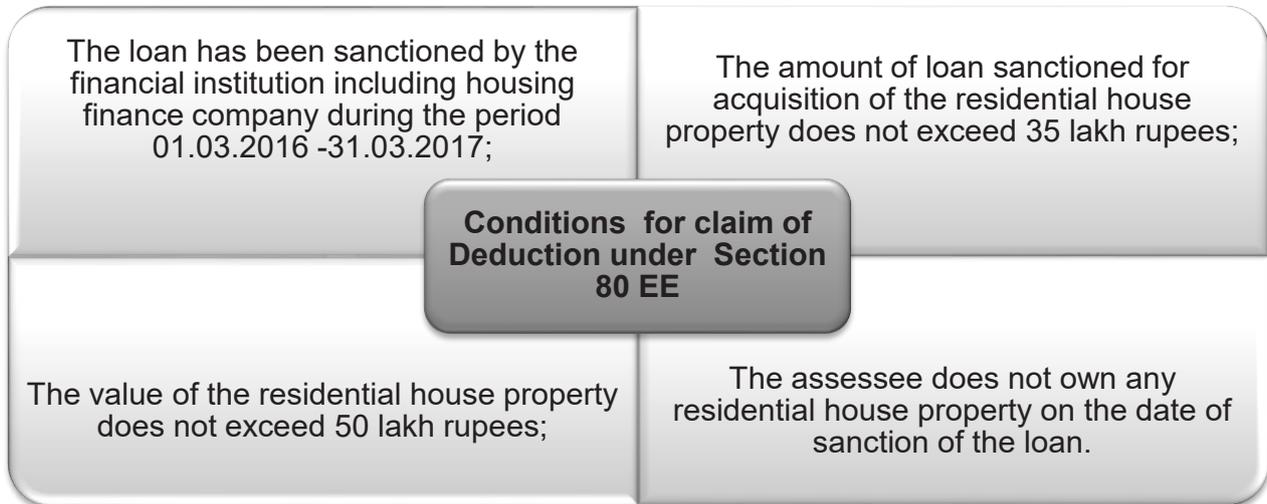
### Illustration

What is the upper limit of deduction (including interest) on loan, taken by an individual from any financial institution or any approved charitable institution for the purpose of pursuing his/her higher education?

- (a) Rs. 30,000
- (b) Rs. 40,000
- (c) Rs. 50,000
- (d) **Any amount**

**Deduction in respect of interest on loan taken for Residential House Property [section 80EE]**

Section 80EE provides deduction to an individual for interest payable on loan taken by him from any financial institution for the purpose of acquisition of a residential house property for the assessment year beginning on 1st day of April, 2017 and subsequent assessment year, subject to maximum of Rs. 50,000.



Where a deduction under this section is allowed for any interest, deduction shall not be allowed in respect of such interest under any other provisions of the Act for the same or any other assessment year. Therefore, this deduction is other than the deduction u/s 24(b) under the head "Income from house property". If in case, the amount of interest exceeds Rs. 50,000 then the individual can claim the balance deduction u/s 24(b), if relevant conditions are satisfied.

For the purposes of this section,

- a) "financial institution" means a banking company to which the Banking Regulation Act, 1949 (10 of 1949) applies including any bank or banking institution referred to in section 51 of that Act or a housing finance company;
- b) "housing finance company" means a public company formed or registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes.

**Illustration**

Find out the amount of deduction under Section 80 EE for the assessment year 2020-21 where an individual has applied for a loan for acquisition of house property on March 15, 2018 for Rs. 50 lakh and the loan is sanctioned on May 10, 2018 for Rs. 40 lakh only. He does not own any other residential house property and pays interest of Rs. 70,000 for previous year 2019-20.

- (a) 70,000
- (b) 50,000
- (c) **NIL**
- (d) 40,000

In the above case can he claim any deduction under section 24? What amount?

- (a) Yes (Rs. 50,000)

- (b) No
- (c) Yes (Rs. 20,000)
- (d) Yes (Rs. 70,000)

### Tax incentives for affordable housing [Section 80EEA]

New Section 80EEA of the Income Tax Act, 1961 has been introduced vide Finance Act, 2019 as per which an Additional tax deduction up to 1.5 Lakh is available for interest paid on loans taken up to 31st March 2020. It is an additional benefit on the top of 2 Lakh benefit extended by section 24. The maximum tax deduction on interest amount paid for home loan will be 3.5 Lakhs i.e. 2 Lakh under section 24 and 1.5 Lakh under section 80EEA. The deduction will be available on loans taken up to 31st March 2020. The benefit will be given only on the interest component of the home loan.

### Eligibility conditions for claiming a deduction

- This benefit will be extended only to the first time homeowner i.e. the assessee should not be owner of any other house at the time of sanction to avail this benefit.
- The stamp duty value of a home should be 45 Lakhs or less.
- The deduction under this scheme is available only to the individuals. HUF, company or any other kind of taxpayer cannot claim benefit under this section.
- In order to claim this benefit the property should be self-occupied and affordable.
- To claim this benefit, the individual must have taken the loan from the financial institution or bank. The loan sanction should be between 1st April, 2019 to 31st March, 2020.
- This tax deduction can be claimed for by individual as well as joint home loan borrower. The joint home loan borrower can individually claim this benefit.
- The above benefit is not applicable for the commercial properties.

Maximum Tax Deduction benefit on Home Loan Interest = 2 Lakh (Section 24) + 1.5 Lakh (Section 80EEA)

*Example* : Rakesh works in pune in IT Company. He lives in pune in a rented house. He purchased property in Surat. His father and family members live in a newly purchased house. He is buying a home for the first time, so he can take benefit of section 80EEA. The cost of a home is 45 Lakh and. He purchased this home by taking a home loan of 40 Lakh in May 2019.

The monthly EMI of this property is Rs.37000. The total of EMI for FY2019-20 will be 4.07 Lakh. This includes principal payment of 0.3 Lakh and 3.77 Lakh of interest component.

As it is self occupied house and fulfilling condition of section 80EEA, Rakesh can claim 3.5 Lakh as tax deduction while filing Income tax return.

### Tax incentives for electric vehicles [Section 80EEB]

In computing the total income of an assessee, being an individual, there shall be deducted, in accordance with and subject to the provisions of this section, interest payable on loan taken by him from any financial institution for the purpose of purchase of an electric vehicle.

The deduction under sub-section (1) shall not exceed one lakh and fifty thousand rupees and shall be allowed in computing the total income of the individual for the assessment year beginning on the 1st day of April, 2020 and subsequent assessment years.

The deduction under sub-section (1) shall be subject to the condition that the loan has been sanctioned by

the financial institution during the period beginning on the 1st day of April, 2019 and ending on the 31st day of March, 2023.

Where a deduction under this section is allowed for any interest referred to in sub-section (1), deduction shall not be allowed in respect of such interest under any other provision of this Act for the same or any other assessment year.

For the purposes of this section, –

- (a) “electric vehicle” means a vehicle which is powered exclusively by an electric motor whose traction energy is supplied exclusively by traction battery installed in the vehicle and has such electric regenerative braking system, which during braking provides for the conversion of vehicle kinetic energy into electrical energy;
- (b) “financial institution” means a banking company to which the Banking Regulation Act, 1949 applies, or any bank or banking institution referred to in section 51 of that Act and includes any deposit taking non-banking financial company or a systemically important non-deposit taking non-banking financial company as defined in clauses (e) and (g) of Explanation 4 to section 43B.’

### **Deduction in respect of donations to certain funds, charitable institutions, etc. [Section 80G]**

Section 80G provides deduction to all assessee’s for donations to specified organizations or institutions or funds. However, any donation of any sum exceeding Rs. 2,000 shall not be allowed as deduction under the section unless such sum is paid by any mode other than cash. Further, where an assessee has claimed and has been allowed any deduction under this section in respect of any amount of donation, the same amount will not again qualify for deduction under any other provision of the Act for the same or any other assessment year. Donations in kind is not eligible as per the Supreme Court Ruling (*Vijaipat Singhania v. CIT*).

The quantum of deduction under this section is the aggregate of deduction permissible under clauses (A), (B), (C) & (D) mentioned below. Together for (C) and (D) below, there is a qualifying limit which is 10% of adjusted Gross Total Income.

Adjusted Gross total income means the “Gross Total Income” as reduced by:

- I. Long-term Capital gains, if any which have been included in the “Gross Total Income”.
- II. All deductions permissible under Sections 80C to 80U excepting deduction under Section 80G.
- III. Exempted Income.
- IV. Income of NRIs and Foreign Companies under Sections 115A, 115AB, 115AC, 115ACA or 115AD.

#### **(A) 100% Deduction without any qualifying limit:**

- (i) National Defense fund.
- (ii) Prime Minister’s National relief fund.
- (iii) Prime Minister’s Earthquake relief fund.
- (iv) Africa fund.
- (v) National Trust for welfare of persons with autism, cerebral palsy, mental retardation and multiple disabilities.
- (vi) National cultural fund set up by the Central Government.
- (vii) The Chief Minister’s relief fund or the lieutenant Governor’s relief fund.
- (viii) National Illness Assistance fund.

- (ix) The Andhra Pradesh Chief Minister's Cyclone Relief Fund, 1996.
- (x) The Army/Air force Central welfare fund or the Indian Naval Benevolent fund.
- (xi) Any fund set up by a State Government to provide medical relief to poors.
- (xii) The National/State Blood transfusion Council.
- (xiii) Zila Saksharta Samiti constituted in any district.
- (xiv) Any fund set up by the State Government of Gujarat, exclusively for providing relief to the victims of earthquake in Gujarat.
- (xv) Maharashtra Chief Minister's Earthquake Relief Fund.
- (xvi) University/Educational Institute of National Eminence approved by the prescribed authority.
- (xvii) National foundation for communal harmony.
- (xviii) Fund for technology development and application, set up by the Central Government.
- (xix) National sports fund set up by the Central Government.
- (xx) National Children's Fund.
- (xxi) the Swachh Bharat Kosh, set up by the Central Government, other than the sum spent by the assessee in pursuance of Corporate Social Responsibility under sub-section (5) of section 135 of the Companies Act, 2013 (18 of 2013);
- (xxii) the Clean Ganga Fund, set up by the Central Government, whereas such assessee is a resident and such sum is other than the sum spent by the assessee in pursuance of Corporate Social Responsibility under sub-section (5) of section 135 of the Companies Act, 2013
- (xxiii) the National Fund for Control of Drug Abuse constituted under section 7A of the Narcotic Drugs and Psychotropic Substances Act, 1985 (61 of 1985);

**(B) 50% Deduction without any qualifying limit:**

- (i) Jawaharlal Nehru Memorial Fund.
- (ii) Indira Gandhi Memorial Trust.
- (iii) Rajiv Gandhi Foundation.
- (iv) Prime Minister's Drought Relief Fund.

**(C) 100% Deduction subject to qualifying limit:**

- (i) Any sum to Government or any approved local authority, institution or association to be utilized for promoting family planning.
- (ii) Any sum paid by the assessee, being a company, in the previous year as donation to Indian Olympic Association or to any other association established in India and notified by the Central Government for:
  - I. Development of infrastructure for sports and games or
  - II. Sponsorship of sports and games in India.

**(D) 50% Deduction subject to qualifying limit:**

- (i) Donation to Government or any approved Local Authority, Institution or Association to be utilized for any Charitable purpose other than promoting family planning.

**324 EP-TL**

- (ii) Any other Fund or Institution, which satisfies the conditions of Section 80G(5).
- (iii) Notified Temple, Mosque, Gurudwara, Church or any other place notified by the Central Government to be of historic, as chorological or artistic importance, for renovation or repair of such place.
- (iv) Any corporation established by the Central or State Government specified under Section 10(26BB) for promoting interests of the members of a minority community.
- (v) Any authority constituted in India by or under any law for satisfying the need for housing accommodation or for the purpose of planning development or improvement of cities, towns and villages or for both.

**Illustration**

If Mr. 'A' had income against the following heads,

Taxable salary income	40,000
Income from house property	75,000
Income from other sources	20,000
Interest on securities of DCM Ltd. (Gross)	8,000
	1,43,000

He made following payments:

Contribution to P.F. (recognised)	2,000
Donation to the Prime Minister's National Relief Fund	2,500
Donation to the Indira Gandhi Memorial Trust	4,000
Donation to an approved association for promoting family planning	4,000
Donation to approved charitable trust	10,000

Compute Mr. A's taxable income for assessment year 2020-21.

**Solution :** His taxable income for assessment year 2020-21 will be computed as follows:

Net income from salary	40,000
Income from house property	75,000
Income from other sources	28,000
Gross Total Income	1,43,000
Less: Deduction under Section 80C	2,000
Less: Deduction permissible: Donation under Section 80G (as worked out below)	13,500
Taxable income	1,27,500
Income-tax on Rs. 1,27,500	NIL
Net tax payable (including Health & Education cess @ 4%)	NIL

**Note:** Under Section 80G the various items of donations will be dealt with as under:

1. Prime Minister's National Relief Fund deductible in full without any restrictions.

2. Donation to Indira Gandhi Memorial Trust is deductible to the extent of 50% of donation without any restrictions.
3. Donation to approved family planning association is deductible in full so long as it is within the 10% limit imposed by Section 80G(4).
4. Donation to an approved charitable trust is deductible to the tune of 50% so long as it is also within the limit imposed by Section 80G(4).

Calculation of deduction under Section 80G:

Gross total income	1,43,000
Less : Deduction under Sections 80C to 80U	2,000
Adjusted gross total income	1,41,000
 (i) Donation on which qualifying limit is not applicable:	
(A) Allowed @ 100%	
Prime Minister's National Relief Fund	2,500
(B) Allowed @ 50%	
I. Indira Gandhi Memorial Trust (4000)	2,000
 (ii) Donation to which qualifying limit is applicable:	
(1) For promotion of family planning	4,000
(2) Charitable trust	10,000
Limited to 10% of Adjusted Gross Total Income:	14,000
i.e. Rs.14,100/- Since donation to family planning are lowest than maximum allowable.	
Therefore, allowable amount is (4,000 + 5,000) Rs. 9,000/-	9,000
Total Deduction for Section 80G	13,500

### Deduction in respect of Rent Paid [Section 80GG]

Section 80GG provides deduction to an individual for rent paid if in case the individual does not receive HRA exempt u/s 10(13A) or rent free accommodation from his employer. The accommodation should be occupied by the assessee for the purpose of his own residence. Further, the individual/spouse/minor child/HUF of which he or she is member does not own a residential accommodation at a place where the individual resides, performs the duties of his office or employment or carries on his or her business or profession. For the purpose of this section, the individual will give declaration in Form 10BA. The amount of deduction admissible under this Section is lower of:

- Actual rent paid less 10% of 'Adjusted Total Income'.
- 25% of such 'Adjusted Total Income'.
- Amount calculated at Rs. 5,000 p.m.

Where Adjusted Total Income means the Gross total income as reduced by long term capital gain if included in the gross total income and income referred to in section 115A to 115D and the amount of deduction under section 80C other than deduction under this section.

**Illustration**

If Mr. 'A' had income against the following heads,

Professional income	6,40,000
Income from STCG (covered under section 111A)	5,000
Income from LTCG	12,000
Income from other sources	10,000
Contribution to P.P.F.	70,000
Payment of Rent	84,000

Compute Mr. A's taxable income for assessment year 2020-21.

**Solution :** His taxable income for assessment year 2020-21 will be computed as follows:

Professional income	6,40,000
Income from capital gains	17,000
Income from other sources	10,000
Gross Total Income	6,67,000
Less : Deduction under Section 80C	70,000
Less : Deduction under Section 80GG (as worked out below)	26,000
Taxable income	571,000

Working Note:

Least of the following is deductible under section 80GG

- $84,000 - (10\% \text{ of } 5,80,000) = 26,000$
- $25\% \text{ of } 5,80,000 = 1,45,000.$
- $\text{Rs. } 5,000 * 12 = 60,000$

Deduction under Section 80GG is lower of three above Rs. 26,000.

Adjusted Total Income =  $6,67,000 - 17,000 - 70,000 = 5,80,000.$

### **Deduction in Respect of Certain Donations for Scientific Research or Rural Development [Section 80GGA]**

Section 80GGA provides 100% deduction to any assessee (other than an assessee whose gross total income includes income chargeable under the head "profits and gains of business or profession") in respect of the following payments/donations:

- a) Sums paid to a research association which has, as its object the undertaking of scientific research, or to a university, college or other institution to be used for scientific research where such association, university, college or institution has been approved by the prescribed authority for the purpose of Section 35(1)(ii).
- b) any sum paid by the assessee in the previous year to a research association which has as its object

the undertaking of research in social science or statistical research or to a University or college or other institution to be used for social science or statistical research where such association or university college or institution is for the time being approved by the prescribed authority for the purpose of Section 35(1)(iii).

- c) Sums paid to an approved association or institution which has as its object the undertaking of any programme of rural development, to be used for the purposes of carrying out any programme of rural development approved for the purposes of Section 35CCA provided the assessee furnishes the certificate referred to in Section 35CCA(2).
- d) Sums paid to an approved association or institution which has as its object the undertaking of any programme of rural development provided the assessee furnishes a certificate referred to in Section 35CCA(2A).
- e) any sum paid by the assessee in the previous year to a public sector company or a local authority or an association or institution approved by the National Committee for carrying out any eligible project or scheme, provided the assessee furnishes a certificate referred to in Section 35AC(2)(a).
- f) For the purposes of this clause, 'National Committee' means the committee constituted by the Central Government from amongst persons of eminence in public life, in accordance with the rules made under Income-tax Act, 1961 and "eligible project or scheme" means such project or scheme for promoting the social and economic welfare of, or the uplift of, the public as may be notified by Central Government on the recommendations of the National Committee.
- g) Sums paid before April 1, 2002 to an approved association or institution which has as its object the undertaking of any programme of conservation of natural resources or afforestation to be used for carrying out any programme of conservation of natural resources or of afforestation approved under Section 35CCB(2).
- h) Sums paid to the National Fund for Rural Development set up and notified by the Central Government for the purpose of carrying out rural development. This section also provides that where deduction under this section is claimed and allowed, deduction will not be allowed in respect of the same payment under any other provision of the Act for the same or any other assessment year.
- i) any sum paid by the assessee in the previous year to the National Urban Poverty Eradication Fund set up and notified by the Central Government.

***No deduction shall be allowed under this section in respect of any sum exceeding ten thousand rupees unless such sum is paid by any mode other than cash.***

#### **Deduction in respect of contributions given by Companies to Political Parties or an Electoral Trust [Section 80GGB]**

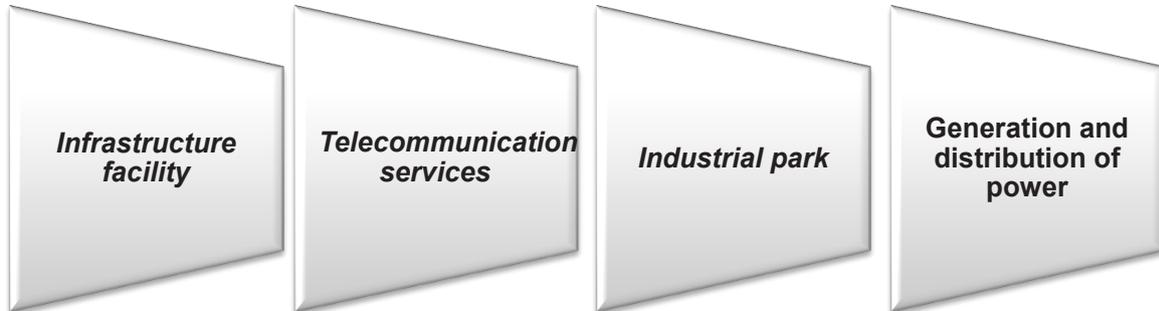
Section 80GGB provides 100 % deduction for any sum contributed by an Indian Company in the previous year to any political party or to an electoral trust while computing its total income by a mode other than cash.

#### **Deduction in respect of contributions given by any person to Political Parties or an Electoral Trust [Section 80GGC]**

Section 80GGC provides 100% deduction for any sum contributed by an assessee being any person to a political party or an electoral trust except local authority and every artificial juridical person wholly or partly funded by the Government while computing its total income by a mode other than cash.

### Deduction in respect of profits and gains from industrial undertakings or enterprise engaged in infrastructure development [Section 80-IA]

Section 80IA provides a deduction to an assessee in respect of profits and gains derived from any business of:



(1) **Infrastructure facility** : The enterprise is carrying on the business of operating any infrastructure facility which fulfills the following conditions:

- (a) It is owned by an Indian company or consortium of companies or by an authority or a board or a corporation or any other body established or constituted under any Central or State Act registered in India;
- (b) It enters into an agreement with the Central or State Government or a local authority or any other statutory body for (i) developing, (ii) operating and maintaining, (iii) developing, operating and maintaining, a new infrastructure facility.
- (c) It transfer such infrastructure facility after the period stipulated in the agreement to such Government or authority or body concerned;
- (d) It starts operating and maintaining the infrastructure facility on or after 1st April, 1995.

It has entered into an agreement with the Central Government or a State Government or a local authority or any other statutory body for developing a special economic zone and maintaining a new infrastructure facility.

Where an infrastructure facility is transferred after 31.3.1999 by an enterprise which has developed it to another enterprise for operating and maintaining it on its behalf, in accordance with the agreement with person mentioned in (b), the transferee will get the benefit of deduction for the unexpired period.

**Explanation** - For the purposes of this clause, "infrastructure facility" means:

- (a) a road including toll road, a bridge or a rail system;
- (b) a highway project including housing or other activities being an internal part of the highway project;
- (c) a water supply project, water treatment system, irrigation project, sanitation and sewerage system or solid waste management system;
- (d) a port, airport, inland waterway or inland port.

*W.e.f. Assessment year 2001-02, infrastructure facility shall also include water treatment system and solid waste management system.*

The benefit of deduction to housing and other development activities which are an internal part of a highway project shall be allowed if the following conditions are satisfied:

- (a) Such profits are transferred to a special reserve account.
- (b) Such profits are utilised for highway project, excluding housing and other activities, before the expiry of three years following the year in which the amount was transferred to the reserve account.

The amount remaining unutilised shall be chargeable to tax as income of the year in which it was transferred to the reserve account.

(2) **Telecommunication services** : Any undertaking which has started or starts providing telecommunication services whether basic or cellular including radio-paging, domestic satellite service or network of trunking and electronic data interchange services at any time after 31.3.1995 but before 31.3.2005.

Domestic Satellite Service means a satellite owned and operated by an Indian Company for providing telecommunication services.

(3) **Industrial park** : Any undertaking which develops a special economic zone and operates an industrial park (notified by the Central Government) after 31.3.1997 but before 1.4.2006 and in case of SEZ, it should begin on or after 1.4.2001 but before 1.4.2006.

Where an undertaking develops industrial park after 31.3.1999 and transfers the operations and maintenance of it to another undertaking, the transferee will get the benefit of deduction for the unexpired period.

However, Investments made to develop industrial park has been extended from 31.3.2006 to 31.3.2011.

(4) **Generation and distribution of power** : An undertaking which:

- (a) is set-up in any part of India for the generation or generation and distribution of power if it begins to generate power at any time during the period beginning on the 1st day of April, 1993 and ending on the 31st day of March 2017.
- (b) starts transmission or distribution by laying a network of new transmission or distribution lines at any time during the period beginning on the 1st day of April, 1999 and ending on the 31st day of March 2017.
- (c) undertakes substantial renovation and modernization of the existing network of transmission or distribution lines at any time during the period beginning on the 1st day of April, 2004 and ending on the 31st day of March, 2017.

Provided that the deduction under this section to an industrial undertaking under sub-clause (b) shall be allowed only in relation to the profits derived from laying of such network of new lines for transmission or distribution.

**Quantum and period of deduction:**

- (1) First five assessment years - 100% of such profits.
- (2) Next five assessment years - In case of companies 30% of such profits. In case of other assesseees 25% of such profits.

The deduction under (4) above shall be allowed if the following conditions are satisfied:

- (a) It is not formed by the splitting up, or the reconstruction, of a business already in existence;
- (b) it is not formed by the transfer to a new business of machinery or plant (exceeding 20%) previously used for any purpose.

(5) Re-construction or revival of a power generating plant

- (a) Such undertaking must be owned by an Indian Company, formed before 30.11.2005 with majority equity participation by public sector companies for the purpose of enforcing the security interest of the lenders to the company owning the power generation plant.
- (b) Such Indian Company is notified before 31.12.2005 by the Central Government for the purposes of this clause and begins to generate or transmit or distribute power before 31.3.2011 (w.e.f 1st April 2008 by Finance Act 2009).

**Option to claim deduction** : The assessee, at his option, can claim deduction in any ten consecutive assessment years out of fifteen years beginning from the year in which it begins operations.

If the assessee is engaged in infrastructure facility mentioned in (b) above he can claim deduction in any ten consecutive assessment years out of twenty years instead of out of fifteen years.

**Computation of Income for Deduction** : For the purpose of computing the deduction at the specified percentage for the assessment year immediately succeeding the initial assessment year and any subsequent assessment year, the profits and gains will be computed as if such business were the only source of income of the assessee in all the assessment years for which the deduction at the specified percentage under this section is available.

It means if the loss or any allowance (e.g. depreciation allowance) of such business is set-off against any other income in an earlier assessment year to find out the income of the current year for deduction under this section the loss so set-off shall be deducted from the current year's income and on the balance so arrived, the deduction shall be computed.

Where goods held for the purpose of eligible business are transferred to any other business of the assessee, or vice-versa, such transfer is required to be done at the market value of such goods. If such goods are not transferred at market value on the date of transfer, then the profits and gains of such eligible business shall be recomputed as if transfer has been made at the market value of such goods, as on that date.

If in the opinion of the Assessing Officer, such recomputation presents exceptional difficulties, the Assessing Officer may compute such profits and gains on such reasonable basis as he may deem fit.

*Market Value in relation to any goods or services, means*

- (i) *the price that such goods or services would ordinarily fetch in the open market; or*
- (ii) *the arm's length price as defined in clause (ii) of section 92F, where the transfer of such goods or services is a specified domestic transaction referred to in section 92BA.*

Where deduction to an industrial undertaking or an enterprise for profit and gains is allowed under this section for any assessment year, deduction to that extent shall not be allowed under any other provision of chapter VIA under the heading deductions in respect of certain incomes.

The deduction shall not exceed the profit and gains of such eligible business of industrial undertaking or enterprise. If the profit shown for the eligible business under this section, appears to the assessing officer as more than the ordinary profits which might be expected to arise in such eligible business, owing to some close connection with a person with whom business transactions are so arranged to yield higher profit, the assessing officer may take the amount of profits as may be reasonably derived therefrom.

Where any undertaking of an Indian company which is entitled to deduction under this section is transferred, before the expiry of the period of tax holiday, to another Indian company in a scheme of amalgamation or demerger, then the deduction will be available as follows:

- (i) No deduction shall be admissible under this section to the amalgamating company/demergered company for the previous year in which amalgamation/ demerger takes place.
- (ii) The amalgamated company or resulting company will be entitled to claim deduction under this section for the unexpired period of tax holiday (including for the previous year in which the amalgamation/ demerger takes place). The provisions of the section shall, as far as may be, apply to the amalgamated or resulting company as they would have applied to the amalgamating or demergered company as if the amalgamation or demerger had not taken place.

Provided that in a case where an undertaking develops an industrial park on or after the 1st day of April, 1999 or a special economic zone on or after the 1st day of April, 2001 and transfers the operation and maintenance

of such industrial park or such special economic zone, as the case may be, to another undertaking (hereafter in this section referred to as the transferee undertaking), the deduction under Sub-section (1) shall be allowed to such transferee undertaking for the remaining period in the ten consecutive assessment years as if the operation and maintenance were not so transferred to the transferee undertaking.

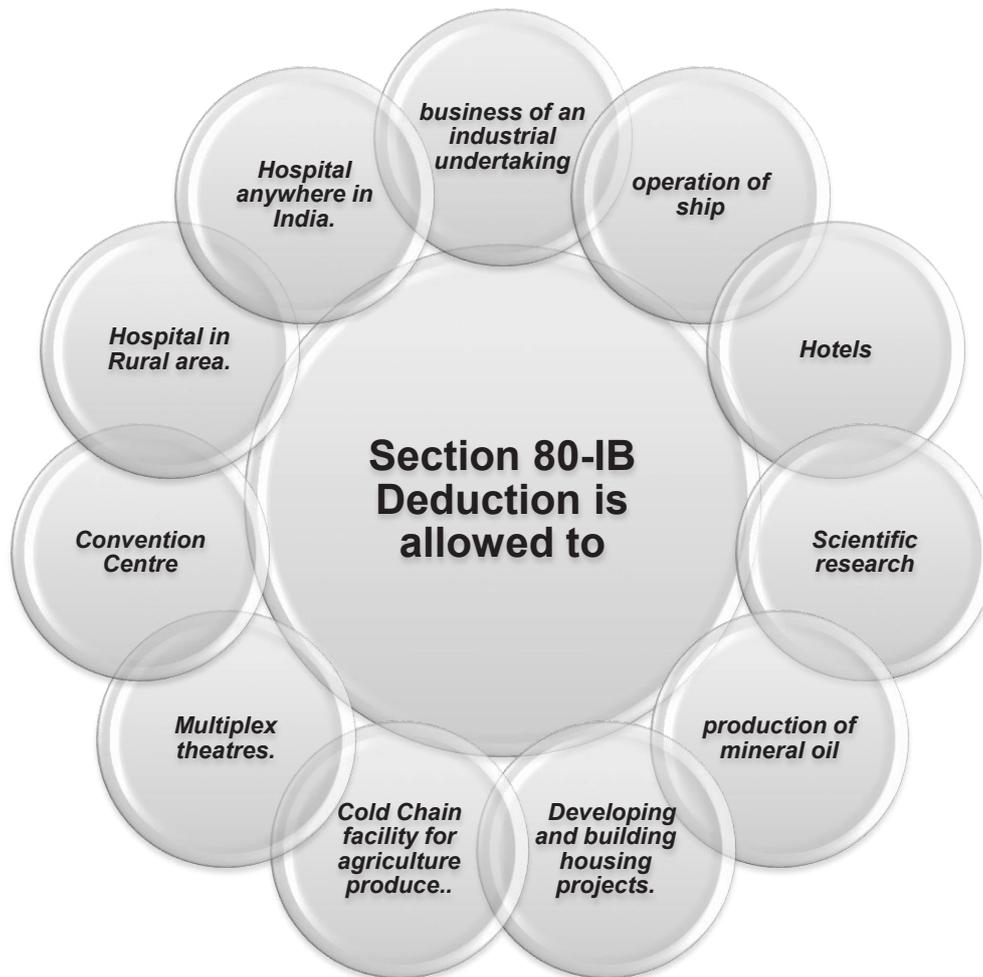
The provisions contained in this section shall not apply to any special economic notified on or after the 1st day of April, 2005 in accordance with the scheme referred to in sub-clause (iii) of clause (c) of Sub-section (4).

**Deduction in respect of profit and gains by an undertaking or an enterprise engaged in development of Special Economic Zone [Section 80-IAB]**

Section 80IB provides a deduction to an assessee which develops Special Economic Zone (SEZ), notified on or after 1.4.2005 under the Special Economic Zones Act, 2005( and development of SEZ should begin before 1st April, 2017) equal to 100% of the profit and gains derived from such business for 10 consecutive assessment years, out of 15 years beginning from the year in which a SEZ has been notified by the central government, at option of the assessee. Such assessee would not be eligible to claim deduction u/s 80-IA.

**Deduction in respect of profits and gains from certain industrial undertakings other than infrastructure development undertakings [Section 80-IB]**

Section 80IB provides deduction to an assessee whose gross total income includes profits and gains derived from the following business. The deduction equal to such percentage and for such number of assessment years as given below:



An industrial undertaking should be mainly engaged in the business of construction of ships or in the manufacture or processing of goods or in mining. Construction of dam, bridge, road or building cannot be characterised as manufacture or production of articles.

The Industrial undertaking claiming deduction under this section, however need to fulfill the following conditions:

1. It is not formed by splitting up, or the reconstruction, of a business already in existence. This condition is not violated, where the business is re-established, reconstructed or revived by the same assessee after the business of any industrial undertaking carried on by him in India is discontinued due to extensive damage to or destruction of, any building, machinery, plant or furniture owned by the assessee (and used for the purpose of such business) as a direct result of (i) flood, typhoon, hurricane, cyclone, earthquake or other convulsion of nature, or (ii) riot or civil disturbance, or (iii) accidental fire or explosion, or (iv) action by any enemy or action taken in combating an enemy (whether with or without a declaration of war).
2. It is not formed by the transfer to a new business of machinery or plant previously used for any purpose. However, plant and machinery, already used for any purpose, can be transferred to the new industrial undertaking, provided value of such plant and machinery does not exceed 20% of the total value of plant and machinery of the new industrial undertaking.
3. It manufactures or produces any article or thing, not being any article or thing specified in the list in the Eleventh Schedule, or operates one or more cold storage plant or plants, in any part of India. However, a small scale industrial undertaking or an industrial undertaking located in an industrially backward state specified in the Eighth Schedule shall be eligible for the deductions, even if it manufactures or produces any article/thing which is specified in the Eleventh Schedule.
4. The undertaking employs ten or more workers in a manufacturing process carried on with the aid of power or employs twenty or more workers in a manufacturing process carried on without the aid of power.

I. The amount of deduction to industrial undertaking shall be as follows:

Sl. No.	Undertaking Industrial	Period within which production should start	Period of deduction (commencing from initial assessment year)	%age of profit eligible for deduction
(1)	(2)	(3)	(4)	(5)
(i)	Any industrial undertaking			
	Owned by a company	1.4.1991 to 31.3.1995* (or any further notified period)	Ten consecutive assessment year	30%
	Owned by a co-operative society		Twelve consecutive assessment year	25%
	Any other assessee		Ten consecutive assessment year	25%

\*However where it is an industrial undertaking being a small scale industrial undertaking, it begins to manufacture or produce article or things or to operate its cold storage plant (other than those specified below) the period shall be construed as the period beginning on 1.4.95 and ending on 31.3.2002.

**(ii) Industrial undertaking set up in an industrial backward state specified in Eighth Schedule\***

Owned by a company	1.4.1993 to 31.3.2002 (extended to 31.3.2012 only in J&K)	First five years	100%
		Next five years	30%
Owned by a co-operative society		First five years	100%
		Next seven years	25%
Any other assessee		First five years	100%
		Next five years	25%

\*However in case of notified industries in the North-Eastern Region, the amount of deduction shall be hundred percent of profits for a period of ten assessment years.

**(iii) Industrial undertaking located in notified industrially backward districts of Category A**

Owned by a company	1.10.1994 to 31.3.2004	First five years	100%
		Next five years	30%
Owned by a co-operative society		First five years	100%
		Next seven years	25%
Any other assessee		First five years	100%
		Next five years	25%

**(iv) Industrial undertaking located in notified industrially backward districts of Category B**

Owned by a company	1.10.1994 to 31.3.2004	First three years	100%
		Next five years	30%
Owned by a co-operative society		First three years	100%
		Next nine years	25%
Any other assessee		First three years	100%
		Next five years	25%

*II. Deduction under this section shall also be available in the case of the business of a ship @ 30% of the profits and gains derived from such ship for a period of ten consecutive assessment years including the initial assessment year.*

However, to claim deduction it is required that the ship -

- (i) is owned by an Indian company and is wholly used for the purposes of the business carried on by it.
- (ii) was not, previous to the date of its acquisition by the Indian company, owned or used in Indian territorial waters by a person resident in India.
- (iii) is brought into use by the Indian company at any time during the period beginning on the 1.4.1991 and ending on 31.3.1995.

Sl. No.	Type of Hotel	Period within which functioning should start	Period of deduction (commencing from initial assessment year)	Profit eligible for deduction
(i)	Hotel located in a hilly area or a rural area or a place of pilgrimage or any other place notified by Central Government having regard to the need for development of infrastructure for tourism in any place and other relevant consideration.	1.4.1990 to 31.3.1994	Ten consecutive years	50%
(ii)	Hotel located in a hilly area or a rural area or a place of pilgrimage or any other place notified by Central Government. However, such hotel should not be located within Municipal Jurisdiction of Calcutta, Chennai, Delhi and Mumbai. Such hotel should however be approved by the prescribed authority.	1.4.1997 to 31.3.2001	Ten consecutive years	50%
(iii)	Hotel located in any place other than those mentioned in (i) above	1.4.1991 to 31.3.1995	Ten consecutive years	30%
(iv)	Hotel located in any other place other than those mentioned in (i) above. However, such hotel should not be located within Municipal Jurisdiction of Calcutta, Chennai, Delhi and Mumbai.	1.4.1997 to 31.3.2001	Ten consecutive years	30%

However, the following conditions need to be satisfied by a hotel in order to claim deduction:

- (i) The business of the hotel is not formed by the splitting up; or the reconstruction of a business already in existence or by the transfer to a new business of a building previously used as a hotel or of any machinery or plant previously used for any purpose.
- (ii) The business of hotel is owned and carried on by a company registered in India with a paid up capital of not less than Rs. 5 lakhs.
- (iii) The hotel is for the time being approved by the prescribed authority. Any hotel approved before 1.4.99 shall be deemed to have been approved for the purpose of this section.

*IV. Deduction in the case of any company carrying on scientific research and development is available @ 100% of the profits and gains of such business for a period of five assessment years beginning from the initial assessment year. However, to claim deduction under this section, it is required that such a company -*

- (i) is registered in India.
- (ii) has the main object of scientific and industrial research and development.
- (iii) is for the time being approved by the prescribed authority at any time before 1.4.1999.

Further, the amount of deduction in the case of any company carrying on scientific research and development shall be hundred per cent of the profits and gains of such business for a period of ten consecutive assessment years, beginning from the initial assessment year, if such company -

- (i) is registered in India;
- (ii) has its main object the scientific and industrial research and development;
- (iii) is for the time being approved by the prescribed authority at any time after the 31st day of March, 2000, but before the 1st day of April, 2007;
- (iv) Fulfills such other conditions as may be prescribed.

*V. Industrial undertaking producing or refining mineral oil in the North Eastern Region or in any part of India:*

The amount of deduction to an undertaking shall be 100% of the profits for a period of seven consecutive assessment years, including the initial assessment year, if such undertaking fulfils any of the following conditions:

- (i) is located in North-Eastern Region and has begun or begins commercial production of mineral oil before the 1st day of April, 1997;
- (ii) is located in any part of India and has begun or begins commercial production of mineral oil on or after the 1st day of April, 1997;

Provided that the provisions of this clause shall not apply to blocks licensed under a contract awarded after the 31st day of March, 2011 under the New Exploration Licencing Policy announced by the Government of India vide Resolution No. O-19018/22/95-ONG.DO.VL, dated the 10th February, 1999 or in pursuance of any law for the time being in force or by the Central or a State Government in any other manner;

- (iii) is engaged in refining of mineral oil and begins such refining on or after the 1st day of October, 1998 but not later than 31st day of March 2012..(w.e.f Assessment year 2001-02) (the words “but not later than the 31st day of March, 2012” shall be inserted w.r.e.f 1st April 2009);
- (iv) is engaged in commercial production of natural gas in blocks licensed under the VIII Round of bidding for award of exploration contracts (hereafter referred to as “NELP-VIII”) under the New Exploration Licencing Policy announced by the Government of India vide Resolution No. O-19018/22/95-ONG. DO.VL, dated 10th February, 1999 and begins commercial production of natural gas on or after the 1st day of April, 2009.
- (v) is engaged in commercial production of natural gas in blocks licensed under the IV round of bidding for award of exploration contracts for Caol Bed Methane blocks and begins commercial production of natural gas on or after the 1st day of April 2009.

*Explanation:* All blocks licensed under a single contract, which has been awarded under the New Exploration Licencing Policy announced by the Government of India vide Resolution No. O-19018/22/95-ONG.DO.VL, dated 10th February, 1999 or has been awarded in pursuance of any law for the time being in force or has been awarded by Central or a State Government in any other manner, shall be treated as a single undertaking.

*VI. Deduction of 100% of the profits of an undertaking engaged in developing and building housing projects approved before the 31st day of March, 2008 by a local authority provided that:*

- (a) such undertaking has commenced or commences development and construction of the housing project on or after 1st day of October, 1998 and completes such construction -
  - (i) in case where a housing project has been approved by the local authority before the 1st day of April, 2004, on or before 31st day of March, 2008;

- (ii) in a case where a housing project has been or, is approved by the local authority on or after the 1st day of April, 2004 but not later than the 31st March 2005, within four years from the end of financial year in which the housing project is approved by the local authority.
- (iii) In a case where a housing project has been approved by the local authority on or after the 1st day of April, 2005, within five years from the end of the financial year in which the housing project is approved by the local authority.
- (b) the project is of the size of a plot of land which has minimum area of one acre;
- (c) the residential unit has a maximum built-up area of one thousand square feet where such residential unit is situated within the cities of Delhi or Mumbai or within twenty-five kilometers from the municipal limits of these cities and one thousand and five hundred square feet at any other place; and
- (d) the build-up area of the shops and other commercial establishments included in the housing project does not exceed three of the aggregate built-up area of the housing project or five thousand square feet whichever is higher.
- (e) not more than one residential unit in the housing project is allotted to any person not being an individual; and
- (f) in a case where a residential unit in the housing project is allotted to a person being an individual, no other residential unit in such housing project is allotted to any of the following persons,
  - (i) the spouse or the minor children of such individual,
  - (ii) the Hindu undivided family in which such individual is the karta,
  - (iii) any person representing such individual, the spouse or the minor children of such individual or the Hindu undivided family in which such individual is the karta.

*VII. Hundred percent of the profits and gains derived by an industrial undertaking from the business of setting up and operating a cold chain facility for agricultural produce shall be deductible:*

<b>Industrial Undertaking</b>	<b>Period within which production should start</b>	<b>Period of deduction (commencing from initial assessment year)</b>	<b>%age of profit eligible for deduction</b>
For a company	1.4.1999 to 31.3.2003	First five years	100%
For a co-operative society		Next five years	30%
Any other assessee		First five years	100%
		Next seven years	25%
		First five years	100%
		Next five years	25%

Where any undertaking of an Indian company which is entitled to the deduction under this section is transferred, before the expiry of the period specified in this section, to another Indian company in a scheme of amalgamation or demerger -

- (a) no deduction shall be admissible under this section to the amalgamating or the demerged company for the previous year in which the amalgamation or the demerger takes place; and
- (b) the provisions of this section shall as far as may be apply to the amalgamated or the resulting company as they would have applied to the amalgamating or the demerged company if the amalgamation or demerger had not taken place.

Further, the amount of deduction in a case of an undertaking deriving profit from the integrated business of handling, storage and transportation of foodgrains, shall be hundred per cent of the profits and gains derived from such undertaking for five assessment years beginning with the initial assessment year and thereafter, twenty-five per cent (or thirty per cent, where the assessee is a company) of the profits and gains derived from the operation of such business in a manner that the total period of deduction does not exceed ten consecutive assessment years and subject to fulfillment of the condition that it begins to operate such business on or after the 1st day of April, 2001.

In the case of an undertaking engaged in the integrated business of handling, storage and transportation of foodgrains, means the assessment year relevant to the previous year in which the undertaking begins such business.

*VIII. Deduction in the case of any multiplex theatre*

Fifty per cent of the profits and gains derived, from the business of building, owning and operating a multiplex theatre, for a period of five consecutive years beginning from the initial assessment year in any place. Multiplex theatre should not be located at a place within the municipal jurisdiction of Kolkata, Chennai, Delhi or Mumbai. Such multiplex theatre should be constructed at any time during the period beginning on the 1st day of April, 2002 and ending on the 31st day of March, 2005. The business should not be formed by splitting up or the reconstruction, of a business or any plant and machinery previously used for any purpose, and assessee should furnish alongwith the return of income, the report of an audit in Form No. 10CCBA.

*IX. Deduction in the case of any convention centre:*

Fifty per cent of the profits and gains derived, by the assessee from the business of building, owning and operating a convention centre, for a period of five consecutive years beginning from the initial assessment year. Such convention centre is constructed at any time during the period beginning on the 1st day of April, 2002 and ending on the 31st day of March, 2005. The business should not be formed by splitting up or the re-construction of a business or any plant and machinery previously used for any purpose.

*X. 100% deduction in case of an undertaking deriving profits from the business of operating and maintaining a hospital in a rural area for a period of five consecutive assessment years beginning with the initial assessment year if (w.e.f. A.Y. 2005-06) -*

- (i) such hospital is constructed at any time during the period from 1.10.2004 to 31.3.2008.
- (ii) the hospital has atleast one hundred beds for patients.
- (iii) construction of hospital is in accordance with the regulations, for the time being in force, of the local authority; and
- (iv) the assessee furnishes alongwith the return of income the report of audit in such form and containing such particulars as may be prescribed and duly signed and verified by a chartered accountant that the deduction has been correctly claimed.

*XI. The amount of deduction in the case of an undertaking deriving profits from the business of operating and maintaining a hospital located anywhere in India, other than the excluded area, shall be hundred per cent of the profits and gains derived from such business for a period of five consecutive assessment years, beginning with the initial assessment year, if -*

- (i) the hospital is constructed and has started or starts functioning at any time during the period beginning on the 1st day of April, 2008 and ending on the 31st day of March, 2013;
- (ii) the hospital has at least one hundred beds for patients;
- (iii) the construction of the hospital is in accordance with the regulations or bye-laws of the local authority; and

- (iv) the assessee furnishes along with the return of income, a report of audit in such form and containing such particulars, as may be prescribed, and duly signed and verified by an accountant, as defined in the Explanation to sub-section (2) of section 288, certifying that the deduction has been correctly claimed.

### Illustration

1. Deduction under Section 80-IB is available to:
  - (a) Charitable Trust
  - (b) Tour and Travels
  - (c) Industrial Research
  - (d) Convention Centre
2. Which of the following gets 50% deduction on the profits and gains derived from its business for a period of five consecutive years beginning from the initial assessment year in any place?
  - (a) Multiplex Theatre
  - (b) Convention Centre
  - (c) Hospital
  - (d) Charitable Trust

### Deduction in respect of eligible Start-Up [Section 80IAC]

Section 80IAC provides a deduction to an assessee, being an eligible start-up, whose gross total income includes any profits and gains derived from eligible Business equal to 100% of the profit and gains derived from such business for 3 consecutive assessment years, at the option of the assessee out of seven years beginning from the year in which the eligible start-up is incorporated. The Eligible Start-up should not be formed by splitting up, or the reconstruction, of a business already in existence and should not be formed by the transfer to a new business of machinery or plant previously used for any purpose.

However any machinery or plant being previously used for any purpose is transferred to a new business and the total value of the machinery or plant or part so transferred does not exceed twenty per cent of the total value of the machinery or plant used in the new business.

- (i) "eligible business" means a business carried out by an eligible start-up engaged in innovation, development or improvement of products or processes or services or a scalable business model with a high potential of employment generation or wealth creation.
- (ii) "eligible start-up" means a company or a limited liability partnership (LLP) engaged in eligible business which fulfils the following conditions: –
  - (a) it is incorporated on or after the 1st day of April, 2016 but before the 1st day of April, 2021.
  - (b) the total turnover of its business does not exceed twenty-five crore rupees in any 3 previous years out of 7 previous years for which deduction under section 80-IAC is first claimed
  - (c) it holds a certificate of eligible business from the Inter-Ministerial Board of Certification.

### Deductions in respect of profits and gains from Housing Projects [Section 80IBA]

Section 80IBA provides deduction to an assessee whose gross total income includes any profits and gains derived from the business of developing and building housing projects, subject to the provisions of this section, of an amount equal to 100% of the profits and gains derived from such business.

A housing project shall be a project which fulfils the following conditions:

- a) the project is approved by the competent authority after the 1st day of June, 2016, but on or before the 31st day of March, 2020 [Amendment vide Finance Act, 2019];
- b) the project is completed within a period of 5 years from the date of approval by the competent authority;
- c) the carpet area of the shops and other commercial establishments included in the housing project does not exceed 3% of the aggregate carpet area
- d) the project is on a plot of land measuring not less than 1000 square metres, where the project is located within the cities of Chennai, Delhi, Kolkata or Mumbai or within the distance, measured aerially, of 25 kilometres from the municipal limits of these cities or 2000 metres, where the project is located in any other place;
- e) The stamp duty value of a residential unit does not exceed Rs. 45 lakhs if project is approved after 30/09/2019.
- f) the carpet area of the residential unit comprised in the housing project does not exceed 30 square meters ( 60 square meters if project approved after 30/09/2019), where the project is located within the cities of Chennai, Delhi, Kolkata or Mumbai or within the distance, measured aerially, of 25 kilometres from the municipal limits of these cities or 60 square metres ( 90 square meters if project approved after 30/09/2019), where the project is located in any other place;

“Carpet Area” means the net usable floor area of an apartment [excluding (i) the area covered by the external walls (ii) areas under the service shafts/exclusive balcony or verandah area/exclusive open terrace area, but including the area covered by the internal partition wall of the apartment.]

### Special provisions in respect of certain undertakings or enterprises in certain special category States [Section 80-IC]

Section 80IC provides deduction from such profits and gains as specified in Sub-section (3) to an assessee whose gross total income includes any profits and gains derived by an undertaking or an enterprise from any business referred to in Sub-section (2), in accordance with and subject to the provisions of this section.

- (1) This section applies to any undertaking or enterprise, –
  - (a) which has begun or begins to manufacture or produce any article or thing, not being any article or thing specified in the Thirteenth Schedule, and undertakes substantial expansion during the period beginning –
    - (i) on the 23rd day of December, 2002 (and ending before the 1st day of April, 2012, in any specified areas, in the State of Sikkim; or
    - (ii) on the 7th day of January, 2003 and ending before the 1st day of April, 2012, in any specified areas, in the State of Himachal Pradesh or the State of Uttaranchal; or
    - (iii) on the 24th day of December, 1997 and ending before the 1st day of April, 2007, in any specified areas, in any of the North-Eastern States;

Specified area means any Export Processing Zone or Integral Infrastructure Development Centre or Industrial Growth Centre or Industrial Park or Theme Park, as notified by the Board in accordance with the scheme framed and notified by the central government in this regard.

- (b) which has begun or begins to manufacture or produce any article or thing, specified in the Fourteenth Schedule or commences any operation specified in that Schedule, and undertakes substantial expansion during the period beginning –
  - (i) on the 23rd day of December, 2002 and ending before the 1st day of April, 2012, in the State of Sikkim; or

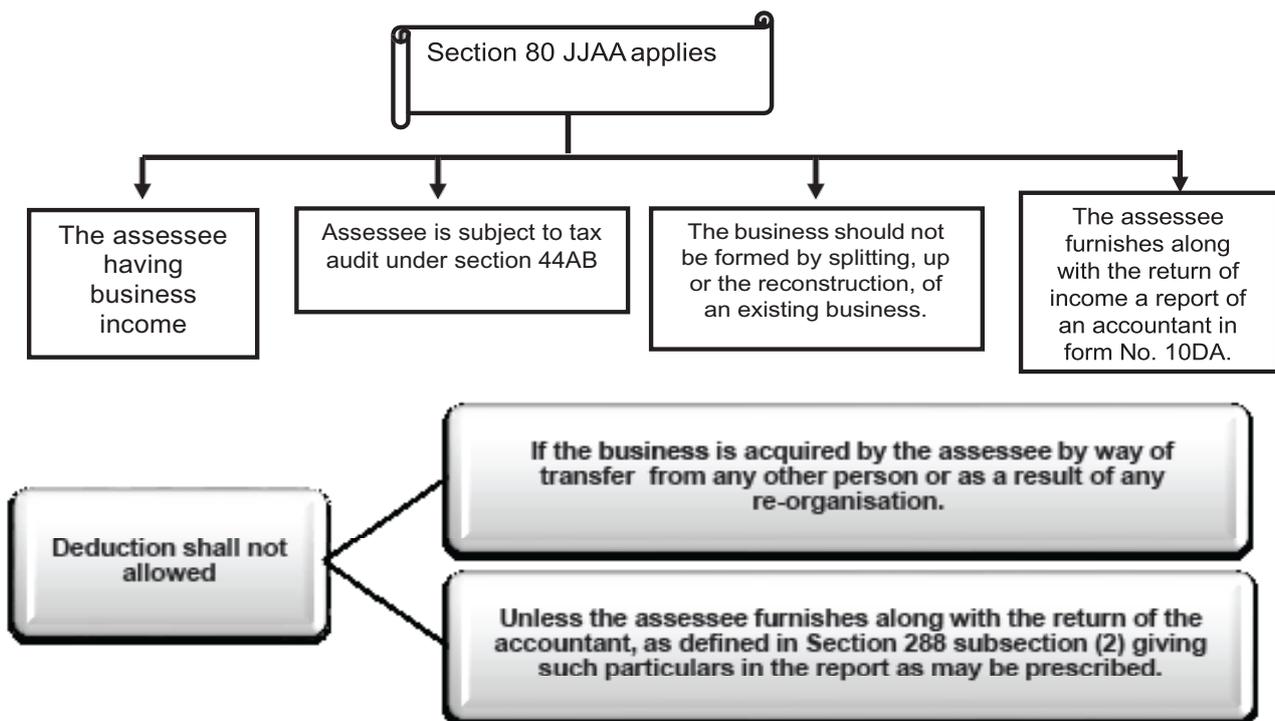
- (ii) on the 7th day of January, 2003 and ending before the 1st day of April, 2012, in the State of Himachal Pradesh or the State of Uttaranchal; or
  - (iii) on the 24th day of December, 1997 and ending before the 1st day of April, 2007, in any of the North-Eastern States.
- (2) The deduction referred to in Sub-section (1) shall be –
- (i) in the case of any undertaking or enterprise referred to in Sub-clauses (i) and (iii) of Clause (a) or Sub-clause (i) and (iii) of Clause (b), of Sub-section (2), 100% of such profits and gains for ten assessment years commencing with the initial assessment year;
  - (ii) in the case of any undertaking or enterprise referred to in Sub-clause (ii) of Clause (a) or Sub-clause (ii) of Clause (b), of Sub-section (2), 100% of such profits and gains for five assessment years commencing with the initial assessment year and thereafter, 25% (or 30% where the assessee is a company) of the profits and gains.
- (3) This section applies to any undertaking or enterprise which fulfils all the following conditions, namely:
- (i) it is not formed by splitting up, or the reconstruction, of a business already in existence;  
 Provided that this condition shall not apply in respect of an undertaking which is formed as a result of the re-establishment, reconstruction or revival by the assessee of the business of any such undertaking as is referred to in Section 33B, in the circumstances and within the period specified in that section;
  - (ii) it is not formed by the transfer to a new business of machinery or plant previously used for any purpose.  
*Explanation.* – The provisions of Explanations 1 and 2 to Sub-section (3) of Section 80-IA shall apply for the purposes of Clause (ii) of this sub-section as they apply for the purposes of Clause (ii) of that sub-section.
- (4) Notwithstanding anything contained in any other provision of this Act, in computing the total income of the assessee, no deduction shall be allowed under any other section contained in Chapter VIA or in Section 10A or Section 10B, in relation to the profits and gains of the undertaking or enterprise.
- (5) Notwithstanding anything contained in this Act, no deduction shall be allowed to any undertaking or enterprise under this section, where the total period of deduction inclusive of the period of deduction under this section, or under the second proviso to Sub-section (4) of Section 80-IB or under Section 10C, as the case may be, exceeds ten assessment years.
- (6) The provisions contained in Sub-section (5) and Sub-sections (7) to (12) of Section 80-IA shall, so far as may be, apply to the eligible undertaking or enterprise under this section.
- (7) For the purposes of this section, -
- (i) “Industrial Area” means such areas, which the Board, may by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;
  - (ii) “Industrial Estate” means such estates, which the Board may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;
  - (iii) “Industrial Growth Centre” means such centres, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;
  - (iv) “Industrial Park” means such parks, which the Board, may by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;

- (v) “initial assessment year” means the assessment year relevant to the previous year in which the undertaking or the enterprise begins to manufacture or produce articles or things, or commences operation or completes substantial expansion;
- (vi) “Integrated Infrastructure Development Centre” means such centres, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;
- (vii) “North-Eastern States” means the States of Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland and Tripura;
- (viii) “Software Technology Park” means any park set up in accordance with the Software Technology Park scheme notified by the Government of India in the Ministry of Commerce and Industry;
- (ix) “substantial expansion” means increase in the investment in the plant and machinery by at least fifty per cent of the book value of plant and machinery (before taking depreciation in any year), as on the first day of the previous year in which the substantial expansion is undertaken;
- (x) “Theme Park” means such parks, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government.

**Deduction in respect of profits and gains from the Business of collecting and processing Bio-Degradable Waste [Section 80-JJA]**

Section 80 JJA provides deduction to an assessee whose gross total income includes any profits and gains derived from the business of collecting and processing or treating of bio-degradable waste for generating power, or producing bio-fertilizers, bio-pesticides or other biological agents or for producing bio-gas, making pellets or briquette for fuel or organic manure, of an amount equal to the whole of such profit and gains for a period of five consecutive assessment years beginning with the assessment year relevant to the previous year in which such business commences.

**Deduction in respect of Employment of New Workmen [Section 80-JJAA]**



**Amount of Deduction:**

If the aforementioned conditions are satisfied the assessee shall be allowed a deduction of an amount equal to 30% of additional wages paid to the new regular workmen employed by the assessee in the previous year for three assessment years including the assessment year relevant to the previous year in which such employment is provided.

1. Additional wages means the wages paid or payable to new regular workman employed during the previous year.

In case of an existing business additional employee cost shall NIL, if-

- a) There is no increase in number employees from the total number of employees employed as on the last day of the preceding previous year.
- b) Wages are paid otherwise than account payee cheque/account payee bank draft/ECS by a bank account or through prescribed electronic mode.

In case of a new business wages/ emoluments paid/ payable to employees shall be treated as additional wages. Hence, in the first year of a new business, thirty percent of all emoluments paid or payable to the employees employed during the previous year shall be allowed as deduction.

*Note:* The word 'Factory' shall have the same meaning assigned to it in clause (m) of section 2 of the Factories Act, 1948.

*Regular workmen does not include:*

- (a) a casual workman
- (b) a workman employed through contract labour
- (c) any other workman employed for a period less than 240 days during the previous year or less than 150 days for apparel, footwear and leather industry.

2. With a view to extend this employment generation incentive to all sectors, an amendment has been made to provide that the deduction under the said provisions shall be available in respect of cost incurred on any employee whose total emoluments are less than or equal to twenty five thousand rupees per month. No deduction, however, shall be allowed in respect of cost incurred on those employees, for whom the entire contribution under Employees' Pension Scheme notified in accordance with Employees' Provident Fund and Miscellaneous Provisions Act, 1952, is paid by the Government.

- a) for whom the entire contribution under Employees' Pension Scheme notified in accordance with Employees' Provident Fund and Miscellaneous Provisions Act, 1952, is paid by the Government.
- b) An employee who does not participate in Recognised provident fund.
- c) An employee who is employed for a period less than 240 days ( 150 days in case of apparel, footwear and leather Industry) during the previous year.

3. Employer's contribution to provident fund or pension fund or any other fund for the benefit of employee is not eligible for deduction. Also amount paid by employer at time of termination of service or superannuation or voluntary retirement etc. not eligible for deduction.

4. Where a new employee is employed for a period less than 240 ( or 150 days in case of apparel/footwear/ leather industry) during a previous year but in next year he is employed for a period of 240 or 150 days as the case may be, then he shall deemed to have been employed in such next year for the purpose of deduction under this section.

**Deduction in respect of certain incomes of Offshore Banking Units [Section 80LA]**

Section 80LA provides deduction to an assessee being a scheduled bank, or any bank incorporated by or under the laws of a country outside India, from income

- (i) Of an offshore banking unit in a special economic zone;
- (ii) from the business, referred to in Sub-section (1) of Section 6 of the Banking Regulation Act, 1949 (10 of 1949), with an undertaking located in a special economic zone or any other undertaking which develops, develops and operates or operates and maintains a special economic zone;
  - (a) received in convertible foreign exchange, in accordance with the regulations made under the Foreign Exchange Management Act, 1999 (42 of 1999).

**Quantum of deduction: upto assessment year 2019-20**

- (a) 100% of such income for five consecutive assessment years beginning with the assessment year relevant to the previous year in which the permission, under Clause (a) of Sub-section (1) of Section 23 of the Banking Regulation Act, 1949 (10 of 1949), was obtained, and thereafter;
- (b) 50% of such income for next five consecutive assessment years.-

**Deduction from Assessment year 2020-21**

100% of such income for any 10 consecutive years out of 15 years beginning with the year in which necessary permission is obtained, at the option of the assessee.

**Conditions to be satisfied** : No deduction under this section shall be allowed unless the assessee furnishes along with the return of income, –

- (i) in the prescribed form (Form No. 10CCF), i.e., the report of a accountant as defined in the Explanation below Sub-section (2) of Section 288, certifying that the deduction has been correctly claimed in accordance with the provisions of this section; and
- (ii) a copy of the permission obtained under Clause (a) of Sub-section (1) of Section 23 of the Banking Regulation Act, 1949 (10 of 1949), in case of a offshore Banking Unit.

**Explanation** - For the purposes of this section:

- (a) “convertible foreign exchange” shall have the same meaning assigned to it in clause (a) of the Explanation below Sub-section (4C) of Section 80HHC;
- (b) “Offshore Banking Unit” means a branch of a bank in India located in the special economic zone and has obtained the permission under Clause (a) of Sub-section (1) of Section 23 of the Banking Regulation Act, 1949 (10 of 1949);
- (c) “scheduled bank” shall have the same meaning assigned to it in Clause (e) of Section 2 of the Reserve Bank of India Act, 1934 (2 of 1934);
- (d) “special economic zone” shall have the same meaning assigned to it in Clause (viii) of the Explanation 2 to Section 10A.”

**Deduction in respect of Income of Co-Operative Societies [Section 80P]**

Section 80P provides deduction to co-operative societies in respect of following incomes, which are included in gross total income:

- A. 100% of the profits of a primary society engaged in supplying milk, oilseeds, fruits or vegetables raised or grown by its members to
  - The government or a local authority; or

344 EP-TL

- A government company or a statutory corporation; or
  - A federal co-operative society, engaged in the business of supplying the above-said products.
- B. 100% of the profits of co-operative society engaged in any one of the following activities:
- Carrying on the business of banking or providing credit facilities to its member, or
  - A cottage industry, or
  - The marketing of agricultural produce grown by its members, or
  - The purchase of agricultural implements for the purpose of supplying them to its members, or
  - The processing, without the aid of power, of agricultural produce of its members, or
  - The collective disposal of the labour of its member, or
  - Fishing or allied activities for the purpose of supplying them to its members.

Provided, in the case of last two types of co-operative societies, the deduction, is available subject to the condition that the rules and bye-laws of the society restrict the voting rights to the members like, State Government, Co-operative Credit Society which provide financial assistance to the society and individual, who contributes their labours.

W.e.f. Assessment Year 2007-08 this exemption is not be available to co-operative banks other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank.

- C. Profits and gains of co-operative society other than those specified in A and B above is exempt up to the specified limits:
- is case of a consumer co-operative society - Rs. 1,00,000
  - is any other case - Rs. 50,000
- D. All profits by way of interest or dividend from its investment with any other co-operative society.
- E. 100% of income or profit of a Co-operative Society from the letting of godowns or warehouse for storage, processing or facilitating the marketing of commodities.
- F. A co-operative society, not being a housing society or an urban consumers society or a society carrying on transport business or a society engaged in the performance of any manufacturing operation with the aid of power, where the gross total income does not exceeds Rs. 20,000. The amount of any income by way of interest on securities or any income from house property chargeable under Section 22 will also be allowed as deduction.

**Deduction in respect of certain income of Producer Companies [Section 80PA inserted vide Finance Act, 2018]**

100% Deduction of the profits derived from eligible business to a Producer Company having a total turnover of less than one hundred crore rupees. Benefit shall be available for the previous year relevant to an assessment year commencing on or after the 1st day of April, 2019, but before the 1st day of April, 2025.

In a case where the assessee is entitled also to deduction under any other provision of this Chapter, the deduction under this section shall be allowed with reference to the income, if any, as referred to in this section included in the gross total income as reduced by the deductions under such other provision of this Chapter.

“eligible business” means –

- (a) the marketing of agricultural produce grown by the members

- (b) the purchase of agricultural implements, seeds, livestock or other articles intended for agriculture for the purpose of supplying them to the members
- (c) the processing of the agricultural produce of the members

“member” and “Producer Company” shall have the meaning assigned to it in section 581A of the Companies Act, 1956.

**Deduction in respect of Royalty Income, etc., of authors of certain books other than text books [Section 80QQB]**

Section 80 QQB provides deduction to a resident individual who is an author or a joint author of a book whose income includes income derived from such profession, received either as a lump sum consideration for the assignment or grant of any of his interests in the copyright of any book or royalty of books other than text books. The amount of deduction is the lower of eligible income or Rs. 3,00,000. Eligible income (before deducting expenditure incurred) is lower of

1. Lump sum consideration for the assignment or grant
2. Royalty not exceeding 15%
3. If such income is earned outside India, the part of the income brought to India in convertible foreign exchange within 6 months from the end of the previous year or the extended period by the RBI will be considered.

Books exclude brochures, diaries, guides, journals, magazines, newspapers, pamphlets, text books for schools, tracts, commentaries or any such publication whatever name may be. No deduction under this section shall be allowed unless an assessee furnishes a certificate in the prescribed form 10CCD/10H.

**Illustration**

**Mr. X receives royalty on books Rs. 1,00,000 at a rate of 18 percent and incurs Rs. 10, 000 as expenditure for earning royalty. The books are covered under section 80QQB and royalty is received from abroad and Rs. 50,000 are remitted to India till September 30, 2020. Determine deduction under section 80 QQB for the assessment year 2020-21.**

**Solution:**

Eligible income (before deducting expenditure incurred) is lower of

1. Lump sum consideration	NIL
2. Royalty not exceeding 15% (1,00,000/18) *15	83,334
3. Income brought to India in convertible foreign exchange	50,000

Eligible income Rs. 50,000

Expenditure incurred Rs. 10,000

Deduction under section 80 QQB Rs. 40,000 (subject to a maximum of Rs. 3, 00,000).

**Deduction in respect of Royalty on Patents [Section 80RRB]**

Section 80RRB provides deduction to resident individual, a patentee who is in receipt of income by way of royalty in respect of a patent registered on or after the 1st day of April, 2003 under the Patents Act, 1970, and his gross total income of the previous year includes royalty, subject to the provisions of this section. This deduction shall be available only to a resident individual who is registered as the true and first inventor in respect of an invention under the Patents Act, 1970, including the co-owner of the patent. The amount of

deduction is lower of 100% of such income or Rs. 300,000. In case, any such income is earned from any sources outside India, so much of the income, shall be taken into account for the purpose of this section as is brought into India by, or on behalf of, the assessee in convertible foreign exchange within a period of six months from the end of the previous year in which such income is earned or within such further period as the competent authority may allow in this behalf.

Provided that where a compulsory licence is granted in respect of any patent under the Patent Act, 1970, the income by way of royalty for the purpose of allowing deduction under this section shall not exceed the amount of royalty under the terms and conditions of a licence settled by the Controller under that Act:

No deduction under this section shall be allowed unless the assessee furnishes a certificate in the prescribed form (Form No. 10CCD), duly signed by the prescribed authority, along with the return of income setting forth such particulars as may be prescribed.

No deduction under this section shall be allowed in respect of any income earned from any source outside India, unless the assessee furnishes a certificate in the prescribed form (Form No. 10H), from the authority or authorities, as may be prescribed, along with the return of income.

**Explanation.** – For the purposes of this section, –

- (a) “Controller” shall have the meaning assigned to it in clause (b) of Sub-section (1) of Section 2 of the Patents Act, 1970;
- (b) “lump sum” includes an advance payment on account of such royalties which is not returnable;
- (c) “patent” means a patent (including a patent of addition) granted under the Patents Act, 1970;
- (d) “patentee” means the person, being the true and first inventor of the invention, whose name is entered on the patent register as the patentee, in accordance with the Patents Act, 1970, and includes every such person, being the true and first inventor of the invention, where more than one person is registered as patentee under that Act in respect of that patent;
- (e) “patent of addition” shall have the meaning assigned to it in clause (q) of Sub-section (1) of Section 2 of the Patents Act, 1970;
- (f) “patented article” and “patented process” shall have the meanings respectively assigned to them in clause (o) of Sub-section (1) of Section 2 of the Patents Act, 1970;
- (g) “royalty”, in respect of a patent, means consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head “Capital gains” or consideration for sale of product manufactured with the use of patented process or of the patented article for commercial use) for -
  - (i) the transfer of all or any rights (including the granting of a licence) in respect of a patent; or
  - (ii) the imparting of any information concerning the working of, or the use of, a patent; or
  - (iii) the use of any patent; or
  - (iv) the rendering of any services in connection with the activities referred to in Sub-clauses (i) to (iii);
- (h) “true and first inventor” shall have the meaning assigned to it in Clause (y) of Sub-section (1) of Section 2 of the Patents Act, 1970.

### **Deduction in respect of interest on deposits in Savings Account [Section 80TTA]**

Section 80TTA provides deduction to an assessee (other than referred to section 80TTB) individual or a Hindu undivided family whose gross total income includes any income by way of interest on deposits (not being time deposits) in a savings account with -

- (a) a banking company to which the Banking Regulation Act, 1949 (10 of 1949), applies (including any bank or banking institution referred to in section 51 of that Act);
- (b) a co-operative society engaged in carrying on the business of banking (including a co-operative land mortgage bank or a co-operative land development bank); or
- (c) a Post Office as defined in clause (k) of section 2 of the Indian Post Office Act, 1898 (6 of 1898)

The maximum amount of deduction is Rs. 10,000.

Further, where the income referred to in this section is derived from any deposit in a savings account held by, or on behalf of, a firm, an association of persons or a body of individuals, no deduction shall be allowed under this section in respect of such income in computing the total income of any partner of the firm or any member of the association or any individual of the body.

For the purposes of this section - "Time deposits" means the deposits repayable on expiry of fixed periods.

**Note :** Under Section 10(15) (i), post office savings bank interest is exempt up to Rs. 3,500.

#### **Deduction in respect of interest on deposits in case of senior citizens (Section 80TTB)**

Where the gross total income of a senior citizen (assessee) includes any income by way of interest on deposits with a banking company, a co-operative bank or Post Office, there shall be allowed a deduction:

- (i) in a case where the amount of such income does not exceed in the aggregate Rs. 50,000, the whole of such amount; and
- (ii) in any other case, Rs. 50,000.

No deduction shall be allowed if deposit held by or on behalf of a firm, an AOP or BOI

"senior citizen" means an individual resident in India who is of the age of sixty years or more at any time during the relevant previous year.

#### **Deduction in case of a Person with Disability [Section 80U]**

Section 80U provides deduction to a resident individual who suffers from 40% or more of any of the disabilities, namely, blindness, low vision, leprosy-cured, hearing impairment, locomotor disability, mental retardation and mental illness.

The amount of deduction is Rs. 75,000 (flat in case of disability) and Rs. 1, 25,000 (flat in case of severe disability, being disability of at least 80%). To claim deduction under this section, a certificate issued by the medical authority authority in the form and manner, as may be prescribed, to be a person with disability is required to be furnished along with the return of income under Section 139, in respect of the assessment year for which the deduction is claimed.

Provided that where the condition of disability requires reassessment of its extent after a period stipulated in the aforesaid certificate, no deduction under this section shall be allowed for any assessment year relating to any previous year beginning after the expiry of the previous year during which the aforesaid certificate of disability had expired, unless a new certificate is obtained from the medical authority in the form and manner, as may be prescribed, and a copy thereof is furnished along with the return of income under Section 139.

**Explanation** - For the purposes of this section, –

- (a) "disability" shall have the meaning assigned to it in clause (i) of Section 2 of the Persons with Disabilities (Equal Opportunities, Protection of Rights and Full Participation) Act, 1995 and includes "autism", "cerebral palsy" and "multiple disabilities" referred to in clauses (a), (c) and (h) of Section 2 of the

National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disabilities Act, 1999;

- (b) “medical authority” means the medical authority as referred to in clause (p) of Section 2 of the Persons with Disabilities (Equal Opportunities, Protection of Rights and Full Participation) Act, 1995, or such other medical authority as may, by notification, be specified by the Central Government for certifying “autism”, “cerebral palsy”, “multiple disabilities”, “person with disability” and “severe disability” referred to in clauses (a), (c), (h), (q) and (o) of Section 2 of the National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disabilities Act, 1999;
- (c) “person with disability” means a person referred to in clause (t) of Section 2 of the Persons with Disabilities (Equal Opportunities, Protection of Rights and Full Participation) Act, 1995, or clause (j) of Section 2 of the National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disabilities Act, 1999;
- (d) “Person with severe disability” means:
  - (i) a person with eighty per cent or more of one or more disabilities, as referred to in Sub-section (4) of Section 56 of the Persons with Disabilities (Equal Opportunities, Protection of Rights and Full Participation) Act, 1995; or
  - (ii) a person with severe disability referred to in clause (o) of Section 2 of the National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disabilities Act, 1999.

### **RELIEF AND REBATE IN RESPECT OF INCOME-TAX**

In addition to the provisions for aggregation discussed earlier, Section 66 lays down that in computing the total income of any assessee, there shall be included certain items of income on which no income-tax is payable under Chapter VII. Accordingly the provisions of Section 86 would be applicable.

### **SHARE OF MEMBER OF AN ASSOCIATION OF PERSONS OR BODY OF INDIVIDUALS IN THE INCOME OF THE ASSOCIATION OR BODY [SECTION 86]**

Section 86 provides that no income tax shall be payable by the assessee who is a member of an association of persons or body of individuals (other than, a company or a co-operative society or a society registered under the Societies Registration Act, 1860 or under any law corresponding to that Act in force in any part of India) in respect of his share in the income of such association or body computed in the manner provided in Section 67A of the Act.

Further, where the association or body is chargeable to tax at the maximum marginal rate or any higher rate under any of the provisions of this Act, the share of a member computed as aforesaid shall not be included in his total income. However, in any other case, the share of a member shall form part of his total income.

It is also provided that where no income-tax is chargeable on the total income of the association or body. The share of a member computed as aforesaid shall be chargeable to tax as part of his total income and nothing contained in this section shall apply to the case.

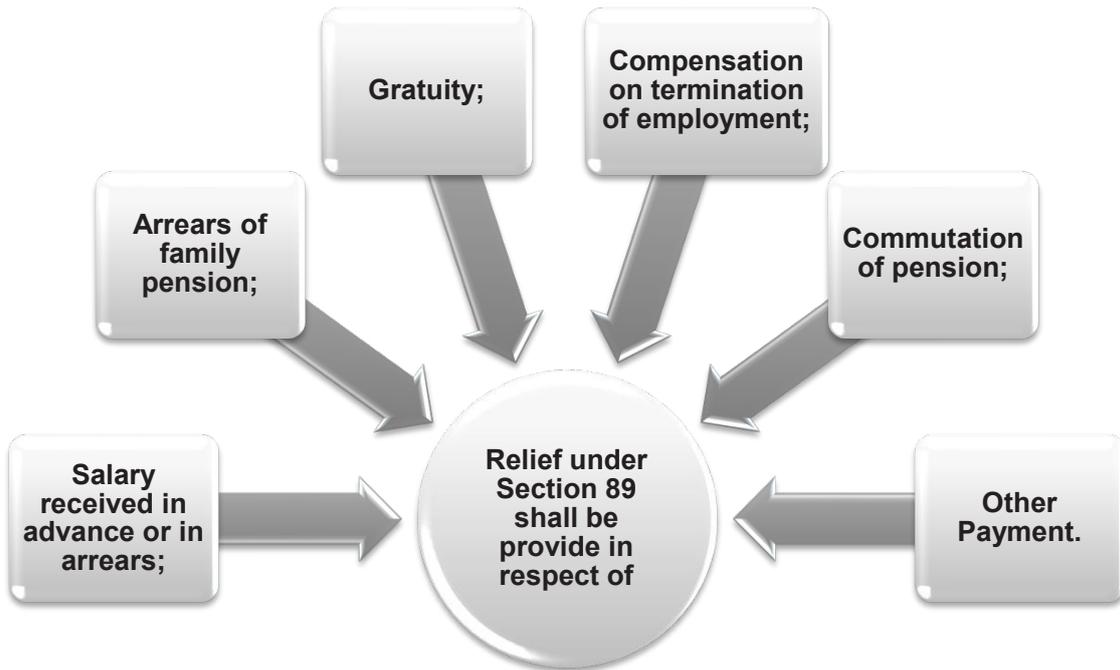
### **REBATE OF INCOME-TAX IN CASE OF CERTAIN INDIVIDUALS [SECTION 87A]**

Section 87A provides rebate of income tax to resident individual, whose total income does not exceed Rs. 5,00,000. The amount of rebate is Rs 12,500 or 100% of income tax whichever is less. It is deductible from income tax before calculating health & education cess.

### **RELIEF WHEN SALARY IS PAID IN ARREARS OR IN ADVANCE [SECTION 89]**

Section 89 provides relief to an individual who receives any portion of his salary in arrears or in advance or

receives profit in lieu of salary during the previous year. The assessee may apply to the Assessing Officer who is been empowered to grant relief in appropriate cases in accordance with Rule 21AA of the Income-tax Rules, 1962. However, no such relief shall be granted in respect of any amount received or receivable by an assessee on his voluntary retirement or termination of his service, in accordance with any scheme or schemes of voluntary retirement or in the case of a public sector company referred to in sub clause (i) of clause (10C) of section 10, a scheme of voluntary separation, if an exemption in respect of any amount received or receivable on such voluntary retirement or termination of his service or voluntary separation has been claimed by the assessee under clause (10C) of section 10 in respect of such, or any other, assessment year.



**Illustration**

Mr. Ram who is a person with disability submit the following information. Compute (a) the Taxable Income (b) the Tax Payable for the assessment year 2020-2021.

(i) Salary (per annum)	3,00,000
(ii) Rent received	48,000
(iii) Dividend from Co-operative Society	1,000
(iv) Interest on Savings Bank Deposits	18,000
(v) Interest on Government securities	1,000
(vi) Winning from Lotteries (gross)	5,000
(vii) NSC (VIII Issue) purchased during the year	10,000
(viii) Deposit under PPF Scheme	30,000

He earned a long-term capital gain of Rs. 15,000 on sale of gold during the year

**350 EP-TL**

**Solution**

(A) Computation of Total Income	Rs.	
Income from Basic Salary		3,00,000
Less : Deduction under section 16(ja) – Standard Deduction		<u>(50,000)</u>
		<u>2,50,000</u>
<i>Income from house property</i>		
Rent Received	48,000	
Less : Statutory Deduction @ 30%	(14,400)	33,600
<i>Capital Gains</i>		
Long-term capital gains		15,000
<i>Income from other sources</i>		
Dividend from co-operative society	1,000	
Interest on saving bank deposits	18,000	
Interest on Government Securities	1,000	
Winning from Lotteries	5,000	25,000
Gross Total Income		3,23,600
Less : Deduction under section 80C to 80U		
(i) Under section 80C Rs. (10,000 + 30,000)	(40,000)	
(ii) Under section 80TTA	(10,000)	
(iii) Under section 80U	(50,000)	(1,00,000)
Total Income		2,23,600
 (B) Computation of tax on Total Income		
Tax on winning from lotteries (30% of Rs.5,000)		1,500
Tax on long-term capital gains (20% of Rs.15,000)		3,000
Balance of Total Income Rs.2,03,600		Nil
Tax Payable, bring total income below Rs. 2,50,000		Nil

**Illustration**

Rahul who is a resident in India, is a person with disability. He provides the following particulars of his income for the year ended 31.3.2020.

(a) Salary for working as a cable operator (per month)	18,000
(b) Interest on government securities (gross)	45,000
(c) Dividend from Indian Company	5,000
(d) Honorarium from school of orphanage for giving his service	49,000

He has donated Rs. 20,000 to the school for orphanage which is approved as a charitable institution and contributed Rs. 2,000 to Prime Minister National Relief Fund. He has also paid Rs.3,000 by credit card as premium of mediclaim policy. His father is also a person with disability and is dependent on him for medical treatment and rehabilitation. Rahul spends Rs. 8,000 during the year on him.

Compute the Total Income for the Assessment Year 2020-21, assuming he has deposited Rs. 20,000 in Public Provident Fund Account.

**Solution** Computation of Total Income for the Assessment Year 2019-20

	Rs.	Rs.
Income from salary		
Gross Salary	2,16,000	
<i>Less:</i> Deduction (Standard)	50,000	1,66,000
<i>Income from other sources</i>		
Interest on Government Securities	45,000	
Dividend from Indian Company	Exempt	
Honorarium	49,000	94,000
Gross Total Income		2,60,000
<i>Less : Deductions:</i>		
Under section 80C	20,000	
(ii) Under section 80D	3,000	
(iii) Under section 80DD	75,000	
(iv) Under section 80U	75,000	
(v) Under section 80G		
Prime Minister Relief Fund (100%of Rs. 2,000)	2,000	
Orphanage School (50% of Rs. 8,700)		
10% of 87,000 Rs. (2,60,000 - 1,73,000)	4,350	6,350
Total Income		80,650

**Illustration**

Following are the particulars of income of Mr. Ram, who is 70 years old resident in India, for the Assessment year 2020-21:

Gross Total Income Rs. 8,10,040 which includes long-term capital gain of Rs. 2,55,000, Short-term capital gain of Rs. 88,000, interest income of Rs. 12,000 from savings bank deposits with banks. Mr. Ram invested in PPF Rs. 1,40,000 and also paid a medical insurance premium Rs. 31,000. Compute the total income of Mr. Ram.

**Solution** Computation of Total Income for the Assessment Year 2020-21

	Rs.
Gross total income	8,10,040
<i>Less:</i> Deductions:	
Under section 80C	1,40,000
Undersection80D	31,000

Undersection80TTA	10,000
Total income	6,29,040

### CASE LAW

#### **1. F&O Transaction carried out through recognized Stock Exchange is not Speculative Transaction can be set off against Ordinary Business Income:**

The Ahmedabad bench of Income Tax Appellate Tribunal recently ruled that the future and option transaction carried out through recognized stock exchange cannot be treated as speculative transaction, can be set off against ordinary business income.

The assessee raised the ground of appeal that CIT(A) has erred in not allowing set off of loss of Rs.3,19,071/- being loss on trading of shares/securities against other business income.

The assessee in the instant case has started trading activities in shares, filed a copy of bank statement and ledger account of M/s. Marfatia Stock Brokings P.Ltd wherein AO held that the loss shown by the assessee as speculative loss and observed that since the assessee has no speculative profit, therefore, he has neither entitled to claim set off nor to claim carry forward.

Dissatisfied with this finding of the AO, the assessee carried the matter in appeal before the CIT (A). On appeal, the CIT (A) and confirmed the order of the AO.

Aggrieved, assessee went in appeal before the tribunal challenging the order of lower authority. The counsel for the assessee submits that loss from F&O carried out through recognized stock exchange cannot be treated as speculative transaction.

After considering the arguments from both sides and identical case laws, the judicial member found that in the assessment order, the AO has observed that return was filed on 4.6.2008 and not 4.8.2008. it was noted that the second aspect is whether the loss from F&O could be considered as speculative loss, has been considered by the Tribunal in the case of Babubhai Ramanlal Patel (supra).

In that case, it was found that the loss from F&O business carried out through recognized stock exchange cannot be treated as speculative loss in view of the exceptions carried out under section 43(5) of the Income Tax Act. Thus the loss arising out from the trading in derivatives must be considered as ordinary business loss.

### LESSON ROUND UP

- Section 80C: Deduction on life insurance premia, contribution to provident fund, etc - Available to individual/HUF for a maximum amount of Rs.1,50,000.
- Section 80CCC: Deduction for contribution to pension fund - Available to individual for maximum amount of Rs.150,000.
- Section 80CCD: Deduction in respect of contribution to pension scheme of Central Government- available to individual.
- Section 80CCE: Limit on deductions under Sections 80C, 80CCC and 80CCD - can not exceed Rs.1,50,000. Additional deduction allowed under section 80CCD(1B) of maximum Rs. 50,000.
- Section 80CCG: Deduction in respect of investment made under any equity saving scheme : Available to resident individual subject to maximum of Rs. 25,000.

- Section 80D: Deduction in respect of medical insurance premia - Available to individual/HUF.
- Section 80DD: Deduction in respect of maintenance including medical treatment of a dependant who is a person with disability or severe disability.
- Section 80DDB read with Rule 11DD: Deduction in respect of medical treatment, etc.: Available to Resident individual/resident HUF.
- Section 80E: Deduction in respect of repayment of loan taken for higher education: Available to individual.
- Section 80G: Deduction in respect of donations to certain funds, charitable institutions, etc. Available to all assessees subject to maximum of 50% of qualifying amount, 100% as the case may be.
- Section 80GG: Deduction in respect of rent paid Available to individual for a maximum of Rs. 60,000.
- Section 80GGA: Deduction in respect of certain donations for scientific research or rural development
- Section 80GGB: Deduction in respect of contributions given by companies to political parties
- Section 80GGC: Deduction in respect of contributions given by any person to political parties
- Section 80-IA: Deduction in respect of profits and gains from industrial undertakings or enterprise engaged in infrastructure development
- Section 80-IAB: Deduction in respect of profit and gains by an undertaking a enterprise engaged in development of Special Economic Zone
- Section 80IAC: Deduction in respect of Eligible start-up
- Section 80-IB: Deduction in respect of profits and gains from certain industrial undertakings other than infrastructure development undertakings
- Section 80IBA: Deductions in respect of profits and gains from housing projects
- Section 80-IC: Special provisions in respect of certain undertakings or enterprises in certain special category States
- Section 80-JJA: Deduction in respect of profits and gains from the business of collecting and processing bio-degradable waste - Available to all assessees carrying on the business of collecting and processing bio-degradable waste.
- Section 80-JJA: Deduction in respect of employment of new workmen - Available to Indian company of 30% of additional wages paid to new regular workmen.
- Section 80LA: Deduction in respect of certain incomes of Offshore Banking Units - 100% of certain income for 5 years, 50% of such income for 5 years.
- Section 80P: Deduction in respect of income of co-operative societies - Specified incomes subject to amount specified in sub section (2).
- Section 80PA: Deduction of specified income of producer company.
- Section 80QQB: Deduction in respect of royalty income, etc., of authors of certain books other than text books - Available to resident individual, for a maximum deduction of Rs. 3,00,000.
- Section 80RRB: Deduction in respect of royalty on patents - Available to Resident Individual, maximum of Rs. 3,00,000.
- Section 80TTA: Deduction in respect of interest on deposits in savings account - Available to Individual/HUF upto Rs. 10,000.

- Section 80TTB: Deduction on time deposit - To senior citizen upto Rs. 50,000.
- Section 80U: Deduction in case of a person with disability - Available to Resident individual subject to maximum of Rs. 125,000

### SELF TEST QUESTIONS

*These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation.*

#### Multiple Choice Questions “MCQs”

1. Deduction u/s 80C, in respect of Life Insurance Premium, Contribution to Provident Fund etc., is allowed to?
  - a) Any assessee
  - b) An individual
  - c) An individual / HUF
  - d) An individual / HUF who is resident in India

Answer: (d)

2. The flat amount of deduction under section 80U is -
  - a) Rs.50,000 and Rs.75,000
  - b) Rs.75,000 and Rs. 1,00,000
  - c) Rs.75,000 and Rs. 1,10,000
  - d) Rs.75,000 and Rs. 1,25,000

Answer: (d)

3. Which of the following is covered under section 80D of the Income Tax Act, 1961 –
  - a) Repayment of loan taken for higher education
  - b) Medical treatment of handicapped dependent
  - c) Medical Insurance Premium
  - d) Reimbursement of medical expenses

Answer: (c)

4. Deduction under section 80E can be claimed for interest on loan for
  - a) Any course of higher education
  - b) Only post graduate courses
  - c) Only graduate courses
  - d) Any course of study after passing the Senior Secondary Examination or its equivalent from any recognised school, board or university

Answer: (d)

5. Maximum qualifying limit for deduction under section 80C is -





# Lesson 7

## Computation of Total Income and Tax Liability of various entities

### LESSON OUTLINE

- Introduction
- Taxation of Individuals
- Taxation of Hindu Undivided Families
- Computation of Income of the HUF
- Taxation of Firms
- Alternate Minimum Tax
- Taxation of Association of Persons/Body of Individual
- Taxation of Co-Operative Societies
- Political Parties
- Electoral Trusts
- Exempt organization – Registration u/s 12A/12AA
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

In this lesson the Income Tax Treatment with relation to Individual, Hindu Undivided Families (HUF), Firms, Associations of Persons and Cooperative Societies is being discussed. The tax implications, rates of tax and other issues relating to the above persons have been discussed elaboratory.

At the end of this lesson, you will learn

- Computation of taxation of Individuals
- What is a HUF, how it comes into existence
- When and how it can be partitioned and What are the tax implications before and after its partition.
- What is partnership firm
- What are the tax implications in the hands of partners and firm
- What are admissible expenses/inadmissible expenses while calculating the book profit of the firm.
- What are the provisions of Alternate Minimum Tax
- How Association of persons is formed
- What is the method of computation of share of a member of AOP.
- What are Co-operative Societies
- How the tax liability of Cooperative societies determined.
- Provision related to Political Parties;
- Provision related to Electoral Trusts;
- Exempt organization – Registration u/s 12A/ 12AA;

## INTRODUCTION

Income tax is a charge on the assessee's income. Income Tax law lays down the provisions for computing the taxable income on which tax is to be charged. Taxable income of an assessee shall be calculated in the following manner :

1. Determine the residential status of the person as per section 6 of the Act.
2. Calculate the income as per the provisions of respective heads of income. Section 14 classifies the income under five heads.
  - (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
3. Consider all the deductions and allowances given under the respective heads before arriving at the net under each head.
4. Exclude the income exempt under section 10 of the Act.
5. Aggregate of incomes computed under the 5 heads of income after applying clubbing provisions and making adjustments of set off and carry forward of losses is known as Gross Total Income.
6. Deduct therefrom the deductions admissible under Sections 80C to 80U. The balance is called Total income.
7. The total income is rounded off to the nearest multiple of Rupees ten. (Section 288A)
8. Add agriculture income (if any) in the total income calculated in (6) above. Then calculate tax on the aggregate as if such aggregate income is the Total Income.
9. Calculate income tax on the net agricultural income as increased by Rs. 2,50,000/3,00,000/5,00,000 as the case may be, as if such increased net agricultural income were the total income.
10. The amount of income tax determined under (9) above will be deducted from the amount of income tax determined under (8) above.
11. Calculate income tax on capital gains under Section 112, 112A, 111A and on other income at specified rates.
12. The balance of amount of income tax left as per (10) above plus the amount of income tax at (11) above will be the income tax in respect of the total income.
13. Deduct the following from the amount of tax calculated under (12) above.
  - Rebate under section 87A (if applicable).
  - Tax deducted and collected at source.
  - Advance tax paid.
  - Double taxation relief (Section 90 or 91).
14. The balance of amount left after deduction of items given in (13) above, shall be the net tax payable or net tax refundable for the assessee. Net tax payable/refundable shall be rounded off to the nearest multiple of Ten rupees (Section 288B).

15. Along with the amount of net tax payable, the assessee shall have to pay penalties or fines, if any, imposed on him under the Income-tax Act.

For calculation of income, amount received is classified under 5 heads of income; it is then to be adjusted with reference to the provisions of the Income Tax laws in the following manner.

Computation of Tax Liability	Sections	Amount
<b>1. Income from Salary</b> <i>Less</i> : Deductions U/s 16 i-a. Standard Deduction of Rs. 50,000 or Gross Salary, whichever is lower. ii. Entertainment Allowance iii. Professional Tax Paid	15 to 17	XXX
<b>2. Income from House property</b> <i>Less</i> : Deduction U/s 24 Standard Deduction Interest on House Property Loan	22 to 27	XXX
<b>3. Income from Profits and gains from business and profession</b>	28 to 44	XXX
<b>4. Income from Capital Gains</b> <i>Less</i> : Deduction U/s 54	45 to 55A	XXX
<b>5. Income from Other Sources</b>	56 to 59	XXX
<b>Add/Less : Apply Clubbing and Set Off &amp; Carry Forward Provisions</b>		
<b>Gross Total Income [GTI]</b>		<b>XXX</b>
<i>Less</i> : Deductions under Chapter VIA	80C to 80U	( XXX )
<b>TOTAL INCOME</b> (Rounded off to nearest Rs.10 U/s 288A)		<b>XXX</b>
<b>Tax on Total Income</b>		XXX
<b>Add : Surcharge</b> on Total Tax (if applicable)		XXX
<b>Less : Rebate U/s 87A</b>		(XXX)
<b>Add</b> : 4% Health & Education Cess on [Total tax + Surcharge – Rebate]		XXX
<b>Net Tax Liability</b>		XXX
<i>Less</i> : (i). TDS (ii). Advance Tax (iii). Relief u/s 89		(XXX)
<b>Balance tax payable on Self Assessment U/s 140A</b>		XXX
<i>Less</i> : Self Assessment tax paid		XXX
Balance Tax		<b>NIL</b>

## TAXATION OF INDIVIDUALS

### Illustration 1:

Gross total Income of Mr. X, a tax consultant based at Mumbai, is Rs. 18,00,000 (income from profession

**360 EP-TL**

Rs. 17,00,000 and interest on bank deposit Rs. 1,00,000). He pays Rs. 3,00,000 as house rent. He deposits Rs. 50,000 in public provident fund. Compute his taxable income for the assessment year 2020-21.

**Answer**

**Computation of taxable Income of Mr. X for the A.Y 2020-21**

<i>Particular</i>		<i>Amount (Rs.)</i>
Professional Income – PGBP		17,00,000
Interest on Bank Deposit – Other sources		1,00,000
Gross Total Income		18,00,000
<i>Less: Deductions under Chapter VI-A</i>		
u/s 80C (PPF)	50,000	
u/s 80 GG (Note-1)	60,000	
		(1,10,000)
<b>Total Income</b>		<b>16,90,000</b>

Note 1: Deduction u/s 80GG is least of the following:

- a) Rs. 60,000 (i.e. Rs. 5000 x 12 months)
- b) Rs. 4,37,500 [25% of total income (Rs. 18,00,000- 50,000)]
- c) Rs. 1,25,000 (Excess of rent paid over 10% of total income (Rs. 3,00,000- 1,75,000))

**Illustration 2:**

From the following profit and loss account of Vinay for the year ended 31st March, 2020, compute his total income and tax liability for the assessment year: 2020-21:

<i>Particulars</i>	<i>Amount Rs.</i>	<i>Particulars</i>	<i>Amount Rs.</i>
Interest on capital	12,000	Gross profit	5,10,000
Insurance	2,000	Brokerage	30,000
Bad debts	30,000	Bad debts recovered (earlier allowed as deduction)	15,000
Depreciation	34,000	Sundry receipts	18,000
Advance tax	25,000	Interest on debentures (gross) [TDS Rs. 4,120]	40,000
General expenses	12,000		
Advertisement	5,000		
Salary (including salary to Vinay Rs.20,000)	85,000		
Interest on loan	8,000		
Net profit	4,00,000		
<b>Total</b>	<b>6,13,000</b>	<b>Total</b>	<b>6,13,000</b>

Additional information:

- (i) The amount of depreciation allowable as per income-tax rules is Rs. 42,000.
- (ii) General expenses include Rs.5,000 given as Health insurance Premium.
- (iii) Vinay pays Rs. 5,200 as premium on his own life insurance policy of Rs. 50,000 issued in 2016-17.
- (iv) Loan was obtained for payment of income-tax.

**Solution**

<b>Particulars</b>	<b>Amount (Rs.)</b>	<b>Amount (Rs.)</b>
(I) Income from business		
Net profit for the year		4,00,000
<i>Add</i> : Expenses not allowed under Income tax act but debited to P & L A/C		
Interest on capital (Note 2)	12,000	
Depreciation as per books of a/c	34,000	
Advance tax	25,000	
General Expenses	5,000	
Salary to Vinay	20,000	
Interest on loan (Note 2)	8,000	1,04,000
<i>Less</i> : Income not related to business and profession but Credited to P& L a/c		
Interest on debentures	40,000	
Deductible expenses not debited to P&L Account		
Depreciation as per Income tax Act	42,000	(82,000)
Profits and Gains of Business & Profession		4,22,000
(II) Income from other sources Interest on debenture		40,000
Gross total income (I + II)		4,62,000
<i>Less</i> : Deduction U/S 80C – 80U		
(i) Premium on life insurance policy (u/s 80C)(Note 1)		(5,000)
(ii) Health insurance Premium (u/s 80 D )		(5,000)
Total Taxable Income		4,52,000

**Note**

1. Under section 80C deduction of life insurance premium cannot exceed 10% of the sum assured.
2. Under Section 36(1)(iii) Interest paid on borrowed capital is allowed as a deduction. Interest on own capital is not deductible. Similarly, interest on money borrowed to pay income tax is not allowed as a deduction.

**Illustration 3:**

For the Assessment year 2020-21, Mr. Ram, who is 58 years old, resident in India, furnishes the following information:

Basic salary	Rs. 15000 pm
Dearness Allowance (20% forming part for retirement benefits)	40% of basic salary

City Compensatory Allowance	Rs. 300 pm
Children education allowance	Rs. 200 pm per child for 2 children
Transport allowance	Rs. 2000 pm
House Rent Allowance	Rs. 6000 pm
Actual rent paid for a house in Delhi	Rs. 7000 pm
He travels via Delhi metro from his residence to office and back in which he spends	Rs. 1500 pm.
Medical allowance	Rs. 1000 pm
Lunch allowance	Rs. 200 pm

He owns a house property in Mumbai whose construction is completed in 2005 and which is let out for Rs. 40,000 pm. The standard rent as per Rent Control Act is Rs. 3, 10,000. He pays Rs. 32,000 for municipal taxes and interest on capital borrowed for construction of house Rs. 75,000. Further, he incurs Rs. 10,000 on repairs of the house.

Long-term capital gains Rs. 225,000

Short term capital gains for the year Rs.1,01,000 (STT not applicable).

Dividend received from Indian Company X Ltd. Rs. 12,000.

Interest received @10% on listed debentures of face value 14,00,000

Diwali Gift of gold coins received from a friend. Market value Rs. 50,000

Share of profit from:

A Firm	40,000
HUF	34,000
Income from Lotteries (gross)	50,000

Mr. Ram invested in PPF Rs.1,50,000 and also paid a life insurance premium of Rs. 21,000. Donation to National Defence Fund Rs.10,000

Compute the total income and Tax liability of Mr. Ram for the Assessment year 2020-21.

### Solution

#### (A) Computation of Total Income

Income from salary	Rs.	Rs.
Basic salary (15000 *12)		180,000
Dearness Allowance (180,000*0.40)		72,000
CCA (fully taxable) (300*12)		3600
Children Education Allowance	4800	
Less: Exempt	2400	2400
Transport allowance	24000	

Less: Exempt (Exemption withdrawn by Finance Act, 2018)	NIL	24000
House Rent Allowance (Note)		7440
Lunch Allowance		2400
Medical Allowance		12000
Less: Deduction under section 16 (ia) Standard Deduction		(50,000)
<b>Taxable Salary</b>		<b>2,53,840</b>
<i>Income from house property</i>		
Gross annual Value (Rent Received 40,000*12)		4,80,000
Less: Municipal Taxes		(32,000)
Net annual Value		4,48,000
Less: Standard Deduction @ 30% of 4,48, 000		(1,34,400)
Less: Interest on capital borrowed		(75,000)
<b>Income from House property</b>		<b>2,38,600</b>
Income from Business/Profession		
A Firm (Exempt)		NIL
HUF (Exempt)		NIL
Income under the head Capital Gains		
<b>Long-term capital gains u/s 112</b>		<b>2,25,000</b>
<b>Short term Capital Gain u/s 111A</b>		<b>1,01,000</b>
Income from other sources		
Dividend received from Indian Company X Ltd. (Exempt)		NIL
Interest received on listed debentures		1,40,000
Winning from Lotteries		50,000
Gift in kind	50,000	240,000
<b>Gross Total Income</b>		<b>10,58,440</b>
Less: Deduction under section 80C to 80U		
(i) Under section 80C(maximum)		(150,000)
(ii) Under section 80G		(10,000)
<b>Total Income</b>		<b>8,98,440</b>

**(B) Computation of tax on Total Income**

Tax on winning from lotteries (30% of Rs. 50,000)	15,000
Tax on long-term capital gains (20% of Rs. 2,25,000)	45000

Balance of Total Income Rs. 6,33,440	37,188
Total tax	97,188
Add: Health and Education cess at 4%	3,888
Total liability	1,01,076
Total liability (round off)	1,01,080

Notes:

1. House Rent Allowance: Least of three is exempt

i. 50% of the salary\* because the house is in Delhi =  $0.50 * 194400 = \text{Rs. } 97,200$

ii. HRA received = Rs. 72,000

iii. Rent paid – 10% of the salary =  $(7000 * 12) - 0.10 * 194400 = 84000 - 19440 = \text{Rs. } 64,560$

Exempted HRA = Rs. 64,560

Taxable HRA =  $72,000 - 64,560 = \text{Rs. } 7,440$

\*Salary here = Basic salary + Dearness allowance (forming part only) =  $180,000 + 180000 * 0.40 * 0.20 = \text{Rs. } 1,94,400$

2. The tax liability is subject to set-off of TDS for winning from lotteries and interest from listed debentures.

#### Illustration 4:

Mr. X aged 62 years, resident individual furnishes the following particulars relevant for the assessment year 2020-21:

Profit and Loss Account			
Particulars	Amount (Rs.)	Particulars	Amount(Rs.)
Salaries	30000	Gross profit	436000
General Expenses	45000	Commission	120000
Bad Debts	15000	Sundry Receipts	40000
Reserve for losses	3000	Short term capital gain	30000
Insurance	5200	Discount	2000
Advertisement 10000		Profit on sale of import license	100000
Add: outstanding 2000	12000		
Interest on capital	4500		
Interest on bank loan	12500		
Expenditure on acquisition of patent and put to use on 30.06.17	16000		
Depreciation on Plant	24000		
Depreciation on building	10000		
Depreciation on Furniture	4000		

Provision for outstanding GST liability	12000		
Taxation reserve	12000		
Loss by fire of a part of building(Uninsured)	8000		
Net profit	514800		
<b>Total</b>	<b>728000</b>	<b>Total</b>	<b>728000</b>

**Other information**

1. Bank loan is used for business purposes.
2. The amount of depreciation as per tax rates, in respect of plant, building, furniture, amounts to Rs. 20000, 12000, 7400 respectively.
3. Salary include payment to a relative which is unreasonable to the extent of Rs. 5000.
4. Out of GST liability Rs. 2000 is paid on 04.07.20 and Rs. 6000 is paid on 03.10.20. The balance is still outstanding. Due date of filling the return of income is 31.7.20
5. Income of X from other sources is Rs. 24000.
6. X paid medical insurance premium Rs. 16000 for himself and Rs. 16000 for his mother (dependent)
7. X repaid housing loan to the extent of Rs. 45000.

Determine the taxable income and tax liability of Mr. X for the assessment year 2020-21 assuming STT is not applicable on STCG.

**Solution:**

**Computation of total income of Mr. X for the AY 2020-21**

Particular	Rs.
Profit and gain from business profession (Note)	537900
Income under the head capital gain [STCG]	30000
Income from other sources	24000
Gross total income	591900
Less: Deduction u/s 80	
80C Repayment of housing loan	(45000)
80D Medical insurance premium	(32000)
<b>Taxable Income</b>	<b>514900</b>

**Computation of Tax on Total Income**

Tax on Rs. 300000	Nil
Tax on Rs. 200000 @ 5%	10000
Balance of Total Income 14900 @ 20%	2980
Total tax	12980
Add: Health and Education cess at 4%	519.2
Total liability	13499.2
Total liability (round off)	13,500

**Working Note:****Calculation of Business Income**

<i>Particular</i>	<i>Rs.</i>
Profit as per P&L A/C	514800
<i>Add: Inadmissible Expenses</i>	
Reserve for losses	3000
Interest on capital	4500
Patent right [16000- 25% of 16000]	12000
Excess salary paid to relative	5000
Outstanding GST liability [12000-2000]	10000
Taxation reserve	12000
Loss by fire of part of building	8000
<i>Less : Admissible Expenses</i>	
Depreciation [39400-38000]	(1400)
<i>Less : Income taxable under head capital gain</i>	
STCG	(30000)
<b>Business Income</b>	<b>537900</b>

**TAXATION OF HINDU UNDIVIDED FAMILIES**

The term 'Hindu undivided family' has not been defined in the Income-tax Act but it is treated as a separate entity or person under section 2(31) of the Income-tax Act, 1961 for the purpose of assessment under the Act. Under Hindu Law, an HUF is a family which consists of all persons lineally descended from a common ancestor and includes their wives and unmarried daughters. Jain and Sikh families even though are not governed by the Hindu Law, but they are treated as HUF under the Act. An HUF cannot be created under a contract and is created automatically in a Hindu Family. Creation of a HUF is a God-gifted phenomenon since birth of a child to a married Hindu, automatically creates a new HUF. It is not at all necessary that every HUF must have joint property or family income. [*R. Subramania Iyer v. CIT (1955) 28, ITR, 352*]. However, to become an assessee under the Income-tax Act, there must be 'income-yielding' joint property of the family.

A HUF may consist of a number of smaller HUFs. A smaller HUF has a legal existence and may be assessable as a unit distinct from the apex joint family even when the bigger HUF is in place [*CIT v. Khanna (1963) 49 ITR 232*].

The Supreme Court's decision in the case of *Surjit Lal Chhabra v. CIT (1975 101 ITR 776)* has come to stay as one of the leading case laws. The ratio laid down by the Supreme Court had been applied by the Andhra Pradesh, Orissa and Madras High Courts, followed by Bombay, Patna, Madhya Pradesh and Delhi High Courts and relied upon by the Punjab High Court. In the latest case, the Delhi High Court held in *Commissioner of Income-tax v. S.P Chopra (1991, 191 ITR 455)* that the income from the half share of the property had to be treated as the individual income of the assessee under the personal law and not as income of the family. The character of the property had to be determined in accordance with the personal law of the assessee and not on the basis of how the property had been treated by the revenue in respect of earlier assessments.

A son conceived or in his mother's womb is equal in many respects to a son actually in existence, viz., inheritance, partition, survivorship etc. But this doctrine does not apply to the Income-tax Act. Hence, a son conceived is not treated a member of the H.U.F. for Income-tax purposes. [*S. Srinivasan v. C.I.T.*, (1966) 60, ITR, p.36 (S.C.)].

Jain and Sikh undivided families are also treated as Hindu undivided families unless, under special circumstances, the assessee claims not to be treated as such. If such claim is made, the assessee shall have to prove that there is some such custom in his family on account of which it cannot be treated as a Hindu undivided family.

A Hindu does not cease to be a Hindu merely because he declared for the purpose of the Special Marriage Act, 1872, that he does not profess Hindu Religion. Such a Hindu does form an H.U.F. with his children from such marriage. [*CIT v. Partap Chand* (1959), 36 ITR, 262]. Similarly, a Muslim family governed by the Marumakkathayam law constitutes 'Tarwad' or 'Thavazhi' and falls within the definition of a H.U.F. [*V.K.P. Abdul Kadar Haji v. Ag. ITO* (1967) 66, ITR, 173].

If a Hindu gets converted as a Christian, the family of such a person will not be a HUF. However a Hindu, along with his son (by a christian wife) who has been brought up as a Hindu will be a HUF. [*CWT v. R. Sridharan* (1976) 104, ITR, 436 (S.C.)].

**A Hindu Joint Family consists of two types of members:**

1. **Coparceners:** The lineal male descendants of a person up to the third generation of such person are known as coparceners. The coparceners acquire, on birth, ownership in the ancestral properties of such ascendant and have a right to claim partition of such property at any time. However, w.e.f. 9.9.2005 due to amendment of Hindu Succession Act, the daughter of a coparcener shall by birth become a coparcener in her own right in the same manner as the son. Hence, the daughter can also ask for partition.
2. **Other members:** Such members include wives of male members of the family and other male members. Widow or widows of deceased male member or members. [*Gowli Buddanna v. C.I.T.* (1966) 60, ITR, p. 293 (S.C.)]

However, an unmarried coparcener who receives share on the partition of joint family properties, cannot form a Hindu undivided family unless he marries. After his marriage, he can hold the property received from family as joint family property consisting of himself and his wife. [*C. Krishna Prasad v. C.I.T.* (1974) 97, p. 493 (S.C.)].

**The joint property of the HUF is managed through Karta:** Property of the family is ordinarily managed by the father or other senior member for the time being of the family. He is called Karta. However, the senior member may give up his right of management and a junior member may be appointed as Karta with the consent of all other members. [*Narendra Kumar J. Modi v. CIT* (1976) 105, ITR, 109 (S.C.)]. In the absence of a male member in the family or when all male members are minors, a woman member can be treated as manager of the family for income-tax purposes. [*Smt. Champa Kumari Singhi v. Addl. Member of the Board of Revenue* (1962) 46, ITR, p. 81].

**School of Hindu Law :** According to Hindu Law, HUFs are governed by two schools viz. Mitakshara and Dayabhaga.

Mitakshara School applies to whole of India except the states of West Bengal and Assam.

Dayabhaga school applies to the States of West Bengal and Assam. The difference between the two schools is as under:

- (i) **Foundation:** In the Mitakshara School, the foundation of a coparcenary is laid down when a child is born to the Mitakshara father. Under the Dayabhaga school the foundation of a coparcenary is laid on the death of the father leaving, as survivors, one or more sons.
- (ii) **Right to partition:** A Mitakshara son, in whom the interest in family property is vested by birth, all along possesses a right to demand partition. A Dayabhaga son, on the other hand acquires no interest in the

family property by birth and, consequently, has no right to demand partition of the HUF property from his father.

- (iii) **Quantum of share:** Under Mitakshara Law, each coparcener takes as undefined share in the coparcenary property. The share of the members decreases by birth in the family and increases upon death of a coparcener. A Dayabhaga coparcener, on the other hand, always takes a defined share in the property left by his deceased father. Thus, the heirs of a deceased governed by the Dayabhaga school do not constitute a HUF automatically on the death of the deceased and cannot be assessed as a HUF unless they have by mutual consent agreed to form a joint family.
- (iv) **Gift out of ancestral property:** A Mitakshara Karta may make a gift of movable property of the family, out of love and affection, within reasonable limits. He can also make a gift of immovable properties, within reasonable limits for pious purposes; i.e., for charitable and religious purposes or to a daughter in fulfilment of a nuptial promise etc. However, a gift to a stranger is void. On the contrary, a Dayabhaga father can alienate ancestral property, both movable as well as immovable, by sale, gift, will or otherwise in the same way as he can dispose of his separate property.

### Position under Hindu Succession Act, 1956

This Act came into force on and from 17th June, 1956. It lays down a uniform and comprehensive system of inheritance and applies to persons governed by the Mitakshara as well as the Dayabhaga Schools, superseding and abrogating all previous law or customs or usage having the force of law.

Under this Act, the heirs of a male Hindu dying intestate on or after 17th June, 1956 are divided into three classes. Class I heirs get the right to the deceased's property simultaneously to the exclusion of all other Classes of heirs. Class II relations succeed only if there is no class I relation and, the heirs in the first entry of class II being preferred to heirs in the second entry, and so on, but heirs in any one entry taking in equal shares amongst themselves.

The students should note that Section 4 of the Hindu Succession Act, 1956 clearly lays down that "save as otherwise expressly provided in the Act, any text, rule or interpretation of Hindu Law or any custom or usage as part of that law in force immediately before the commencement of the Act shall cease to have effect with respect to any matter for which provision is made in the Act." And, Section 8 of the Hindu Succession Act, 1956, lays down the scheme of succession to the property of a Hindu dying intestate. The schedule classifies the heirs on which such property shall devolve.

The preferential heirs of class I are as under:

(1) Son (2) Daughter (3) Widow (4) Mother (5) Son/daughter/widow of a predeceased son (6) son/daughter of a predeceased daughter (7) Son/daughter/ widow of a predeceased son of a predeceased son.

A son's son is not mentioned as an heir under Class I of the schedule and, therefore, he cannot get any right in the property of his grandfather under the provision. The right of a son's son in his grandfather's property during the lifetime of his father which existed under the Hindu Law as in force before the Act, is not saved expressly by the Act and, therefore the earlier interpretation of Hindu Law giving a right by birth in such property 'ceased to have effect'.

Therefore, the property which devolves on a Hindu on the death of his father intestate after coming into force of the Hindu Succession Act, 1956, does not constitute H.U.F. property consisting of his own branch including his sons. [*Shri Vallabhdas Modani v. C.I.T. (1982) 138, ITR, p. 673*].

The Allahabad High Court's decision *supra* in the case of *Shri Vallabhdas Modani v. Commissioner of Income-tax* was followed by the Andhra Pradesh High Court (1983, 144 ITR 18) and later approved by the Supreme Court in the case of *Commissioner of Wealth-Tax v. Chander Sen* (1986, 161 ITR 370) holding that it is not

possible to say that when a son inherits the property in the situation contemplated by the Hindu Succession Act, 1956, he takes as Karta of his own undivided family.

## COMPUTATION OF INCOME OF THE HUF

Income of the HUF is assessed as joint family income of HUF if there exists a coparcenership and joint property of the family till partition is claimed by any of its coparceners.

*Joint Property of the family consists of:*

- (i) ancestral property which a man inherits from any of his three immediate male ancestors, namely, father, grandfather, great grandfather;
- (ii) accretion thereto;
- (iii) acquisition with joint funds; and
- (iv) self-acquired property of any member thrown by him into the common stock to be treated as family property. In the case of *Pushpa Devi v. C.I.T.* the Supreme Court has held that a Hindu female, not being a coparcener, cannot blend her separate property with Joint family property. However, she can make a gift of her property or sell the property to the family. [(1977) 109, ITR p. 730].

The gross total income of the family for the relevant previous year shall be computed under the relevant heads (as per the provisions of the Income-tax Act) as it is computed for other assessee's. Incomes exempt under section 10 to 13A are exempt and deductions allowable under chapter VIA are to be provided. However, in this connection the following points are worth noting:

- (i) The holder, who is the senior most male member of the family, of an impartible estate is liable to tax on income from that estate in his individual capacity though the estate belongs to HUF.
- (ii) Conversion of self-acquired property into joint family property. Section 64(2) provides that where an individual being a member of Hindu undivided family transfers his separate property after 31st December, 1969 to the family for the common benefit of the family, otherwise than for adequate consideration, such property is known as converted property. The income derived from the converted property or any part thereof shall be included in the total income of the transferor individual and not in the income of the family.
- (iii) If the funds of a Hindu Undivided family are invested in a company or a firm, fees or remuneration received by the member as a director, or a partner in the company or firm may be treated as income of the family in case the fees or remuneration is earned essentially as a result of investment of funds. But, if the fees or remuneration is earned essentially for services rendered by the member in his personal capacity, the income shall constitute the personal income of the member.
- (iv) Where a member of a HUF is a partner in a firm on behalf of the family and on partition of the property of the family, the share in the firm is allotted to such a member, subsequent to such allotment when the firm settles its accounts the whole income for that year would be the income of the individual member and no part of the income would be added to the income of the family. [*CIT v. Ashok Bhai Chiman Bhai (1965) 56, ITR, 42 (S.C.)*].
- (v) The personal earning, including income from self acquired property of a member of the HUF, even though he has sons, would not be included in the income of the family. Such income shall be assessed as income of that individual. [*Kalyanji Vithal Das v. CIT (1937) 5 ITR 90 (PC)*].
- (vi) Any sum paid by an HUF to a member of the family out of its income is not deductible in computing the income of the family. However, such amount will not be included in the income of such individual whether the family had paid tax on its income or not [Section 10(2)].
- (vii) If any remuneration is paid by the Hindu Undivided family to the karta or any other member for services

rendered by him in conducting family's business, the remuneration is deductible if remuneration is (a) paid under a valid and bona fide agreement; (b) in the interest of, and expedient for, the business of family; and (c) genuine and not excessive. *Jugal Kishore Baldeo Sahai v. CIT [1967] 63 ITR 238 (SC)*.

- (viii) If salary is paid by the Hindu undivided family to its karta for looking after its interest in firms in which it is partner through said karta, such salary is allowable as deduction - *CIT v. Prakash Chand Agarwal [1982] 11 Taxman 55 (MP)*.
- (ix) Income from 'stridhan' is not includible in the income of the family. Property derived by a woman from her father or brother or husband or any other relative either before or after her marriage is known as 'stridhan'.
- (x) Under the Dayabhaga School of law, as stated in a preceding page, no son has any right in the ancestral property during the lifetime of his father. If, therefore, the father does not have any brother as a coparcener, income arising from ancestral property is taxable as his individual income.

### Partition of a Hindu undivided family [Section 171]

'Partition' signifies division of property. In the cases of property capable of physical division, share of each member is determined by making physical division thereof. It must be noted that a division of income without physical division of property does not amount to partition. Where, however, the property is not capable of physical division, partition implies such division as the property may admit.

#### **Who is entitled to share on partition**

Though only coparceners can demand partition, once the partition takes effect, the following persons are entitled to a share:

- (a) all coparceners;
- (b) a son in the womb of his mother at the time of partition;
- (c) mother, who gets an equal share if the partition takes place among her sons after the death of her husband; and
- (d) wife, who gets a share equal to that of a son at the time of a partition between father and sons.

#### **Assessment after partition (Section 171)**

Section 171 applies to an HUF which is assessed as such. Therefore, if incase a family is not assessed as a hindu undivided family this section does not apply. A joint family, once assessed as a HUF, continues to be assessed as such till one or more coparceners claim partition. Such claim must be made by the coparceners before the assessment of the income of the HUF for the relevant assessment year is completed. On the receipt of such a claim, the Assessing Officer must make an inquiry after giving due notice to the members and record a finding whether there has been a partition and, if so, the date of the partition. The income of the family from the first day of the previous year to the date of partition is assessed as income of the HUF and from the next date of the partition to the date of close of the previous year, as the individual income of the recipient-members. If the recipient member forms another HUF along with his wife and son(s), the income of the property which was subject to partition is chargeable to tax in the hands of the new H.U.F.

#### **A partition of the HUF can be both total and partial**

Where the entire joint family property is divided among all coparceners and the family ceases to exist as an undivided family, the partition is total. A partial partition may be as regards: (a) the persons constituting the joint family, or (b) the properties belonging to the joint family, or (c) both. In case of partial partition, some coparceners continue as a joint family or some properties continue as a joint estate as against some coparceners or properties which separate from HUF. The device of partial partition has been used as a medium for reduction of proper tax

liability. To curb such a practice, the Finance (No. 2) Act, 1980 inserted Sub-section 9 in Section 171 which lays down that partial partitions of HUFs assessed as such (Union of India vs MV Valliappan 1999 AIR SCW 2689), effected after 31st December 1978 will not be recognised for tax purposes.

The provisions made by Sub-section (9) in Section 171 are as follows:

- (i) In a case where a partial partition of a HUF has taken place after 31.12.1978, no claim of such partition will be enquired into and the Assessing Officer will not record a finding as to whether there has been a partition of the family property. Further, any finding regarding partial partition recorded under Section 171(3) will be null and void and of no legal effect.
- (ii) Such family will continue to be assessed as if no such partial partition has taken place, i.e., the property or source of income will be deemed to continue to belong to the Hindu undivided family and no member will be deemed to have separated from the family.
- (iii) Each member or group of members of such family will be jointly and severally liable for any tax, interest, penalty, fine or other sum payable under the Act by the family, whether before or after such partition. The several liability of any member or group of members of such family will be computed according to the portion of the joint family property allotted to him on such partial partition. This amendment has come into force with effect from April 1, 1980 and has, accordingly, been applicable with effect from assessment year 1980-81 and onwards.

**Illustration 1 :** *Ram Manhar & Sons HUF, running Raghuvveer Departmental Stores consists of Karta, his wife, two sons and daughter. Both the sons who are having professional/technical qualifications as a Chartered Accountant and as an Automobile Engineer started in partnership, a garage for the repairing of motor cars, with a clear understanding that the technical side of the business be looked after by the Engineer while the general administration and finance part be taken care by the Chartered Accountant. They had taken an interest-free loan of Rs. 5,00,000 from the HUF for starting the venture. The business of garage resulted in a net profit of Rs. 15,00,000 for the year ended 31.03.2020. The Assessing Officer proposes to assess the income from the business of motor garage in the hands of HUF. Examine the validity of the proposition of the Assessing Officer in the light of a decided case law.*

### Solution

The facts of the case are similar to that of the case of *CIT v. Charan Dass Khanna & Sons (1980) 123 ITR 194*, where the Delhi High Court observed that if the investment made by the HUF in the business started by the coparceners plays a minor role and it is primarily the personal efforts, specialized skill and enterprise of the individual coparceners which resulted in setting up of a new business and earning of goods profits, then it may not essentially be said that the income belongs to the HUF.

The Supreme Court has also supported this view in the case of *K.S. Subbiah Pillai v. CIT (1999) 237 ITR 11* and held that where the remuneration and commission earned by the Karta were on account of the personal qualifications and exertions and not on account of the investment of the family funds, such income cannot be treated as income of the HUF.

Thus, in the given case, profits were earned primarily because of the specialized skills acquired by both the partners in their respective fields and used in the business of motor garage. The initial capital taken from the HUF as interest free loan, of course, has its role but it is nevertheless a minor one. Therefore, the income from the business set up by the brothers is assessable in their individual hands and not as the income of the family.

Further, the proposition of the Assessing Officer to tax the profits of the business of motor garage earned by the two sons in the hands of the HUF is not valid.

### Illustration 2:

Ram (59 years) and his two brothers (Ramesh (57 years) and Somesh (50 years) are engaged in family

**372 EP-TL**

business of cultivation of wheat. Last year they had losses to the extent of Rs. 12,000 but this year, due to good season the Business earned a Profit of Rs. 220,000.

The family owns a house property, the municipal valuation of which is Rs. 280000 and the market rent of similar property is Rs. 285000. The standard rent as per Rent Control Act is Rs. 3,50,000. The family pays Rs. 48,000 for municipal taxes during the previous year out of which Rs. 20,000 pertains to earlier year which could not be paid due to business loss. Interest on capital borrowed for repaying original loan for construction of house Rs. 75,000. Further, the rental income of the property is Rs. 310000.

Dividend received from Indian Company X Ltd. Rs. 12,000.

Interest received on listed debentures Rs.8,10,000 (net)

Compute the total income and Tax liability of the family X (HUF) for the Assessment year 2020-21.

**Solution:**

**Computation of Total Income of X (HUF) for the assessment year 2020-21**

*Income from house property*

Gross annual Value	310,000
Less: Municipal Taxes	48,000
<i>Net annual Value</i>	<i>262,000</i>
Less: Standard Deduction @ 30% of 262, 000	78600
Less: Interest on capital borrowed	75000
Income from House property	<b>108400</b>

*Income from Business/Profession*

Agricultural income (Exempt)	NIL
<i>Income from other sources</i>	
Dividend received from Indian Company X Ltd. (Exempt)	NIL
Interest on listed debentures	<b>9,00,000</b>
Gross Total Income	<b>10,08,400</b>
Less: Deduction under section 80C to 80U	NIL
<b>Total Income</b>	<b>10,08,400</b>

**Note :** The share of Karta and other coparceners in the profits of HUF will be exempt under section 10(2)

**Computation of tax on Total Income of X (HUF) for the assessment year 2020-21**

Computation of tax is as follows:

	<b>Particulars</b>	<b>Amount</b>
(a)	Agricultural income (2,20,000-12,000)	2,08,000
(b)	Non-agricultural income	10,08,400
(c)	Total of (a) and (b)	12,16,400

<b>(d)</b>	<b>Tax payable on (c)</b>	<b>177420</b>
a.	Tax on first 2,50,000 NIL	
b.	Tax on next 250,000 @ 5% = Rs. 12,500	
c.	Tax on next 500,000 @ 20% = Rs. 100,000	
d.	Tax on remaining income Rs. 216400@ 30% = 64920	
(e)	Total of agricultural income and basic exemption limit (As per slab)	458000
(f)	Tax payable on (e)	10400
(g)	Net tax payable = (d)-(f)	167020
(h)	Add: Health and Education cess of 4% on Rs.167020	6680.8
(i)	Total tax (round off)	173700

**Illustration 3:**

Ram, 66 years is the karta of a HUF with his two sons Ramesh (39 years) and Somesh (25 years). The family owns a house property, the rental income of the same is Rs. 310000. Family business profits Rs. 280,000.

Long-term capital gains Rs. 25,000 and short term capital gains for the year Rs.11,000 (STT applicable). Dividend received from Indian Company X Ltd. Rs. 12,000. Interest received on listed debentures Rs.8,000 (gross)

Ram invested in PPF Rs. 1,50,000 out of family funds and received share of profits from a firm in which he represented HUF being Karta. Ram gifts Rs. 100,000 to family.

Salary income of Ramesh Rs. 600,000

Interest on Government Securities Rs. 10,000(gross) out of own funds of Ram.

Compute the total income and Tax liability of the family X (HUF) and Ram, Ramesh and Somesh for the Assessment year 2020-21.

**Solution**

**Computation of Total Income of X (HUF) for the assessment year 2020-21**

<i>Income from house property</i>	
Rent	310000
Less: Standard Deduction @ 30%	93000
Income from House property	2,17,000
<i>Income from Business/Profession</i>	
Business Profits	280000
A Firm (Exempt)	NIL
<i>Income under the head Capital Gains</i>	
Long-term capital gains	25,000
Short term Capital Gain	11,000

<i>Income from other sources</i>	
Dividend received from Indian Company X Ltd. (Exempt)	NIL
Interest received on listed debentures	8,000
Gift (Exempt)	NIL
<b>Gross Total Income</b>	<b>541000</b>
<i>Less: Deduction under section 80C to 80U</i>	
Under section 80C(maximum)	150,000
<b>Total Income</b>	<b>391000</b>

**Note :** The share of Karta and other coparceners in the profits of HUF will be exempt under section 10(2)

**(B) Computation of tax on Total Income of HUF for the assessment year 2020-21**

Tax on long-term capital gains (20% of Rs. 25,000)	5000
Tax on short-term capital gains (15% of Rs. 11,000)	1650
Balance of Total Income Rs. 355000	5250
Total tax	11900
Add: Health and Education cess at 4%	476
Total liability (round off)	12380

**Note :** The share of Karta and other coparceners in the profits of HUF will be exempt under section 10(2)

**Computation of taxable income of Ram, Ramesh and Somesh for the assessment year 2020-21**

Particulars	Ram	Ramesh	Somesh
Salary Income		600,000	
Business Income:	Exempt	Exempt	Exempt
Profit share in HUF			
Income from other sources	10,000		
Interest on Government Securities			
<b>Gross Total Income</b>	<b>10,000</b>	<b>600000</b>	
<b>Deductions u/s 80C to 80U</b>			
Taxable Income	10,000	600000	
<b>Tax liability</b>	<b>NIL</b>	<b>33800</b>	<b>NIL</b>

## TAXATION OF FIRMS

Under Section 2(23) of the Income-tax Act, the terms “firm”, “partner”, and “partnership” have the meanings respectively assigned to them in the Indian Partnership Act, 1932 and Limited Liability Partnership Act, 2008.

The expression “partner” also includes a minor who has been admitted to the benefits of partnership and a partner of a Limited Liability Partnership Act 2008. However a minor cannot validly enter into any partnership as a ‘full partner’ with other persons but he can be admitted to the benefits of partnership only.

A joint Hindu family as such cannot be a partner in a firm. However, through its Karta it may enter into a valid partnership with a third person or with a member of the undivided family in his individual capacity. In such a case, the Karta occupies a dual position. On the partnership he functions in his individual capacity; on the relations to other members of the Hindu undivided family, in his representative capacity.

An incorporated company being a legal person may form a partnership with an individual or with another

company. In considering the maximum number of partners comprising a firm, the company will be considered as one person only.

A partnership firm as such is not entitled to enter into a partnership with another firm, H.U.F., individual, or a company. However, its partners in their individual capacity can enter into another partnership.

Scheme of taxation of a firm and its partners

### Assessment as a Firm [Section 184]

As per the scheme, a partnership firm in the first assessment year shall be assessed as a firm if the following conditions are satisfied:

1. The partnership is evidenced by an instrument i.e. partnership deed which is to be in writing containing necessary clauses.
2. The individual shares of the partners as specified in that instrument (including how the loss will be borne by major partners in case of a minor admitted for benefits only).
3. A copy of the partnership deed certified by all the partners or their duly authorized agents, in writing (other than the minors) is submitted along with the return of income in respect of which assessment as a firm is first sought.

Where the return is made after the dissolution of the firm, the copy of the partnership deed should be certified in writing by all persons (excluding minors) who were partners of the firm immediately before its dissolution and by the legal representative of any deceased partner.

When a firm is assessed as such for any assessment year, it shall be assessed in the same capacity for every subsequent year if there is no change in the constitution of the firm or in the shares of partners as evidenced by the partnership deed on the basis of which assessment as a firm was first sought.

Where any such change has taken place in the previous year, the firm shall furnish a certified copy of the revised instrument of partnership along with the return of income for the assessment year relevant to such previous year. In doing so all the provisions of Section 184 will apply to the firm. Further, any change in remuneration or interest to partners is to be notified in the same manner to comply with section 40(b).

Circumstances where the firm will be assessed as a firm but shall not be eligible for deduction on account of interest, salary, bonus, etc.

Where the firm -

- (a) fails to make the return required under Section 139(1) and has not made a return or revised return under Section 139(4) or 139(5), or
- (b) fails to comply with all the terms of a notice issued under Section 142(1) or fails to comply with a direction issued under Section 142(2A), or
- (c) having made a return, fails to comply with all the terms of a notice issued under Section 143(2),
- (d) does not comply with three conditions mentioned above u/s 184.

then the firm shall not be eligible for any deduction on account of interest to a partner and remuneration to a working partner although the same is mentioned in the partnership deed.

### Computation of income and tax thereon of firm

*The income of the firm shall be computed as per the normal provisions of the Act under various heads of income excluding incomes exempt from tax and deductions under section 80 as applicable.*

**Rate of tax**

In the case of a firm which is assessable as such (i.e. as a firm), tax is chargeable on its total income at the rate of 30%.

**Surcharge @12%** shall be applicable where the total income exceeds Rs. 1 crore. Health and Education cess shall be added as 4% of tax plus surcharge. However, firm and LLP is subject to alternate minimum tax under section 115JC ( discussed in detail later in this chapter) .

Partnership is not a separate entity distinct from the partners, but for tax purposes a partnership is taxed as a separate entity and therefore total income will be computed under various heads of income. A partnership firm is also entitled for deductions under section 30 to 38 for expenditures incurred. However, for payment of remuneration to partners and interest on capital are allowed subject to conditions laid down under section 40(b).

Section 40(b), contain the following conditions which need to be complied with while making payment of remuneration and interest on borrowed capital to the partners:

- (i) Payment of salary, bonus, commission or remuneration by whatever name called to a non-working partner shall not be allowed as deduction. Such payments are allowed only to working partners if it is authorised by the partnership deed and are in accordance with partnership deed. Also, such payments should pertain to the period after the partnership deed.
- (ii) Interest payable to a partner, authorised by the partnership deed for period after the partnership deed shall be allowable as deduction subject to a maximum of 12% p.a. If the partnership deed provides for interest at less than 12% p.a, the deduction of interest shall be allowed to the extent provided by the partnership deed.
- (iii) the payment of remuneration to working partner, although authorised by partnership deed however it is subject to maximum of the following limits.

Finance Act, 2009 provides for uniform limits for both professional firms and nonprofessional firms:	
I. On the first Rs. 3,00,000 of the book-profit or in case of a loss	Rs. 1,50,000 or 90% of the book-profit, whichever is more.
II. On the balance of the book-profit	60% of the book profits.

**Meaning of Book Profit [Explanation 3 to section 40(b)]**

Book-profit” means the net profit, as shown in the profit and loss account and make the additions and deductions as per section 28 to 44DB explained under the head income from Business and Profession increased by the aggregate amount of the remuneration paid or payable to all the partners of the firm if such amount has been deducted while computing the net profit. Interest paid/payable to partners in excess of 12% shall also be disallowed as per section 40(b).

**Change in Constitution of a Firm [Section 187]**

Where at the time of making an assessment under Section 143 or Section 144 of the Act it is found that a change has occurred in the constitution of a firm, the assessment will be made on the firm as constituted at the time of making the assessment.

For the purposes of this section there is a change in the constitution of a firm if:

- (a) one or more of the partners cease to be partners or one or more new partners are admitted, in such circumstances that one or more of the persons who were partners of the firm before the change continue as partner or partners after the change (this clause, however, shall not apply to a case where the firm is dissolved on the death of any of its partners) or

- (b) where all the partners continue with a change in their respective shares or in the shares of some of them.

### Losses of Registered Firms [Section 75]

Where the assessee is a firm, any loss in relation to the assessment year commencing on or before the 1st day of April, 1992, which could not be set off against any other income of the firm and which had been apportioned to a partner of the firm but could not be set off by such partner prior to the assessment year commencing on the 1st day of April, 1993, then, such loss shall be allowed to be set off against the income of the firm subject to the condition that the partner continues in the said firm and to be carried forward for set off under sections 70, 71, 72, 73, 74 and 74A.

### Carry forward and set off of losses in case of change in constitution of firm or on succession [Section 78(1)]

Where a change has occurred in the constitution of a firm on account of death or retirement, the firm is not entitled to carry forward and set off so much of the loss as is proportionate to the share of a deceased or retired partner in the firm in respect of the previous year.

Method of computation of amount not to be allowed to be set off and carried forward

Step 1: In the year of change first ascertain the share of outgoing partner in the profit or loss of the firm.

Step 2: Compute share of loss of the outgoing partner for each of the preceding years from which the loss is carried forward.

Step 3: Amount not allowed to be set off and carried forward:

- (i) Sum of [Amounts computed in Steps (1) and (2) where there is loss in the year of change].
- (ii) Difference of [Amounts computed in Steps (1) and (2) in case of profit in the year of change].

### Carry forward of unabsorbed depreciation

*Unabsorbed depreciation and unabsorbed capital expenditure on scientific research can be carried forward by the reconstituted firm (without deducting share of the outgoing partner) as these are not covered under section 78.*

### Assessment of Partners

As per Section 10(2A) of the Act, any person who is a partner of a firm which is assessed as such, his share in the total income of the firm will not be included in computing his total income. Partner includes a minor admitted to the benefits of partnership as per Section 2(23) of the Act.

Further, the explanation to Sub-clause (2A) provides that the share of a partner in the total income of the firm assessed as a firm shall be an amount which bears to the total income of the firm the same proportion as the amount of his share in the profits of the firm (in accordance with the partnership deed) bears to such profits.

In terms of a formula, the amount exempt would be:

Partners share in the profit of the firm = as shown in the partnership deed  $\frac{\text{Total Profits of the Firm}}{\text{Total income of the firm}}$

Any interest, salary, bonus, commission or remuneration by whatever name called which is due to or received by a partner of a firm from the firm will be chargeable to tax in the hands of the partner (to the extent allowed as deduction to the firm) under the head "profits and gains of business or profession". However, if such salary, interest, bonus, commission or remuneration (or any part thereof) has not been allowed as deduction as per

Section 40(b) in the hands of the firm, the amount not allowed as deduction shall not be charged to tax in the hands of partners.

Further, deductions under Sections 32 to 37 can be claimed by a partner from any income where any expenditure was incurred to earn such income.

### **Succession of one firm by another firm [Section 188]**

When all the partners in the predecessor firm are replaced by new partners in the successor firm, it is known as succession of one firm by another firm. If a firm is dissolved and some of the partners take over the firm's business or carry on a similar business with or without new partners, it would be a case of succession by a new firm (62 I.T.R. 75).

In *CIT v. K.H. Chambers (1965) 55 ITR 674*, the Supreme Court laid down the following requisites of succession:

- (i) There is a change of ownership.
- (ii) The whole business is transferred.
- (iii) Substantially the identity and the continuity of the business are preserved.

Where the partnership deed does not provide specifically for continuance of the firm on the death of a partner, there would be no change in constitution of the firm but it would be a case of succession. [*Addl. CIT v. Thyagasundara Mudaliar (1981) 127 ITR 520*].

Where a firm is succeeded by another firm, separate assessments are made on the predecessor and successor firms respectively in accordance with the provisions of Section 170. Section 170 provides that the predecessor shall be assessed in respect of the income of the previous year in which the succession took place up to the date of succession and the successor shall be assessed in respect of the income of the previous year after the date of succession. If the predecessor cannot be found, or the tax assessed on the predecessor cannot be recovered from him for the previous year (in which the succession took place) and the previous year immediately preceding such previous year, the unrealised tax payable by the predecessor shall be recovered from the successor.

However, the successor firm is entitled to recover from the predecessor firm any tax paid by it on behalf of the former. If any tax is due against any partner of the predecessor firm, it cannot be recovered from the successor firm.

### **Joint and several liability of partners for tax payable by firm [Section 188A]**

Section 188A provides that every person who was, during the previous year, a partner of a firm, and the legal representative of any such person who is deceased, shall be jointly and severally liable along with the firm for the amount of tax, penalty or other sum payable by the firm for the assessment year to which such previous year is relevant, and all the provisions of Income-tax Act, so far as may be, shall apply to the assessment of such tax or imposition or levy of such penalty or other sum.

### **Firm Dissolved or Business Discontinued [Section 189]**

Where any business or profession carried on by a firm has been discontinued or where a firm is dissolved, the assessment of the total income of the firm shall be made as if no such discontinuance or dissolution had taken place and all the provisions of the Act, including the provisions relating to penalty or any other sum (interest, fine) chargeable under the Act, shall apply. Consequently, every person who was a partner of the firm at the time of discontinuance of business or dissolution of the firm and legal representative of the deceased partner shall be jointly and severally liable to the amount of tax penalty and any other sum. Where the dissolution or discontinuance of business takes place after any proceedings in respect of an assessment year have

commenced, the proceedings may be continued against the partners or legal representative of a deceased partner from the stage at which the proceedings stood at the time of such dissolution or discontinuance.

Thus, every partner of the firm and the legal representative of the deceased partner is liable to pay the tax which is already due or may have become due after the dissolution, irrespective of his interest in the firm.

However, if there was any irrecoverable amount at the time of dissolution or discontinuance of business and later on it was recovered by the partners, the partners shall personally pay the tax on their share so recovered.

**ALTERNATE MINIMUM TAX (AMT) [SECTION 115JC]**

The provisions of section 115JC are applicable to all assessees except companies where the regular income tax payable for a previous year is less than the alternate minimum tax payable for such previous year then the adjusted total income shall be deemed to be the total income of that person for such previous year and it shall be liable to pay income tax on such adjusted total income @ 18.5% plus Health and Education Cess @ 4%.

12% surcharge if Adjusted Total income of the firm or LLP exceeds INR 1 crore plus 4% Health & Education cess in all cases. In case of individual surcharge will be 10% if Adjusted Total income of the firm or LLP exceeds INR 50 Lacs and 15% if it exceeds INR 1 crore and 25% if it exceeds INR 2 crores and 37% if it exceeds INR 5 crores.

It is further provided that the provisions of AMT under Chapter XII-BA shall only apply to an individual or a Hindu undivided family or an association of persons or a body of individuals (whether incorporated or not) or an artificial juridical person if the adjusted total income of such person exceeds **twenty lakh rupees**.

However, AMT is levied @ 9% in case of a non-corporate assessee being a unit located in International Financial Services Centre and deriving its income solely in convertible foreign exchange. Surcharge and cess as applicable will also be levied. (Applicable from Assessment Year 2020-21)

The regular income tax payable shall be the income-tax payable for a previous year by a person other than a company on his total income in accordance with the provisions of the Act other than the provisions of Chapter XII-BA i. e section 115JC to 115JF.

Adjusted total income shall be the total income before giving effect to provisions of Chapter XII-BA as increased by the deductions claimed under any section 80H to Section 80RRB (other than section 80P) included in Chapter VI-A under the heading "C - Deductions in respect of certain incomes" and deduction claimed under section 10AA. Further, total income shall be increased by the deduction claimed under section 35AD for purpose of computation of adjusted total income. The amount of depreciation allowable under section 32, as if no deduction u/s 35 AD in respect of such assets was allowed, shall however, be reduced in computing the adjusted total income.

Particulars	(Rs.)
Taxable income of the taxpayer	XXXX
Add : Amount of deduction claimed under section 80H to 80RRB (except 80P)	XXXX
Add : Amount of deduction claimed under section 35AD (as reduced by the amount of depreciation allowable in accordance with the provisions of section 32)	XXXX
Add : Amount of deduction claimed under section 10AA	XXXX
Adjusted total income	XXXX

The provisions can be summarized as:

1. If regular income tax payable is more than or equal to the alternate minimum tax (18.5% plus Health

and Education cess @ 4% of adjusted total income), the regular income tax payable is the tax liability of the assessee.

2. If regular income tax payable is less than the alternate minimum tax (18.5% plus Health and Education cess @ 4% of adjusted total income), the adjusted total income is the deemed income of the assessee for that year and alternate minimum tax is the tax liability.

However, it is also provided that the credit for tax (tax credit) paid by a person on account of AMT under Chapter XII- BA shall be allowed to the extent of the excess of the AMT paid over the regular income-tax. This tax credit shall be allowed to be carried forward up to the fifteen assessment year immediately succeeding the assessment year for which such credit becomes allowable and set off against regular tax liability. In other words, it shall be allowed to be set off for an assessment year in which the regular income-tax exceeds the AMT, to the extent of the excess of the regular income-tax over the AMT.

The amount of AMT credit shall not be allowed to be carried forward to the subsequent year to the extent such credit relates to the difference between the amounts of foreign tax credit (FTC) allowed against AMT and FTC allowable against the tax computed under regular provisions of the Act.

Every person to which this section applies shall obtain a report, in such form as may be prescribed from a chartered accountant certifying that the adjusted total income and the alternate minimum tax have been computed in accordance with the provisions of this Chapter and furnish such report on or before the due date of filing of return under sub-section (1) of section 139.

All other provisions of the Act, like advance tax, interest u/s 234A/B/C shall apply to assessee who is liable to pay AMT.

#### Illustration 1

A, B and C are the partners for 3:2:1 share respectively, in a firm engaged in medical profession. Compute the total income of the firm for the year ended 31st March, 2020:

Particular	Rs.	Particular	Rs.
Office Expenses	15,400	Gross Profit	40,000
Income Tax	1,000	Net Loss A	8,700
Salary to A	5,000	Net Loss B	5,800
Salary to B	4,000	Net Loss C	2,900
Salary to C	10,000		
Bonus to A	10,000		
Bonus to C	12,000		
Total	57,400	Total	57,400

#### Solution:

Computation of Book Profit of the Firm			Rs.
Net Loss as per P & L A/c			(17,400)
<i>Add:</i> Inadmissible Expenses:			
Income-tax		1000	
Salary to partners:			
A	5000		

B	4000		
C	10000	19000	
Bonus to partners A			
C	10,000		
Book Profit	12,000	22,000	42,000
			24,600

**Permissible remuneration to partners:**

90% of first Rs. 3,00,000 of Book-profit or Rs. 1,50,000 whichever is more, is allowed as deduction. Here the permissible remuneration comes to Rs. 1,50,000, but as the partners have claimed Rs. 41,000 only, hence the entire amount will be allowed.

**Computation of total income of the firm**

Book Profit		24,600
Less: Salary to Partners	19,000	
Bonus to Partners	22,000	41,000
Loss of the firm		(16,400)

Note : Loss of the firm will be carried forward by the firm to the next year(s).

**Illustration 2**

M, N and O are partners sharing profits and losses in the ratio of 2:1:1 respectively. Their summarised Profit and Loss A/c for the year ending 31st March, 2020 is appended below:

Particulars	Amount Rs.	Particulars	Amount Rs.
Office salaries	5,680	Gross Profit	60,570
Telephone and Telegram	2,000	Rent received	6,000
Interest on loan from M	2,000	Interest on securities	4,000
Local taxes (let out property)	1,000		
Salary to N	3,000		
Commission to partners			
M	4,000		
N	5,000		
O	6,000		
Collection charges of interest on securities	50		
Bad debts reserve	1,000		
Net Profit to partners:			
M	20,420		
N	10,210		

O	10,210		
Total	70,570	Total	70,570

Compute total income of the firm for the assessment year 2020-21 and tax liability thereon. Interest paid to M has been calculated at the rate of 20% p.a. simple.

**Solution:**

#### Computation of Book-Profit

Particulars	Rs.	Rs.
Net Income as per P & L A/c		40,840
<i>Add:</i> Inadmissible items -		
Local taxes (on let out property)	1000	
Salary to N (Partner)	3000	
Commission to partners	15,000	
Collection charges	50	
Bad debts reserve	1,000	20,050
		60,890
<i>Less:</i> Other Incomes -		
Rent received	(6,000)	
Interest on securities	(4,000)	(10,000)
Book Profit		50,890

Maximum remuneration payable to partners

Here Rs. 1,50,000 will be allowed as maximum remuneration. But as the partners have drawn only Rs. 18,000 by way of salary and commission, the entire amount will be allowed as deduction.

#### Computation of total income of the firm for the Assessment Year 2020-21

Particulars		Rs.
Book Profit:		50,890
<i>Less :</i> Salary and commission to partners		(18,000)
– Taxable Business Profit		32,890
– Income from house property		
Rent received		6,000
<i>Less :</i> Municipal taxes		(1,000)
Net adjusted annual value (NAAV)		5,000
<i>Less :</i> Repairs (30% of NAAV) u/s 24		(1,500)
Income from House Property		3500
– Income from other sources:		
Interest on Securities	4,000	
<i>Less:</i> Collection charges	(50)	3,950
GROSS TOTAL INCOME (A) + (B) + (C)	= Rs. 32,890 + 3,500 + 3,950 =	Rs. 40,340

The firm will have to pay tax on Rs. 40,340 @ 30%, which comes to Rs. 12,102 plus health and education cess @ 4% on 12,102 making the total liability as Rs. 12,586.

**Illustration 3 :**

Compute tax liability of the firm X & Co. for the assessment year 2020-21 considering the provisions of Section 115JC. The business income of the firm is Rs. 21,00,500 before deduction under section 32 and before deduction under section 35AD Rs. 11,00,000, because of which depreciation of Rs. 40,000 cannot be claimed. Deduction under section 80IB Rs. 1,00,000. Donation paid to a political party Rs. 85,000.

**Solution:**

Particulars	Rs.
GTI - Business Income (Rs. 21,00,500 less 11,00,000)	10,00,500
Less Deductions	
Under section 80IB	1,00,000
Under section 80GGC	85,000
Net Income	8,15,500
Tax on Rs. 8,15,500 @ 30%	2,44,650
Add : Health and Education Cess @ 4%	9786
Tax liability	2,54,436
Adjusted total income and alternate minimum tax for the purpose of section 115JC	
Net Income	8,15,500
Add: Under section 80IB	1,00,000
Add: under section 35AD (Rs. 11,00,000 less 40,000)	10,60,000
Adjusted total income	19,75,500
AMT on Rs. 19,75,500 @ 18.5%	3,65,467
Add: Health and Education Cess @ 4%	14,618
AMT liability	3,80,085
	3,80,090 (round off)
Tax payable is Rs. 3,80,090 being higher of tax liability Rs. 2,54,436 and AMT Rs. 3,80,090.	

**Illustration**

**Income & Expenditure A/c of Lawyers & Co. for the year ending March 31, 2020**

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Expenses	1,50,000	By Professional Receipts	3,80,000
To Depreciation	20,000		
To Remuneration to partners	1,50,000	By Other fees	90,000
Interest on Capital to partners @ 20 per cent	20,000		
To Net Profit	1,30,000		
Total	4,70,000	Total	4,70,000

**384 EP-TL**

Other Information:

1. Expenses include Rs. 18,000 and Rs. 12,000 paid in cash as brokerage to a single party on a single day.
2. Depreciation calculated as per section 32 is Rs. 40,000

Compute the total income of the firm.

**Solution :**

**Computation of Total Income of Lawyers & Co. for A. Y. 2020-21**

Particulars		Amount Rs.
Net profit as per profit and loss account		1,30,000
Add : Expenses not allowable		
Section 40A(3)- Cash payments to a broker exceeding Rs. 10,000 (Note 1)	30,000	
Section 40(b)-Excess interest on capital to partners 20%-12% i.e. (20000*8/20) (Note 2)	8,000	38,000
Add : Remuneration to partners debited to profit and loss account		1,50,000
Less : Depreciation u/s 32 (Rs. 40,000-Rs. 20,000 debited in profit and loss account)		(20,000)
Book profit (Note 3)		2,98,000
Maximum permissible remuneration (higher of the two : (i.e. 90 per cent of Rs. 2,98,000 or Rs. 1,50,000)	2,68,200	
Actual (Subject to actual)	1,50,000	(1,50,000)
Business Income of the Firm		1,48,000
Tax Liability (30% of 1,48,000)		44,400
Add : Health and Education Cess @ 4%		1,776
Total Tax Liability		46,176

Notes :

1. As per section 40A(3) of the Act, if the aggregate payment made (otherwise than by an account payee cheque/draft) to the same person during a day exceeds Rs. 10,000/- the entire amount of such payment is disallowed.
2. As per section 40 (b) of the Act, if the interest payable to the partners exceeds simple interest of 12% per annum, the excess amount is not deductible.
3. The remuneration paid to the working partners cannot exceed the permissible limits specified under section 40 (b) of the Act.

**Illustration 5:**

*Mr. X, carrying on the business of operating a warehousing facility for storage of sugar, has a total income of*

Rs. 80 lakh. In computing the total income, he had claimed deduction under section 35AD to the tune of Rs. 70 lakh on investment in building (on 1.4.2019) for operating the warehousing facility for storage of sugar. Compute his tax liability for A.Y. 2020-21. Show the calculations of Alternate minimum Tax also.

**Answer**

**Computation of Tax payable by Mr. X for AY 2020-21**

**Computation of Normal Tax**

Particulars	Amount (Rs. in lakh)
Tax liability under the normal provisions of the Income-tax Act, 1961	22.125
Add: Surcharge @ 10% of Total income > 50 lacs	2.2125
Add: Health and Education Cess @ 4% of 24.3375	0.9735
Total Tax Liability	25.311

**Computation of Alternate Minimum Tax**

Particulars	Amount (Rs. in lakh)
Adjusted Total Income	80.00
Add : Deduction under section 35AD	70.00
Less : Depreciation under section 32	(7.00)
Adjusted Total Income	143.00
AMT @18.5%	26.46
Surcharge @ 15% (since adjusted total income> Rs. 100 lakh)	3.97
Tax	30.43
Add: Health and Education Cess @ 4%	1.217
Total tax Liability	31.647

Since the regular income tax payable is less than the AMT payable, the adjusted total income of Rs. 143 lakhs shall be deemed to be the total income of Mr. X and tax is payable @18.5% thereof plus surcharge @ 15% and cess @4%. Therefore, tax liability is 31.647 lakhs.

However, Mr. X would be eligible for credit in 15 subsequent years to the extent of difference between the AMT and Normal Tax i.e. Rs. 6.336 lakhs.

**Illustration 6:**

Mr. A, 42 years, and Mr. B , 50 years, are equal partners in a partnership firm AB and Co. engaged in furniture business. From the profit and loss account of the firm compute net income and tax liability of the firm as well as the partner's for the assessment year 2020-21.

**Profit and Loss Account**

**For the year ending March 31, 2020**

Particulars	Amount (Rs.)	Particulars	Amount(Rs.)
Cost of goods sold	5,10,000	Sales	1,90,0000
Salary to staff	6,00,000	Long term capital gain	1,00,000
Depreciation	1,20,000	Lottery prize	35,000

Fees for technical service	40,000	Other business receipts	1,47,000
Remuneration to partners A 140000 B 60000	2,00,000		
Other Expenses	2,10,000		
Interest on capital@20% A 43000 B 60000	10,3000		
Provision for bad debts	10,000		
Net profit	3,89,000		
<b>Total</b>	<b>2,18,2000</b>	<b>Total</b>	<b>2,18,2000</b>

## Other Information

- 1) Remuneration and interest to partners is paid as per partnership deed
- 2) Depreciation as per income tax rules Rs. 100000
- 3) Firm paid bonus to employees Rs. 20,400 relating to last year on 15-12-2019.
- 4) Other expenses include donation to approved charitable institution for the purpose of family planning Rs. 45,000.
- 5) Fees for technical services are paid out of India wherein TDS rules apply. Tax has been deducted at source on time on 31 July 2019 but it is deposited to Government 21 days late on 31 August , 2019.
- 6) The firm complies with conditions of section 184 and 40(b)
- 7) Income and investments of Mr. A and Mr. B are as follows:

Particulars	Mr. A (Rs.)	Mr. B (Rs.)
Interest on Government Securities	60000	56000
Interest on Bank Deposit (gross)	4500	5000
Dividend from Indian Company	20000	22000
Contribution to PPF	100000	110000
Interest on listed Debentures (net)	6300	6300

- 8) Mr. A received gift of Rs. 80,000 from a friend.

**Solution:****Computation of Total Income of AB and Co. for the assessment year 2020-21****Calculation of Business Income**

Net Profit as per P&L A/C	389000	
<i>Add:</i> Inadmissible Expenses		
Excess depreciation [120000-100000]	20000	
Remuneration to partners	200000	
Interest on capital in excess of 12% p.a.		

A: $43000 \times 8/20$ 17200		
B: $60000 \times 8/20$ 24000	41200	
Provision for bad debts	10000	
Donations	45000	
Less: Admissible Expenses		
Bonus to employees	(20400)	
Less: Income taxable under head capital gain and other sources		
LTCG	(100000)	
Lottery prize	(35000)	
Book profit	549800	
Less: Remuneration to partners		
On First 300000 of book profit @90%	270000	
Balance 234800 @60%	140880	
410880 or Rs. 200000 whichever is less	(200000)	
Business Income		349800
Income under the head capital gain [LTCG]		100000
Income from other sources		
Lottery prize $35000 \times 100/70$		50000
Gross total income		499800
Less: Deduction u/s 80		
80G [100% of 45000 or 10% of {499800 – 100000}]		(39980)
Taxable Income		459820

Share of A and B in the income of the firm Rs. 2,29,910 (4,59,820/2)

**Computation of tax on Total Income of AB and Co. for the assessment year 2020-21**

Tax on winning from lotteries (30% of Rs. 50,000)	15,000
Tax on long-term capital gains (20% of Rs. 100,000)	20000
Balance of Total Income 309820 @30%	92946
Total tax	127946
Add: Health and Education Cess @ 4%	5117.8
Total liability	133063.8

Rs. 1,33,060 (round off, subject to setoff of TDS for winning from lotteries )

**Computation of taxable income of partners for the assessment year 2020-21**

<b>Particulars</b>	<b>A</b>	<b>B</b>
Business Salary:		
Remuneration	140000	60000
Interest on capital	25800	36000
Profit share in firm	Exempt	Exempt
Income from other sources		
Interest on Government securities	60000	56000
Interest on Bank deposits	4500	5000
Dividend from Indian companies (being less than Rs. 10 Lacs)	Exempt	Exempt
Interest on listed debentures (6300*100)/90	7000	7000
Gift from a friend	80,000	-
<b>Gross Total Income</b>	<b>317800</b>	<b>164000</b>
<b>Deductions u/s 80-80C PPF</b>	<b>100000</b>	<b>110000</b>
<b>Taxable Income</b>	<b>217800</b>	<b>54000</b>
<b>Tax liability</b>	<b>NIL</b>	<b>NIL</b>
<b>TDS amounting to Rs. 700 to be claimed for refund.</b>		

**Illustration 7:**

Mr. A (40 years) and Mr. B (49 years) are equal partners in a firm of Chartered Accountants, AB Co. On April 1, 2019 they amended their partnership deed and provided for salary and interest to partners as follows:

<b>Particulars</b>	<b>Amount (Rs.)</b>
Salary to A	250,000 p.a.
Salary to B	3,00,000 p.a.
Interest to A and B	24 % p.a.

From the income and expenditure account of the firm compute net income and tax liability of the firm as well as the partner's for the assessment year 2020-21.

**Income and Expenditure Account**  
**For the year ending March 31, 2020**

<b>Particulars</b>	<b>Amount (Rs.)</b>	<b>Particulars</b>	<b>Amount (Rs.)</b>
Office expenses	2,51,000	Receipts from clients	8,40,000
Salary to staff	82,000	Interest on drawings	3,500
Income Tax	39,000		
Salary to A	2,50,000		
Salary to B	3,00,000		
Interest on loan to minor son of X @15%	6000		
Interest on capital@24%	36,000		
A 17000			
B 19000			
Net profit	1,14,500		
<b>Total</b>	<b>843500</b>	<b>Total</b>	<b>8,43,500</b>

Other Information

- 1) Office expenses include expenses not deductible under sections 30 to 37 Rs. 48,000.
- 2) The firm does not comply with conditions of section 184 and 40(b)
- 3) The firm sells a capital asset on August 10, 2019 and LTCG on the same amounts to Rs. 5,50,000.
- 4) The firm has received funds from minor son of X as loan.
- 5) Income and investments of Mr. A and Mr. B are as follows:

Particulars	Mr. A (Rs.)	Mr. B (Rs.)
Investment in 5% Government Loan	12,00,000	11,20,000
Interest from Post office savings bank	4500	5000
Medical Insurance Premium	12000	15000
Dividend from foreign Companies	40000	30000

**Solution:**

**Computation of Total Income of AB and Co. for the assessment year 2020-21**

**Calculation of Business Income**

Particulars	Rs.
Net Profit as per P&L A/C	114500
<i>Add:</i> Inadmissible Expenses	
Income Tax	39000
Salary to A	250000
Salary to B	300000
Interest on capital in excess of 12% p.a.	
A: 17000*12/24	8500
B: 19000*12/24	9500
	18000
Book profit	721500
<i>Less:</i> Remuneration to partners (not allowed as conditions of section 184 & 40(b) are not met )	NIL
Business Income	721500
Taxable Income	721500

Share of A and B in the income of the firm Rs. 721500/2= 360750

**Computation of tax on Total Income for the assessment year 2020-21**

Tax on Rs. 721500@30%	216450
Add: Health and Education Cess @ 4%	8658
Total liability	2,25,108
Total	225110 (round off)

**Computation of taxable income of partners for the assessment year 2020-21**

<b>Particulars</b>	<b>A</b>	<b>B</b>
Business Salary:		
Remuneration	–	–
Interest on capital	–	–
Profit share in firm	Exempt	Exempt
Income from other sources		
Interest on Government Loan (5% of 12,00,000; 5% of 11,20,000)	60000	56000
Interest on Post office savings bank (exempt upto Rs. 3500 u/s 10(15)(i))	1000	1500
Dividend from Foreign companies	40000	30000
Gross Total Income	101000	87500
Deductions u/s 80		
80D Mediclaim Insurance	12000	15000
Taxable Income	89000	72500
Tax liability	NIL	NIL

**TAXATION OF ASSOCIATION OF PERSONS /BODY OF INDIVIDUALS**

'Association of persons' has not been defined in the Income-tax Act. However in the case of *CIT v. Indira Balkrishna* [(1960) 39 ITR 546] the Supreme Court has defined it as:

**"Association of persons"** means an association in which two or more persons join in for a common purpose or common action to produce income, profits or gains.

An association of persons may consist of non-individuals (Companies, firms joint families) [*Ipoth v. CIT (1968) 67 ITR 106 (S.C.)*]. A minor can join an AOP if his lawful guardian gives his consent. [*Murugesan & Bros. v. CIT (1973) 88 ITR 432 (SC)*].

Applying the ratio laid down by the Supreme Court in the case of *G Murugesan and Bros. v. Commissioner of Income-tax (1973, 88 ITR 432)*, the Kerala High Court held in the case of *Commissioner of Income-tax v. Goel C. Dalal and Perin C. Dalal (1990, 184 ITR 248)* that in order to acquire the status of an association of persons, the persons must join in a common purpose or action and the object of the association must be to produce income. It is not enough that the persons receive the income jointly.

For the formation of an AOP, the association need not necessarily be on the basis of a contract, consent and understanding may be presumed [*Shanmugham & Co. v. CIT(1971) 81 ITR 310 (S.C.)*].

Applying the ratio laid down by the Supreme Court in the case of *N.V. Shanmugham & Co. v. Commissioner of Income-tax (1971, 81 ITR 310)* the Calcutta High Court held in the case of *Gopal Chand Sen v. Income-tax Officer and others (1977, 109 ITR 820)* that an assessment of business income has to be done in the hands of receivers and in such an assessment, the receivers are never assessed as independent earners of income. The income in the hands of the receiver is assessable in the like manner and to the same extent as it would have been assessed on the real owners.

However, co-owners, co-heirs or co-legatees do not constitute an AOP in respect of the income of the joint or common asset by reason only of their jural relationship. But if they write themselves with the objective of earning income they constitute an AOP for assessment purposes. [*Estate of Mohamed Rowther v. CIT (1963, 49 ITR*

39)]. Section 26 of the Income-tax Act provides that where property consisting of building or buildings and lands appurtenant thereto is owned by two or more persons in definite and ascertainable shares, such persons shall not, in respect of such property be assessed as an AOP, but on their respective share of income therefrom.

In order to constitute an association of persons, there must be joining together in a common purpose or in a common action, the object of which is to produce income, profits and gains. Though a body of individuals is not identical with an association of persons, they have some similarities. An association of persons may consist of non-individuals also but a body of individuals has to consist only of human beings. The word 'body' would require an association for some common purpose or for a common cause or there must be unity under some common tie or occupation. A mere collection of individuals without a common tie or common aid cannot be taken to be a body of individuals failing under Section 2(31) of the Income-tax Act, 1961. [See *CITv. Deghamwala Estates (1980, 121 ITR 684)*].

### Tax Liability of Association of Persons /Body of individuals

With effect from assessment year 1989-90, the following provisions are applicable to assessees other than companies, co-operative societies and societies registered under the Societies Registration Act, 1860 or any law corresponding to that Act in force in any part of India.

- (1) Interest paid by the AOP to a member will not be allowed as deduction from the income of the AOP [(Section 40(ba)]. In cases where interest is paid by the AOP to any member, who has also paid interest to the AOP, the amount of interest, that will be disallowed, is the amount of interest paid by the AOP to the member less the amount of interest paid to the AOP by the member [(Explanation 1 to section 40(ba)].
- (2) In cases where an individual is a member of an AOP in a representative capacity, any interest paid by the AOP to such individual or by such individual to the AOP, otherwise than in a representative capacity will not be subject to disallowance under explanation 2(i) to Section 40(ba).
- (3) In the cases of interest paid by AOP to such individual or by such individual to the AOP in a representative capacity any interest paid by the AOP to the person represented by such person or vice versa, will not be allowed under Section 40(ba) [Explanation 2(ii) to Section 40(ba)].
- (4) Explanation 3 to Section 40(ba) further provides that where an individual is a member of the AOP otherwise than as member in a representative capacity, any interest paid by the AOP to such individual will not be disallowed if the interest is received by him on behalf of any other person.
- (5) Any salary, bonus, commission or remuneration (by whatever name called) paid by the AOP to a member will not be allowed as a deduction.

Section 167B makes the following provisions as regards the incidence of charge of tax on the association of persons.

#### A. Where shares of members are determinate

In this case, tax is chargeable on the income of the association of persons at the same rate as applicable to an individual. However, where the total income of any member of the association of persons for the previous year (excluding his share of income from the association of persons) exceeds the maximum amount not chargeable to tax in the case of an individual, tax will be charged on the total income of the AOP at the maximum marginal rate of 30%, i.e. the highest slab applicable to an individual.

More so, where the total income of any member of the AOP, irrespective of whether or not it exceeds the maximum amount not chargeable to tax in the case of an individual, is chargeable to tax at a rate higher than the maximum marginal rate (e.g. foreign company), tax will be charged on the total income of the AOP at such higher rate for that portion of the income of AOP which relates to the share of such member and the balance of income at a maximum marginal rate of tax.

Note: 1. Some incomes are taxable at special rates.

2. Provisions of alternate minimum tax under section 115JC to 115JF shall apply.

**Illustration 1:**

Mr. A, Mr. B and a foreign company X Ltd. are members of a AOP sharing profits and losses in the ratio of 2:2:1. The total income of the AOP is Rs. 2,50,000 including long term capital gains Rs. 40, 000. Calculate tax liability of the AOP for AY 2020-21.

**Solution :** Foreign company X Ltd. is taxable at a rate higher than maximum marginal rate ( i.e. 40%)

Tax on LTCG	40,000 at 20%	8,000
Tax on share of X Ltd. (2,10,000 *40%*1/5)		16,800
Balance	(2,10,000 *40%*1/5)	50,400
Total Tax		75,200
Add Cess (4%)		3008
Tax liability		78,208
Total		78,210 (round off)

**B. Where the shares of the members are indeterminate**

In this case, tax will be charged on the total income of the AOP at the maximum marginal rate, that is, the rate of tax as well as surcharge, if any, applicable to the highest slab of income in the case of an individual as specified in the Finance Act of the relevant year. However, if income of any member of AOP is chargeable to tax at a rate higher than maximum marginal rate, then the rate of tax for the entire income of AOP shall be such higher rate.

The individual shares of the members in the whole or any part of the income of the AOP will be deemed to be indeterminate or unknown if such shares are indeterminate or unknown on the date of formation of the AOP, or at any time thereafter.

**Method of Computing Share of a Member of Association of Persons / Body of individuals [Section 67A]**

Section 67A seeks to provide for the method of computing a member's share in the income of an association of persons or a body of individuals, wherein the shares of the members are determinate, in the same manner as provided for in Sub-sections (1) to (3) of Section 67 for computing a partner's share in a firm.

This section lays down the following methods of computing the member's share:

- (a) Any interest, salary, bonus, commission or remuneration, by whatever name called, paid to any member in respect of the previous year shall be deducted from the total income of the association or body and the balance ascertained and apportioned among the members in the proportion in which they are entitled to share the income of the association or body.
- (b) Where the amount apportioned to a member under (a) hereinabove is a profit, any interest, salary, bonus, commission or remuneration paid to the member by the AOP in respect of the previous year shall be added to that amount - the result shall constitute the member's share in the income of the association or body.
- (c) Where the amount apportioned to a member under (a) is a loss, any interest, salary, bonus, commission or remuneration aforesaid paid to the member by the association or body in respect of the previous year

shall be adjusted against that amount, the result shall be adjusted against that amount, and the result shall be treated as the member's share in the income of the association or body.

**Notes:**

1. The share of each member of AOP/BOI shall be apportioned under the various heads of income as is determined while computing the income of the AOP/BOI.
2. Deductions under section 80 to the extent allowed to AOP/BOI shall not be allowed to the members.

**Taxation of share of income of a member of AOP/BOI**

Section 86 relates to shares of members of an association of persons or a body of individuals in the income of the association or body. This section provides that if the assessee is a member of an association of persons or a body of individuals (other than a company or a Co-operative society or a Society registered under the Societies Registration Act, 1860, or any law corresponding to that Act in force in any part of India), his share in the income of the association or body, computed in the manner provided in Section 67A shall not be liable to tax.

Further,

The taxability of share of income of a member of AOP/BOI depends on the rate at which income of such AOP/BOI is taxable:

1. Where AOP/BOI is chargeable to tax on its total income at the maximum marginal rate or any higher rate, the share of the member shall not be included in his total income.
2. Where AOP/BOI is chargeable to tax on its total income at the rate applicable to individuals (normal rate) and tax is paid, share of income of a member shall be chargeable to tax as part of his total income and rebate under section 86 shall be claimed.
3. Where AOP/BOI is chargeable to tax on its total income at the rate applicable to individuals (normal rate) and no tax is chargeable, share of income of a member shall be chargeable to tax as part of his total income and no rebate under section 86 shall be claimed.

**Assessment in case of Dissolution of an Association of Persons [Section 177]**

Where any business or profession carried on by an AOP has been discontinued or an AOP is dissolved, the Assessing Officer shall make an assessment of the total income of the AOP as if no such discontinuance or dissolution had taken place, and all provisions of this Act, including the provisions relating to the levy of penalty or any other sum chargeable under any provisions of the Income-tax Act shall apply.

Every person who was at the time of such discontinuance or dissolution a member of the AOP and the legal representative of any such person who is deceased, shall jointly and severally be liable for the amount of tax, penalty or other sum payable.

Where such discontinuance or dissolution takes place after any proceeding in respect of an assessment year have commenced, the proceedings may be continued against the members from the stage at which the proceedings stood at the time of such discontinuance or dissolution.

**TAXATION OF CO-OPERATIVE SOCIETIES**

**Meaning [Section 2(10)]**

'Co-operative Society' means a co-operative society registered under the Co-operative Societies Act, 1912, or under any other law for the time being in force in any state for the registration of co-operative societies. The Income of the co-operative society is computed in the same manner as provided for other assesses. A co-operative society is entitled to the deductions from its gross total income u/s 80G, 80GGA, 80GGC, 80IA, 80-IB,

80JJA and 80P.

A regional rural bank (to which provisions of the Regional Rural Bank Act, 1976, apply) is deemed to be a co-operative society [Circular No. 319 dated 11.1.1982].

### Computation of Income of Co-operative Societies

The income of a co-operative society is computed in the same manner as provided for other assessee's under the Act.

The provisions under various heads of income, clubbing of incomes, set off and brought forward losses, deductions under section 80 shall apply.

Further, the subsidy given by the government to a co-operative society for meeting managerial expenses and admission fee collected by the society is treated as revenue receipt and liable to tax. [*Ludhiana Central Co-operative Consumers' Stores Ltd. v. C.I.T (1980) 122, I.T.R. 942*]. There is, however difference of opinion with regard to tax treatment of 'subsidy' received from the Government. Distinguishing the ratio laid down by the Punjab & Haryana High Court in the case of *Ludhiana Central Co-operative Consumers' Stores Ltd. v. Commissioner of Income-tax (1980, 122 ITR 942)*, the Punjab & Haryana High Court held in the case of *Commissioner of Income-tax v. Jindal Brothers Rice Mills (1989, 179 ITR 470)* that depreciation is allowable on the cost of the machinery or plant reduced by the amount of the subsidy as actual cost stands reduced by the percentage allowed by the subsidy. Though this case was followed by it in the case of *Commissioner of Income-tax v. Janak Steel Tubes (Pvt.) Ltd. (1989, 179 ITR 536)* (the capital subsidy should be deducted from the value of plant and machinery) but had been dissented from by the Bombay, Madras and Rajasthan High Courts in the following cases:

- (i) *Srinivas Industries v. Commissioner of Income-tax (1991, 188 ITR 22)*: The Madras High Court held that the subsidy really partook the character of cash grant expendable for any purpose-consequently, the amount of subsidy granted could not be deducted from the capital cost of the machinery.
- (ii) In *Commissioner of Income-tax v. Elys Plastics Pvt. Ltd. (1991, 188 ITR 11)* the Bombay High Court held that the subsidies were not deductible in computing the cost of plant and machinery for purposes of allowing depreciation.
- (iii) In *Commissioner of Income-tax v. Ambica Electrolytic Capacitors (P) Ltd. and others (1991, 191 ITR 494)* the Rajasthan High Court held that the subsidy or investment subsidy given by the Government cannot be deducted from the actual cost for purposes of investment or depreciation allowance.

### Rates of Income-tax on Co-operative Society

The rates of income-tax applicable to a co-operative society for the assessment year 2018-19 are as follows:

1. Where the total income does not exceed Rs. 10,000	10% of total income
2. Where the total income exceeds Rs. 10,000 but total income does not exceeds Rs. 20,000.	Rs. 1,000 plus 20% of the amount by which income exceeds Rs. 10,000
3. Where the total income exceeds Rs. 20,000	Rs. 3,000 plus 30% of the amount by which income exceeds Rs. 20,000

Health and Education cess @ 4%.

Surcharge @12% shall be applicable where the total income exceeds Rs. 1 crore

Note : 1. Some incomes are taxable at special rates.

2. Provisions of alternate minimum tax under section 115JC to 115JF shall apply.

**Deduction in respect of income of co-operative societies [Section 80P]**

Section 80P provides for certain deductions from the gross total income of a Co-operative Society. These deductions are:

- (a) In the case of Co-operative Society engaged in:
- (i) the business of Banking or providing credit facilities to its members, or
  - (ii) a cottage industry, or
  - (iii) the marketing of the agricultural produce grown by its members, or
  - (iv) the purchase of agricultural implements, seeds, livestock or other articles intended for agriculture for purpose of supplying them to its members, or
  - (v) the processing, without the aid of power, of the agricultural produce of its members, or
  - (vi) the collective disposal of the labour of its members, or
  - (vii) fishing or allied activities, i.e., catching, curing, processing, preserving, storing or marketing of fish or the purchase of materials and equipment in connection therewith for the purpose of supplying them to its members,

the whole of the amount of profits and gains of business attributable to any one or more of such activities shall be deducted from the gross total income provided that in the case of a co-operative society falling under Sub-clause (vi) or (vii), the rules and bye-laws of the society restrict the voting rights to the following classes of its members:

- (i) the individuals who contribute their labour or carry on the fishing or allied activities;
  - (ii) the co-operative credit societies which provide financial assistance to the society;
  - (iii) the State Government.
- (b) In the case of primary co-operative society engaged in supplying milk, oilseeds, fruits, vegetables raised or grown by its members to
- (i) a federal co-operative society engaged in supplying the above mentioned products; or
  - (ii) a Government or a local authority; or
  - (iii) a Government Company or a Corporation established by or under a Central, State or a Provincial Act (being a company or corporation engaged in supplying the above mentioned products to the public).

the whole of the amount of profits and gains of such business shall be deducted from the gross total income.

In the case of a co-operative society engaged in activities other than those specified in clauses (a) or (b) either independently of, or in addition to, profits and gains attributable to the activities mentioned at clauses (a) and (b) deduction from the gross total income will be allowed to the extent of Rs. 50,000.

- (c) Where such co-operative society is a Consumers' Co-operative Society, the deduction shall be Rs. 1,00,000.
- (d) In the case of every co-operative society, the whole of the income by way of interest or dividends derived from its investments with any other co-operative society shall be deducted from the gross total income.
- (e) In the case of every co-operative society, the whole of the income derived by the society from the letting

of godowns or warehouses for storage, processing or facilitating the marketing of commodities shall be deducted from its gross total income.

- (f) In the case of every co-operative society, not being a housing society or an urban consumers' society, or a society carrying on transport business or a society engaged in the performance of any manufacturing operations with the aid of power, where the gross total income does not exceed Rs. 20,000 the amount of any income by way of interest on securities or any income from house property shall be deducted from the gross total income.

#### *Urban Consumers' Co-operative Society*

An urban consumers' co-operative society means a society for the benefit of consumers, within the limits of a municipal corporation, municipality, notified areas committee, town area or, cantonment [Explanation to Section 80P(2)].

The provisions of this Section shall not apply in relation to any cooperative bank other than a primary agricultural credit society or a primary cooperative agricultural and rural development bank.

#### **Other points**

- Amount received for letting of godowns, incidental services of taking delivery of stock at rail-head and transporting it to godowns were also rendered and amount received was described as 'commission' was wholly exemption I.T. v. South Arcot District Co-operative Marketing Society Ltd. (1989) 43 Taxman 328/176 ITR 117 (SC).
- Income from ginning and pressing of cotton is exempt. Broach Distt. Co-operative Cotton Sales, Ginning & Pressing Society Ltd. v. CIT (1989) 177 ITR 418/44 Taxman 439 (SC).
- Where assessee, an apex co-operative society, derived (i) interest on cash security furnished by it for carrying on sugar agency business, and (ii) interest on temporary loans given by it for financing sugar business, while former interest was not exempt, latter was exempt under Section 14(3)(iii) of the 1922 Act, CIT v. U.P. Co-operative Federation Ltd. (1989) 176 ITR 435/43 Taxman 20 (SC).
- Amount of subsidy received by assessee from National Co-operative Development Corpn. towards loss incurred on account of price fluctuation qualifies for deduction under Section 81 (1)(c) - CIT v. Punjab State Co-operative Supply & Marketing Federation Ltd. (1989) 46 Taxman 156 (Punj. & Har.).
- Proportionate expenditure relating to such business activities of assessee co-operative society as are contemplated by Section 80P(2) is not to be disallowed. Baghapurana Co-operative Marketing Society Ltd. v. CIT (1989) 178 ITR, 653/44 Taxman 92 (Punj. & Har.).
- In the cases of agricultural produce, the agricultural produce marketed by assessee co-operative society need not have been produced by assessee's members - CIT v. Punjab State Co-operative Supply & Marketing Federation Ltd. (1989) 46 Taxman 156 (Punj. & Har.).
- The expression "the marketing of the agricultural produce of its members means that agricultural produce should be owned by its members, whether supplied by them (that is, the members) or purchased from the market or acquired from any other producer. C.I.T. v. Haryana State Co-operative Supply & Marketing Federation Ltd. (1989) 79 CTR (Punj. & Har.) 94.
- Short-term call deposits are investment within the meaning of Section 80P(2)(d) CIT v. Haryana Co-operative Sugar Mills Ltd. (1989) 46 Taxman 28 (Punj. & Har.).

#### **Assessment of Co-operative Societies**

The following are the provisions which are specifically applicable to the assessment of Co-operative Societies -

- I. **Co-operative Housing Society.** Under Section 27(iii), a member of co-operative society, company or other association of persons to whom a building or part thereof is allotted or leased under a house building scheme of the society, company or association, as the case may be, shall be deemed to be owner of that building or part thereof.

Clause (iiia) further provides that a person who is allowed to take or retain possession of any building or part thereof in part performance of a contract of the nature referred to in Section 53A of the Transfer of Property Act, 1882 shall be deemed to be the owner of that building or part thereof; and

As per Clause (iiib), a person who acquires any rights (excluding any rights by way of a lease from month to month or for a period not exceeding one year) in or with respect to any building or part thereof, by virtue of any such transaction as is referred to in Clause (f) of Section 269UA, shall be deemed to be the owner of that building or part thereof.

Clause (f) of Section 269UA, it may be noted, defines “transfer” for the purposes of Chapter XX-C of the Income- tax Act, dealing with purchase by Central Government of immovable properties in certain cases of transfer.

- II. **Profits and Gains of Co-operative Society from insurance business [Section 44].** The profits and gains of any business of insurance carried on by a Co-operative Society shall be computed in accordance with the rules contained in the First Schedule.

In this connection, the First Schedule and Rule 6E of the Income-tax Rules, 1962 provides as under:

The profits of non-life insurance business, e.g., Fire insurance business, marine insurance business, general insurance business etc. shall be the profits disclosed by the annual accounts required to be prepared under the Insurance Act, 1938 subject to the following adjustments:

- (i) If such profits are arrived at after deducting any expenditure or allowance which is not admissible under Sections 30 to 43B of the Income-tax Act, such expenditure or allowance shall be added back to the profits.
- (ii) The reserve for unexpired risks shall be allowed as a deduction to the following extent:
  - (a) where the insurance business relates to fire insurance or miscellaneous insurance - 50% of the net premium income of such business of the previous year;
  - (b) where the insurance business relates to marine insurance, 100% of the net premium income of such business of the previous year.

‘Net premium income’ means the amount of premium received, as reduced by the amount of re-insurance premiums paid during the relevant previous year.

In the context of computing the total income of co-operative society, the following cases are worth noting.

(1) Where the credit facility is extended to members of the society by virtue of sale of goods to them by consumers’ co-operative society, the exemption is not available. When the society sells goods on credit to its members, such transaction cannot be construed as a credit society to which the benefit of Section 80P(2)(a)(i) can be extended. [*Rodier Mill Employees’ Co-operative Stores Ltd. v. CIT (1982) 135 ITR 355*].

Following the ratio laid down by the Madras High Court in the case of *Rodier Mill Employees’ Co-operative Stores Ltd. v. Commissioner of Income-tax (1982, 135 ITR 355)*, the Kerala High Court held in the case of *Kerala Co-operative Consumers Federation Ltd. v. Commissioner of Income-tax (1988, 170 ITR 455)* that the words ‘providing credit facilities’, occurring in Section 80P(2)(a)(i) of the Income-tax Act, 1961 should be construed as similar to, or akin to the ‘carrying on the business of banking’, preceding the words “or providing credit facilities” in the same sub-section. The words ‘providing credit facilities to its members’ means providing credit by way of loans and not selling goods on credit.

(2) Where society purchases auto-rickshaws and sells them to members on hire-purchase, it is not providing credit facility to members and not entitled to exemption [*C.I.T. v. Madras Auto Rickshaw Drivers' Co-operative Society (1983) 143 ITR 981*]. In this case it was held that the tax relief under Section 80P(2)(a)(i) of the Income-tax Act, is a grant not to a category of income but to a category of assessee namely, a co-operative society answering the description of a society engaged in carrying on the business of providing credit facilities to its members. If the society in question does not answer to this description, it is not entitled to the relief.

(3) In *Bihar State Co-operative Bank Ltd. v. C.I.T. [(1960) 39 I.T.R. 114]* the Supreme Court has held that if a co-operative society carrying on banking business invests its circulating capital in such a manner that it is readily available, the interest on such investment shall constitute income from banking business and therefore shall be exempt in the hands of the co-operative society.

(4) Interest received on Government Securities held by co-operative society as its stock-in-trade qualifies for deduction from gross total income. But the deduction is inapplicable to interest received from Government Securities held as investments. [*CIT v. Bombay State Co-operative Bank Ltd. (1968) 70 ITR 86 (S.C.)*].

The Madhya Pradesh High Court held in the case of *M.P. State Co-operative Bank Ltd. v. Addl. Commissioner of Income-tax (1979, 119 ITR 327)* that income from investment of reserve capital in securities was not a part of the income from banking business and did not qualify for exemption. Similarly, the interest income from investment of provident fund income did not form part of the income from the banking business and did not qualify for exemption under Section 80(i)(a) (now Section 80P). Distinguishing the ratio laid down in this case, the Madhya Pradesh High Court held in the case of *Commissioner of Income-tax v. Bhopal Co-operative Central Bank Ltd. (1987, 164 ITR 713)* that the security deposits made are in accordance with the Banking Regulation Act, 1949 and interest income received on deposits formed part of income from business of banking and exempt under Section 80P(2)(i) of the Income-tax Act, 1961.

The Allahabad High Court held in the case of *Addl. Commissioner of Income-tax v. U.P. Co-operative Cane Union (1978, 114 ITR 70)* that selling goods on credit was only a mode of carrying on business. It did not become a business of providing credit facility. Following this case, the Allahabad High Court held in the case of *Commissioner of Income-tax v. U.P. Co-operative Cane Union Federation Ltd. (1980, 122 ITR 913)* that the expression 'providing credit facilities' in Section 80P(2)(a)(i) would comprehend the business of lending money on interest. It would also comprehend the business of lending services on profit for guaranteeing payments because guaranteeing payment is as much a part of banking business for affording credit facility as advancing loans.

However, where a co-operative society holds securities as per requirements of Banking Regulation Act and directions of the RBI, the deduction is available on such interest income. Similarly, subsidy from Government for opening new branches and giving loans to poorer sections at lower rate of interest, is income attributable to banking business [*CIT v. Madurai District Central Co-operative Bank Ltd. (1984) 148 ITR 196*].

(5) The Income earned by a co-operative society carrying on the business of banking and providing credit facilities to its members from commission and brokerage by dealing in bills of exchange, subsidy from Government, admission fee from members, incidental charges and financial penalties is attributable to the business of banking of providing credit facilities to its members and hence deductible under Section 80P(2)(a) (i) [*CIT v. Dhar Central Co-operative Bank (1984) 149 ITR 438 (MP)*].

Following its decision in the case of *Commissioner of Income-tax v. Dhar Central Co-operative Bank (1984, 149 ITR 438)*, the Madhya Pradesh High Court held in the case of *Commissioner of Income-tax v. Bhopal Co-operative Central Bank Ltd. (1988, 172 ITR 423)* that a co-operative society carrying on the business of banking is entitled to exemption in respect of interest on securities, commission, subsidy, donation and locker rent. Again, the said decision was followed by it in the case of *Madhya Pradesh Rajya Sahakari Bank v. Commissioner of Income-tax (1988, 174 ITR 150)* holding that the income from commission, exchange and other miscellaneous

income was attributable to the business of banking and that the assessee was entitled to exemption under Section 81 (now 80P) of the Income-tax Act, 1961 in respect thereof.

(6) A society which buys and sells products of other societies or individuals is not entitled to exemption. Where a society manufactures and sells its own products or the products of its members, such society is entitled to exemption. Hence, the Central Cottage Industries Emporium, New Delhi, is not entitled to exemption under Section 80P [Addl. C.I.T. v. Indian Co-operative Union Ltd. (1982) 134 ITR 108 (Delhi)].

If the godown or warehouse is let for a purpose other than storage, processing of facilitating the marketing of commodities, the income derived therefrom by a co-operative society would not be deductible under Section 80P C.I.T. v. Ahmedabad Maskati Cloth Dealers Co-operative Warehouses Society Ltd. [(1986) 162 ITR 142 (Guj.)] it was also held in this case that shops in which wholesale or retail business in cloth is carried on cannot come within the meaning of 'godowns' or 'warehouses'.

The Gujarat High Court's decision in the case of *Commissioner of Income-tax v. Ahmedabad Maskati Cloth Dealers Co-operative Warehouses Society Ltd.* (1986, 162 ITR 142) had since been approved by the Supreme Court in the case of South Arcot District Co-operative Marketing Society Ltd. (infra). The Gujarat High Court had, inter alia, held that the words facilitating the marketing of commodities' would not lend colour to the words 'godowns or warehouses' so as to enlarge their meaning.

**Illustration 1:**

*Delhi Co-operative Society derived the following incomes during the previous year (1.4.2019 to 31.3.2020 - Assessment Year 2020-21).*

(1)	Marketing of agricultural produce of its members	10,000
(2)	Interest from members on delayed payment of the price of goods purchased	1,000
(3)	Processing (without aid of power) of agricultural produce of its members	8,000
(4)	Supplying milk to the Government (raised by its members)	15,000
(5)	Agency business	25,000
(6)	Dividends from other Co-operative Societies	15,000
(7)	Income from letting of godowns	20,000
(8)	Income from House Property	30,000

Compute the total income of the Delhi Co-operative Society.

**Solution:**

Computation of total income of Delhi Co-operative Society

(1) Income from House Property	30,000	
Letting of godowns	20,000	50,000
(2) Income from Business:		
Marketing of agricultural product	10,000	
Processing of goods	8,000	
Supplying milk	15,000	
Agency business	25,000	58,000

(3) Income from other sources:		
Interest from members	1,000	
Dividends	15,000	16,000
Gross Income		1,24,000
Deductions under Section 80P:		
(1) Letting of godowns	20,000	
(2) Marketing of agricultural produce	10,000	
(3) Processing of goods	8,000	
(4) Supplying milk	15,000	
(5) Agency business	25,000	
(6) Dividends	15,000	93,000
Total income		31,000

Notes:

- (1) Interest from members Rs. 1,000 is not deductible as it is not from the credit facilities provided to the member and for this purpose society cannot be said to be a credit society [*Rodier Mill Employees' Co-operative Stores Ltd. v. CIT (1982) 135 ITR 355*].
- (2) The gross total income of the society exceeds Rs. 20,000 hence deduction regarding income from house property is not available.

### TAX EXEMPTIONS TO POLITICAL PARTIES (SECTION 13A)

'Political party' means an association or body of individual citizens of India registered with the Election Commission of India as a political party and includes a political party deemed to be registered with that Election Commission of India.

Political parties are liable to pay tax on their income and they are assessed as 'An association of persons'. However, the income derived by these parties as income by way of voluntary contributions, Income from House Property; and Income from Other Sources or Capital Gains are exempt from subject to the following conditions:

- (i) the party keeps and maintains such books of account and other documents as would enable the Assessing Officer to properly deduce the income;
- (ii) in respect of each such voluntary contribution in excess of 20,000, the party keeps and maintains a record of the contributions and names and addresses of the persons who have made such contribution; and
- (iii) the accounts of the party are audited by a Chartered Accountant or other qualified accountant.
- (iv) No donation of Rs. 2000 or more can be received by a Political Party otherwise than by an account payee cheque/draft/ECS through a bank account or through electoral bonds. (w.e.f. AY 2018-19)

Return of income under section 139(4B) should be filed by the Political Party on or before due date of filing of return u/s 139(1), otherwise exemption under section 13A will not be given. (w.e.f. AY 2018-19)

The Chief Executive Officer of the political party is required to file a return of income if the total income (computed under this Act without giving effect to the provisions of Section 13A) exceeds the maximum amount which is not chargeable to income-tax. In this connection, the provisions of Section 139(1) shall apply.

## ELECTORAL TRUST

'Electoral Trust' means a trust so approved by the Board in accordance with the scheme made in this regard by the Central Government

### Voluntary contributions received by an Electoral Trust (Section 13B)

Any voluntary contributions received by an electoral trust shall not be included in the total income of the previous year of such electoral trust, if -

- (a) such electoral trust distributes to any political party, registered under section 29A of the Representation of the People Act, 1951, during the said previous year, ninety-five per cent of the aggregate donations received by it during the said previous year along with the surplus, if any brought forward from any earlier previous year; and
- (b) such electoral trust functions in accordance with the rules made by the Central Government.

## TAX EXEMPTIONS FOR CHARITABLE TRUSTS AND INSTITUTIONS

**Trust** : Section 3 of the Indian Trusts Act defines a trust to mean "an obligation annexed to the ownership of property and arising out of a confidence reposed in and accepted by the owner, or declared and accepted by him for the benefit of another and the owner".

**Institution**: An organisation with a constitution composed of a President, Vice-President, Secretary, Committee Members and ordinary members, is known as an Institution. The activities of the institution and its office-holders are regulated by rules and bye-laws of the institution. A university or a Chamber of Commerce is an Institution.

**Charitable purpose**: The term 'charitable purpose' has been defined in this Act in a wider sense than what is commonly understood. According to Section 2(15) of the Act, it includes relief of the poor, education, yoga medical relief, preservation of environment (including watersheds, forests and wildlife) and preservation of monuments or places or objects of artistic or historic interest and advancement of any other object of general public utility not involving the carrying on of any activity for profit.

In order to qualify for tax exemptions the charity must be of a public character, and the trust or institution should not be created or established for the benefit of any particular religious community or caste, if the trust or institution is established for the benefit of the member of a club or employees of a factory, it would not be a public charitable trust. Vide Circular No. 395 dated Sept. 24, 1984 promotion of sports and games is considered to be a charitable purpose within the meaning of Section 2(15). Accordingly an association or institution, engaged in the promotion of sports or games can claim exemption under Section 11, even if it is not approved under Section 10(23).

Provided that the advancement of any other object of general public utility shall not be a charitable purpose, if it involves the carrying on of any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business, for a cess or fee or any other consideration, irrespective of the nature of use or application, or retention, of the income from such activity, unless -

- (i) such activity is undertaken in the course of actual carrying out of such advancement of any other object of general public utility; and
- (ii) the aggregate receipts from such activity or activities during the previous year, do not exceed twenty per cent of the total receipts, of the trust or institution undertaking such activity or activities, of that previous year;

### Income not to be included in the Total Income

According to Section 11(1), the following items of income are not to be included in the total income of the previous year of the assessee who is in receipt of the same:

- (i) **Income derived from property held under trust wholly for charitable or religious purposes:** Income derived from property held under trust wholly for charitable or religious purposes shall be exempt to the extent to which such income is applied for such purposes in India and where any such income is accumulated or set apart for application to such purposes in India, to the extent to which the income so accumulated or set apart is not in excess of 15% of the income from such property.
- (ii) **Income derived from property held under trust in part only for charitable or religious purposes:** Income derived from property held under trust in part only for charitable or religious purposes shall be exempt. This exemption would, however, be available only for trusts created before 1.4.1962. Further, where any such income is finally set apart for application to such purposes in India, shall be exempt to the extent to which the income so set apart is not in excess of 15% of the income from such property.
- (iii) **Income from property held under trust created on or after 1.4.1952:** for a charitable purpose which tends to promote international welfare in which India is interested shall be exempt to the extent to which such income is applied for such charitable purposes outside India.
- (iv) **Income from property held under trust created before 1.4.1952** for charitable or religious purposes shall be exempt to the extent to which such income is applied for such purposes outside India. This exemption is, however, subject to the condition that the Central Board of Direct Taxes has, by a general or special order, issued a direction in either of the above two cases that the income in question would not be included in the total income of the person in receipt of such income.
- (v) **Income in the form of voluntary contributions** made with a specific direction that they shall form part of the corpus of the trust or institution shall be fully exempt.

#### Explanation :

In respect of items (i) and (ii) above:

- (1) In computing the 15% of the income which may be accumulated or set apart, any such voluntary contributions as are referred to in Section 12 (dealt with later in this Chapter) shall be deemed to be part of the income.
- (2) If, in the previous year, the income applied to charitable or religious purposes in India falls short of 85% of the income derived during that year from property held under trust, by any amount on account of (i) not receiving the income during that year, or (ii) for any other reason, then:
  - (a) In case referred to in (i), so much of the income applied to such purpose in India during the previous year in which the income is received or during the previous year immediately following as does not exceed the said amount shall be deemed to be income applied to such purposes during the previous year in which the income was derived; and the income so deemed to have been applied shall not be taken into account in calculating the amount of income applied to such purposes during the previous year in which the income is received or during the previous year immediately following, as the case may be.
  - (b) In case referred to in (ii), so much of the income applied to such purposes in India during the previous year immediately following the previous year in which the income was derived as does not exceed the said amount shall be deemed to be income applied to such purposes during the previous year in which the income was derived; and the income so deemed to have been applied shall not be taken into account in calculating the amount of income applied to such purposes during the previous year immediately following the previous year in which the income was derived.

Any amount credited or paid, out of income referred to in clause (a) or clause (b) read with Explanation 1, to any other trust or institution registered under section 12AA, being contribution with a specific direction that they shall form part of the corpus of the trust or institution, shall not be treated as application of income for charitable or religious purposes. (w.e.f. AY 2018-19)

For the purposes of determining the amount of application of income, the provisions of section 40(a)(ia) relating to 30% disallowance for non deduction of TDS and section 40A(3) and 40A(3A) relating to payment exceeding Rs. 10,000, shall, mutatis mutandis, apply as they apply in computing the income chargeable under the head “Profits and gains of business or profession”

Where any income as discussed in (a) and (b) above is not applied to charitable or religious purposes in India within the prescribed time, then such income shall be deemed to be the income of the person in receipt thereof:

- (a) In case of not receiving the income: Such income shall be deemed to be the income of the previous year immediately following the previous year in which the income was received.
- (b) In any other case: Such income shall be deemed to be the income of the previous year immediately following the previous year in which the income was derived [Clause (1B)].

### Capital Gains [Section 11(1A)]

#### Asset held wholly for religious purposes or charitable purposes

Sometimes a capital asset held under trust wholly for charitable or religious purposes is transferred resulting in a capital gain. The net consideration received on such transfer may be utilised wholly or in part in acquiring another capital asset to be so held wholly for religious or charitable purposes. In such cases the capital gains arising from the transfer shall be deemed to have been applied for charitable or religious purposes to the extent stated herein below:

- (i) Where the whole of the net consideration is utilised for acquiring the new capital assets, so much of the capital gains.
- (ii) Where only a part of the net consideration is utilised for acquiring the new capital asset, so much of the capital gain as is equal to the amount by which the amount so utilised exceeds the cost of the transferred asset.

**Example 1 :** A charitable trust had a capital asset the cost of which was Rs.80,000 and it sold the same for Rs. 1,00,000. The whole of the consideration, i.e., Rs. 1,00,000 will be exempt from capital gains tax if a new capital asset is bought for Rs. 1,00,000.

**Example 2 :** If a trust had a capital asset costing Rs.1,00,000 and sold the same for Rs. 1,50,000 and then bought a capital asset for Rs. 1,30,000, then the working will be as follows:

Particulars	Rs.
Sale proceeds of old asset	1,50,000
Cost of the old asset	(1,00,000)
Capital gain	50,000
Cost of the new asset	1,30,000
Cost of the old asset	(1,00,000)
Capital gain utilised is	30,000
Capital gain taxable is	20,000

### Assets held partly for religious or charitable purposes

It is quite possible that a capital asset is held by a trust partly for religious or charitable purposes. Where such a capital asset is transferred and the whole or any part of the net consideration is utilised for acquiring another capital asset, the appropriate fraction of the capital gain arising from the transfer shall be deemed to have been applied to charitable or religious purposes to the extent specified here under:

- (i) where the whole of the net consideration is utilised in acquiring the new capital asset, the whole of the appropriate fraction of such capital gain;
- (ii) in any other case, so much of the appropriate fraction of the capital gain as is equal to the amount, if any, by which the appropriate fraction of the amount utilised for acquiring the new asset exceeds the appropriate fraction of the cost of the transferred asset.

“Explanation” to Section 11(1A) provides:

‘Appropriate fraction’ means the fraction which represents the extent to which the income derived from the capital asset transferred was immediately before such transfer applicable to charitable or religious purposes.

‘Cost of the transferred asset’ means the aggregate of the cost of acquisition (as ascertained for the purposes of Section 48 and 49 of the capital asset which is the subject of the transfer and the cost of any improvement thereto within the meaning assigned to that expression in sub-clause (b) of clause (1) of Section 55.

‘Net consideration’ means the full value of the consideration received or accruing as a result of the transfer of the capital asset as reduced by any expenditure incurred wholly and exclusively in connection with such transfer.

#### Illustration 1

*A trust has a capital asset costing Rs. 2,00,000 and 1/2 of its income is utilised for charitable purpose. It is sold for Rs. 3,50,000. If the trust buys another capital asset for Rs. 3,50,000 then appropriate fraction of the capital gain deemed to have been applied for charitable purpose. Supposing that the trust buys another asset for Rs. 2,90,000:*

Particulars	Rs.
Sale proceeds of Capital asset	3,50,000
Cost of the asset sold	2,00,000
Capital gain on transfer of capital asset	1,50,000
Appropriate fraction i.e. 1/2	75,000
Another asset purchased	2,90,000
Appropriate fraction utilised (1/2 of Rs. 2,90,000)=	1,45,000
Appropriate fraction of the original capital asset	
1/2 of Rs. 2,00,000	(1,00,000)
Capital gain utilised	45,000
Capital gain not utilised	30,000

### Accumulations of Income [Section 11(2)]

While dealing with Section 11 it has been stated that accumulation of income from trust property held for charitable purpose is permissible up to 15 per cent on the gross receipts without attracting any liability to tax. Where the balance 85 per cent of the income is not applied or is not deemed to have been applied to charitable or religious purposes in India during the previous year, such income so accumulated or set apart shall not be included in the total income if the following conditions are fulfilled:

- (a) such person furnishes a statement in the prescribed form and in the prescribed manner to the Assessing Officer, stating the purpose for which the income is being accumulated or set apart and the period for which the income is to be accumulated or set apart, which shall in no case exceed five years;
- (b) the money so accumulated or set apart is invested or deposited in the forms or modes specified in sub-section (5);
- (c) the statement referred to in clause (a) is furnished on or before the due date specified under sub-section (1) of section 139 for furnishing the return of income for the previous year:

Provided that in computing the period of five years referred to in clause (a), the period during which the income could not be applied for the purpose for which it is so accumulated or set apart, due to an order or injunction of any court, shall be excluded.

**Explanation :** Any amount credited or paid, out of income referred to in clause (a) or clause (b) of sub-section (1), read with the Explanation to that sub-section, which is not applied, but is accumulated or set apart, to any trust or institution registered under section 12AA or to any fund or institution or trust or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via) of clause (23C) of section 10, shall not be treated as application of income for charitable or religious purposes, either during the period of accumulation or thereafter.

It is important to note that to claim exemption subject to Section 11(2) it is enough to invest in Government securities etc., only that part of the unspent balance which falls over and above 15% of the total income derived from the property held under trust [*C.I.T. v. H.H. Marthanda Varma Elayaraja of Travancore Trust and others (1981) 129 I.T.R. 191 (Ker.)*].

Section 11(3) provides that:

- (i) if the income accumulated for the specific purpose under Section 11(2) is applied to purposes other than charitable or religious, or ceases to be accumulated or set apart for application thereto, it will be chargeable to tax as income of that year. Further, such accumulated income will become liable to be taxed if,
- (ii) it ceases to remain invested in any security or deposited in the manner provided under Section 11(5), or
- (iii) it is not utilised for the purpose for which it is so accumulated or set apart during the specified period, or in the year immediately following the expiry thereof;
- (iv) is credited or paid to any trust or institution registered under Section 12AA or to any fund or institution or trust or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via) of clause (23C) of Section 10.

it shall be deemed to be the income of the previous year in which it ceases to remain so invested or deposited or is not so utilised, as the case may be.

Section 11(3A) provides that where due to circumstances beyond the control of the person in receipt of the income, any income invested or deposited in accordance with the provisions of Section 11(2) cannot be applied for the purpose for which it was accumulated or set apart, the Assessing Officer may, on an application made to him in this behalf allow such person to apply such income for such other charitable or religious purpose in India, as is specified by the person in the application subject further to the condition that it is in conformity with the objects of the trust.

Provided that the Assessing Officer shall not allow application of such income by way of payment or credit made for the purposes referred to in clause (d) of Sub-section (3) of section 11.

For the purposes of Section 11, 'property held under trust' includes a business undertaking so held and where a claim is made that the income of any such undertaking shall not be included in the total income of the persons in receipt thereof, the Assessing Officer shall have power to determine the income of such undertaking in accordance with the provisions of the Income-tax Act relating to assessment and where any income so determined is in excess of the income as shown in the accounts of the undertaking, such excess shall be deemed to be applied to purposes other than charitable or religious.

Provided that the Assessing Officer shall not allow application of such income by way of payment or credit made for the purposes referred to in clause (d) of Sub-section (3) of Section 11:

Provided further that in case the trust or institution, which has invested or deposited its income in accordance with the provisions of clause (b) of Sub-section (2), is dissolved, the Assessing Officer may allow application of such income for the purposes referred to in clause (d) of Sub-section (3) in the year in which such trust or institution was dissolved.

Sub-section (4A) as substituted by Finance Act, 1991 with effect from 1.4.1992 states that Sub-sections (1) or (2) or (3) or (3A) of Section 11 shall not apply in relation to any business income of a trust or institution unless the business is incidental to the attainment of the objectives of the trust or institution and separate books of accounts are maintained by such trust or institution in respect of such business.

### Forms and Modes of Investment [Section 11(5)]

The forms and modes for investing funds of charitable and religions trusts and institutions are given hereunder:

- (i) investment in saving certificates as defined in clause (c) of Section 2 of the Government Savings Certificates Act, 1959 (46 of 1959), and any other securities or certificates issued by the Central Government under the Small Savings Schemes of that Government. Investments in Indira Vikas Patra and Kisan Vikas Patra also qualify for the purpose of this Section;
- (ii) deposit in any account with the Post Office Savings Bank;
- (iii) deposit in any account with a scheduled bank or a co-operative society engaged in carrying on the business of banking (including a co-operative land mortgage bank or a co-operative land development bank);

*Explanation* : In this clause, "scheduled bank" means the State Bank of India constituted under the State Bank of India Act, 1955 (23 of 1955), a subsidiary bank as defined in the State Bank of India (Subsidiary Banks) Act, 1959 (38 of 1959), a corresponding new bank constituted under Section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 (5 of 1970), or under Section 3 of the Banking Companies (Acquisition and Transfer of Undertaking Act, 1980 (40 of 1980), or any other bank being a bank included in the Second Schedule to the Reserve Bank of India Act, 1934 (2 of 1934);

- (iv) investment in units of the Unit Trust of India established under the Unit Trust of India Act, 1963 (52 of 1963);
- (v) investment in any security for money created and issued by the Central Government or a State Government;
- (vi) investment in debentures issued by, or on behalf of, any company or corporation both the principal whereof and the interest whereon are fully and unconditionally guaranteed by the Central Government or by a State Government;

- (vii) investment or deposit in any public sector company;

Provided that where an investment or deposit in any public sector company has been made and such public sector company ceases to be a public sector company:

- (A) such investment made in the shares of such company shall be deemed to be an investment made under this clause for a period of three years from the date on which such public sector company ceases to be a public sector company;

Investment in debt instruments issued by and infrastructure Finance Company registered with RBI.

- (B) such other investment or deposit shall be deemed to be an investment or deposit made under this clause for the period up to the date on which such investment or deposit becomes repayable by such company;

- (viii) deposits with or investment in any bonds issued by a financial corporation which is engaged in providing long-term finance for industrial development in India and which is eligible for deduction under clause

- (viii) of Sub-section (1) of Section 36;

- (ix) deposits with or investment in any bonds issued by a public company formed and registered in India with the main object of carrying on the business of providing long-term finance or construction or purchase of houses in India for residential purposes and which is approved by the Central Government for the purposes of clause (viii) of Sub-section (1) of Section 36;

- (ixa) deposits with or investment in any bonds issued by a public company formed and registered in India with the main object of carrying on the business of providing long-term finance for urban infrastructure in India.

*Explanation:* For the purpose of this clause:

- (a) “long-term finance” means any loan or advance where the terms under which moneys are loaned or advanced provide for repayment along with interest thereof during a period of not less than five years;
- (b) “public company” shall have the meaning assigned to it in Section 3 of the Companies Act, 1956 (1 of 1956);
- (c) “urban infrastructure” means a project for providing potable water supply, sanitation and sewerage, drainage, solid waste management, roads, bridges and flyovers or urban transport.

- (x) investment in immovable property.

*Explanation:* “Immovable property” does not include any machinery or plant (other than machinery or plant installed in a building for the convenient occupation of the building) even though attached to, or permanently fastened to, anything attached to the earth;

- (xi) deposits with the Industrial Development Bank of India established under the Industrial Development Bank of India Act, 1964 [(18 of 1964)];

- (xii) any other form or mode of investment or deposit as may be prescribed including investments in units of Mutual Fund and Transfer of Deposits to Public Account of India.

According to section 11(6), where any income is required to be applied or accumulated or set apart for application, then, for such purposes the income shall be determined without any deduction or allowance by way of depreciation or otherwise in respect of any asset, acquisition of which has been claimed as an application of income under this section in the same or any other previous year.

According to section 11(7), where a trust or an institution has been granted registration under clause (b) of sub-section (1) of section 12AA or has obtained registration at any time under section 12A and the said registration is in force for any previous year, then, nothing contained in section 10 [other than clause (1) and clause (23C) thereof] shall operate to exclude any income derived from the property held under trust from the total income of the person in receipt thereof for that previous year.

### **Income of trusts or institutions from contributions [Section 12]**

(1) The income of a trust by way of voluntary contributions would also be treated for all purposes as income deemed to have been derived by the trust from property held by it under trust except, however, in case where the voluntary contribution is received with a specific direction that it shall form part of the corpus of the trust. As a result, voluntary contribution received by a trust should also be applied for charitable purposes before the end of the accounting year or within 3 months following so that income-tax exemption could be availed of. However, voluntary contributions could be accumulated for future obligation for charitable purposes in the same manner as specified earlier.

(2) The value of any services, being medical or educational services, made available by any charitable or religious trust running a hospital or medical institution or an educational institution, to any person referred to in Clause (a) or Clause (b) or Clause (c) or Clause (cc) or Clause (d) of Sub-section (3) of Section 13, shall be deemed to be income of such trust or institution derived from property held under trust wholly for charitable or religious purposes during the previous year in which such services are so provided and shall be chargeable to income-tax notwithstanding the provisions of Sub-section (1) of Section 11.

*Explanation:* For the purposes of this sub-section, the expression "value" shall be the value of any benefit or facility granted or provided free of cost or at concessional rate to any person referred to in Clause (a) or Clause

(a) or Clause (c) or Clause (cc) or Clause (d) of Sub-section (3) of Section 13.

(3) Notwithstanding anything contained in Section 11, any amount of donation received by the trust or institution in terms of Clause (d) of Sub-section (2) of Section 80G which has been utilised for purposes other than providing relief to the victims of earthquake in Gujarat or which remains unutilised in terms of Sub-section 5(C) of Section 80G in respect of which accounts of income and expenditure have not been rendered to the authority prescribed under clause (v) of sub-section (5C) of that section, in the manner specified in that clause, and not transferred to the Prime Minister's National Relief Fund on or before the 31st day of March, 2004 shall be deemed to be the income of the previous year and shall accordingly be charged to tax.

### **Registration of Trusts [Section 12A]**

The provisions of Sections 11 and 12 shall not apply in relation to any trust or institution unless the following conditions are fulfilled:

1. (aa) the person in receipt of the income has made an application for registration of the trust or institution on or after the 1st day of June, 2007 in the prescribed form and manner to the Principal Commissioner or Commissioner and such trust or institution is registered under section 12AA;
- (ab) the person in receipt of the income has made an application for registration of the trust or institution, and subsequently, it has adopted or undertaken modifications of the objects which do not conform to the conditions of registration, in the prescribed form and manner, within a period of thirty days from the date of said adoption or modification, to the Principal Commissioner or Commissioner and such trust or institution is registered under section 12AA; (w.e.f. AY 2018-19)
- 1.(b) where the total income of the trust or institution as computed under this Act without giving effect to the provisions of section 11 and section 12 exceeds the maximum amount which is not chargeable to income-tax in any previous year, the accounts of the trust or institution for that year have been audited by an accountant as defined in the Explanation to sub-section (2) of section 288 and the person in

receipt of the income furnishes along with the return of income for the relevant assessment year the report of such audit in the prescribed form duly signed and verified by such accountant and setting forth such particulars as may be prescribed.

- (ba) the person in receipt of the income has furnished the return of income for the previous year in accordance with the provisions of sub-section (4A) of section 139, within the time allowed under that section. **(w.e.f. AY 2018-19)**
- (2) Where an application has been made on or after the 1st day of June, 2007, the provisions of sections 11 and 12 shall apply in relation to the income of such trust or institution from the assessment year immediately following the financial year in which such application is made:

Provided that where registration has been granted to the trust or institution under section 12AA, then, the provisions of sections 11 and 12 shall apply in respect of any income derived from property held under trust of any assessment year preceding the aforesaid assessment year, for which assessment proceedings are pending before the Assessing Officer as on the date of such registration and the objects and activities of such trust or institution remain the same for such preceding assessment year:

Provided further that no action under section 147 shall be taken by the Assessing Officer in case of such trust or institution for any assessment year preceding the aforesaid assessment year only for non-registration of such trust or institution for the said assessment year

Rule 17A of the Income-tax Rules, 1962 provides that an application for registration of a trust shall be made in duplicate in Form No. 10A and shall be accompanied by the following documents:

- (i) where the trust is created or the institution is established under an instrument, the instrument in original together with a copy thereof and where it is created otherwise than under an instrument, the document evidencing the creation of the trust or the establishment of the institution together with one copy thereof. The Principal Commissioner or Commissioner may accept a certified copy instead of the original where the original cannot be conveniently produced.
- (ii) where the trust is in existence during any year or years prior to the financial year in which the application for registration is made, two copies each of the accounts of the trust for the three years (immediately) preceding the years in which the application for which the accounts have been made-up.

### **Procedure for Registration [Section 12AA]**

In terms of Section 12AA, on receipt of application for registration, the Principal Commissioner or Commissioner shall call for such documents or information from the trust or institution as he thinks necessary in order to satisfy himself about the genuineness of activities of the trust or institution and may also make such inquiries as he may deem necessary in this behalf. Sub-section 12AA. He has to either grant or decline registration within six months from the end of the month in which the application was received. If no order is passed within the said six months then it shall be deemed that the trust has been registered

Where the Principal Commissioner or Commissioner is satisfied that the activities of the trust or institution are not genuine or are not carried out in accordance with the objects of the trust or institution then the commissioner may pass an order in writing for the cancellation of registration granted under section 12AA or under section 12A after giving an opportunity of being heard.

Further, where a trust or an institution has been granted registration or has obtained registration at any time under section 12A and subsequently it is noticed that the activities of the trust or the institution are being carried out in a manner that the provisions of sections 11 and 12 do not apply to exclude either whole or any part of the income of such trust or institution due to operation of sub-section (1) of section 13, then, the Principal Commissioner or the Commissioner may by an order in writing cancel the registration of such trust or institution.

However the registration shall not be cancelled under this sub-section, if the trust or institution proves that there was a reasonable cause for the activities to be carried out in the said manner.

**Levy of tax where the charitable institution ceases to exist or converts into a non-charitable organization**

Sections 11 and 12 of the Act provide for exemption to trusts or institutions in respect of income derived from property held under trust and voluntary contributions, subject to various conditions contained in the said sections. The primary condition for grant of exemption is that the income derived from property held under trust should be applied for the charitable purposes, and where such income cannot be applied during the previous year, it has to be accumulated and invested in the modes prescribed and applied for such purposes in accordance with various conditions provided in the section. If the accumulated income is not applied in accordance with the conditions provided in the said section within a specified time, then such income is deemed to be taxable income of the trust or the institution. Section 12AA provides for registration of the trust or institution which entitles them to be able to get the benefit of sections 11 and 12. It also provides the circumstances under which the registration can be cancelled. Section 13 of the Act provides for the circumstances under which exemption under section 11 or 12 in respect of whole or part of income would not be available to a trust or institution.

A society or a company or a trust or an institution carrying on charitable activity may voluntarily wind up its activities and dissolve or may also merge with any other charitable or non-charitable institution, or it may convert into a non-charitable organization. In such a situation, the existing law does not provide any clarity as to how the assets of such a charitable institution shall be dealt with.

In order to ensure that the intended purpose of exemption availed by trust or institution is achieved, a new chapter has been introduced that provide for levy of additional income-tax in case of conversion into, or merger with, any non-charitable form or on transfer of assets of a charitable organization on its dissolution to a non-charitable institution. The elements of the regime are under:

- i. The accretion in income (accreted income) of the trust or institution shall be taxable on conversion of trust or institution into a form not eligible for registration u/s 12AA or on merger into an entity not having similar objects and registered under section 12AA or on non-distribution of assets on dissolution to any charitable institution registered u/s 12AA or approved under section 10(23C) within a period twelve months from dissolution.
- ii. Accreted income shall be amount of aggregate of total assets as reduced by the liability as on the specified date. The method of valuation is proposed to be prescribed in rules. The asset and the liability of the charitable organisation which have been transferred to another charitable organisation within specified time will be excluded while calculating accreted income.
- iii. The taxation of accreted income shall be at the maximum marginal rate.
- iv. This levy shall be in addition to any income chargeable to tax in the hands of the entity.
- v. This tax shall be final tax for which no credit can be taken by the trust or institution or any other person, and like any other additional tax, it shall be leviable even if the trust or institution does not have any other income chargeable to tax in the relevant previous year.
- vi. In case of failure of payment of tax within the prescribed time, a simple interest @ 1% per month or part of it shall be applicable for the period of non-payment.
- vii. For the purpose of recovery of tax and interest, the principal officer or the trustee and the trust or the institution shall be deemed to be assessee in default and all provisions related to the recovery of taxes shall apply. Further, the recipient of assets of the trust, which is not a charitable organisation, shall also be liable to be held as assessee in default in case of non-payment of tax and interest. However, the recipient's liability shall be limited to the extent of the assets received.

### LESSON ROUND UP

- The term 'Hindu undivided family' has not been defined in the Income-tax Act. However, in general parlance it means an undivided family of Hindus. Creation of a HUF is a God-gifted phenomenon. As soon as a married Hindu gets a child, a new HUF comes into existence. It is not at all necessary that every HUF must have joint property or family income.
- A Hindu Joint Family consists of Coparceners & members.
- The gross total income of the family for the relevant previous year shall be computed under the relevant heads (as per the provisions of the Income-tax Act) as it is computed for other assesseees.
- 'Partition' signifies division of property. In the cases of property capable of physical division, share of each member is determined by making physical division thereof. It must be noted that a division of income without physical division of property does not amount to partition.
- Partnership Firm: Under Section 2(23) of the Income-tax Act, the terms "firm", "partner", and "partnership" have the meanings respectively assigned to them in the Indian Partnership Act, 1932 and Limited Liability Partnership Act, 2008.
- As per the scheme, a partnership firm shall be assessed as a firm if the following conditions are satisfied:
  - The partnership is evidenced by an instrument i.e. partnership deed.
  - The individual shares of the partners are specified in that instrument.
  - A copy of the partnership deed certified by all the partners in writing (other than the minors) is submitted along with the return of income in respect of which assessment as a firm is first sought.
- As per Section 10(2A) of the Act, any person who is a partner of a firm which is assessed as such, his share in the total income of the firm will not be included in computing his total income. Partner includes a minor admitted to the benefits of partnership as per Section 2(23) of the Act.
- When all the partners in the predecessor firm are replaced by new partners in the successor firm, it is known as succession of one firm by another firm. If a firm is dissolved and some of the partners take over the firm's business or carry on a similar business with or without new partners, it would be a case of succession by a new firm .
- Where a change has occurred in the constitution of a firm on account of death or retirement, the firm is not entitled to carry forward and set off so much of the loss proportionate to the share of a retired or deceased partner as exceeds his share of profits, if any, in the firm in respect of the previous year.
- Alternate Minimum Tax: From the assessment year 2012-13 onwards, where the regular income tax payable for a previous year by a person other than a company is less than the alternate minimum tax payable for such previous year then the adjusted total income shall deemed to be the total income such person for such previous year and it shall be liable to pay income tax on such adjusted total income @ 18.5% + SC plus health and education cess @ 4%. AMT is applicable if adjusted total income exceeds Rs. 20 lakh.
- Association of persons: "Association of persons" means an association in which two or more persons join in a common purpose or common action to produce income, profits or gains.
- For the formation of an AOP the association need not necessarily be on the basis of a contract, consent and understanding may be presumed.
- Section 167B makes the following provisions as regards the incidence of charge of tax on the association of persons.
  - Where shares of members are determinate In this case, tax is chargeable on the income of the association of persons at the same rate as applicable to an individual. However, where the total income

of any member of the association of persons for the previous year (excluding his share of income from the association of persons) exceeds the maximum amount not chargeable to tax in the case of an individual, tax will be charged on the total income of the AOP at the maximum marginal rate of 30%, i.e. the highest slab applicable to an individual.

- Where the shares of the members are indeterminate In these cases, tax will be charged on the total income of the AOP at the maximum marginal rate, that is, the rate of tax as well as surcharge, if any, applicable to the highest slab of income in the case of an individual as specified in the Finance Act of the relevant year
- Section 67A seeks to provide for the method of computing a member's share in the income of an association of persons or a body of individuals, wherein the shares of the members are determinate, in the same manner as provided for in Sub-sections (1) to (3) of Section 67 for computing a partner's share in a firm.
- Co-operative Society means a co-operative society registered under the Co-operative Societies Act, 1912, or under any other law for the time being in force in any State for the registration of co-operative societies.
- The income of a co-operative society is computed in the same manner as provided for other assesseees.
- Section 80P provides for certain deductions from the gross total income of a Co-operative Society.

### SELF TEST QUESTIONS

*(These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation.)*

#### Multiple Choice Questions "MCQs"

1. Alternative Minimum Tax (AMT) is applicable if adjusted Total Income of individual, AOP, artificial juristic person, Firm etc. exceeds:
  - a) 15 lakhs
  - b) 20 lakhs
  - c) 25 lakhs
  - d) 10 lakhs

Answer: (b)

2. Share in the profits of the firm is taxable in the hands of partner under the head:
  - a) Salary
  - b) Business & Profession
  - c) Income from other sources
  - d) Exempt from tax

Answer: (d)

3. Salary, fees, bonus received by a partner from the firm is Taxable in the hands of partner under the head:
  - a) Salary

- b) Business & Profession
- c) Income from other sources
- d) Exempt from tax

Answer: (b)

4. Income earned from sale of Stridhan is taxable in the hands of:
- a) HUF
  - b) Husband of such woman
  - c) Such woman herself
  - d) None of above

Answer: (c)

5. Personal earning including income from Self Acquired Property of a member of the HUF is included in Income of:
- a) HUF income
  - b) Son's income
  - c) Individual's income
  - d) None of these

Answer: (c)

### SUGGESTED READINGS

**1. Direct Taxes Law and Practice**

Author : Dr. Vinod K. Singhania & Dr. Kapil Singhania

Publisher : Taxmann

Year : 2019

Edition : 2019

**2. Direct Taxes Ready Reckoner with Tax Planning**

Author : Dr. Girish Ahuja & Dr. Ravi Gupta

Publisher : Wolters Kluwer

Year : 2019

Edition : 20th Edition



# Lesson 8

## Classification and Tax Incidence on Companies

### LESSON OUTLINE

- Background & Types of Companies
- Tax incidence under Income-tax Act, 1961
- Minimum Alternate Tax 'MAT'
- MAT Credit
- Dividend Distribution Tax u/s 115-O
- Carbon Credit
- Equalization Levy
- Buyback of Shares Listed on Recognized Stock Exchange
- Conversion of an Indian Branch of a foreign company into an Indian subsidiary company
- Tax on Income distributed by specified company or Mutual Fund
- Taxation aspects related to Conversion of Company into an LLP
- Tax liability of company in the event of liquidation
- Taxation of Share Premium
- Taxation aspects of Amalgamation, Mergers and De-mergers
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

In the previous lessons we have learn the tax provisions of persons not being the company. Here, we will go through the income tax provisions of corporate entity. Company is also defined as person and liable to pay taxes on the income earned in the previous year. Section 2(17) of the Act, has defined the company as domestic company and foreign company. Now, the question arises why the foreign companies are required to pay tax in India. As it is discussed in earlier lessons that tax liability is determined on the basis of residential status and source of income, therefore the tax liability of company is also determined on the basis of residency and source of income accruing or arising in India.

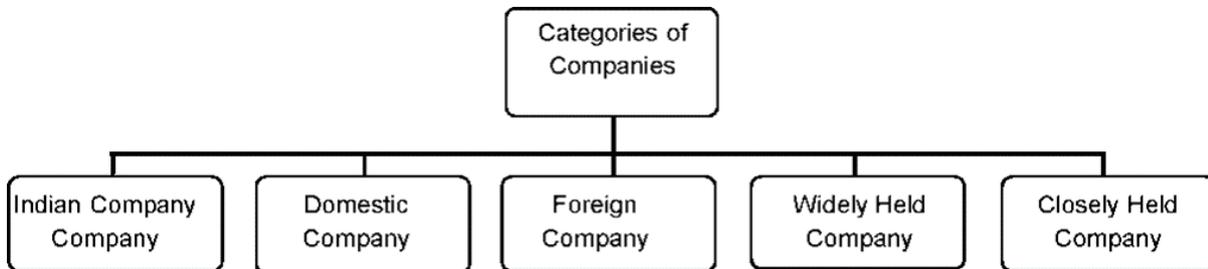
At the end of this lesson, you will learn:

- what are the constitutional provisions for companies with regard to income tax,
- which companies are domestic and which are foreign companies,
- when the provisions of Minimum Alternate Tax shall be applicable
- what are the provisions of dividend distribution tax
- Provision related to Equalization Levy
- Specific provisions related to,
  - Buyback of Shares Listed on Recognized Stock Exchange
  - Conversion of an Indian Branch of a foreign company into an Indian subsidiary company
  - Tax on Income distributed by specified company or Mutual Fund
  - Taxation aspects related to Conversion of Company into an LLP
  - Tax liability of company in the event of liquidation
  - Taxation of Share Premium
  - Taxation aspects of Amalgamation, Mergers and De-mergers

***Income tax being direct tax is a major source of revenue for the Central Government. The entire amount of income tax collected by the Central Government is classified under the head: (a) Corporation Tax (Tax on the income of the companies) and (b) Income Tax (Tax on income of the non-corporate assesses).***

## BACKGROUND & TYPES OF COMPANIES

Before we begin to examine and understand the taxability and tax incidence on companies, we must understand the types of Companies that are in existence today post the Companies Act, 2013.



### Indian Company

**Section 2(26)** of the Income Tax Act, 1961 defines the expression '**Indian Company**' as a company formed and registered under the Companies Act, 2013 and includes:

- (a) a company formed and registered under any law relating to companies formerly in force in any part of India (other than the State of Jammu and Kashmir, and the Union Territories specified in (e) below);
- (b) any corporation established by or under a Central, State or Provincial Act;
- (c) any institution, association or body which is declared by the Board to be a company under Section 2(17) of the Income Tax Act, 1961;
- (d) in the case of State of Jammu & Kashmir, any company formed and registered under any law for the time being in force in that State; and
- (e) in the case of any of the Union Territories of Dadra and Nagar Haveli, Goa, Daman and Diu and Pondicherry, a company formed and registered under any law for the time being in force in that Union Territory;

Provided that the registered or, as the case may be, principal office of the company, corporation, institution, association or body in all cases is in India.

From the above definition, it may be seen that statutory corporations as well as government companies are automatically treated as Indian companies for purposes of the Income Tax Act, 1961. The definition of an Indian company has been specifically given under the Income Tax Act, 1961 because of the fact that Indian companies are entitled to certain special tax benefits under this Act. It must be noted that all companies falling within the definition given in Section 2(17) of the Act are not necessarily Indian companies whereas all Indian companies are companies within the meaning of Section 2(17) of the Act.

### Infrastructural capital company is defined under Section 2(26A)

- It means a company which makes investments by way of acquiring shares or
- Providing long-term finance to any enterprise or undertaking wholly engaged in the business referred to in Section 80-IA(4) or Section 80-IAB(1) or
- An undertaking developing and building a housing project referred to in Section 80-IB(10) or
- A project for constructing a hotel of not less than three-star category as classified by the Central Government or a project for constructing a hospital with at least one-hundred beds for patients.

## Domestic Company

**Section 2(22A)** of the Income Tax Act, 1961, defines –

- Domestic company as an Indian company or
- Any other company which, in respect of its income liable to tax under the Income Tax Act
- Has made the prescribed arrangements for the declaration and payment within India, of the dividends (including dividends on preference shares) payable out of such income.

From this definition, it is clear that –

- All Indian companies are domestic companies while
- All domestic companies need not necessarily be Indian companies. In other words, a non-Indian company would be considered as a domestic company if it makes the prescribed arrangements for the declaration and payment of dividends in India on which tax is deductible under Section 194.

**Under Rule 27 of Income tax rules, the prescribed arrangements are as follows:**

- (i) the **share register of the company concerned, for all its shareholders, shall be regularly maintained at its principal place of business within India** in respect of any assessment year from a date not later than the first day of April of such year.
- (ii) the **general meeting** for passing the accounts of the previous year relevant to the assessment year declaring any dividends in respect thereof shall be **held only at a place within India**;
- (iii) the **dividends declared**, if any, shall be **payable only within India** to all shareholders.

## Foreign Company

**Section 2(23A)** of the Income Tax Act defines –

- Foreign company as a company, which, is not a domestic company.
- However, all non-Indian companies are not necessarily foreign companies. If a non-Indian company has made the prescribed arrangements for declaration and payments of dividends within India, such a non-Indian company must be treated as a “**domestic company**” and not as a “**foreign company**”.

**Company in which public are substantially interested (A widely-held company)**

**Section 2(18)** of the Income Tax, Act defines the expression “**company in which the public are substantially interested**”.

A company is said to be one in which public are substantially interested in the following cases, namely -

- (i) **A company owned by Govt./ RBI** – If it is a company owned by the Government or the Reserve Bank of India or in which not less than 40 per cent of the shares, whether singly or taken together, are held by the Government or the Reserve Bank of India or a corporation owned by the Reserve Bank of India; or
- (ii) **Section 8 company** – If it is a company which is registered under Section 8 of the Companies Act, 2013 ; or
- (iii) **A company having no share capital declared by CBDT** – If it is a company, having no share capital and if, having regard to its objects, the nature and composition of its membership and other relevant considerations, it is declared by an order of the Board (CBDT) to be a company in which the public are substantially interested. However, such a company shall be deemed to be one in which the public are substantially interested only for the assessment year(s) as may be specified in the declaration; or

- (iv) **Nidhi/ Mutual Benefit Society** – If it is mutual benefit finance a company which carries on, as its principal business, the business of acceptance of deposits from its members and which is declared by the Central Government under Section 406 of the Companies Act, 2013 to be a Nidhi or Mutual Benefit Society; or
- (v) **A company owned by co-operative Society** – If it is a company in which shares carrying not less than 50 per cent of the voting power have been allotted unconditionally to or acquired unconditionally by, and are throughout the relevant previous year beneficially held by, one or more cooperative societies; or
- (vi) **Listed company** – If it is a company which is not a private company as defined in Companies Act, and equity shares of the company (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in the profits, i.e. preference shares) were, as on the last day of the relevant previous year, listed in a recognised stock exchange in India;
- (vii) **Public company owned by Govt. and/ or public limited company** – If it is a company which is not a private company within the meaning of the Companies Act, and the shares in the company (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in profits) carrying not less than 50 per cent (40 per cent in case of an industrial company) of the voting power have been allotted unconditionally to, or acquired unconditionally by, and were throughout the relevant accounting year beneficially held by (a) the Government, or (b) a corporation established by a Central or State or Provincial Act, or (c) any company in which the public are substantially interested or a wholly owned subsidiary company.

**Note –**

**Industrial Company** means an Indian company where business consists mainly in the construction of ships or in the manufacture or processing of goods or in mining or in the generation or distribution of electricity or any other form of power.

It may be noted that, a public company under the Companies Act, need not necessarily fall within the meaning of a company in which the public are substantially interested under the Income-tax Act, 1961 because a public company under the Companies Act, may be considered as one in which the public are not substantially interested under the Income-tax Act, 1961 after considering the nature and extent of shareholding.

**Illustration** : State with the reason whether in the following cases Companies are widely held or closely held:

- (a) The shares of ABC Private Limited are held as follows:
- |     |                            |     |
|-----|----------------------------|-----|
| i   | A corporation owned by RBI | 15% |
| ii  | Central Govt.              | 18% |
| iii | R.B.I.                     | 10% |
| iv  | Mr. Raman                  | 28% |
| v   | Mr. Bhuvan                 | 27% |
- (b) 85% equity shares of Progressive Private Limited were held by the public and its affairs during the relevant previous year were controlled by seven persons.

**Solution:**

- (a) Shares held by Govt., RBI and Corporation owned by RBI =  $18\% + 10\% + 15\% = 43\%$ .  
As shares held by CG along with RBI are more than 40%, therefore, ABC Pvt. Ltd. is a Govt. Participating company. Hence it is a company in which Public is substantially interested i.e. widely held.
- (b) As none of the criteria mentioned in Section 2(18) are met in case of Progressive Pvt. Ltd. (such as

Govt. Participating, Section 8 Company or Nidhi etc.) therefore, it is a closely held company.

### Closely held company

A Company in which the public is not substantially interested is known as a closely held company.

The distinction between a closely held and widely held company is significant from the following viewpoints.

- (i) Section 2(22) (e), which deems certain payments as dividend, is applicable only to the shareholders of a closely-held company; and
- (ii) A closely held company is allowed to carry forward its business losses only if the conditions specified in Section 79 are satisfied.

### TAX INCIDENCE UNDER INCOME TAX ACT, 1961

The incidence of Income tax depends upon the residential status of a company in India during the relevant previous year. A Company may be either resident or non-resident in India, i.e., company cannot be ordinary or not-ordinary resident.

According to Section 6(3) of the Act, a company is said to be resident in India (resident company) in any previous year, if:

- (i) It is an Indian company; or
- (ii) Its place of effective management, in that year, is in India.

If any of the above two tests is satisfied the company would be a resident company in India during that previous year.

From Assessment Year 2017-18 a foreign company is resident in India if its Place of Effective Management (POEM) during the previous year is in India. For this purpose, the Place of Effective Management means a place where Key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance are made.

According to Section 5(1) of the Act, the total income of any previous year of a resident company would consist of:

- (i) income received or deemed to be received in India during the previous year by or on behalf of such company;
- (ii) income which accrues or arises or is deemed to accrue or arise to it in India during the previous year;
- (iii) income which accrues or arises to it outside India during the previous year.

It is important to note that under clause (iii) only income accruing or arising outside India is included. Income deemed to accrue or arise outside India is not includible in the hands of residents. Hence, net dividends received from foreign companies are includible in income and not the gross dividends [CIT v. Shaw Wallace & Co. Ltd. (1981) 132 ITR 466].

In this context, the Calcutta High Court had followed the Supreme Court's decision in Commissioner of Income-tax v. Clive Insurance Co. Ltd. (1978, 113 ITR 636) holding that the assessee could be said to have paid Income Tax in U.K, by deduction or otherwise, in respect of the net dividend so as to be eligible for relief contemplated by Section 49D of the Indian Income Tax Act, 1922. Following the Supreme Court's decision, the Bombay High Court held in the case of Commissioner of Income tax v. Tata Chemicals Ltd. (1986, 162 ITR 556) that the assessee was entitled to double taxation relief under Section 91 of the Income Tax Act, 1961 in respect of dividends from the United Kingdom. Following its decision in the case of Shaw Wallace & Co. Ltd. (supra), the Calcutta High Court held in the case of the same assessee (1983, 143 ITR 207) that dividends from foreign

companies are to be assessed not on the gross amount of the dividends but on the gross amount of the dividends less tax deducted there from in foreign countries. In other words, only the net foreign dividends are to be included in the total income of a resident assessee under Section 5(1)(c) of the Income Tax Act, 1961.

**Under Section 5(2) of the Act**, the total income of any previous year of **non-resident company** would consist of:

- (i) Income received or deemed to be received in India in the previous year by or on behalf of such company;
- (ii) Income which accrues or arises or is deemed to accrue or arise to it in India during the previous year.

The decision of the Supreme Court in the case of *Standard Triumph Motor Co. Ltd. v. CIT* (1993) 201 ITR 391 to the effect that when an Indian resident passes an entry crediting a non-resident with amount payable to him, that would tantamount to the latter receiving income in India, is having grave consequences. In this case, the royalty payable to non-resident in pound sterling was credited to the non-residents accounts in the books of the assessee. The Supreme Court held that the plea to accept royalty income in U.K. was immaterial because the amount was available for the use of the non-resident in India in any manner he liked. Hence, the income was received in India. In the wake of this decision, non-residents who have all along been held to be not liable to Indian Income-tax if the contract was signed outside India, executed outside India and paid for outside India could well fall into the Indian- tax net, should their clients/customers credit them for the amount due before making payments to them outside India. In other words, a non-resident's tax liability depends upon the accounting entry passed by his client customer.

### Corporate Taxation Rates

<i>Domestic Company</i>	<i>Assessment Year 2020-21</i>
- Where it opted for Section 115BAA [This benefit shall be available when total income of the company is computed without claiming specified deductions, incentives, exemptions and additional depreciation available under the Income-tax Act.]	22%
- Where it opted for Section 115BAB [This regime shall be available only for the manufacturing companies incorporated in India on or after 01-10-2019. Hence, old companies will not be able to take the benefit of this section.]	15%
- Where it has not opted for Section 115BAA and the Total Turnover or Gross receipts of the company in the last previous year does not exceeds 400 crore rupees	25%
- Any other domestic company	30%
<b>Foreign Company</b>	40%

**Add:**

#### a) Surcharge:

**Domestic Company:** The amount of income-tax shall be increased by a surcharge at the rate of 7% of such tax, where total income exceeds one crore rupees but not exceeding ten crore rupees and at the rate of 12% of such tax, where total income exceeds ten crore rupees. However, the rate of surcharge in case of a company opting for taxability under Section 115BAA or Section 115BAB shall be 10% irrespective of amount of total income.

**Foreign Company:** The amount of income-tax shall be increased by a surcharge at the rate of 2% of such tax, where total income exceeds one crore rupees but not exceeding ten crore rupees and at the rate of 5% of such tax, where total income exceeds ten crore rupees.

**b) Health and Education Cess:** The amount of income-tax and the applicable surcharge, shall be further increased by health and education cess calculated at the rate of 4% of such income-tax and surcharge.

*The Taxation Laws (Amendment) Ordinance, 2019 was promulgated by the President of India on 20.9.2019 to amend the Income-tax Act, 1961 and the Finance (No.2) Act, 2019 and is in force. This Ordinance has inserted two new sections, section 115BAA and 115BAB, in the Income-tax Act, 1961 to be applicable from A.Y.2020-21.*

*Section 115BAA provides for concessional rate of tax@22% (plus surcharge@10% and HEC@4%) for domestic companies, subject to certain conditions, like non-availability of profit-linked deductions and investment-linked tax deduction under the Act, non-availability of deduction (weighted or otherwise) for contribution to research and development, additional depreciation etc.*

*Section 115BAB provides for concessional rate of tax@15% (plus surcharge@10% plus HEC@4%) to new manufacturing domestic companies set up and registered on or after 1.10.2019, and commences manufacturing on or before 31.3.2023, subject to certain conditions, like non-availability of profit-linked deductions and investment-linked tax deduction under the Act, non-availability of deduction (weighted or otherwise) for contribution to research and development, additional depreciation etc.*

*Domestic Companies have to exercise the option to be governed by these special provisions of the Act. The option for section 115BAB has to be exercised in the very first year in which the eligible company is set up, failing which it cannot exercise such option in the future years. However, a company eligible to exercise option u/s 115BAA can defer exercise of such option to a future year, if it is availing sizable profit-linked or investment-linked deductions or additional depreciation in the P.Y.2019-20. However, once the company exercises such option under section 115BAA or 115BAB, as the case may be, in a year, it would continue to be governed by the special provisions u/s 115BAA or 115BAB, as the case may be, thereafter and cannot opt for regular provisions in any subsequent year.*

*It may be noted that companies exercising option under section 115BAA or section 115BAB are not liable to minimum alternate tax under section 115JB.*

## MINIMUM ALTERNATE TAX (MAT)

Section 115J which was a special provision applicable to a company if its total income as computed under the Income Tax Act was less than thirty per cent of its book profit was introduced with effect from 1.4.1988 but was discontinued with effect from 1.4.1991. It was revived as Section 115JA with effect from 1.4.1997 as a provision deeming total income equal to 30% of book profit of companies referred to earlier. This provision was also discontinued with effect from 1.4.2001 but was substituted by Section 115JB effective from the same date. This provision imbibes the concept of Minimum Alternate Tax.

As provided out in the Explanatory Memorandum to the Finance Bill, 2000, the Minimum Alternate Tax had been levied from the assessment year 1997-98 as the number of zero tax companies and companies paying marginal tax had proliferated. The efficacy of that provision, however, had declined in view of the exclusions of various sectors from the operation of MAT and the tax credit systems.

Hence, in its place the new provisions of Section 115JB were inserted which are simpler in application. They provide that all companies having book profits under the Companies Act shall have to pay a minimum alternate tax at a rate of 15%. These provisions are applicable to all corporate entities.

According to this section, if the income tax payable by a company on its total income as computed under the

Income Tax Act in respect of any previous year relevant to the assessment year, is less than 15% of such book profit plus surcharge plus education cess then such book profit shall be treated as total income of the company and the tax payable for the relevant previous year shall be deemed to be 15% of such book profit. This non-absolute provision will override any other provision of the Income Tax Act.

Thus, where the Income-tax payable is less than 15% of Book Profit, such book profit will be deemed to be total Income and Income Tax will be payable @ 15% on such Book Profit. **[9% of book profits, in case of the assessee is a unit located in an International Financial Services Centre and derives its income solely in convertible foreign exchange] [section 115JB(7) w.e.f. AY 2017-18]**

Such company assessee has to prepare the Profit & Loss A/c in accordance with the provisions of Part II of Schedule VI of the Companies Act, 2013 or statement of profit and loss as per Schedule III of companies Act 2013.

However, while preparing the annual accounts including profit and loss account -

- (a) the accounting policies;
- (b) the accounting standards followed for preparing such accounts including profit and loss accounts; and
- (c) the method and rates adopted for calculating the depreciation,

shall be the same as have been adopted for the purpose of preparing such accounts including profit and loss account and laid before the company at its annual general meeting. But where the company has adopted or adopts the "financial year", which is different from the previous year under the Income Tax Act, (a), (b) and (c) aforesaid shall correspond to the accounting policies, accounting standards and the method and rates for calculating the depreciation which have been adopted for preparing such accounts including profit and loss account for such financial year or part of such financial year falling within the relevant previous year.

As per section 115JB, every company is required to prepare its accounts as per Schedule III of the Companies Act, 2013. However, as per the provisions of the Companies Act, certain companies, e.g. Insurance, Banking or Electricity Company, are allowed to prepare their profit and loss account in accordance with the provisions specified in their regulatory Acts.

In order to align the provisions of Income-tax Act with the Companies Act, 2013, with effect from assessment year 2013-14, section 115JB has been amended to provide that the companies which are not required to prepare their profit and loss account in accordance with the Schedule III of the Companies Act, 2013, profit and loss account prepared in accordance with the provisions of their regulatory Acts shall be taken as a basis for computing the book profit under section 115JB.

From the above it can be observed that the provisions of MAT are applicable to every company whether public or private and whether Indian or foreign. However MAT shall not apply to :

- (i) any income arising to a company from life insurance business.
- (ii) any shipping income arising to a company liable to tonnage taxation.
- (iii) a foreign company resident of a country with which India has an Double Taxation Avoidance Agreement (DTAA) and such company does not have a permanent establishment in India.
- (iv) the foreign company is a resident of a country with which India does not have an agreement (DTAA) and such company is not required to seek registration under any law for the time being in force relating to companies.
- (v) Further by Finance Act, 2018, MAT provisions shall not be applicable to a foreign company, whose total income comprises of profits and gains arising from business referred to in section 44AB, 44BB, 44BBA, or 44BBB and such income has been offered to tax at the rates specified in those sections.

Due to applicability of Ind AS Section 115JB has been amended to calculate MAT in case of Ind AS compliant companies. Following are steps for computation of book profit-

**Step 1 :** Find out the net profit [before other comprehensive income (OCI)] as per statement of profit and loss of the company.

**Step 2 :** Make adjustments which are given in existing provisions under section 115JB(2).

**Step 3 :** Make specific adjustments in the case of demerger as given by new sub-section 2B to section 115JB.

**Step 4 :** Make further adjustments pertaining to OCI items that will be permanently recorded in reserves (i.e. never to be reclassified to the statement of profit and loss).

### Detailed Discussion of Steps to Calculate Book Profit is as Under

**Step 1 :** Find out Net profit (before other comprehensive income) as shown in profit and loss account (prepared in accordance with provisions of Part II and III of Schedule VI to Companies Act, 2013) or Statement of profit and loss (prepared in accordance with Schedule III of Companies Act, 2013).

**Step 2 :** Adjustments to be made to the Net Profit in Step 1 as given in existing provisions under Section 115JB (2) –

**Following amounts shall be added; if debited to Profit and Loss account :**

- (a) the amount of **Income tax paid or payable, and the provision therefor;**

The amount of income-tax shall include:

- (i) any tax on distributed profits under Section 115O or on distributed income under section 115R;
- (ii) any interest charged under this Act; and
- (iii) Surcharge
  - (1) Health and Education Cess [(Explanation 2 to section 115JB)].

The amount of income tax shall not include following taxes:

- STT, Banking cash transaction tax, wealth tax, gift tax, FBT, indirect taxes
- Interest, penalty, fine, surcharge, education cess on above taxes.

- (b) the **amounts carried to any reserves**, by whatever name called; or
- (c) the amount or amounts set aside to **provisions made for meeting liabilities, other than ascertained liabilities**, (i.e. unascertained liabilities); or
- (d) the amount by way of **provision for losses of subsidiary companies**; or
- (e) the amount or amounts of **dividends paid or proposed**; or
- (f) the amount or amounts of expenditure relatable to any incomes to which Section 10 or Section 11 or Section 12 apply.
- (fa) the amount or amounts of expenditure relatable to, income, **being share of the assesseees in the income of an association of persons or body of individuals**, on which no income-tax is payable in accordance with the provisions of section 86; or
- (fb) the amount or amounts of **expenditure relatable to income accruing or arising to an assesseees, being a foreign company**, from, -
  - the capital gains arising on transactions in securities; or

- the interest, royalty or fees for technical services chargeable to tax at the rate or rates specified in Chapter XII (i.e. Section 115A to 115BBE)

if the income-tax payable thereon in accordance with the normal provisions of this Act, other than the provisions governing MAT, is at a rate less than the rate specified in Section 115JB (1) i.e., 15%; or

- (fc) – the amount representing **notional loss on transfer of a capital asset**, being share or a special purpose vehicle to a business trust in exchange of units allotted by the trust referred to in section 47(xvii)

Or

- the amount representing notional loss resulting from any change in carrying amount of said units or

- the amount of loss on transfer of units referred to in clause (xvii) of section 47 whether or not it appears in profit and loss account.

- (fd) the amount or amounts of **expenditure relatable to income by way of royalty** in respect of patent chargeable to tax under section 115BBF; or
- (g) the amount of **depreciation**.
- (h) the amount of **deferred tax and provisions**.
- (i) the amount or amounts set aside as **provision for diminution in the value of any asset** e.g. provision for bad and doubtful debts and provision for impairment losses.
- (j) the **amount standing in revaluation reserve** relating to revalued asset on the retirement or disposal of such asset if such profit is not credited to profit and loss account.
- (k) the amount of **gain on transfer of units referred to in clause (xvii) of section 47** computed by taking into account the
  - cost of the shares exchanged with units referred to in the said clause or
  - the carrying amount of the shares at the time of exchange where such shares are carried at a value other than the cost through profit or loss account, as the case may be.

#### **Amounts to be deducted from Net profit mentioned in step 1 –**

- (i) the **amount withdrawn from any reserves or provisions if any** such amount is credited to the profit and loss account;

Provided that, where this section is applicable to assesseees in any previous year, the amount withdrawn from reserves created or provisions made in a previous year relevant to the assessment year commencing on or after the 1st day of April, 1997 shall not be reduced from the book profit unless the book profit of such year has been increased by those reserves or provisions (out of which the said amount was withdrawn) under this Explanation or Explanation below second proviso to Section 115JA, as the case may be; or

In other words, if amount is withdrawn from provisions/reserve not allowed as deduction earlier, it will not be added (taxed) again; however, in any other case the withdrawal will be taxed.

- (ii) the amount of income to which any of the provisions of Section 10 or Section 11 or Section 12 apply, if any such amount is credited to the profit and loss account; or
- (iia) the amount of **depreciation debited to the profit and loss account (excluding** the depreciation on account of revaluation of assets); or

- (iib) the **amount withdrawn from revaluation reserve** and credited to the profit and loss account, to the extent it does not exceed the amount of depreciation on account of revaluation of assets referred to in Clause (iia); or
- (iic) the amount of income, being the **share of the assesseees in the income of an association of persons or body of individuals**, on which no income-tax is payable in accordance with the provisions of section 86, if any, such amount is credited to the profit and loss account; or
- (iic) the amount of **income accruing or arising to assesseees, being a foreign company**, from, -
  - (A) the capital gains arising on transactions in securities; or
  - (B) the interest, royalty or fees for technical services chargeable to tax at the rate or rates specified in Chapter XII, (i.e. under section 115A to 115BBE)
 if such income is credited to the profit and loss account and the income-tax payable thereon in accordance with the normal provisions of this Act, other than the provisions of MAT, is at a rate less than the rate specified in section 115JB (1) i.e., 15%; or
- (iie) the amount representing, -
  - (A) **notional gain on transfer of a capital asset**, being share of a special purpose vehicle to a business trust in exchange of units allotted by that trust referred to in clause (xvii) of section 47; or
  - (B) notional gain resulting from any change in carrying amount of said units; or
  - (C) gain on transfer of units referred to in clause (xvii) of section 47, if any, credited to the profit and loss account; or
- (iif) the amount of **loss on transfer of units referred to in clause (xvii) of section 47** computed by taking into account the cost of the shares exchanged with units referred to in the said clause or the carrying amount of the shares at the time of exchange where such shares are carried at a value other than the cost through profit or loss account, as the case may be;
- (iig) the amount of **income by way of royalty in respect of patent chargeable to tax under section 115BBF**; or
- (iih) **Aggregate amount of unabsorbed depreciation and loss brought forward in case of a –**
  - *company, and its subsidiary and the subsidiary of such subsidiary, where, the Tribunal, on an application moved by the Central Government under section 241 of the Companies Act, 2013 has suspended the Board of Directors of such company and has appointed new directors who are nominated by the Central Government under section 242 of the said Act;*
  - the aggregate amount of unabsorbed depreciation and brought forward loss in case of a co against whom an application for corporate insolvency resolution is admitted under the Insolvency and Bankruptcy Code, 2016

*It may be noted that loss does not include depreciation.*

***A company would be a subsidiary of another company if such other company holds more than half in the nominal value of equity share capital of the company.***

- (iii) the **amount of loss brought forward or unabsorbed depreciation, whichever is less, as per books of account**. For the purposes of this clause, the loss shall not include depreciation. Therefore, in a case where an assessee has shown profit in a year, but after adjustment of depreciation it results profit or loss, no adjustment in book profit is allowed; or (in case of a company other than company under going insolvency proceedings under Insolvency and Bankruptcy Code, 2016)
- (iv) the amount of **profits of sick industrial company** for the assessment year commencing on and from

the assessment year relevant to the previous year in which the said company has become a sick industrial company under Sub-section (1) of Section 17 of the Sick Industrial Companies (Special Provisions) Act, 1985 and ending with the assessment year during which the entire net worth of such company becomes equal to or exceeds the accumulated losses. "Net Worth" shall have the meaning assigned to it in Clause (ga) of Sub-section (1) of Section 3 of the Sick Industrial Companies (Special Provisions) Act, 1985.

- (v) The amount of **deferred tax**, if any such amount is credited to the profit and loss account.

**Computation of Book Profit for Ind AS compliant companies:**

The Central Government has notified the Indian Accounting Standards (Ind AS) which are converged with International Financial Reporting Standards (IFRS) and prescribed the Companies (Indian Accounting Standards) Rules, 2015 which lay down the roadmap for implementation of these Ind AS.

**As the book profit based on Ind AS compliant financial statements is likely to be different from the book profit based on existing Indian GAAP, sub-sections (2A), (2B) and (2C) of section 115JB provides the framework for computation of book profit for Ind AS compliant companies in the year of adoption and thereafter.**

**MAT on Ind AS compliant financial statement [Section 115JB(2A)]**

**In case of a company whose financial statements are drawn up in compliance with the Indian Accounting Standards (Ind ASs) specified in Annexure to the Companies (Indian Accounting Standards) Rules, 2015, the following additional adjustments shall be done to the book profit as computed above in point no. (iii) as per section 115JB(2) read with Explanation 1 –**

- (a) increased by all amounts credited to other comprehensive income in the statement of profit and loss under the head "Items that will not be re-classified to profit or loss";
- (b) decreased by all amounts debited to other comprehensive income in the statement of profit and loss under the head "Items that will not be re-classified to profit or loss";

However, no adjustment shall be made where the amount credited or debited to other comprehensive income under the head "Items that will not be re-classified to profit or loss", in respect of –

- (i) Revaluation surplus for assets in accordance with the Indian Accounting Standards 16 and Indian Accounting Standards 38; or
- (ii) Gains or losses from investments in equity instruments designated at fair value through other comprehensive income in accordance with the Indian Accounting Standards 109. [First proviso to section 115JB(2A)]

**However, the book profit of the previous year, in which such asset or investment is retired, disposed, realised or otherwise transferred, shall be increased or decreased, as the case may be, by the amount or the aggregate of the amounts as referred to in the first proviso for the previous year or any of the preceding previous years and relatable to such asset or investment [Second proviso to section 115JB(2A)]**

The OCI includes certain items that will permanently be recorded in reserves and hence never be reclassified to statement of profit and loss included in computation of book Profit. Following items shall be included in the book profits for the MAT purposes as explained under:

1. **Changes in revaluation surplus of Property, Plant or Equipment (PPI) and Intangible assets (Ind AS 16 and 38)**
  - Revaluation reserve credited or debited to OCI shall not be adjusted in the book profits in the

year in which it is debited or credited. **[First proviso to section 115JB (2A)]**

- It shall be included in the book profit in the year in which the Asset/Investment is retired, disposed, realized or otherwise transferred. **[Second Proviso to section 115JB(2A)]**
2. Gains and losses from Investments in equity instruments designated at fair value through OCI (Ind AS 109)
    - Gain or loss from such Investments debited/credited to OCI shall not be adjusted in book profits in the year in which it is credited/debited. First proviso to section 115JB (2A)
    - It shall be adjusted in book profits in the year in which investment is retired/disposed/realized. **[Second proviso to section 115JB (2A)]**
  3. **Re-measurements of defined benefit plans (Ind AS 19)** - It shall be adjusted in book profits every year in which such re-measurement gain/loss arises.
  4. **Any other Item** - It will be adjusted in book profits every year in which such profit/loss arises.
- (c) Increased by amounts or aggregate of the amounts debited to the statement of profit and loss on distribution of non-cash assets to shareholders in a demerger in accordance with Appendix A of the Indian Accounting Standards 10;
- (d) Decreased by all amounts or aggregate of the amounts credited to the statement of profit and loss on distribution of non-cash assets to shareholders in a demerger in accordance with Appendix A of the Indian Accounting Standards 10;

As per Appendix A of Ind AS 10 any distribution of non-cash assets to shareholders in case of demerger shall be accounted at fair value and the difference between carrying value and fair value of such assets is adjusted in profit and loss.

Reserves of such company are debited with fair value of assets to record distribution of “deemed dividend” to shareholders. Since such difference between fair value and carrying amount is included in retained earnings, therefore, such difference arising on demerger shall be excluded from book profits.

**Sub-section (2B)** states that in demerger, in the case of a resulting company, the property and the liabilities of the undertaking or undertakings being received by it are recorded at values different from values appearing in the books of account of the demerged company immediately before the demerger, any change in such value shall be ignored for the purpose of computation of book profit of the resulting company under this section.

**MAT on first time adoption [Section 115JB(2C)]:**

In case of Ind AS compliant company, the book profit of the year of convergence and each of the following four previous years, shall be further increased or decreased, as the case may be, by one fifth of the **transition amount**.

**Note:**

In the first year of adoption of Ind AS, the companies would prepare Ind AS financial statement for reporting year with a comparative financial statement for immediately preceding year. As per Ind AS 101, a company would make all Ind AS adjustments on the opening date of the comparative financial year. The entity is also required to present an equity reconciliation between previous Indian GAAP and Ind AS amounts, both on the opening date of preceding year as well as on the closing date of the preceding year.

For the purposes of computation of book profits of the year of adoption and for adjustments, the amounts adjusted as on the opening date of the first year of adoption shall be considered.

For example, companies which adopt Ind AS with effect from 1 April 2016 are required to prepare their financial statements for the year 2016-17 as per the requirements of Ind AS. Such companies are also required to prepare an opening balance sheet as of 1st April 2015 and restate the financial statements for the comparative period 2015-16.

In such a case, the first time adoption adjustments as of 31 March 2016 shall be considered for computation of MAT liability for previous year 2016-17 (Assessment year 2017-18) and thereafter.

Further, in this case, the five years period shall be previous years 2016-17, 2017-18, 2018-19, 2019-20 and 2020-21.

However, the book profit of the previous year in which the asset or investment referred to in sub clauses (B) to (E) of clause (iii) of the Explanation is retired, disposed, realised or otherwise transferred shall be increased or decreased, as the case may be, by the amount of the aggregate of the amounts referred to in the said sub-clause relating to such asset or investment: **[First proviso to section 115JB(2C)]**

Further, the book profit of the previous year in which the foreign operation referred to in sub clause (F) of clause (iii) of the Explanation is disposed or otherwise transferred, shall be increased or decreased, as the case may be, by the amount of the aggregate of the amounts referred to in the said sub-clause relating to such foreign operations. **[Second proviso to sub-section (2C)]**

**Meaning of certain terms** [Explanation to Section 115JB(2C)]

1. **Year of convergence** : the previous year within which the convergence date falls.
2. **Convergence date** : the first day of the first Indian Accounting Standards reporting period as defined in the Ind AS 101.
3. **Transition amount** : the amount or aggregate of the amounts adjusted in other equity (excluding capital reserve and securities premium reserve) on convergence date but not including the following:
  - (A) Amount or aggregate of the amounts adjusted in the other comprehensive income on the convergence date which shall be subsequently re-classified to the profit and loss;
  - (B) Revaluation surplus for assets in accordance with the Indian Accounting Standards 16 and Indian Accounting Standards 38 adjusted on the convergence date;
  - (C) Gains or losses from investments in equity instruments designated at fair value through other comprehensive income in accordance with the Indian Accounting Standards 109 adjusted on the convergence date;
  - (D) Adjustments relating to items of property, plant and equipment and intangible assets recorded at fair value as deemed cost in accordance with paragraphs D5 and D7 of the Indian Accounting Standards 101 on the convergence date;
  - (E) Adjustments relating to investments in subsidiaries, joint ventures and associates recorded at fair value as deemed cost in accordance with paragraph D15 of the Indian Accounting Standards 101 on the convergence date; and
  - (F) Adjustments relating to cumulative translation differences of a foreign operation in accordance with paragraph D13 of the Indian Accounting Standards 101 on the convergence date. [clause (iii)]

**Transitional adjustments: Analysis**

- (i) The adjustments arising on account of transition to Ind AS from existing Indian GAAP is required to be

recorded directly in Other Equity at the date of transition to Ind AS. These adjustments has to be made in the following manner:

- (a) The book profit of the year of convergence and the following four previous years shall be increased or decreased with the transitional adjustments recorded directly in Other Equity excluding capital reserve and securities premium reserve and excluding the amounts referred in (A) to (F) (in the definition of Transition Amount), on the convergence date.
- (b) Those adjustments recorded in other comprehensive income referred in (A) above (in the definition of Transition Amount) and which would subsequently be reclassified to the profit and loss, shall be included in book profits in the year in which these are reclassified to the profit and loss, therefore these amounts are excluded from the transition amount.
- (c) Those adjustments recorded in other comprehensive income referred in (B) and (C) (in the definition of Transition Amount) above and which would never be subsequently reclassified to the profit and loss shall be included in book profits as specified hereunder:
  - i. *Changes in revaluation surplus of Property, Plant or Equipment (PPI) and Intangible assets (Ind AS 16 and 38)* – It shall be included in the book profit in the year in which the Asset/Investment is retired, disposed, realized or otherwise transferred.
  - ii. *Gains and losses from Investments in equity instruments designated at fair value through OCI (Ind AS 109)* – It shall be adjusted in book profits in the year in which investment is retired/disposed/realized.
  - iii. *Re-measurements of defined benefit plans (Ind AS 19)* – It shall be adjusted in book profits equally over a period of 5 years starting from the year of first time adoption of Ind AS.
  - iv. *Any other Item* – It shall be adjusted in book profits equally over a period of 5 years starting from the year of first time adoption of Ind AS.

- (d) The other adjustments referred in (D), (E) and (F) (in the definition of Transition Amount) above shall be made in the following manner:

**I. Property, Plant and Equipment (PPE) and intangible assets at fair value as deemed cost [referred in (D) (in the definition of Transition Amount) above]**

An entity may use fair value in its opening Ind AS Balance Sheet as deemed cost for an item of PPE or an intangible asset as mentioned in paragraphs D5 and D7 of Ind AS 101. In such cases the treatment shall be as under –

- The existing provisions for computation of book profits under section 115JB of the Act provide that in case of revaluation of assets, any impact on account of such revaluation shall be ignored for the purposes of computation of book profits. Further, the adjustments in retained earnings on first time adoption with respect to items of PPE and Intangible assets shall be ignored for the purposes of computation of book profits.
- Depreciation shall be computed ignoring the amount of aforesaid retained earnings adjustment.

Similarly, gain/loss on realization/ disposal/ retirement of such assets shall be computed ignoring the aforesaid retained earnings adjustment.

**II. Investments in subsidiaries, joint ventures and associates at fair value as deemed cost [referred in (E) (in the definition of Transition Amount) above]**

An entity may use fair value in its opening Ind AS Balance Sheet as deemed cost for investment

in a subsidiary, joint venture or associate in its separate financial statements as mentioned in paragraph D15 of Ind AS 101. In such cases retained earnings adjustment shall be included in the book profit at the time of realisation of such investment.

**III. Cumulative translation differences [referred in (F) (in the definition of Transition Amount) above]**

- An entity may elect a choice whereby the cumulative translation differences for all foreign operations are deemed to be zero at the date of transition to Ind AS. Further, the gain or loss on a subsequent disposal of any foreign operation shall exclude translation differences that arose before the date of transition to Ind AS and shall include only the translation differences after the date of transition.
- In such cases, to ensure that such Cumulative translation differences on the date of transition which have been transferred to retained earnings, are taken into account, these shall be included in the book profits at the time of disposal of foreign operations as mentioned in paragraph 48 of Ind AS 21.

(ii) All other adjustments to retained earnings (recorded as other equity) at the time of transition (including for example, Decommissioning Liability, Asset retirement obligations, Foreign exchange capitalisation/ decapitalization, Borrowing costs adjustments etc.) shall be included in book profits, equally over a period of five years starting from the year of first time adoption of Ind AS.

(iii) Section 115JB of the Act already provides for adjustments on account of deferred tax and its provision. Any deferred tax adjustments recorded in Reserves and Surplus on account of transition to Ind AS shall also be ignored.

The following points should also be noted in this context:

**1. Losses and unabsorbed Depreciation allowed to be carried forward (Section 115JB (3))**

Provisions of MAT under Section 115JB (1) shall not affect the determination of the amounts unabsorbed depreciation under Section 32(2), business loss u/s 72(1), speculation loss u/s 73, capital loss u/s 74 and loss u/s 74A in relation to the relevant previous year to be carried forward to the subsequent year or years. In other words, these are allowed to be carried forward in usual manner.

**2. Report from a Chartered Accountant to be submitted [Section 115JB (4)]**

Every company to which this section applies, shall furnish a report in the prescribed form from a Chartered Accountant as defined in the Explanation below Section 288(2), certifying that the book profit has been computed in accordance with the provisions of this section along with the return of income filed under Section 139(1) or along with the return of income furnished in response to a notice Section 142(1)(i).

**3. All other provisions to be applicable as usual [Section 115JB (5)]**

Save as otherwise provided in this section, all other provisions of this Act shall apply to such companies, i.e. all the provisions such as Advance tax, Interest under Section 234A, 234B and 234C, penalty etc shall also apply to such companies.

**4. Applicability of Provisions to SEZ enterprises and SEZ developers –**

The provisions of this section shall not apply to the income accrued or arising on or after 1/04/05 but before 01/04/11 from any business carried on, or service rendered, by an entrepreneur or a Developer in a unit or SEZ, as the case may be. [Section 115JB (6)]. However, provisions of this section are applicable to SEZ enterprises and SEZ Developers from AY 2012-13.

### 5. Rate of MAT in case of a unit located in International Financial Service Centre

Notwithstanding anything contained in Section 115JB (1), where the assessee referred to therein, is a unit located in an International Financial Services Centre and derives its income solely in convertible foreign exchange, the rate of MAT shall be 9% instead of 18.5% of Book Profits. [section 115JB (7) by the Finance Act, 2016, w.e.f. 1-4-2017]

### 6. Applicability of provisions of MAT applicable to foreign companies

Since 'company' defined u/s 2(17) includes any body corporate incorporated under the laws outside India, so foreign companies are also liable to MAT in respect of their income in India.

However, foreign companies shall not liable u/s 115JB without physical presence.

The Authority for Advance Ruling ("AAR") has delivered a ruling in the case of Timken India Ltd. In re (2005) 273 ITR 67 (AAR) where it holds that the provisions of section 115JB of the Income-tax Act, 1961 ("the Act") levying Minimum Alternate Tax ("MAT") on the book profit of a Company would not apply to a Foreign Company not having any physical presence in India. In this case, the AAR distinguished its earlier ruling of 1998 (234 ITR 828) wherein it had held that a foreign company would be subject to MAT provisions. The critical factor for distinguishing was on the basis that in the earlier ruling the applicant had a project office in India, which constituted a Permanent Establishment and was preparing its financial statements as required under Indian Companies Act, 1956. In order to comply with the requirement of MAT provisions regarding preparing Profit & Loss Account in accordance with the provisions of the Indian Companies Act, it is essential that the foreign company should have a place of business within India.

Similar view has been upheld by AAR in the recent ruling of Praxair Pacific Ltd., In re [2010] 326 ITR 276 (AAR)

Further, in case of a foreign company any income chargeable at a rate lower than the rate specified in section 115JB shall be reduced from the book profits and the corresponding expenditure will be added back.

With a view to provide certainty in taxation of foreign companies, an amendment has been made vide Finance Act, 2016 so as to provide that with effect from 01.04.2001, **the provisions of section 115JB shall not be applicable to a foreign company if -**

- the assessee is a resident of a country or a specified territory with which India has an agreement referred to in sub-section (1) of section 90 or the Central Government has adopted any agreement under sub-section (1) of section 90A and the assessee does not have a permanent establishment in India in accordance with the provisions of such Agreement; or
- the assessee is a resident of a country with which India does not have an agreement of the nature referred above and the assessee is not required to seek registration under any law for the time being in force relating to companies.

For the removal of doubts, it is hereby clarified that the provisions of this section shall not be applicable and shall be deemed never to have been applicable to an assessee, being a foreign company, where its total income comprises solely of profits and gains from business referred to in section 44B or section 44BB or section 44BBA or section 44BBB and such income has been offered to tax at the rates specified in those sections.

### 7. Whether Assessing officer has the power to examine correctness of net profit shown in profit and loss Account [Apollo Tyres Ltd. V. CIT (2002) 255 ITR 273 (SC)]

The AO does not have the power to question correctness of P&L A/c prepared by assessee and certified by the statutory auditors of the company as having been prepared in accordance with the provisions of

Parts II and III of Schedule VI to the Companies Act, 2013. The AO does not have the jurisdiction to go behind the net profits shown in the P&L A/c except to the extent provided in the Explanation 1 to Section 115JB.

In the following cases Assessing officer has power to rework or rewrite the profit and loss account:

- Where the profit and loss account submitted is not as per Part II and III of Schedule VI of companies Act, 2013.
- Where accounting policies or accounting standards or rate of depreciation adopted are different from those adopted for the profit and loss prepared for the AGM.

### **MAT CREDIT [SECTION 115JAA]**

MAT Credit for taxes paid as per Section 115JB in earlier years (in which MAT liability was more than tax liability as per normal provisions of the Act) is available in the Assessment year in which Tax payable on the total income computed under the normal provisions of this Act is more than tax payable u/s 115JB for that Assessment year.

MAT Credit to be set off in an AY = Regular Income tax - Minimum alternate tax

Credit of MAT in respect of tax excess paid under Section 115JB will be available and it can be carried forward for 15 assessment years succeeding the assessment year in which the credit became allowable.

The amount of MAT credit shall not be allowed to be carried forward to the subsequent year to the extent such credit relates to the difference between the amount of foreign tax credit (FTC) allowed against MAT and FTC allowable against the tax computed under regular provisions of the Act. **[w.e.f. AY 18-19]**

In case of conversion of a company into LLP, MAT Credit available in the hands of company shall not be allowed to LLP.

**Illustration.** Number of years for which credit of MAT excess paid under section 115JB can be carried forward is –

- (a) 7 Assessment years      (b) 8 Assessment years  
(c) 15 Assessment years      (d) 9 Assessment years.

**Answer:**

(c) 15 Assessment years

### **Illustration**

A domestic Company, ABC Ltd., furnishes the following particulars in respect of AY 2020-21 and solicits your advice on the application of Section 115 JB. You are also required to compute the total income tax payable.

	<b>Particulars</b>	<b>INR</b>
	Profits per P&L Account as per Co. Act, 2013	2,15,00,000
	This includes:	
a)	Credit of Dividends from Indian Cos.	20,00,000
b)	Excess realized on sale of land held as investment	30,00,000
c)	Depreciation on SLM basis	1,00,00,000
d)	Provision for losses of subsidiaries	60,00,000

	Depreciation allowable per Income Tax Rules, 1962	1,50,00,000
	STCG on sale of land mentioned above	40,00,000
	B/f losses	50,00,000
	Unabsorbed Depreciation	60,00,000

The Company has also represented to you that the excess realized on sale of land cannot form part of the book profits u/s 115 JB. You will have to deal with the issue assuming that the Co. is not required to comply with Ind. AS. The annual turnover of ABC Ltd. was INR 40 Crores.

**Solution:**

Computation of Total Income per Income Tax Act, 1961			
	Net Profit per P&L Account		2,15,00,000
Less:	Dividends from Indian Cos. (exempt u/s 10(34) )	20,00,000	
	Excess realized on sale of land (treated separately)	30,00,000	
		50,00,000	
			1,65,00,000
Add:	Depreciation on SLM Basis	1,00,00,000	
	Provisions for losses of subsidiaries	60,00,000	
		1,60,00,000	
			3,25,00,000
Less:	Depreciation allowable per Income Tax Act		1,50,00,000
	Business Income		1,75,00,000
Less:	Set-off of B/f losses		50,00,000
	Net Business Income		1,25,00,000
	Capital Gains		40,00,000
	Total Income		1,65,00,000
Less:	Unabsorbed Depreciation		60,00,000
	<b>Total Income per as Income Tax Act, 1961</b>		<b>1,05,00,000</b>

Computation of Book Profit u/s 115JB			
	Net Profit per P&L Account		2,15,00,000
Less:	Dividends from Indian Cos. (exempt u/s 10(34) )	(20,00,000)	(20,00,000)
			1,95,00,000

Add:	Depreciation on SLM Basis	1,00,00,000	
	Provisions for losses of subsidiaries	60,00,000	1,60,00,000
			3,55,00,000
Less:	Depreciation		1,00,00,000
	Business Income		2,55,00,000
Less:	B/f Business Loss as it's less than Unabsorbed Depreciation		50,00,000
	<b>Book Profits</b>		<b>2,05,00,000</b>
	<i>Note that the profit on sale of land held as investment is not excluded from the P&amp;L for purposes of computing the Book Profits!</i>		
	<i>Note that the least of the B/f loss and the Unabsorbed Depreciation is reduced to compute Book Profits</i>		

<b>Income Tax Liability under Normal Provisions</b>			
	Tax Liability @ 25% as the Turnover is < 400 Crores		26,25,000
Add:	Surcharge @ 7% as the Income is > 1 Cr.		1,83,750
	Total Tax Payable		28,08,750
Add:	Health and Education Cess @ 4%		1,12,350
	<b>Total Income Tax Liability</b>		<b>29,21,100</b>

<b>Income Tax Liability per MAT Provisions</b>			
	15% of Book Profits		3075000
Add:	Surcharge @ 7% as the Income is > 1 Cr.		215250
	Total Tax Payable		3290250
Add:	Health and Education Cess @ 4%		131610
	<b>Total Income Tax Liability</b>		<b>3421860</b>

**Note:**

- Since 15% of book profits exceeds the tax payable per Income Tax Act, 1961, the book profit would be deemed to be the total income and the tax payable on such total income, which is INR 34,21,860 (rounded off) would become the liability for AY 2020-21 for the Co.
- With regards to the company's representation, in respect of the capital gains, whether liable for book profit tax u/s 115JB, it may be noted that since the excess realised on sale of land which was held as investment, has been included in the net profit computed per Sch. III of the Companies Act, 2013, it shall form part of Book Profits (Bombay HC Judgement in CIT vs. Veekay Lal Investment Co Pvt Ltd.)

**Illustration**

Mona Ltd., a resident Co., earned a profit of INR 15,00,000/- after debit / credit of the following amounts:

**Items debited**

- a) Provisions for the losses of Subsidiaries; INR 70,000
- b) Provision for doubtful debts; INR 75,000
- c) Provision for Income Tax; INR 105,000
- d) Provision for Gratuity basis actuarial valuation; INR 200,000
- e) Depreciation; INR 360,000
- f) Interest to Financial Institution (unpaid before filing of return); INR 100,000
- g) Penalty for infraction of law; INR 50,000

**Items credited**

- a) Profits from unit(s) established in SEZ; INR 500,000
- b) Share in income of an AOP as a member; INR 100,000
- c) Income from units of UTI; INR 75000
- d) Long Term Capital Gains; INR 300,000

**Other Information**

- a) Depreciation includes INR 150,000 on account of revaluation of fixed assets
- b) Depreciation per Income Tax Rules is INR 280,000
- c) Balance of P&L Account on the assets side of B/S as at 31st Mar'19 was INR 10,00,000; of which the unabsorbed depreciation was INR 400,000
- d) Capital Gains has been invested in specified assets u/s 54EC
- e) The AOP, of which the Co. is a member has paid the tax at maximum marginal rate
- f) Provision for Income Tax includes INR 45,000 as interest

You are required to compute the MAT u/s 115JB of the Income Tax Act, 1961 for AY 2020-21, assuming that the Co. is not required to comply with IND AS.

<b>Computation of Book Profit u/s 115JB</b>			
	Net Profit per P&L Account		15,00,000
Add:	Provisions for subsidiaries' losses	70,000	
	Provision for doubtful debts	75,000	
	Provision for Income Tax	1,05,000	
	Depreciation	3,60,000	
		6,10,000	
			21,10,000
Less:	Share in income of an AOP	1,00,000	

	Income from units of UTI	75,000	
	Depreciation (excl. Reval. Amounts)	2,10,000	
	Unabsorbed Business Losses	4,00,000	
			(7,85,000)
	<b>Book Profits</b>		<b>13,25,000</b>
	MAT Liability @ 15%		19,87,50
Add:	Health and Education Cess @ 4%		7,950
	<b>MAT Liability (rounded off)</b>		<b>20,6700</b>

**Note:**

1. Interest to FI's / Banks which are unpaid prior to filing of return and penalties are not specified items u/s 115JB and hence not added back
2. Provision for Gratuity Liability based on actuarial valuation is an ascertained liability and hence should not be added back to ascertain book profits (CIT vs. Echjay Forgings P. Ltd.)
3. Capital Gains reflected in the P&L will form a part of the book profits even if the investments u/s 54EC have been made. Therefore, these cannot be reduced. (CIT vs. Veekaylal Investment Co. P. Ltd)
4. Income from units in UTI is exempt u/s 10(35) and hence reduced
5. Share of the AOP's income as a member is reduced as the AOP has already paid the tax at maximum marginal rate

**Illustration**

The table below highlights and explains the modus of MAT Credit, and how it is utilised and carried forward.

<b>MAT CREDIT UTILISATION AND C/F</b>					
<b>A.Y</b>	<b>Normal Tax Liability</b>	<b>Liability (MAT)</b>	<b>Tax Payable</b>	<b>Credit utilised</b>	<b>Credit c/f</b>
2008-09	100	300	300	-	200
2009-10	120	90	120	30	170
2010-11	150	110	150	40	130
2011-12	180	200	200	-	150
2012-13	200	190	200	10	140
2013-14	300	280	300	20	120
2014-15	250	230	250	20	100
2015-16	225	175	225	50	50
2016-17	250	240	250	10	40
2017-18	275	270	275	5	35
2018-19	350	315	350	35	0

**DIVIDEND DISTRIBUTION TAX [SECTION 115-O]**

**Dividend Distribution Tax** : It is a tax on dividend (interim or final) declared, distributed or paid by a company (whether out of current or accumulated profits) on or after June 1, 1997 (excluding previous year 2002-03). Dividend distribution tax is in addition to income tax on total income. Term “Dividend” has the same meaning as defined under section 2(22). This tax is applicable on Domestic Company only.

**Dividend distribution tax is not applicable in following cases:**

- I. the amount of dividend, if any paid to any person for, or on behalf of, the New Pension System Trust referred to in Section 10(44).
- II. any amount declared, distributed or paid by the specified domestic company by way of dividends (whether interim or otherwise) to a business trust out of its current income on or after the specified date.

*Explanation.*

- (a) “**specified domestic company**” means a domestic company in which a business trust has become the holder of whole of the nominal value of equity share capital of the company (excluding the equity share capital required to be held mandatorily by any other person in accordance with any law for the time being in force or any directions of Government or any regulatory authority, or equity share capital held by any Government or Government body);
- (b) “**specified date**” means the date of acquisition by the business trust of such holding as is referred to in clause (a).]
- III. Any Dividend (interim or final) declared, distributed or paid on or after April 1, 2016 by a Company, being a unit established on or after April 1, 2016 in an International Financial Services Centre, deriving income solely in convertible foreign exchange out of its current income. Such dividend is not taxable in the hands of receiver also.

*Explanation* : For the purposes of this sub-section,

- (a) “**International Financial Services Centre**” shall have the same meaning as assigned to it in clause (q) of section 2 of the Special Economic Zones Act, 2005 (28 of 2005);
- (b) “**unit**” means a unit established in an International Financial Services Centre, on or after the 1st day of April, 2016;
- (c) “**convertible foreign exchange**” means foreign exchange which is for the time being treated by the Reserve Bank of India as convertible foreign exchange for the purposes of the Foreign Exchange Management Act, 1999 (42 of 1999) and the rules made thereunder.
- IV. Any dividend distributed by the recipient out of the III above.
- V. Dividend declared, distributed or paid during April 1, 2005 and May 31, 2011 by a SEZ enterprise or SEZ developer. (However, As per proviso 6 of section 115-O inserted by finance Act 2011, Provisions of section 115-O are also applicable to an enterprise/undertaking developing, operating or maintaining SEZ).

**Inter-corporate Dividend relief** : According to Section 115-O(1A) Where a holding company receives dividend from its subsidiary company in a financial year and in the same financial year such holding company also declares dividend, then dividend tax shall be levied on dividend declared by holding company after reducing dividend received from subsidiary company. This relief is available only in the following situations:

- (a) where such subsidiary is a domestic company, the subsidiary has paid the tax which is payable under this section on such dividend; or

- (b) where such subsidiary is a foreign company, the tax is payable by the domestic company under section 115BBD on such dividend.

However, the same amount of dividend shall not be taken into account for reduction more than once.

*Explanation* - a company shall be a subsidiary of another company, if such other company, holds more than half in nominal value of the equity share capital of the company.

**Dividend tax is to be paid within 14 days from the date of declaration or distribution or payment of dividend, whichever is earlier. [Section 115-O (3)]**

**Calculation of Dividend distribution tax:** Dividend tax is to be calculated @15% (+SC+HEC) of the Gross amount of dividend. Deemed dividend under section 2(22)(e) is taxable at a gross rate of 30% + SC + HEC. The Finance Act 2014 has inserted sub-section (1B) in section 115-O to ensure that tax is levied on a proper base. In order to ensure that tax is levied on a proper base, the dividend actually received need to be grossed up for the purpose of computing the dividend distribution tax.

With the grossing up, the effective tax rate will be 20.555% as under:

Suppose if dividend of INR 85 is to be distributed by the company, then DDT would be calculated as follows

Particulars	Amount (INR)
Dividend distributed	85
Increased amount (as would after reduction of tax on such increased amount @15% would give dividend distributed of INR 85)	100
DDT @15% of INR 100	15
Effective rate of DDT of INR 15 on dividend distributed of INR 85 (15 / 85 X 100)	17.647%
Add : Surcharge @ 12% of 17.64706	2.117%
Total Tax	19.764%
Add : Health & Education Cess	0.791%
Total effective DDT rate applicable	20.555%

However it is also possible to take a view that grossing up should be done at the rate of 17.472% (i.e. 15% + surcharge 12% + HEC4%) which is the effective rate of dividend distribution tax.

$$\frac{15}{100-15} \times 100 + \text{Surcharge} + \text{HEC}$$

There will be no grossing up for deemed dividend u/s 2(22)(e). So company shall pay DDT @ 34.944% i.e., 30% + 12% surcharge + 4% HEC

For the purpose of determining the tax on distributed profits payable in accordance with this section, any amount by way of dividends referred to in section 115-O (1) as reduced by the amount referred to in section 115-O(1A) shall be called net distributed profits. This net distributed profit shall be increased to such amounts as would, after reduction of the tax on such increased amount at the rate of 15% plus surcharge and SHEC, be equal to the net distributed profits.

Therefore, to take another example, let's say the net distributed profits are 29 Lacs. Hence, the Grossed-up Dividend (100/85) would be as under:

	Alternative I	Alternative II
Grossed Up Dividend	35.139	34.12
15% DDT	5.271	5.12
Net Distributed Profits	29.000	29.00
SC	0.632	0.61
Cess	0.236	0.23
DDT + SC + Cess	6.139	5.96

Similarly, section 115R is amended by the Finance Act 2014 to provide that for the purposes of determining the additional income-tax payable in accordance with section 115R (2), the amount of distributed income shall be increased to such amount as would, after reduction of the additional income-tax on such increased amount at the rate specified in section 115R (2), be equal to the amount of income distributed by the Mutual Fund.

### Illustration

Xavier Ltd., a domestic company, has distributed dividend of Rs. 230 lakhs to its shareholders on 1/11/2015. On 1/10/2015, it has received dividend of Rs. 60 lakhs from its domestic subsidiary company Yale Ltd., on which Yale Ltd. has paid dividend distribution tax under section 115-O. Compute the additional income-tax payable by Xavier Ltd. under section 115-O.

### Solution:

Particulars	Figures in Lacs	
Div distributed by Xavier Ltd.	230	
Div received from Yale Ltd	60	
Net distributed profits	170	
Grossed Up Dividend	200.00	100/85 of 170
15% DDT	30.00	
Net Dividends	170.00	
SC @ 12%	3.60	of DDT
Cess @ 4%	1.344	of DDT + SC
DDT + SC + Cess	34.944	
17.472% of Grossed up Div	34.944	

### Taxability of Dividend income of an Indian company from a Specified foreign company [Section 115BBD]

Dividend Income of an Indian company out of dividend declared, distributed or paid by a Specified foreign company is taxable @ 15%. No deduction in respect of any expenditure or allowance shall be allowed to the assessee under any provision of this Act in computing its income by way of dividends.

“**Specified Foreign Company**” means a foreign company in which the Indian company holds 26% or more in nominal value of the equity share capital of company.

### Illustration

X Ltd. an Indian Company received dividend of Rs. 15 lakhs from a foreign company in which it holds 28% in nominal value of the equity share capital of the company. X Ltd. incurred expenditure of Rs. 0.25 lakhs on earning this income. Examine the taxability of the dividend under the provisions of the Income Tax Act, 1961.

## Solution

Under section 115BBD, dividend received by an Indian company from a foreign company in which it holds 26% or more in nominal value of the equity share capital of the company, would be subject to a concessional tax rate of 15% plus surcharge and cess, as against the tax rate of 30% applicable to other income of a domestic company. This rate of 15% plus surcharge and cess would be applied on gross dividend, in the sense, that no expenditure would be allowable in respect of such dividend. Therefore, dividend of Rs. 15 lakhs received by X Ltd. from a foreign company, in which it holds 28% in nominal value of equity share capital of the company, would be subject to tax@15% under section 115BBD. Such dividend would be taxable under the head "Income from other sources". No deduction is allowable in respect of Rs. 0.25 lakhs spent on earning this income.

The Finance (No.2) Act, 2014 extended the benefit of concessional rate of taxation@15% on gross dividend received by Indian companies from specified foreign companies without limiting it to a particular assessment year, in order to encourage Indian companies to repatriate foreign dividends into the country.

**Taxability of Dividend in hands of Recipient :** Dividend received from a Domestic company on which company has paid Dividend tax u/s 115-O is exempt in the hands of the shareholder.

However from AY 18-19, if in case of a resident Individual/HUF/Firm or any person (not being a domestic company, or a fund/ institution / trust / university / educational institution / hospital / medical institution referred to in section 10(23C)(iv)(v)(vi)(via), or a trust/institution registered under section 12A/12AA) the aggregate dividend income from domestic company is in excess of 10 lakhs, then it is taxable @ 10% (+SC+HEC) under Section 115BBDA.

For AY 17-18 this provision was applicable to resident Individual/HUF/Firm.

1. No assessee can claim any deduction from taxable income in respect of dividend tax paid by him. Also, no deduction is available from tax on dividend under any section.
2. Interest @ 1% per month or part of month shall be payable on the amount of dividend tax not paid in specified time limit of 14 days. Interest shall be calculated from the period starting from the next date after the last date of payment and ending on the date of actual payment. [ Section 115P]
3. Penalty under section 271C equal to amount of tax which company fails to pay shall be levied. Penalty is not applicable if assessee shows that there was reasonable cause for failure to pay.
4. As per Section 276B Person shall be punishable with rigorous imprisonment for a term of three months to seven years and fine, if he fails to pay tax as per provisions of Section 115-O. However, such punishment is not applicable if it could be proved that there was reasonable cause for default/failure.

## CARBON CREDIT [SECTION 115BG]

Where total income of the assessee includes any income from the transfer of carbon credit then such income shall be taxable at concessional rate of 10% (+SC+HEC) on the gross amount of such income. No expenditure or allowance in respect of such income shall be allowed. **[New section inserted vide Finance Act, 2017 w.e.f. AY 18-19]**

## BUY-BACK OF SHARES

### (i) Levy of additional income-tax @ 20% on buyback of shares [Section 115QA]

*The Finance (No. 2) Act, 2019 has extended the levy of additional income-tax on buy back to all companies including listed companies with effect from 5.7.2019. Thus, hereafter, In case of buyback of shares (whether listed or unlisted) by domestic companies, additional income-tax @20% (plus surcharge@12% and cess@4%) is leviable in the hands of the company.*

*Consequently, the income arising to the shareholders in respect of such buyback of shares by the domestic*

company would be exempt under section 10(34A), since the domestic company is liable to pay additional income-tax on the buyback of shares.

It means additional income tax is applicable to all companies, whether listed or unlisted, with effect from 5th July, 2019. However, the provision of this sub-section shall not apply to such buy of shares being the shares listed on recognized stock exchange in respect of which public announcement has been made before 5th July, 2019 in accordance with the provisions of SEBI (Buy Back Of Securities) Regulation 2018 made under the SEBI Act, 1992 as amended from time to time.

**Note: Prior to 5.7.2019, additional income-tax was attracted only in case of buy-back of unlisted shares by domestic companies. Consequently, only holders of unlisted shares were entitled to exemption under section 10(34A).**

### Taxation provisions in respect of buyback effected on or after 5.7.2019

I	II	III	IV
Taxability in the hands of	<b>Buyback of shares by domestic companies</b>	<b>Buyback of shares by a company, other than a domestic company</b>	<b>Buyback of specified securities by any company</b>
Company	Subject to additional income-tax@23.296%.	Not subject to tax in the hands of the company.	Not subject to tax in the hands of the company.
Shareholder/ holder of specified securities	Income arising to shareholders exempt under section 10(34A)	Income arising to shareholder taxable as capital gains u/s 46A.	Income arising to holder of specified securities taxable as capital gains u/s 46A.

Such tax should be paid to the credit of the Central Government within 14 days from the date of payment of any consideration for such buyback to the shareholder

#### Meaning of buyback and distributed income :

- 1. Buyback :** Purchase by a company of its own shares in accordance with the provisions of any law for the time being in force to companies [clause (i) of Explanation to section 115QA]
- 2. Distributed income :** The consideration paid by the company on buy-back of shares as reduced by the amount which was received by the company for issue of such shares, determined in the manner as may be prescribed [clause (ii) of Explanation to section 115QA]

#### Section 115QB

The principal officer of the domestic company and the company will be liable to pay simple interest on such additional tax which has not been paid in time.

Such interest is leviable @ 1% for every month or part of the month on such amount of tax not paid / short paid, for the period beginning the date immediately after the last date on which such tax was payable and ending with the date when it was actually paid.

#### Section 115QC

The principal officer of the domestic company and the company would be deemed to be an assessee in default if such additional tax is not paid to the credit of the Central Government.

In such a case hence, all provisions of collection and recovery of the tax would apply.

### Case Study

ABC Ltd.; a domestic company purchases its own unlisted shares, on 14th Oct'19. The consideration for the buyback amounted to INR 50,00,000, which was paid the very same day. The amount received by the company 2 years ago, for the issue of such shares was INR 27,00,000.

The tax on such buy back was deposited by the company to the credit of the Central Government on 27th Feb'20.

You are required to compute the tax and the interest payable.

### Solution

	Buy Back Consideration	50,00,000
Less:	Cost of Shares	27,00,000
	Net paid for buy-back	23,00,000
	Tax payable	4,60,000
	SC	55,200
	Cess (on Tax + SC) @ 4%	20,608
	Total additional tax payable	5,35,808
	Additional Tax Payable (rounded off)	5,35,810
	Interest payable	21,432

**Note:** The tax had to be deposited to the credit of the Central Government within 14 days of the payment of buy-back consideration, i.e., on or before 28th Oct'18. However, the tax was deposited on 27th Feb, and hence interest for 4 months @ 1% per month is applicable.

### CONVERSION OF AN INDIAN BRANCH OF A FOREIGN COMPANY INTO AN INDIAN SUBSIDIARY COMPANY

The provisions of this section apply to a foreign company engaged in the banking business in India, through its branch situated in India, and which is converted in to an Indian Subsidiary Company in accordance with the scheme framed by RBI.

If the conditions notified by the Central Government are satisfied, then the Capital Gains arising from such conversion would not attract any tax in the assessment year relating to the previous year in which such conversion takes place.

However, if the conditions notified by the Central Government are not complied with, then, all the provisions of this Act would apply to both the Foreign Company and the Indian Subsidiary, without any benefit / exemption / relief under the Act.

Additionally, if there has been any benefit, relief or exemption granted to the Foreign Subsidiary or Indian Subsidiary, in any previous year, and thereafter, there is a failure to comply with the conditions so notified, then such benefit / exemption / relief would be deemed to have been wrongly allowed. In such a case, the Assessing Officer is allowed to recompute the income of the assesseees for the said Previous Year and make the necessary amendment. The provisions of rectification shall apply and the four-year period within which such rectification must be made, has to be reckoned from the end of the previous year in which the failure to comply with the conditions take place.

**TAX ON INCOME DISTRIBUTED BY SPECIFIED COMPANY OR MUTUAL FUND**

**Section 115R (2)**

Any amount of income distributed by a Mutual Fund, to its unit holders after 1st Apr'03 shall be chargeable to tax and the Mutual Fund becomes liable to pay additional tax on such distribution.

<p><b>Money Market Mutual Fund (MMMF)</b></p>	<ul style="list-style-type: none"> <li>• 25% if the distribution is to Individual / HUF</li> <li>• 30% if the distribution is to any other person</li> </ul>
<p><b>Fund other than MMMF / Liquid Fund</b></p>	<ul style="list-style-type: none"> <li>• 25% if the distribution is to Individual / HUF</li> <li>• 30% if the distribution is to any other person</li> </ul>
<p><b>Infrastructure Debt Fund set up as Mutual Fund</b></p>	<ul style="list-style-type: none"> <li>• 5% if the distribution is to a Non-Corporate Non Resident or a Foreign Company</li> </ul>
<p><b>Equity Oriented Fund</b></p>	<ul style="list-style-type: none"> <li>• 10% if the distribution is to any person</li> </ul>

However, this does not apply in respect of any income distributed by the Administrator of the specified undertaking to the unit holders. Further, no additional income-tax shall be chargeable in respect of any amount of income distributed on or after 1st September, 2019 by a specified Mutual Fund, out of its income derived from transactions made on a recognised stock exchange located in any International Financial Services Centre and where the consideration for such transaction is paid or payable in convertible foreign exchange.

**Section 115R (2A)**

For the purposes of determining the additional tax payable, the amount of income so distributed shall be increased to such amount as would, after the reduction of the additional income tax on such increased amount at the rates specified, be equal to the amount of income so distributed by the Mutual Fund.

**Section 115R (3)**

The person responsible for making the payment of such incomes distributed by the Mutual Fund would be responsible to ensure that the applicable income tax on such distribution is deposited to the credit of the Central Government within 14 days of such distribution / payment.

**No deduction under any other provision [Section 115R(4)]**

No deduction under any provision of the Income-tax Act, 1961 shall be allowed to the UTI or to a Mutual Fund in respect of income, which has been subject to tax under section 115R(2).

**Section 115S**

The person responsible for making the payments of the income distributed by the Mutual Fund, will be liable to pay simple interest on such additional tax which has not been paid in time.

Such interest is leviable @ 1% for every month or part of the month on such amount of tax not paid / short paid,

for the period beginning the date immediately after the last date on which such tax was payable and ending with the date when it was actually paid.

### Section 115T

The person responsible for making the payments of the income distributed by the Mutual Fund, will be deemed to be an assessee in default if such additional tax is not paid to the credit of the Central Government.

In such a case hence, all provisions of collection and recovery of the tax would apply.

## EQUALISATION LEVY

The rapid growth of the information and communication technology has resulted in substantial expansion of the supply and procurement of digital goods and services globally, including India, and the digital economy is growing at approximately 10% per annum, faster than the economy as a whole.

These new business models have brought along with themselves, challenges. The typical issues / concerns around taxation vis-à-vis e-commerce are:

- a) difficulty in characterizing the nature of payment and establishing a link / nexus between taxable transaction, activity and taxing jurisdiction
- b) the difficulty in locating the transaction, activity and identifying the tax payer

The Organization for Economic Cooperation and Development (OECD), has recommended several options to tackle these challenges.

In order to address these challenges, Chapter VIII of the Finance Act, 2016 titled "Equalization Levy" provides for an equalization levy of 6% on the amount of consideration for specified services, received / receivable by a non-resident, not having permanent establishment in India, from a resident in India, who carries out business / profession, or from a non-resident who has a permanent establishment in India.

Refer to the table below to understand the various parameters and aspects involved.

Section	Subject	Provisions
166	Person responsible for deduction of equalization levy	Every person being a resident in India, who carries out business / profession, or a non-resident who has a permanent establishment in India shall deduct equalization levy from the amount paid / payable to a non-resident in respect of the specified service
	Rate	6% of the amount of consideration for a specified service, received / receivable by a non-resident, not having permanent establishment in India, from a resident in India, who carries out business / profession, or from a non-resident who has a permanent establishment in India, rounded off to the nearest ten rupees
	Threshold	Equalization Levy is deductible if the aggregate amount of consideration for a specified service in a previous year exceeds INR 100,000
	Time-period	The Equalization Levy so deducted during any calendar month shall be paid by every assessee to the credit of the Central Government by the 7th of following month
	Consequence of failure	Any assessee who fails to deduct, would anyway continue to be liable to pay to the credit of the Central Government, the Equalization Levy by 7th of the following month

167	Furnishing the statement	Every assessee shall, within the time prescribed after the end of the FY, submit a statement in the prescribed Form # 1, on or by 30th June immediately following the FY, setting forth all details for specified services pertaining to that FY
	Revised Statement	If the assessee notices omissions / errors / wrong details, he can furnish a revised statement before the expiry of 2 years from the end of the FY in which the specified service was provided
	Notice by the Assessing Officer (A.O.)	Where any assessee has failed to file the statement within the prescribed time, the A.O. is empowered to issue a notice calling for the statement and in which case the statement has to be furnished within 30 days of date of serving of such notice
168	Processing of the Statement	The statement shall be processed, and the amount payable along with interest if any, shall be computed towards the Equalization Levy. The net amount payable by or refundable to the assessee has to be worked out and an intimation must be served upon the assessee. However, no intimation is to be sent after the expiry of one year, from the end of the FY in which the statement is furnished
169	Rectification of mistake	With a view to rectifying a mistake apparent on the record, the A.O. may amend the intimation and such intimation must be amended within one year from the end of the FY in which the intimation sought to be amended was issued
170	Interest on delayed payments	Every assessee who fails to deposit to the credit of the Central Government, the applicable Equalization Levy, within 7th of the month following the month in which it was deducted, the assessee shall be liable to pay Interest @ 1% of such levy for every month / part of the month of delay
171	Penalty	If the assessee fails to deduct the Equalization Levy, in addition to the Equalization Levy and Interest, penalty equal to the amount of Equalization Levy that he failed to deduct would be applicable
		If the assessee fails to remit the Equalization Levy so deducted to the credit of the Government by 7th of the following month, a penalty of INR 1000 per day would be leviable, subject to a maximum of the equalization levy that he was to deduct
172	Penalty for delay in furnishing the statement	If the assessee fails to furnish the statement within 30th June of the following FY, or within 30 days of the notice served by the A.O., a penalty of INR 100 per day is leviable on the assessee

An assessee aggrieved by an order of the A.O., may appeal to the Commissioner of Income Tax (Appeals) within 30 days of receipt of date of order.

An assessee aggrieved by an order of the Commissioner, may appeal to the Appellate Tribunal within 60 days of receipt of date of order.

### Case Studies

DEF Ltd. is in the business of manufacture and sale of formal apparels and in order to expand its footprints globally, has launched a massive online campaign. For the purpose of the online advertisements, it utilized the

services of GHI Ltd, based out of Singapore. During the PY, DEF Ltd. paid a consideration of INR 20,00,000 to GHI Ltd. for such services.

Entail the implications if:

- a) GHI Ltd. has no permanent establishment in India
- b) GHI Ltd. has a permanent establishment in India

#### Answer

- a) In case GHI Ltd. has no permanent establishment in India, the consideration paid to GHI Ltd. by DEF Ltd. would attract Equalization Levy to be deducted @ 6%. Hence, INR 120,000 has to be deducted by DEF Ltd. and deposited to the credit of the Central Government within 7th of the following month. Non-deduction of equalization levy would attract a disallowance u/s 40(a)(ib) of 100% of the amount paid, while computing business income.
- b) In case GHI Ltd. has a permanent establishment in India, Equalization Levy would not be attracted. Therefore DEF Ltd. need not deduct Equalization Levy from the payment of consideration to GHI Ltd. However, tax has to be deducted u/s 195 in respect of such payments towards TDS. Non-deduction of TDS would attract a disallowance u/s 40(a)(i) of 100% of the amount paid, while computing business income.

### TAXATION ASPECTS RELATED TO CONVERSION OF COMPANY INTO AN LLP

The following shall not be regarded as “transfer”, and therefore, no capital gain shall arise on the following:

- Any transfer of a capital asset or intangible asset by a private company or unlisted public company to a limited liability partnership
- Any transfer of a share or shares held in the company by a shareholder as a result of conversion of the company into a limited liability partnership in accordance with the provisions of section 56 or section 57 of the Limited Liability Partnership Act, 2008

The below mentioned conditions would be applicable to avail the exemption.

S. No.	Condition	Explanation
a.	Assets and Liabilities	All the assets and liabilities of the company immediately before the conversion become the assets and liabilities of the limited liability partnership.
b.	Shareholders/Capital Contribution /Profit Sharing Ratios on conversion	a) All the shareholders of the company immediately before the conversion become the partners of the limited liability partnership. b) The capital contribution and profit sharing ratio of the shareholders in the limited liability partnership are in the same proportion as their shareholding in the company on the date of conversion.
c.	No other benefit to the shareholders	The shareholders of the company do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of share in profit and capital contribution in the limited liability partnership.

d.	Profit sharing ratio after conversion	The aggregate of the profit sharing ratio of the shareholders of the company in the limited liability partnership shall not be less than fifty per cent at any time during the period of five years from the date of conversion.
e.	Turnover Limit	The total sales, turnover or gross receipts in the business of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed sixty lakh rupees.
ea.	Value of assets (Inserted by Finance Bill 2016)	The total value of the assets as appearing in the books of account of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed five crore rupees.
f.	Accumulated profit (reserves)	No amount is paid, either directly or indirectly, to any partner out of balance of accumulated profit standing in the accounts of the company on the date of conversion for a period of three years from the date of conversion.

Exemption shall be available only if the conversion satisfies all the below mentioned conditions –

- The above exemption is limited to capital assets and not any other assets like inventory
- The limit on turnover is to restrict the tax benefit of this clause to smaller entities which will render a big section of companies willing to convert as ineligible
- Size of assets is an additional parameter to judge the eligibility of the company to claim benefit
- The point around Distribution from / of Reserves are a safeguard against misuse by a company to escape Dividend Distribution Tax since a LLP is not liable to DDT

Where any of the conditions specified above are not complied with, exemption from capital gains shall not be available. The conditions should be satisfied at the time of conversion.

Where any of the conditions specified above are not complied with, exemption from capital gains shall not be available. The conditions should be satisfied at the time of conversion. Additionally, conditions d and f should be satisfied for respective period specified therein.

Where benefit is taken under section 47(xiii b) at the time of conversion, and subsequently there is non-compliance of condition d or f, benefit availed shall be charged to tax in the manner specified below –

- Capital Gains exempted of the predecessor company will become income of LLP by way of capital gain in the year in which non-compliance takes place, and
- Capital Gains exempted of the shareholder of the predecessor company on transfer of shares at the time of conversion shall become income by way of capital gain in the year in which non-compliance takes place.

**Other Relevant Points:**

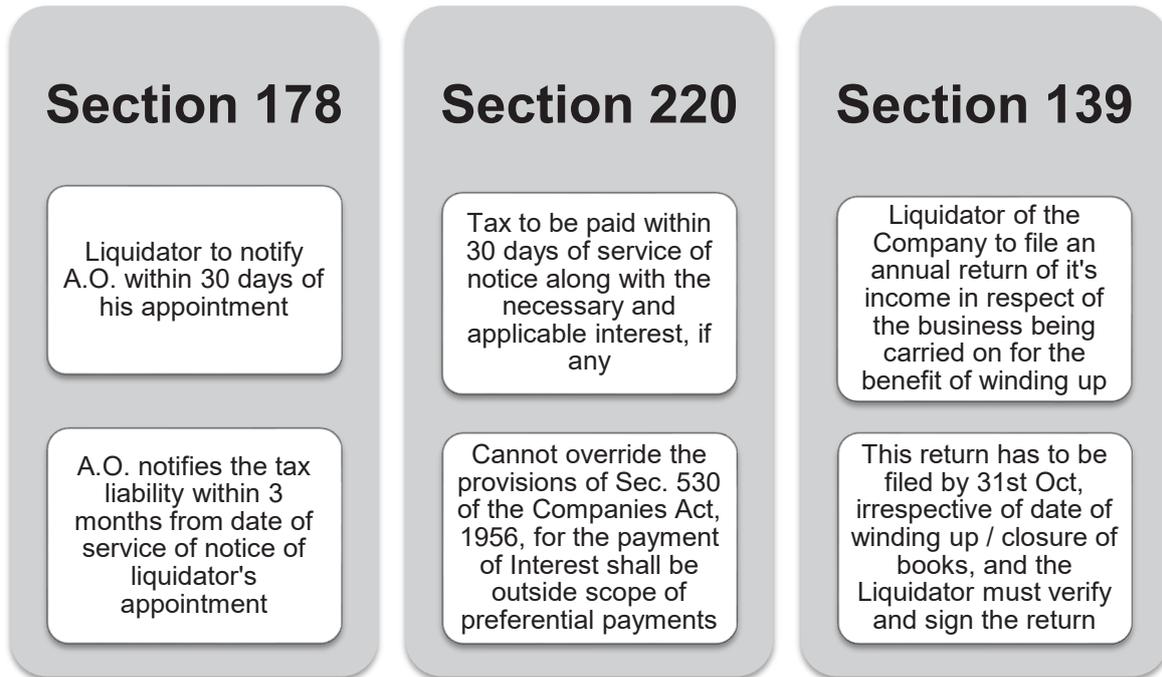
- Cost of acquisition of the asset: Shall be deemed to be the cost of acquisition of predecessor company.
- Cost of Improvement: Any cost incurred on improvement of the assets by Predecessor Company and LLP shall be the cost of improvement.
- Period of holding of asset: As per Section 2(42A) (b), for the purpose of determining period of holding of

capital asset for determining nature of capital gain, period for which the asset was held by predecessor company shall be included.

*Note* : MAT credit of the company is not allowed to be carried forward in the hands of LLP on conversion of company into LLP.

## TAX LIABILITY OF COMPANIES IN THE EVENT OF LIQUIDATION

The table / diagram below explain the various aspects that require careful reading and evaluation.



### Key Points:

#### Section 178

- Until the liquidator receives the intimation of tax liability, he is not permitted to part with the assets of the Company
- If the A.O. fails to notify the tax liability within the 3 months' time period, then the demand of made by the A.O. after the expiry of the statutory period, of 3 months falls outside the scope of preferential payment within the meaning of Sec. 530 of the Act and hence, such tax liability then assumes the same preference, i.e. ranks pari passu with the claims of ordinary creditors
- In case the liquidator fails to notify his appointment, or parts with any assets of the Company in contravention with the provisions of the section, he will be personally liable for the payment of tax which otherwise the company was liable to pay

#### Section 220

- The Kerala High Court has held that a Company in Liquidation cannot be deemed to be an assessee in default on the same footing as any other assessee for the purposes of Sec 200 of the Income Tax Act, because the Company is under the control of a Liquidator, who acts as such, in accordance to the Companies Act. Hence, he cannot be equated to be a defaulter and thereafter asked to pay the interest u/s 220 or penalty u/s 221

- It is settled law that a “company in liquidation” is not the same kind of assessee as a “working company”. Interest claim in respect of tax due from the company, prior to the date of winding up, is not entitled to priority u/s 530 of the Companies Act
- The High Court of Kerala held that the provisions of Companies Act are special and those of the Income Tax Act are general and if there is an apparent conflict between the two enactments, the provisions of the Companies Act shall prevail

### Section 139

- If the company fails to file the return, such eventualities could be serious in nature as the company may then lose its exemptions and the tax liabilities may then interfere with and adversely affect the claims of its creditors

It must be noted that u/s 46, where the assets of the Company are distributed to the Shareholders, on its liquidation, such distribution will not be regarded as a transfer vis-à-vis Capital Gains.

### Liability of Directors & Shareholders

- Section 179 of the Income Tax Act fastens the directors of a private company with a personal liability in the event of non-recovery of its tax dues. This liability is “joint and several”
- Section 2(22)(c) of the Income Tax Act, any distribution made to the shareholders of the company on liquidation, to the extent to which the distribution is attributable to the accumulated profits of the company immediately before the liquidation, whether capitalized or not, would be deemed to be dividend

## TAXATION OF SHARE PREMIUM

1. Section 56(2)(viib) of the Income Tax Act, 1961 states that –

- where a company, not being a company in which the public are substantially interested,
- receives in any previous year, from any person being a resident,
- any consideration for issue of shares that exceeds the face value of such shares,
- the aggregate consideration received for such shares as exceeds the fair market value (FMV) of the shares, shall be chargeable to tax under the head “Income from other sources”

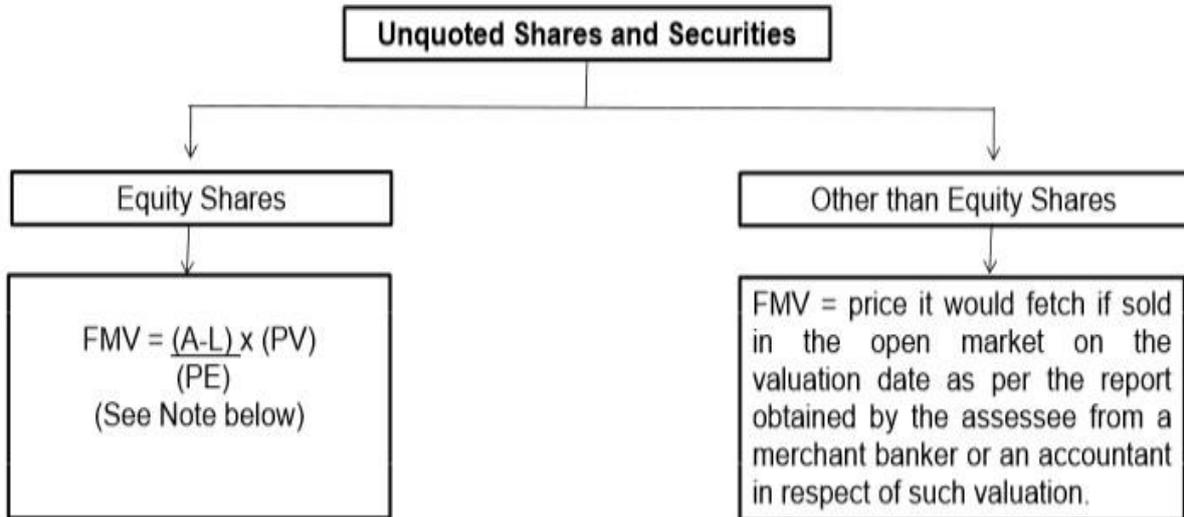
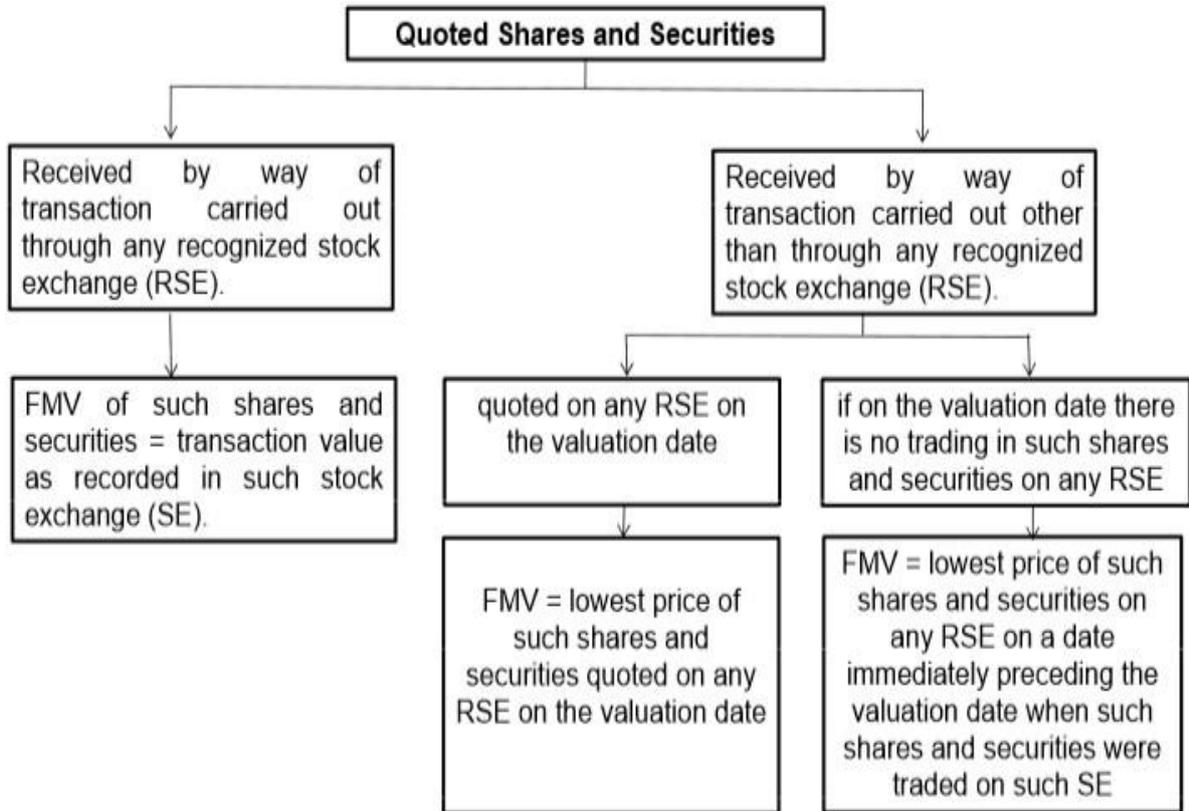
In case of issue of shares at premium by listed companies, share premium is not considered as income. However, in case of un-listed companies, premium can be considered as income in case the price charged at the time of issue of share is more than face value (that is at premium) and is also higher than fair market value.

**Provided that this clause shall not apply where the consideration for issue of shares is received:**

(i) by a venture capital undertaking from a venture capital company or a venture capital fund; or (ii) by a company from a class or classes of persons as may be notified by the Central Government in this behalf.

### Rule 11UA

The rules prescribe separate framework for quoted and unquoted securities in the context of determination of FMV.



**Note :**

A = Book value of the assets in Balance Sheet as reduced by certain amounts specified in Rule 11UA(c)(b).

L = Book value of liabilities shown in the Balance Sheet but not including amounts stated in (i) to (vii) in Rule 11UA(c)(b).

PE = Total amount of paid up equity share capital as shown in Balance Sheet.

PV = The paid up value of such equity shares.

**Illustration**

The following details of the shares issued by the following closely held companies are available. You are required to advise the Company on the applicability or otherwise of Sec 56(2) (viib).

Co.	No. of Shares	FV of Shares (INR)	FMV of Shares (INR)	Issue Price (INR)	Applicability & Chargeable Tax
A (P) Ltd.	10000	100	120	130	Sec. 56(2) (viib) attracted as the shares are issued at premium.  10000 X (130-120) = INR 100,000 would be chargeable to tax under the head "Income from other sources"
B (P) Ltd.	20000	100	120	110	Sec. 56(2) (viib) attracted as the shares are issued at premium.  However, no amount is chargeable to tax as the Issue Price is < the FMV
C (P) Ltd.	30000	100	90	98	Sec. 56(2) (viib) are not attracted as the shares are not issued at premium, rather at a discount on FV, even though the issue price is > FMV
D (P) Ltd.	40000	100	90	110	Sec. 56(2) (viib) attracted as the shares are issued at premium.  40000 X (110-90) = INR 800,000 would be chargeable to tax under the head "Income from Other Sources"

### TAXATION ASPECTS OF AMALGAMATIONS, MERGERS AND DEMERGERS

Section 2(1B) of the Income Tax Act, 1961, defines the term "amalgamation" as follows:

“Amalgamation in relation to Companies, means the merger of one or more companies with another company or the merger of two or more companies to form one company, the companies which so merge being referred to as the “amalgamating company” and the company with which they merge or which is formed as a result of the merger, being referred to as the “amalgamated company”, in such a manner that:

- a) all the property of the amalgamating company(ies) before the amalgamation become the property of the amalgamated company by virtue of the amalgamation
- b) all the liabilities of the amalgamating company(ies) before the amalgamation become the liabilities of the amalgamated company by virtue of the amalgamation
- c) shareholders holding not less than 3/4ths in value of the shares in the amalgamating company become shareholders of the amalgamated company by virtue of the amalgamation

otherwise than as a result of the acquisition of the property of one company by another company pursuant to the purchase of such property by the other company or as a result of the distribution of such property to the other company after the winding up of the first mentioned company.

### **Business Losses & Unabsorbed Depreciation**

A special provision is made which relaxes the provision relating to carrying forward and set off of accumulated business loss and unabsorbed depreciation allowance in certain cases of amalgamation. Where there has been an amalgamation of a company owning an industrial undertaking or a ship or a hotel with another company, or an amalgamation of a banking company with a specified bank, then the accumulated losses or the unabsorbed depreciation of the amalgamating company shall be deemed to be the loss or the unabsorbed depreciation of the amalgamated company for the PY in which the transfer was effected. Consequently, the amalgamated company can carry forward such loss for 8 AY's immediately succeeding the relevant AY in which the amalgamation was effected.

**However, the above relaxations shall not be allowed if:**

- a) the amalgamated company is engaged in the business in which the accumulated loss or depreciation remains unabsorbed for  $\geq 3$  years
- b) the amalgamated company has held continuously as on date of the amalgamation  $\geq 3/4$ ths of the book value of fixed assets 2 years prior to the date of amalgamation
- c) the amalgamated company holds continuously for  $\geq 5$  years from the date of amalgamation,  $\geq 3/4$ ths of the book value of fixed assets of the amalgamating company so acquired
- d) the amalgamated company continues the business of the amalgamating company for  $\geq 5$  years from the date of amalgamation

If any of the above conditions are not complied with, then the set off of loss / depreciation, made in any PY, in the hands of the amalgamated company, shall be deemed to be the income of the amalgamated company chargeable to tax for the year of non-compliance.

### **Capital Gains**

Under Section 47(vi) and (vii) transfer does not include any transfer in a scheme of amalgamation of a capital asset by the amalgamating company to the amalgamated company if the latter is an Indian company. From the assessment year 1993-94, any transfer of shares in an Indian company held by a foreign company to another foreign company in pursuance of a scheme of amalgamation between the two foreign companies will not be regarded as a transfer for the purpose of levying tax on capital gains This provision will apply if  $\geq 25\%$  of the shareholders of the amalgamating company continue to remain shareholders of the amalgamated foreign company and such transfer does not attract tax in the country in which the amalgamating company is situated.

Further, the term “transfer” does not include any transfer by a shareholder in a scheme of amalgamation, of a capital asset, being shares held by him in the amalgamating company, if the transfer is made in consideration of

allotment to him, shares in the amalgamated company, and the amalgamated company is an Indian Company. Even, per se, amalgamation doesn't entail exchange or relinquishment of assets, and hence, capital gains tax is not attracted. The same was upheld in the case CIT vs. Rasik Lal Manek. However, the benefit doesn't continue if the shareholders of amalgamating company are allotted something more than the share in the amalgamated company, viz. bonds / debentures etc. as this was upheld in the case of CIT vs. Gautam Sarabhai Trust.

### Preliminary Expenses

The benefit of amortization of preliminary expenses under section 35D are ordinarily available –

- Only to the assessee who incurred the expenditure.
- However, the benefit will not be lost in case the undertaking of an Indian company which is entitled to the amortization is transferred to another Indian company in a scheme of amalgamation within the 10 years / 5-year period of amortization.
- In that event, the deduction in respect of previous year in which the amalgamation takes place and the following previous year within the 10 years / 5 years period will be allowed to the amalgamated company and not to the amalgamating company.

### Capital Expenditure on Scientific Research & Know-how

In case of an amalgamation, if the amalgamating company –

- transfers to the amalgamated company, which is an Indian company,
- any asset representing capital expenditure on scientific research,
- provision of section 35 would apply to the amalgamated company as they would have applied to amalgamating company if the latter had not transferred the asset. The same principle applies in essence for the expenditure on know-how.

### Expenditure on Amalgamation

Section 35DD provides that –

- where an assessee being an Indian company
- incurs any expenditure,
- wholly and exclusively for the purposes of amalgamation or demerger of an undertaking, the assessee shall be allowed
- a deduction of an amount equal to one-fifth of such expenditure for each of the five successive previous years beginning with the PY in which such amalgamation / demerger takes place.

## LESSON ROUND UP

- Article 366(6) of the Constitution defines corporate tax.
- As per section 2(17) of the Income Tax Act, Company means any Indian Company, or any body corporate incorporated by or under the laws of a country outside India, or any institution, association or body which is or was assessable or was assessed as a company for any assessment year under the Indian Income Tax Act, 1922 (11 of 1922) or was assessed under this Act, as a company for any assessment year commencing on or before April 1, 1970; or any institution, association or body, whether incorporated or not and whether Indian or non-Indian, which is declared by general or special order of the CBDT to be a company.

- Companies under the Income Tax Act are companies in which the public are substantially interested also referred to as widely-held companies and companies in which public are not substantially interested and also referred to as closely held company.
- Minimum Alternate Tax (“MAT”) on the book profit of a Company would not apply to a Foreign Company not having any physical presence in India.
- A domestic company is liable to pay tax on the amounts distributed, declared or paid as dividend (whether interim or otherwise), it shall be payable @ 15% plus surcharge @ 12% and health and education cess @ 4% in addition to the income tax payable.
- Section 115BBD provides for taxing foreign dividends received from a foreign company at the rate of 15% plus surcharge @7% and health and education cess @ 4%.

### SELF TEST QUESTIONS

*These are meant for recapitulation only. Answers to these questions are not to be submitted for evaluation.*

#### Multiple Choice Questions “MCQs”

1. Tax credit in respect of MAT paid as per section 115JB will be allowed only in the previous year in which the tax payable on the total income at the normal rate is –
  - (a) More than the tax payable under section 115JB
  - (b) Less than the tax payable under section 115JB
  - (c) Equal to the tax payable under section 115JB
  - (d) All of the above.

**Answer:** (a) More than the tax payable under section 115JB
2. Metro Ltd., a domestic company, is assessed with a total income of Rs. 11.25 crore. The surcharge payable by the company shall be at the rate of –
 

(a) 2%	(b) 5%
(c) 10%	(d) 12%.

**Answer:** (d) 12%
3. Dividend distribution tax under section 115-O shall be deposited within ..... days from the date of declaration/distribution/payment of dividend, whichever is earlier.
 

(a) 7 Days	(b) 10 Days
(c) 14 Days	(d) 20 Days.

**Answer:** (c) 14 Days
4. Provisions of Section 115JB are applicable in case of –
 

(a) Domestic companies only	(b) Foreign companies only
(c) All companies	(d) Closely held companies.

**Answer:** (c) All companies.
5. For computing the Book Profit under section 115 JB, which of the following is not added back to the profits?
  - (a) Income- Tax

- (b) Provision for Tax
- (c) Dividend Distribution Tax U/S 115-O
- (d) Securities Transaction Tax

**Answer:** (d) Securities Transaction Tax

6. Mr. Ganapathy a resident individual received Rs. 12 lakhs during the financial year 2019-20 by way of dividend from domestic companies. The companies have paid dividend distribution tax under Section 115-O on the dividend declared. The applicable rate of tax on such dividend income is:

- (a) 10.4%      (b) 31.2%
- (c) Nil          (d) 15.60%

**Answer:** (a) 10.4%

7. A domestic company whose turnover for the previous year 2017-18 Rs. 4.20 crores; for previous year 2018-19 Rs. 8 crore and for previous year 2019-20 Rs. 12 crores. Its total income (computed) for the assessment year 2020-21 is Rs. 3 crores. The rate of income tax applicable for such company (without cess) is:

- (a) 30%          (b) 40%
- (c) 29%          (d) 25%

**Answer:** (d) 25%

8. ABC Pvt. Ltd. has a business loss of Rs. 10 lakh. There is unexplained share application money to the tune of Rs. 25 lakh. The total income of the company will be :

- (a) Rs. 15 lakh      (b) Rs. 35 lakh
- (c) Rs. 25 lakh      (d) None of the above

**Answer:** (c)

9. Provisions of Minimum Alternate Tax (MAT) are applicable to the companies which are :

- (i) Indian companies
  - (ii) Foreign companies in certain situations
  - (iii) LLP
- (a) (i) and (iii)      (b) (i) and (ii)
  - (c) All the three      (d) None of the above

**Answer:** (b)

10. In order to be entitled to concessional rate of tax for dividend received from a foreign company, the Indian company should have the following minimum shareholding in such foreign company –

- (a) 10%          (b) 25%
- (c) 26%          (d) 51%.

**Answer:** (c) 26%

11. Dividend distribution tax under section 115-O is payable by –

- (a) Domestic companies only



# Lesson 9

## Procedural Compliance

### LESSON OUTLINE

- Permanent Account Number 'PAN'
- Tax Collection Account Number 'TAN'
- Payment of Tax
- Tax Deduction at Source 'TDS'
- Tax Collection at Source 'TCS'
- Time Limit for Depositing of TDS
- TDS Forms
- TDS Chart
- Minimum threshold upto which TDS not applicable
- Advance Tax
- Self-Assessment Tax 'SAT'
- Returns
- Signatures
- E-Filing
- Fee and interest
  - Interest for default in furnishing Return of Income [Section 234A]
  - Interest for default in payment of Advance Tax [Section 234B]
  - Interest for deferment of Advance Tax [Section 234C]
- Collection
- Recovery of Tax
- Refunds
- Case Law
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

The Income-tax Act provides for collection and recovery of income-tax in the following ways, namely, (i) deduction of tax at source in respect of income by way of salaries, interest on securities, interest other than interest on securities, winnings from lotteries and crossword puzzles, winnings from horse race, insurance commission, dividends, payment to contractors or subcontractors and payments to non-residents;

(ii) advance payment of income-tax before the assessment by the assessee himself;

(iii) direct payment of income-tax by the assessee on self-assessment; and

(iv) payment made after the assessment is made by the Assessing Officer.

Once the tax is deducted, it is duty to deposit the same to the credit of the Central Government under prescribed procedures stated under the Income Tax Act, 1961. In this chapter TDS related aspects of the Income Tax Act have been elaborately discussed with special emphasis on e-TDS and other relevant issues.

At the end of this lesson, you will learn;

- What is tax deducted at source and tax collected at source
- What are the rates of TDS and TCS
- The due dates for payment of TDS and TCS and Advance Tax
- The provisions related to Returns, Signature
- E-Filing
- Fee and Interest
- Collection and Recovery of Tax
- Refunds

***The Tax on income is collected in four ways- Tax Deduction at source (TDS), Advance Tax, direct payment of income-tax by the assessee on self-assessment basis and payment after the assessment is made by the Assessing Officer.***

## PERMANENT ACCOUNT NUMBER [SECTION 139A]

Every person, who has not been allotted any permanent account number, is obliged to obtain permanent account number, if;

- if his total income assessable during the previous year exceeds the maximum amount which is not chargeable to tax or
- any person carrying on business or profession whose total sales turnover or gross receipts are or is likely to exceed Rs. 5,00,000 in any previous year or
- is required to furnish a return of income under Section 139(4A) i.e. trust/charitable institutions.
- Every non-individual resident persons (entity) and persons associated with them shall apply for PAN if the financial transaction entered into by them during the financial year exceeds Rs. 2,50,000 Persons associated with such resident entity includes every managing director, director, partner, trustee, author, founder, karta, chief executive officer, principal officer or office bearer of such entity.

Besides above cases, the Assessing Officer may also allot a permanent account number to any other person by whom tax is payable. Any other person may also apply for a permanent account number. However, Section 139 has been amended w.e.f. August 1, 1998 and provides the alternative of quoting GIR (General Index Register) number till such time the permanent account number is allotted.

Permanent Account Number (PAN) is a ten-digit alphanumeric number, issued in the form of a laminated card, by the Income Tax Department. The structure of the ten characters of PAN is as under :

- a. The first three characters represent the alphabetic series running from AAA to ZZZ.
- b. The fourth character of PAN represents the status of the PAN holder i.e. "P" stands for Individual; "C" stands for Company; "H" stands for Hindu Undivided Family (HUF); "A" stands for Association of Persons (AOP); "B" stands for Body of Individuals (BOI); "G" stands for Government Agency ;"J" stands for Artificial Juridical Person; "L" stands for Local Authority; "F" stands for Firm/ Limited Liability Partnership and "T" stands for Trust.
- c. Fifth character of PAN represents the first character of the PAN holder's last name/surname in case of an individual. In case of non-individual PAN holders fifth character represents the first character of PAN holder's name.
- d. Next four characters are sequential numbers running from 0001 to 9999.
- e. Last character, i.e., the tenth character is an alphabetic check digit.

PAN enables the department to link all transactions of the "person" with the department. These transactions include tax payments, TDS/TCS credits, returns of income, specified transactions, correspondence, and so on. PAN, thus, acts as an identifier for the "person" with the tax department.

PAN was introduced to facilitates linking of various documents, including payment of taxes, assessment, tax demand, tax arrears etc. relating to an assessee, to facilitate easy retrieval of information and to facilitate matching of information relating to investment, raising of loans and other business activities of taxpayers collected through various sources, both internal as well as external, for detecting and combating tax evasion and widening of tax base.

### Inter-changeability of PAN & Aadhaar and mandatory quoting in prescribed transactions.

To ensure ease of compliance, it is provided for inter-changeability of PAN with the Aadhaar number. Accordingly the provisions of section 139A is amended so as to provide that,-

- i. every person who is required to furnish or intimate or quote his PAN under the Act, and who, has not

been allotted a PAN but possesses the Aadhaar number, may furnish or intimate or quote his Aadhaar number in lieu of PAN, and such person shall be allotted a PAN in the prescribed manner;

- ii. every person who has been allotted a PAN, and who has linked his Aadhaar number under section 139AA, may furnish or intimate or quote his Aadhaar number in lieu of a PAN.

### Process to apply for PAN

Income Tax Department has authorised UTI Infrastructure Technology and Services Limited (UTIITSL) and National Securities Depository Limited (NSDL) to set-up and manage PAN Service Centers. UTIITSL and NSDL have established PAN Service Centers and TIN Facilitation Centers at various places in major cities of India (hereinafter referred to as PAN application centers of UTIITSL/NSDL).

Thus, a person wishing to obtain PAN can apply for PAN by submitting the PAN application form (Form 49A/49AA) along with the related documents and prescribed fees at the PAN application center of UTIITSL or NSDL. An online application can also be made from the website of UTIITSL or NSDL.

### Quoting of PAN

It shall be the duty of every person who has been allotted permanent account number to quote such number in all his returns or correspondence with Income tax authorities, quote such numbers in all challans for the payment of any sum, quote such number in all documents pertaining to such transactions as may be prescribed by the Board in the interest of revenue.

Now quoting PAN is compulsory in the following transactions :

- (a) Sale/purchase of any immovable property valued at Rs. 10 lakhs or more, valued by the stamp valuation authority under section 50C at an amount exceeding Rs. 10 lakhs.
- (b) Sale/Purchase of Motor vehicle or a vehicle (excluding two wheeled vehicle, inclusive of any detachable side-car having an extra wheel) which requires registration under Motor Vehicles Act, 1988.
- (c) Time deposit exceeding Rs. 50,000 with a Bank/Banking Company/Banking Institution.
- (d) Deposit exceeding Rs. 50,000 in Post Office Savings Bank.
- (e) Contract for sale/purchase of securities exceeding Rs. 1 lakh.
- (f) Opening an account [not being time deposit mentioned in (c)] with a Bank/Banking Company/Banking Institution.
- (g) Application for installation of a telephone connection including mobile phone.
- (h) Payments to hotels of bills exceeding Rs. 50,000 at any one time.
- (i) Payment in cash for purchase of bank drafts or pay orders or banker's cheque for an amount of Rs. 50,000 or more during any one day.
- (j) Deposit in cash aggregating Rs. 50,000 during any one day.
- (k) Payment in cash in connection with travel to any foreign country of an amount exceeding Rs. 50,000 at any one time.
- (l) Making an application to any banking company or to any other company or institution for issue of a credit or debit card.
- (m) Payment of an amount of Rs. 50,000 or more to a Mutual Fund for purchase of its units.
- (n) Payment of Rs. 50,000 or more to a company for acquiring shares or debentures or bonds issued by it.
- (o) Payment of Rs. 50,000 or more to RBI for acquiring bonds issued by it.

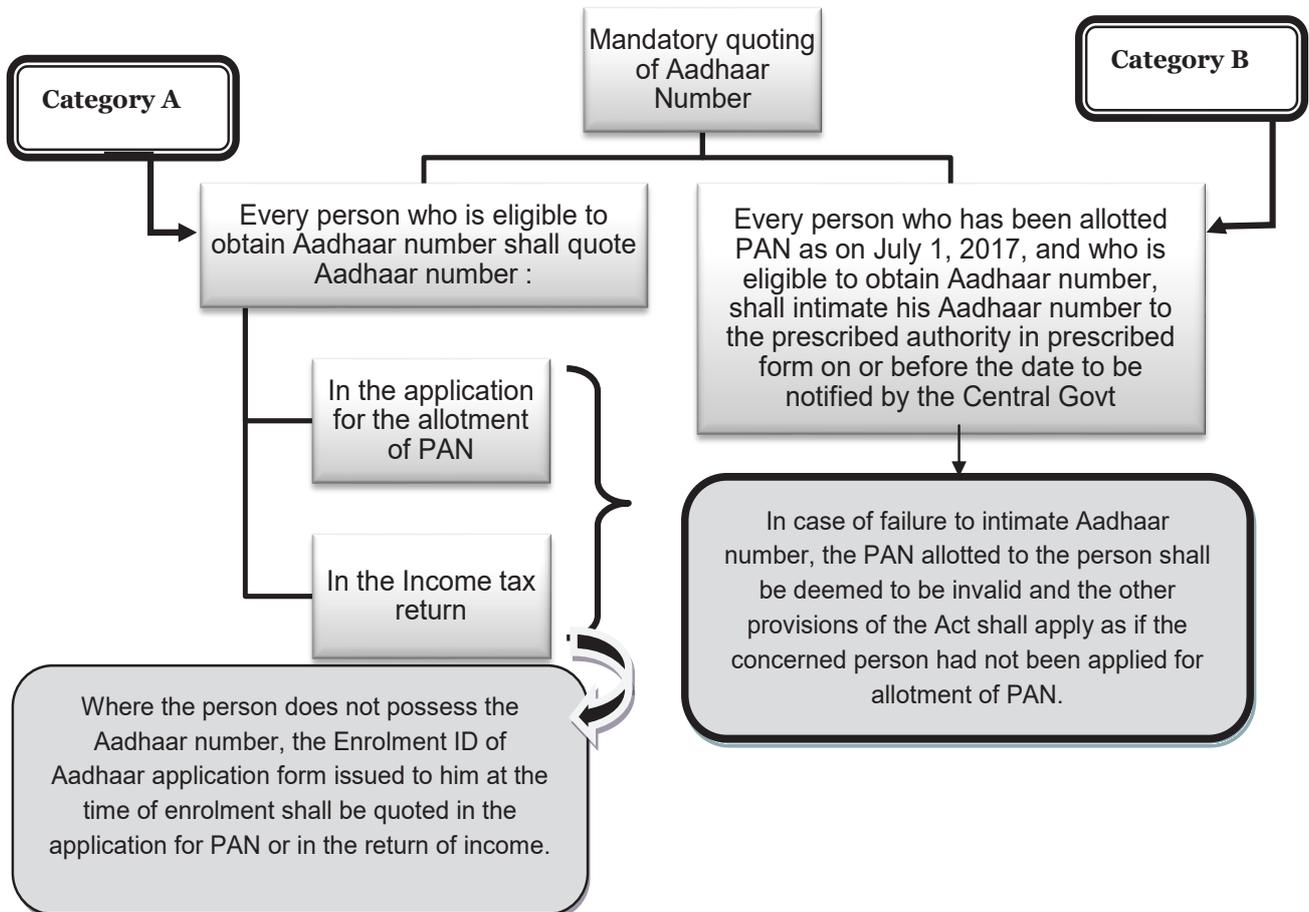
- (p) Payment of an amount of Rs. 50,000 or more as life insurance premium to an insurer.
- (q) Payment to a dealer
  - (i) of an amount of Rs. 5 lakh or more at any one time, or
  - (ii) against a bill for an amount of Rs. 5 lakh or more for purchase of bullion or jewellery.
- (r) Payment as life insurance premium to an insurer of Rs. 50,000 or more.
- (s) Sale or purchase, by any person of goods or services of any nature other than those specified above - Amount exceeding two lakh rupees, per transaction.

Every person, receiving any document relating to the prescribed transactions, shall ensure that the permanent account number has been duly quoted in the document. The Board has been empowered to make rules in relation to the form and the manner in which the application for the allotment of a permanent account number and the particulars which such application will contain, prescribing the categories of transactions and the categories of documents pertaining to business or profession in which the permanent account numbers shall have to be quoted by every person.

The expression "Assessing Officer" has been defined to include an income tax authority to whom the job of allotting permanent account numbers has been assigned.

**Quoting of AADHAAR NUMBER [Section 139AA]**

Provisions of this section applicable from April 1, 2017 are as under :



**Note :** *The provisions of this section are not applicable to such person or class or classes of persons or state or part of state, as may be notified by the Central Govt.*

Persons who are not required to quote Aadhar Number or Enrolment ID in application form for allotment of PAN and in return of income [Notification No. 37/2017 dated 11.05.2017]

The Central Government has, vide this notification effective from 01.07.2017, notified that the provisions of section 139AA relating to quoting of Aadhar Number would not apply to an individual who does not possess the Aadhar number or Enrolment ID and is:

- (i) residing in the States of Assam, Jammu & Kashmir and Meghalaya;
- (ii) a non-resident as per Income-tax Act, 1961;
- (iii) of the age of 80 years or more at any time during the previous year;
- (iv) not a citizen of India.

CBDT has further extended the time for linking PAN with Aadhar till 31st March, 2020.

### Power Delegated to Central Government

The Central Government may, by notification in the Official Gazette, specify, any class or classes of persons by whom tax is payable under this Act or any tax or duty is payable under any other law for the time being in force including importers and exporters whether any tax is payable by them or not and such persons shall, within such time as mentioned in that notification, apply to the Assessing Officer for the allotment of a permanent account number.

### Penalty for not complying with provisions relating to PAN or Adhaar

Penalty of Rs.10,000/- is imposable u/s 272B for failure to comply with the provisions of section 139A i.e failure to obtain, quote, or authenticate PAN or holding of more than one PAN. Precisely as under:

- a. If assessee fails to quote or intimate his PAN or Aadhaar or quotes or intimates invalid PAN or Aadhaar.
- b. If assessee fails to quote or authenticate his PAN or Aadhaar in specified transactions.
- c. If receiver (i.e., banks, financial institution, etc.) of documents in respect of specified transactions fails to ensure that the PAN or Aadhaar are duly quoted and authenticated..

### TAX DEDUCTION ACCOUNT NUMBER (TAN)

TAN Number is a 10 Digit Alphanumeric Number and is used as an abbreviation for Tax Deduction and Collection Account Number. Every Assessee liable to deduct TDS is required to apply for a TAN No. and shall quote this number in all TDS Returns, TDS Payments and any other communication regarding TDS with the Income Tax Department.

As per Section 203A of the Income Tax Act 1961, it is mandatory for all asseesee's liable to deduct TDS to quote this TAN Number in all communications regarding TDS with the Income Tax Department and failure to do so attracts a penalty.

### Steps for making TAN application

TAN Number can be applied for online as well as offline. For making a TAN Application online, a person shall file his application in Form No. 49B on the following website of NSDL

#### Step – I

Visit <https://tin.tin.nsdl.com/tan/index.html> and select “Online Application for TAN (Form 49B)”

**Step – II**

Select Category of Deductors from the drop down menu and click on “Select Button”;

**Step – III**

Fill out the requisite details on the form

**Step – IV**

If the data submitted by applicant fails in any format level validation, a response indicating the error(s) will be displayed on the screen;

**Step – V**

Forms need to be re-submitted after rectifying the error(s);

**Step - V**

In case form level error(s) do not exists a confirmation screen with data filled by the applicant will be displayed.

**Step – VI**

In case applicant required any amendment to the data displayed in the confirmation screen, it may choose the edit option.

**Step – VII**

In case the displayed information is correct, applicant shall choose the confirm option.

**Step – VIII**

On successful payment of Fees (in case the mode of payment is other than DD or Cheque) an acknowledgment slip will be generated

**Step – IX**

Applicant shall save and print the acknowledgment and send it to NSDL alongwith requisite documents at

NSDL e-Governance Infrastructure Limited,  
5th floor, Mantri Sterling,  
Plot No. 341, Survey No. 997/8,  
Model Colony,  
Near Deep Bungalow Chowk,  
Pune – 411016

The envelope should be superscribed as ‘APPLICATION FOR TAN - Acknowledgment Number’ (e.g. ‘APPLICATION TAN - 88301020000244’).

## **PAYMENT OF TAX**

There are two modes of payment of direct taxes (i) physical mode i.e. payment by furnishing the hard copy of the challan at the designated bank; and (ii) e-payment mode i.e. making payment by using the electronic mode.

It is compulsory for the following taxpayers to pay tax using the e-payment mode only (i.e., using internet banking facility). In other words, following persons cannot use the physical mode of payment of tax and have to pay the tax electronically using the epayment facility:

- a. All companies
- b. All taxpayers other than company who are liable to get their accounts audited as per section 44AB.

## TAX DEDUCTED AT SOURCE (TDS)

Income Tax Act provides for scope of the total income of a person chargeable to tax on an annual basis. The tax liability is determined as per the provisions of the Income-tax Act and such tax liability is discharged vide any of the following mode :



**A brief discussion about the various ways by which income tax is collected by the Government is given below : -**

**Tax Deducted at Source (TDS)** is a one of the mode or mechanism of collecting income tax under the Indian Income Tax Act of 1961 i.e. 'the Act'. As per the provision of section 191 of the Act, notwithstanding the regular assessment in respect of any income take place in a subsequent year called as assessment year, but in case of certain specified income, tax is deducted at source by the payer at the prescribed rate at the time of accrual or payment of such incomes to the payee. The tax so deducted is required to be deposited with the government within the specified time limit.

The concept of TDS was introduced with an aim to collect tax from the very source of income as per which, a person (deductor) who is liable to make payment of specified nature to any other person (deductee) shall deduct tax at source and remit the same into the account of the Central Government. The deductee from whose income, tax has been deducted at source would be entitled to get credit of the amount so deducted on the basis of Form 26AS or TDS certificate issued by the deductor.

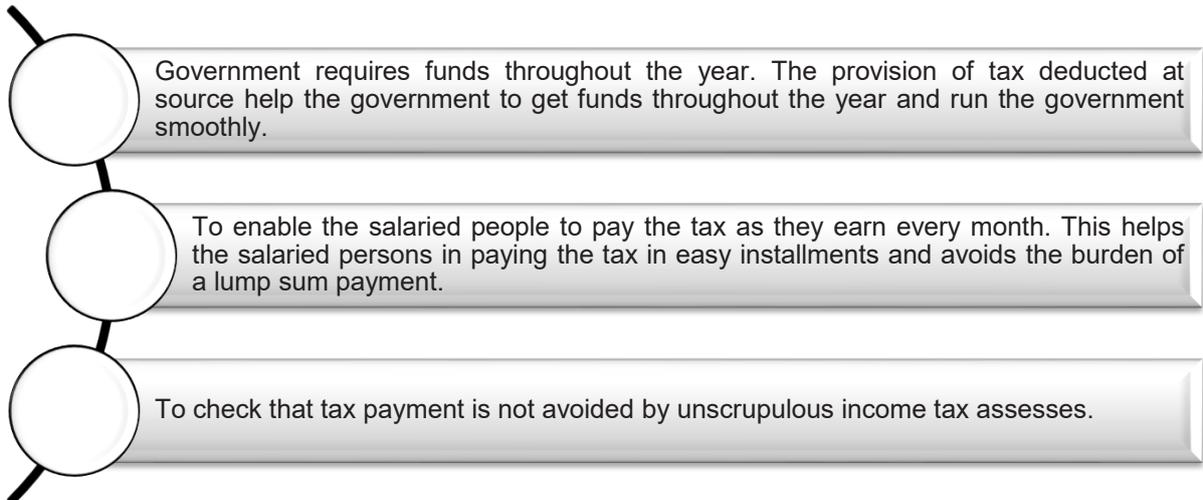
Tax deducted at source (TDS) is an indirect mechanism of collecting tax which combines twin concepts of "pay as you earn" and "collect as it is being earned." Its value lies in the fact that it provides the Government with a continuous flow of funds and at the same time eases the burden on the taxpayer.

It is managed by the Central Board for Direct Taxes (CBDT) and is part of the Department of Revenue managed by Indian Revenue Service (IRS).

### Objectives of Tax Deducted at Source

There are various objective of introducing the TDS provision under the Act. One is also to make sure that tax payment is not avoided by unscrupulous income tax assesses and the government receives its actual share of taxes. Therefore, to achieve this goal, the responsibility of deduction and deposition of part of the taxes was put on the payer rather than the receiver of payments of different nature.

The basic objective of introducing tax deducted at source provision under the Act are as follows :



### Scheme of Tax Deduction at Source

The obligation to deduct/collect tax at source is upon the person responsible for paying the income/amount which is subject to TDS. Therefore such person i.e. the payer is required to follow the procedure for deducting/collecting tax at source mentioned as under :

#### Step – 1

The payer has to apply for tax deduction account number (TAN) in Form No-49B.

#### Step – 2

He is to deduct tax from the income/payment mentioned in the various sections i.e. Section 192 to 196D.

#### Step – 3

The amount so deducted/collected should be deposited within the requisite stipulated time to the credit of central government.

#### Step – 4

The payer should prepare TDS Return statements for every quarter and file the same with the authority designated by the Income-Tax department (NSDL in this case) in such form and verified in such manner as may be prescribed.

#### Step – 5

Lastly, the payee should be issued certificate of tax deduction/collected at source within the specified date. The TDS certificate to be downloaded from tax portal.

**Sections 192 to 206 of the Income-tax Act lay down the provisions relating to deduction of tax at source. The provisions in respect of different incomes are as follows :**

**Clarification regarding TDS on Goods and Services Tax (GST) component comprised in payments made to residents [Circular No. 23/2017 dated 19.07.2017]**

With the new system for taxation of services under the GST regime w.e.f. 01.07.2017, the CBDT has clarified that wherever in terms of the agreement or contract between the payer and the payee, the component of 'GST on services' comprised in the amount payable to a resident is indicated separately, tax shall be deducted at source on the amount paid or payable without including such 'GST on services' component.

GST shall include Integrated Goods and Services Tax, Central Goods and Services Tax, State Goods and Services Tax and Union Territory Goods and Services Tax.

## Salary [Section 192]

An employer paying any income chargeable under head 'salary' is responsible for deducting TDS on an average rate of income tax based on the prevailing rate during the particular Financial Year by considering the estimated Income of assessee. Accordingly all employers making such payments like Individual, HUF, Partnership Firms, Companies, Co-operative societies, trust, and artificial judicial persons are liable to deduct TDS.

The following are the pre-requisites for TDS deduction u/s 192

1

There exist an employer – employee relationship between deductor and deductee and the payment is in the nature of salary

2

Any person responsible for making payment to resident / non-resident employees

3

Payment is made by the employer to the employee

4

The income under the head salaries is above the maximum amount not chargeable to tax

The deduction should be made at the time of making payment and not on when it becomes due or obligation arises. The employer is required to deduct tax at source on the amount payable by applying the average rate of income tax. Average rate of Income tax is calculated on the basis of rates in force for the particular financial Year in which payment is made. The rate varies for persons under various slab rate, may vary in different financial year and depends on total Income earnings and available deductions per year.

**Rate of deduction of tax :** As per Section 192, the employer is required to deduct tax at source on the amount payable at the average rate of income tax. This has to be computed on the basis of rates in force for the financial Year in which payment is made. Tax on salary is to be deducted after including surcharge if applicable and health & education cess.

**TDS on simultaneous employment with more than one employer or on change of employment :** In cases wherein, during the financial year, an assessee is employed simultaneously under more than one employer, or where he has held successively employment under more than one employer, he may furnish to the person responsible for making the payment (being one of the said employers as the assessee may, having regard to the circumstances of his case, choose), details of the income under the head "Salaries" due or received by him from the other employer or employers, the tax deducted at source therefrom and thereupon the person responsible for making the payment referred to above shall take into account the details so furnished for the purposes of making the deduction.

The person responsible for making the payment chargeable under the head salary shall, for the purposes of estimating income of the assessee or computing tax deductible, obtain from the assessee the evidence or proof or particulars of prescribed claims (including claim for set-off of loss) under the provisions of the Act in such form and manner as prescribed in this regard.

**Payment of tax by employer on non-monetary perquisite :** Sections 192 (1A) and 192 (1B) of the Income Tax Act, enable the employer at his option, to make payment of the entire tax or a part of the tax due on non-monetary perquisites given to the employee. The tax payable is to be determined at the average rate of the income tax computed on the basis of rates in force and the payment will have to be made when such tax was otherwise deductible, i.e. at the time of payment of income chargeable under the head salaries, to the employee. Further, the tax so paid shall be deemed to be the TDS made from the salary of the employee. However, as per proviso to section 198, tax so paid will not be deemed to be income of the employee

**TDS where the salary paid is net of tax** : Where the employee enters into an agreement or an arrangement as per which the tax chargeable on the income is borne by the employer then for the purpose of deduction of tax, the income is to be increased to such an amount as would, after deduction of tax thereon be equal to the net amount payable as per the agreement or arrangement (Section 195A). However, this provision is not applicable where the employer has made payment of tax on non-monetary perquisites as provided in section 192(1A).

**Salary paid in Foreign Currency [Rule 26 & 115]** : For the purpose of deduction of tax at source on any income payable in foreign currency, the rate of exchange for the calculation of the value in rupees of such income payable to an assessee outside India shall be the telegraphic transfer buying rate of such currency as on the date on which the tax is required to be deducted at source under the provisions of Chapter XVIIIB by the person responsible for paying such income.

It may be noted that this rule is applicable only for determination of TDS. However, in computing the salary income, the rate of conversion to be applied is the telegraphic transfer buying rate on the last day of month immediately preceding the month in which the salary is due or is paid in advance or arrears (Rule 115).

“Telegraphic transfer buying rate (TTBR)”, means the rate or rates of exchange adopted by the State Bank of India.

**Issue of Form 16 & Form 12 BA** : The TDS deducted to be deposited to Government and a FORM 16 should be issued to employees. The employees claim the TDS amount while submitting tax return against the total tax payable. The cut-off date for issuing Form 16 is 31 May of the Next Financial year in which tax is deducted.

Apart from issue of form 16 Form, Form 12BA is also issued that contains details of perquisites & Profit lieu of salary chargeable under section 17(3) of the Act.

With effect from 1 June 2016, as per Rule 26C, an employee shall furnish to employer evidence or particulars of the claims made in Form No.12BB for purpose of estimation of his income and TDS

### **Premature Withdrawal from Employees' Provident Fund Scheme (EPFS) [Section 192A]**

Withdrawal of the accumulated balance lying in a Recognised Provident Fund (RPF) account, is exempt from tax if the employee renders continuous service with the employer for a period of five years or more. In case of cessation of employment, if the employee takes up an employment with another employer and the accumulated balance in her/his RPF account is transferred to her/his RPF account maintained by such other employer, then also the exemption is available.

In case the above mentioned conditions are not satisfied, the accumulated balance due to the employee is taxable in the hands of the employee. In such a case, tax is required to be calculated by re-computing the tax liability of the years for which the contribution to RPF has been made, by treating the same as contribution to unrecognised provident fund.

The trustees of an RPF are required to deduct tax at source on such accumulated balance at the time it is paid, as if such withdrawn amount were income chargeable under the head Salaries. However, often, the trustees did not have the requisite information to be in a position to compute the TDS correctly. With a view to simplify the process of deduction in such cases, Section 192A provides that trustees of RPFs shall, at the time of payment of the accumulated balance due to the employee, deduct tax at source at the rate of 10%, where the aggregate withdrawal is Rs. 50,000/- or more.

At the same time, if the concerned employee fails to furnish her/his permanent account number (PAN) to the person responsible for deducting such tax, then tax shall be deducted at the rate of 20% as per Section 206AA. It has also been provided that tax shall not be deducted if the employee furnishes to the payer a self-declaration in the prescribed Form No. 15G/15H, declaring that the tax on her/his estimated total income of the relevant previous year would be nil.

### Interest on Securities [Section 193]

The person responsible for paying to a resident any income by way of interest on securities shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier deduct income-tax at the rates in force on the amount of the interest payable.

Credit of any income by way of interest on securities to any account, whether called "Interest payable account" or "Suspense account" or by any other name in the books of account of the person liable to pay such income, is, for the purposes of Section 193, deemed to be credit of such income to the payee and attracts applicability of the provisions of Section 193.

However, tax shall not be deducted from the interest on the following securities :

- (i) Debentures issued by Co-operative Society (including Co-operative Land Mortgage Banks or Co-operative Land Development Banks) or any other institution or authority as the Central Government may specify in the Official Gazette.
- (ii) Gold bonds provided the assessee is a resident individual and the nominal value of the bonds did not exceed Rs. 10,000 at any time during the period to which the interest relates Gold Deposit Bond 1999 dematerialised Bonds.
- (iii) Securities of the Central Government or State Government.
- (iv) Interest paid or payable to an individual, HUF through account payee cheque upto Rs. 5,000 on debentures listed/unlisted interest on dematerialised securities.

TDS can be made at the time of payment or at the time of credit to the account of the payee or transfer to interest payable amount or suspense account, whichever comes earlier. The identity of the person in whose hand it is includible have to be identified. Case law : [IDBI v. ITO (2006) 10 SOT 497/104 TTD 230 (Mum.)].

#### Rate of TDS :

The rate of TDS on Interest on securities is 10%. No health and education cess shall be added to the rate. The rate of TDS shall be 20% if PAN is not quoted by the payee.

### Interest other than Interest on Securities [Section 194A]

Any person not being an individual or a H.U.F. who is responsible for paying to a resident any income by way of interest other than income by way of interest on securities amounting to more than rupees 5,000 or Rs. 40,000 or Rs. 50,000 in case of senior citizen w.e.f. 01.04.2018 as the case may be, shall, at the time of crediting to the payee or at the time of payment or the interest, deduct tax at the prescribed rates.

#### Rate of Tax :

- (i) 10%, No surcharge, or HEC shall be added.
- (ii) When the payee does not furnish his PAN to deductor, tax will be deducted @ 20%.

However, the tax shall not be deducted in the following cases :

- (i) Where the payee is a banking Company, a co-operative society engaged in carrying on the business of banking or any deposit with post office under any scheme framed by the Central Government and notified by it in this behalf, and the aggregate amount of interest credited or paid during the financial year does not exceed Rs. 40,000 or Rs. 50,000 in case of senior citizen.
- (ii) Where the payee is other than the (i) above and the aggregate amount of interest paid or credited does not exceed Rs. 5,000.

The aforesaid limits were computed with reference to the income credited or paid by a branch of the banking company or the cooperative society, as the case may be. Many bank depositors avoided TDS from interest on bank fixed deposits by splitting their deposits amongst different branches of the same bank. With a view to curbing this practice, proviso to Section 194A(3) provides that TDS under Section 194A will be with reference to income credited or paid by the banks as a whole (in those cases where core banking solutions have been adopted by the concerned bank).

- (iii) Where the interest credited or paid to a banking company, a co-operative society doing banking business, Financial Corporation established by a Central or State Act, the Life Insurance Corporation of India, the Unit Trust of India, any company or co-operative society carrying on the insurance business and any other institution which the Central Government may notify in this behalf.
- (iv) Interest credited or paid by a firm to its partners.
- (v) Interest credited or paid by a co-operative society paid by a co-operative society (other than a co-operative bank) to a member thereof or to such income credited or paid by a co-operative society or to any other co-operative society.
- (vi) Where interest credited or paid in respect of deposits under any scheme framed by Central Government.
- (vii) Interest credited or paid in respect of deposits other than time deposits with a banking company to which the Banking Regulation Act, 1949 applies.
- (viii) Income credited or paid in respect of deposits with a primary agricultural credit society or cooperative society engaged in carrying on the business of banking including a cooperative land mortgage bank or a cooperative land development bank.
- (ix) Income credited or paid by the Central Government under Income Tax Act, 1961 or Indian Income Tax Act, 1922 or the Estate Duty Act, 1953 or the Companies (Profits) Surtax Tax Act, 1964.
- (x) Income which is paid or payable by an infrastructure capital company or infrastructure capital fund or a public sector company in relation to a zero coupon bond issued by such company or fund or public sector company.
- (xi) to such income credited or paid by way of interest on the compensation amount awarded by the Motor Accidents Claims Tribunal ;
- (xia) to such income paid by way of interest on the compensation amount awarded by the Motor Accidents Claims Tribunal where the amount of such income or, as the case may be, the aggregate of the amounts of such income paid during the financial year does not exceed fifty thousand rupees;
- (xii) to any income by way of interest referred to in clause (23FC) of section 10.

The definition of the term time deposits under Explanation 1 to Section 194A (3) includes recurring deposits within its scope. As a result, now for all banks, whether cooperative or commercial, interest paid on both time deposits and recurring deposits would attract the TDS provisions.

The responsible person may, at the time of making any deduction increase or reduce the amount to be deducted for the purpose of adjusting any excess or deficiency arising out of any previous deductions or failure to deduct during the financial year.

Note : 1. Individuals and HUF covered under Section 44AB(a) and (b) i.e. whose gross turnover of the business in the immediately preceding financial year exceeds Rs. 1 crore (or receipts from the profession Rs. 50 Lakhs are also required to deduct tax at source.

2. Cheque discounted charges are different from interest payments and provisions of Section 194A are not attracted. *ITO v. A.S. Babu Sah (2003) 86 ITD 283 (Mad.)*

**Winnings from Lotteries or Crossword Puzzles [Section 194B]**

The person responsible for paying to any person any income by way of winnings from lotteries or crossword puzzles or card game and other game of any sort, an amount exceeding Rs. 10,000 shall deduct tax at the prescribed rates at the time of such payment and a statement in Form No. 26 has to be filed by the end of the month of June falling in the financial year immediately following the previous year.

**Rate of Tax :**

The prescribed rate is 30%. No surcharge, cess shall be added.

**Important Points**

- (i) When the prize is given partly in cash and partly in kind, income-tax will be deducted from cash prize with reference to the aggregate amount of the cash prize and the value of the prize in kind.
- (ii) Tax shall be deducted from value of the prize money given only in kind.
- (iii) When the prize is given in installments, the tax will be deducted only at the time of actual payment of each installment.
- (iv) Income-tax is deductible from the income by way of bonus or commission paid to lottery agent or sellers of lottery tickets on the sales made by them under Section 194H.

Prizes won by lottery agent under “Lucky dip draws” are lotteries for the purposes of deduction of tax at source.

**Winnings from Horse Races [Section 194BB]**

Income-tax has to be deducted at source from any income by way of winnings from horse races at rate of 30%. Deduction of tax at source will be made only in cases where the income by way of winnings from horse races to be paid to a person exceeds Rs. 10,000. The obligation to deduct tax at source will apply only where such winnings are paid by a book maker or a person to whom a licence has been granted by the Government under any law for the time being in force for horse racing in any race course or for arranging for wagering or betting in any race course.

**Rate of Tax :**

The prescribed rate is 30%. No surcharge, cess shall be added.

**Payment to Resident Contractor or Sub-contractor [Section 194C]**

Any person responsible for paying to any of the contractor for carrying out any work (including supply of labour for carrying out any work) in pursuance of a contract shall, at the time of credit of such sum to the account of the contractor or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier deduct income-tax thereon.

**Rate of Tax :**

- (i) 1% where the payment is being made or credit is being given to an individual or a Hindu undivided family;
- (ii) 2% where the payment is being made or credit is being given to a person other than an individual or a Hindu undivided family, of such sum as income-tax on income comprised therein.
  - No surcharge, cess shall be added from 1st October, 2009.
  - When the payee does not furnish his PAN to deductor, tax will be deducted @ 20%.

#### 470 EP-TL

- No individual or Hindu undivided family shall be liable to deduct income-tax on the sum credited or paid to the contractor where such sum is credited or paid exclusively for personal purposes of such individual or any member of Hindu undivided family.
- No deduction shall be made from the amount of any sum credited or paid to, the contractor, if such sum does not exceed Rs. 30,000

Provided that where the aggregate of the amounts credited or paid during the financial year exceeds Rs. 1,00,000 the person responsible for paying shall be liable to deduct income-tax.

Further, no deduction shall be made from any sum credited or paid or likely to be credited or paid during the previous year to the account of a contractor during the course of business of plying, hiring or leasing goods carriages, where such contractor owns ten or less than ten goods carriages at any time during the previous year and furnishes a declaration to that effect along with his Permanent Account Number, to the person paying or crediting such sum.

**Explanation.** - For the purposes of this section, -

- (i) Any person, being an individual or a Hindu undivided family or an association of persons or a body of individuals, if such person, -
  - (A) is not covered above and
  - (B) is liable to audit of accounts under clause (a) or clause (b) of section 44AB during the financial year immediately preceding the financial year in which such sum is credited or paid to the account of the contractor; shall be liable to deduct income tax from such sum paid or credited.
- (ii) "contract" shall include sub-contract;
- (iii) "work" shall include -
  - (a) advertising;
  - (b) broadcasting and telecasting including production of programmes for such broadcasting or telecasting;
  - (c) carriage of goods or passengers by any mode of transport other than by railways;
  - (d) catering;
  - (e) manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from such customer, but does not include manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from a person, other than such customer.

#### **Insurance Commission [Section 194D]**

Any person responsible for paying to a resident any income by way of commission or otherwise for soliciting or procuring insurance business (including continuance or renewal of policies) shall, at the time of crediting the account of the payee or at the time of payment thereof, whichever is earlier deduct income-tax thereon. No deduction shall be made from the amount of any sum credited or paid to, if such sum does not exceed Rs.15,000.

#### **Rate of Tax :**

The prescribed rate is 5% for individual and HUF and 20% for corporate assessee. No surcharge, cess shall be added from 1st October 2009. When the payee does not furnish his PAN to deductor, tax will be deducted with effect from 1st April 2010 @ 20%.

The benefit of self declaration under this section has been extended to section 194D (w.e.f. June 1, 2017). No tax will be deducted under 194D if the recipient of insurance commission submits Form No. 15G/15H to the Payer.

### **Payment in respect of Life Insurance policy [Section 194DA]**

Any person responsible for paying to a resident any sum under a life insurance policy, including the sum allocated by way of bonus on such policy, other than the amount not includible in the total income under clause (10D) of section 10, shall at the time of payment thereof, deduct income-tax on income component of the sum paid by the person.

#### **Rate of Tax :**

The prescribed rate of tax to be deducted at source is 1%. Provided that no deduction shall be made where the aggregate amount of such payment made to the payee in a financial year is less than 1 lakh.

Section 197A provides that tax shall not be deducted under Section 194DA if the recipient of the payment on which tax is deductible furnishes to the payer a self-declaration in the prescribed Form No. 15G/15H declaring that the tax on his estimated total income for the relevant previous year would be nil.

### **Payment in respect of Deposits under National Savings Scheme etc. [Section 194EE]**

The person responsible for paying to any person any amount referred to in Section 80CCA(2)(a) shall, at the time of payment thereof, deduct income-tax at the rate of 10%. No deduction shall, however, be made under Section 194EE where the amount of such payment or the aggregate of such payment to the payee during the financial year is less than Rs. 2,500. Further, nothing contained in Section 194EE shall apply to the payment of the said amount to the heirs of the assessee.

#### **Rate of Tax :**

The prescribed rate is 10%. No surcharge, cess shall be added. When the payee does not furnish his PAN to deductor, tax will be deducted @ 20%.

### **Commission on sale of lottery tickets [Section 194G]**

Any person paying any income by way of commission, remuneration or prize (by whatever name called) on lottery tickets on amounts exceeding Rs. 15,000 shall deduct income-tax at the rate of 5%. No surcharge, cess shall be added. When the payee does not furnish his PAN to deductor, tax will be deducted @ 20%.irrespective of the fact whether the payment is made in cash or by the issue of a cheque or draft or by any other mode. The provisions of Section 194G have been extended to any account, whether called 'suspense account' or by any other name in the books of account of the person liable to pay.

### **Commission or Brokerage [Section 194H]**

Any person, not being an individual or a Hindu Undivided Family, who is responsible for paying, or after 1st day of June, 2001, to a resident any income by way of commission (not being insurance commission referred to in Section 194D) or brokerage, shall, at the time of credit of such income to the account of the payee or at the time of payment of such income in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rate of 5%. No surcharge, cess shall be added. When the payee does not furnish his PAN to deductor, tax will be deducted @ 20%.

Provided that no deductions shall be made under this section in a case where the amount of such income or, as the case may be, the aggregate of the amounts of such income credited or paid or likely to be credited or paid during the financial year to the account of, or to, the payee, does not exceed Rs. 15,000.

Individuals and HUF covered under Section 44AB(a) and (b) i.e. whose gross turnover of the business in the immediately preceding financial year exceeds Rs. 1 crore [or receipts from the profession Rs. 50,00,000] are also required to deduct tax at source.

### Rent [Section 194-I]

Any person other than an individual or a HUF who is responsible for paying to a resident any income by way of rent is required to deduct tax from rent if such rent is in excess of Rs. 2,40,000 for each co-owner per financial year. Tax is to be deducted @ 2% for use of any machinery or plant or equipment; and @ 10% for the use of any land or building (including factory building) or furniture or fittings. No surcharge, cess shall be added. When the payee does not furnish his PAN to deductor, tax will be deducted @ 20%.

**Explanation :** For the purpose of this section :

- (i) "rent" means any payment, by whatever name called, under any lease, sub-lease, tenancy or any other agreement or arrangement for the use of any land or any building (including factory building), together with furniture, fittings and the land appurtenant thereto, whether or not such building is owned by the payee.
- (ii) where any income is credited to any account, whether called "suspense account" or by other name, in the books of account of the person liable to pay such income, such crediting shall be deemed to be credit of such income to the account of the payee and the provisions of this section shall apply accordingly.

Individuals and HUF covered under Section 44AB(a) and (b) i.e. whose gross turnover of the business in the immediately preceding financial year exceeds Rs.1 crore (or receipts from the profession Rs. 50,00,000), are also required to deduct tax at source.

Payment made to C&F agent are regarded as payment made for carrying out work under Section 194C instead of treating it as rent - *National Panasonic India (P) Ltd. v. CIT (TDS) (2005) 35 OT 16 Del.*

Payment for advertisement for boarding site is dealt under Section 194C. - *ITO v. Roshan Publcity (P.) Ltd. (2005) 45 OT 105 Mum.*

Landing and Parking Fee received by Airport Authorities is treated as rent as was decided in the case *United Airlines v. CIT (2006) 152 Taxman 516 Del.*

### No requirement to deduct tax at source under section 194-I on remittance of Passenger Service Fees by an Airline to an Airport Operator [Circular No. 21/2017, dated 12.06.2017]

On the issue of whether payment of passenger service fees (PSF) by an airline to an Airport Operator qualifies as rent to attract TDS under section 194-I, the Bombay High Court relied on the Apex Court ruling in Japan Airlines and Singapore Airlines case, wherein it was observed that the primary requirement for any payment to qualify as rent is that the payment must be for the use of land and building and mere incidental use of the same while providing other facilities and service would not make it a payment for use of land and building only so as to attract section 194-I.

### Payment on transfer of certain immovable property other than agricultural land [Section 194-IA]

Any person, being a transferee, responsible for paying (other than the person referred to in section 194LA) to a resident transferor any sum by way of consideration for transfer of any immovable property (other than agricultural land), shall, at the time of credit of such sum to the account of the transferor or at the time of payment of such sum in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct an amount equal to one per cent (1%) of such sum as income-tax thereon.

No deduction shall be made where the consideration for the transfer of an immovable property is less than 50 lakh rupees.

- (a) “agricultural land” means agricultural land in India, not being a land situate in any area referred to in items (a) and (b) of sub-clause (iii) of clause (14) of section 2;
- (b) “immovable property” means any land (other than agricultural land) or any building or part of a building.

The provisions of section 203A shall not apply to a person required to deduct tax in accordance with the provisions of this section.

The term ‘consideration for immovable property’ shall include all charges of the nature of club membership fee, car parking fee, electricity and water facility fees, maintenance fee, advance fee or any other charges of similar nature, which are incidental to transfer of the immovable property.

### Procedure to be followed for Depositing of Tax

*There was a confusion regarding the depositing the tax and claim of such tax deposited. Whether the deductor would have to apply for a TAN and how and when the tax is to be deposited.*

*As per section 194-IA, every person (even individuals) making a payment for consideration of an immovable property, not including agricultural land, will withhold tax @ 1% of the transaction amount.*

*As per notification no. 39/2013 dated 31 May, 2013 the following things were made clear :*

1. *Depositing of withholding tax*
2. *Issuance of certificates for such tax*
3. *Filing a return of withholding tax*

*The following procedure is followed :*

*The amount deducted under section 194-IA shall be deposited with the Central Government within 7 days from the end of the month in which the amount was deducted. For example, if amount is deducted on 15th June, then amount shall be paid to the credit of Central Government by 7th July.*

*TDS payment made u/s 194-IA is to be necessarily accompanied by a challan-cum-statement in Form No.26QB.*

*The amount shall be deposited electronically within the time specified above with the RBI or the SBI or any other authorized bank. Deductor is liable to furnish the certificate of the tax deducted at source in Form No. 16B to the deductee within 15 days from the due date of furnishing Form No. 26QB. TDS deductor shall provide a certificated under Form 16B which is to be generated online from the web portal.*

### **TDS on payment of Rent by certain Individuals/HUF [Section 194IB]**

This section is applicable to an Individual/HUF, whose accounts are not liable to audit u/s 44AB(a)/(b) in preceding financial year, responsible for paying to a resident rent of land or building in excess of Rs. 50,000 per month or part of month.

TDS is to be deducted only at the time of credit of rent (for the last month of the previous year or last month of tenancy if the property is vacated during the year) to the account of payee or the payment thereof in cash or by cheque / draft, whichever is earlier.

Tax is to be deducted at rate of 5% of the rent paid/credited during the financial year. If PAN of recipient is not available, then tax is to be deducted at rate of 20% but it cannot exceed rent payable for last month of the previous year or last month of tenancy.

No tax to be deducted if rent is Rs 50,000 or less per month or when the individual of HUF is cover u/s 194I. Provisions of section 203A (pertaining to TAN) shall not apply.

#### **TDS at on Joint Development Project [Section 194-IC]**

TDS is to be deducted @ 10% under this section by any person responsible for paying any sum by way of consideration to a resident (not being in kind) under a Joint Development Project.

Tax is deductible at the time of credit of such sum to the account of Payee or at the time of payment thereof in cash or by issue of a cheque/draft or by any other mode, whichever is earlier. Threshold limit is Nil.

**Note** - Joint Development Agreement means a registered agreement in which a person owning land or building or both, agrees to allow another person to develop a real estate project on such land or building or both, in consideration of share, being land or building or both in such project, whether with or without payment of part of consideration in cash.

#### **Professional and Technical Fees [Section 194J]**

Any person other than an individual or a HUF who is responsible for paying to a resident following income :

1. Fees for professional services, (CA, CS, CWA, Lawyers, MBA, all film industries)
2. Fees for technical services, (Engineers, Architects)
3. Royalty
4. Non-competing fees specified under section 28(v).
5. Remuneration or fees or commission paid to a director of a company (not being salaries chargeable u/s 15). e.g. Board sitting fees.

shall deduct tax at source @ 10%. However, no TDS shall be deducted if the aggregate of such fees given to a person is likely to be upto an amount of Rs. 30,000 in the previous year or where professional service are for the personal purpose of the individual of HUF. When the payee does not furnish his PAN to deductor, tax will be deducted with effect from 1st April 2010 @ 20%.

**Note : TDS shall be deducted at rate of 2% only in case of payment/credit to a person engaged only in the business of operation of call centre.**

#### **Payment of Compensation on acquisition of Capital Asset [Section 194LA]**

It applies to any person responsible for paying to a resident any sum being in the nature of compensation or enhanced compensation or consideration or enhanced consideration on account of compulsory acquisition of any asset under any law for the time being in force. Such person, at the time of payment of such sum in cash or by issue of a cheque or draft or by any other mode whichever is earlier, shall deduct an amount equal to 10% and no surcharge, cess shall be added. When the payee does not furnish his PAN to deductor, tax will be deducted @ 20%.of such sum as income tax on income comprised therein. However, no deduction shall be made where the amount of such payment or aggregate of such payments during the financial year does not exceed Rs. 2.5 Lakh.

No TDS shall be deducted under this section in respect of payment made in respect of any award/agreement made which has been exempted from levy of income tax under Section 96 (except those made under section 46) of RFCTLARR (Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement) Act.

#### **Income by way of interest from infrastructure debt fund [Section 194LB]**

Where any income by way of interest is payable to a non-resident, not being a company, or to a foreign company, by an infrastructure debt fund referred to in clause (47) of section 10, the person responsible for making the

payment shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon @ 5% + Surcharge, if applicable + HEC.

#### **Income from units of a Business Trust [Section 194LBA]**

Where any distributed income referred to in section 115UA, being of the nature referred to in clause (23FC or 23FCA) of section 10, is payable by a business trust to its unit holder being a resident, the person responsible for making the payment shall at the time of credit of such payment to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rate of 10 percent.

In case the unit holder is a non-resident, not being a company or a foreign company, the person responsible for making the payment shall at the time of credit of such payment to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rate of 5% + Surcharge, if applicable + HEC.

#### **Income by way of interest from Indian company engaged in certain Business [Section 194LC]**

Where any income by way of interest is payable to a non-resident, not being a company or to a foreign company by a specified company or a business trust, the person responsible for making the payment, shall at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct the income-tax thereon @ 5% + Surcharge, if applicable + HEC.

The interest shall be the income by way of interest payable by the specified company,

- (i) in respect of monies borrowed by it in foreign currency from a source outside India,
  - (a) under a loan agreement at any time on or after the 1st day of July, 2012 but before the 1st day of July, 2020; or
  - (b) by way of issue of long-term infrastructure bonds at any time on or after the 1st day of July, 2012 but before the 1st day of October, 2014; or
  - (c) by way of issue of any long-term bond including long-term infrastructure bond at anytime on or after the 1st day of October, 2014 but before the 1st day of July, 2020.

as approved by the Central Government in this behalf; and

- (ii) to the extent to which such interest does not exceed the amount of interest calculated at the rate approved by the Central Government in this behalf; having regard to the terms of the loan or the bond and its repayment.
  - (a) "foreign currency" shall have the meaning assigned to it in clause (m) of section 2 of the Foreign Exchange Management Act, 1999(42 of 1999);
  - (b) "specified company" means an Indian company.

#### **Income by way of interest on certain bonds and Government securities [Section 194LD]**

Any person who is responsible for paying to a person being a Foreign Institutional Investor or a Qualified Foreign Investor, any income by way of interest shall, at the time of credit of such income to the account of the payee or at the time of payment of such income in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax @ 5% + Surcharge, if applicable + HEC.

The income by way of interest shall be the interest payable on or after the 1st day of June, 2013 but before the 30th day of June, 2020 in respect of investment made by the payee in –

- (i) a rupee denominated bond of an Indian company ; or
- (ii) a Government security;

However, the rate of interest in respect of bond referred to in clause (i) shall not exceed the rate as may be notified by the Central Government.

- (a) *“Foreign Institutional Investor” shall have the meaning assigned to it in clause (a) of the Explanation to section 115AD;*
- (b) *“Government security” shall have the meaning assigned to it in clause (b) of section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956);*
- (c) *“Qualified Foreign Investor” shall have the meaning assigned to it in the Circular, No. Cir/IMD/DF/14/2011, dated the 9th August, 2011, as amended from time to time, issued by the Securities and Exchange Board of India, under section 11 of the Securities and Exchange Board of India Act, 1992 (15 of 1992).*

#### **Payment by Individual/HUF to contractors and professionals [Section 194M]**

Any sum or the aggregate of sums(exceeds INR 50 lacs in a year) paid or credited in a year by Individual/HUF (who are not required to deduct tax at source under section 194C and 194J of the Act) to contractors or professionals on account of contractual work or professional fees are required to deduct TDS at the rate of 5%. To deposit the tax deducted, assessee shall not be required to obtain Tax deduction Account Number (TAN).

#### **TDS on cash withdrawal to discourage cash transactions [Section 194N]**

Every person, being a banking company including any co-operative bank or a post office, who is responsible for paying any sum in cash, in excess of 1 crore rupees during the previous year, to any person (herein referred to as the recipient) from an account maintained by the recipient with it shall, at the time of payment of such sum, deduct an amount equal to 2% of sum exceeding 1 crore rupees. Provided that nothing contained in this sub-section shall apply to any payment made to Government, banking company, cooperative society engaged in carrying on the business of banking, post office, banking correspondents and white label ATM operators.

#### **Payments of other sums to Non-Residents [Section 195]**

Any person responsible for paying to a non-resident or foreign company any interest or any other sum chargeable to income-tax in India, not being salaries, shall at the time of payment, deduct tax at the rates in force. However, no such deduction shall be made in respect of any dividends referred to in Section 115-O.

In the case of interest payable by the government or a public sector bank or a public financial institution within the meaning of Section 10(23D), deduction of tax shall be made only at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode.

Credit of any amount to ‘Suspense Account’ or any other account in the books of account of the person liable to pay such income is also deemed to be ‘credit’ of the income to the account of the payee and makes the provisions of this section applicable to such cases.

If the person responsible for such payments, feels that the whole amount would not be income chargeable in the case of recipient he may make an application to the Assessing Officer to determine the chargeable portion and he shall deduct tax on the sum so determined. Further, the assessee may apply to the Assessing Officer to grant a certificate for either no deduction of tax at source or deduction at a lower rate. If the Assessing Officer is satisfied, he can issue a certificate accordingly and the certificate shall remain in force till the expiry of the period specified therein or its cancellation by the Assessing officer whichever is earlier.

Where payer is responsible for paying any sum to a non resident can make an application in such form and manner to the Assessing Officer, to determine the portion of sum chargeable to tax in such manner, as may be prescribed.

Payment made by Indian company to U.S. Company for use of its data base is not subjected to TDS under Section 195 of the Income Tax Act. - *WIPRO Ltd. v. I.T.O. (2005) 94 ITD 9 (Bang.)*].

**Rate of TDS under Section 195** : Rates prescribed under the Act has to be increased by surcharge and health and education cess at the prescribed rate. If the payment is being made as per DTAA rates, then there is no need to add surcharge and cess. The rates are as follows :

Particulars	TDS rates
Income in respect of investment made by a NRI	20%
Income by the way of long term capital gains in Section 115E in case of a NRI	10%
Income by way of long-term capital gains	10%
Short Term Capital gains under section 111A	15%
Any other income by way of long-term capital gains	20%
Interest payable on money borrowed in Foreign Currency	20%
Income by way of royalty payable by Government or an Indian concern	10%
Income by way of royalty, not being royalty of the nature referred to be payable by Government or an Indian concern	10%
Income by way of fees for technical services payable by Government or an Indian concern	10%
Any other income	30%

**Income payable “Net of Tax” [Section 195A]**

In a case other than that referred to in sub-section (1A) of section 192, where under an agreement or other arrangement, the tax chargeable on any income referred to in the foregoing provisions of this Chapter is to be borne by the person by whom the income is payable, then, for the purposes of deduction of tax under those provisions such income shall be increased to such amount as would, after deduction of tax thereon at the rates in force for the financial year in which such income is payable, be equal to the net amount payable under such agreement or arrangement.

**Interest or dividend or other sums payable to Government, Reserve Bank or certain corporations [Section 196]**

Section 196 provides that no deduction of tax shall be made (notwithstanding anything contained in the foregoing provisions of Chapter XVII) by any person from any sums payable to :

- (i) the Government; or
- (ii) the Reserve Bank of India; or
- (iii) a corporation established by or under a Central Act which is, under any law for the time being in force, exempt from income-tax on its income; or
- (iv) a Mutual Fund specified under Section 10(23D);

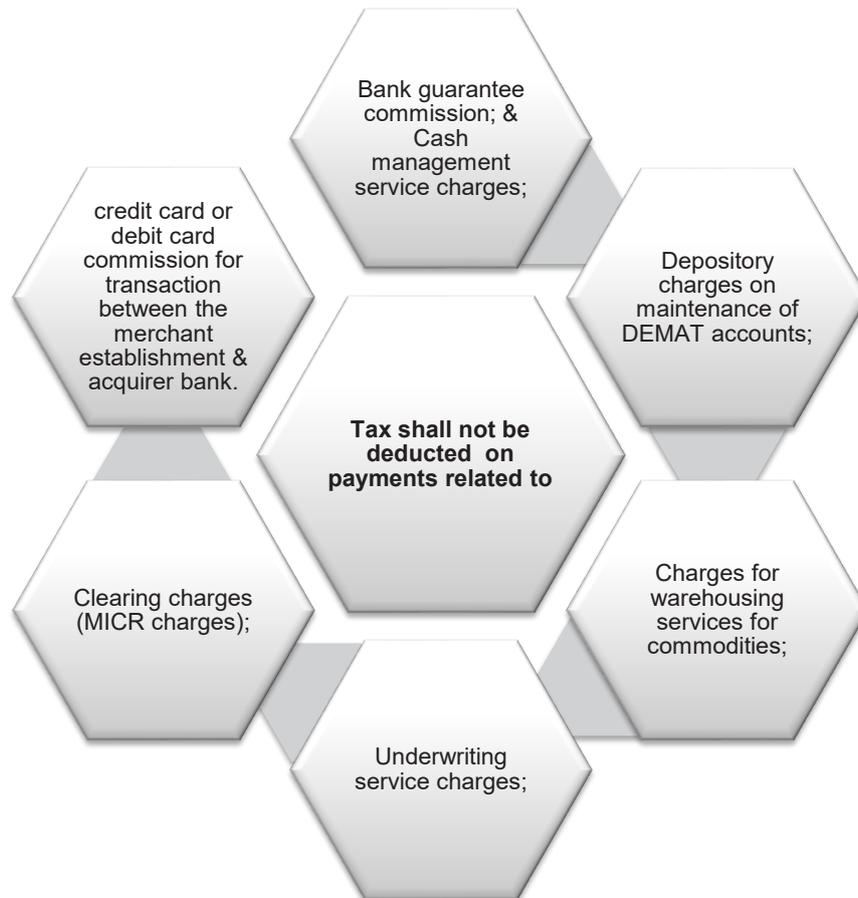
where such sum is payable to it by way of interest or dividend in respect of any securities or shares owned by it or in which it has full beneficial interest, or any other income accruing or arising to it.

Where in the case of any income of any person, the Assessing Officer is satisfied that the total income of the person justifies the deduction of income-tax at any lower rate or no deduction of income-tax, he shall, on an

application made by the assessee in this behalf, give to him such certificate as may be appropriate. Where such certificate is given, the person responsible for paying the income shall, until such certificate is cancelled by the Assessing Officer, deduct income-tax at the rates specified in the certificate or deduct no tax, as the case may be [Section 197].

With effect from 1st January 2013, no tax shall be deducted on the following payments where such payment is made by a person to a bank listed in the Second Schedule to the Reserve Bank of India Act, 1934, excluding a foreign bank;

**Tax shall not be deducted on payments related to :**



**Income from units [Section 196B]**

According to Section 196B the person responsible for making the payment in respect of units referred to in Section 115AB or by way of long-term capital gains arising from the transfer of such units is payable to an offshore fund shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rate of ten percent + Surcharge, if applicable + 4% HEC.

**Income from foreign currency bonds or shares of Indian Company [Section 196C]**

Section 196C provides for a deduction of income-tax at the rate of ten percent from the interest income or dividend income in respect of bonds or shares referred to in Section 115AC or by way of long-term capital gains arising from the transfer of such bond or share capital to a non-resident. However, no such deduction shall be made in respect of any dividends referred to in Section 115-O.

The person responsible for making such payment shall at the time of credit of such income to the account of the

payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode whichever is earlier, deduct the income-tax thereon @ 10% + Surcharge, if applicable + 4% HEC.

### **Income of Foreign Institutional Investors from securities [Section 196D]**

According to Section 196D, where any income in respect of securities referred to in clause (a) of Sub-section (1) of Section 115AD is payable to a Foreign Institutional Investor, the person responsible for making the payment shall, at the time of credit of such income to the account of the payee or at the time of payment thereof, whichever is earlier, deduct income-tax at the rate of twenty per cent. However, no such deduction shall be made in respect of any dividends referred to in Section 115-O.

Also no deduction of tax shall be made from any income by way of capital gains arising from the transfer of securities referred to in Section 115AD payable to a Foreign Institutional Investor.

### **RATIONALIZATION OF TAX DEDUCTION AT SOURCE PROVISIONS RELATING TO PAYMENTS BY CATEGORY-I AND CATEGORY-II ALTERNATE INVESTMENT FUNDS TO ITS INVESTORS**

The Finance Act, 2015 had inserted a special taxation regime in respect of Category-I and II Alternative Investment Funds (investment fund) registered with SEBI. The special taxation regime is intended to ensure tax pass through status in respect of these investment funds which are collective investment vehicles. The special regime is contained in sections 10(23FBA), 10(23FBB), 115UB and 194LBB of the Act. Under this regime, the income of the investment fund (not being in the nature of business income) is exempt in the hands of investment fund but income received by the investor from the investment fund (other than income which is taxed at the level of investment fund) is taxable in the hands of investor. The taxation in the hands of investors is in the same manner and in the same proportion as it would have been, had the investor received such income directly and not through the investment fund. The existing provisions of section 194LBB provides that in respect of any income credited or paid by the investment fund to its investor, a tax deduction at source (TDS) shall be made by the investment fund @ 10% of the income. Under section 197 of the Act, facility for certificate for deduction of tax at lower rate or no deduction is available in respect of sections enumerated therein, if the Assessing Officer is satisfied that total income of the recipient justifies issue of such certificate, section 194LBB is currently not included in this provision.

It has been represented that the existing TDS regime has created certain difficulties. The non-resident investor is not able to claim benefit of lower or NIL rate of taxation which is available to him under the relevant Double Taxation Avoidance Agreement (DTAA), and deduction of tax @10% is to be undertaken mandatorily even if under DTAA, the income is not taxable in India. There is no facility for any investor to approach the Assessing Officer for seeking certificate for TDS at a lower or NIL rate in respect of deductions made under section 194LBB.

In order to rationalise the TDS regime in respect of payments made by the investment funds to its investors, section 194LBB of the Act has been amended to provide that the person responsible for making the payment to the investor shall deduct income-tax under section 194LBB at the rate of ten per cent where the payee is a resident and at the rates in force where the payee is a non-resident (not being a company) or a foreign company. Further, it is provided to amend section 197 to include section 194LBB in the list of sections for which a certificate for deduction of tax at lower rate or no deduction of tax can be obtained. Consequential changes are also made to the definition of "rates in force" so as to include section 194LBB in it.

These amendments will take effect from 1st June, 2016.

### **No deduction to be made in certain cases [Section 197A]**

Section 197A provides that no deduction of tax at source is to be made from (i) interest on securities, (ii) dividends, and (iii) payments in respect of deposits under NSS, etc. if the following conditions are satisfied :

- (i) The recipient of such income is an individual and resident in India.
- (ii) Such person furnishes a declaration in writing in duplicate, in the prescribed form and verified in the prescribed manner, to the payer of such income to the effect that the tax on his estimated total income of the previous year in which such income is to be included for computing his total income will be nil.

Sub-section 197A(1A) has been inserted with effect from June 1, 1992. This sub-section provides that in case of interest other than interest on securities, a declaration referred to above can be furnished by any person (other than a company or a firm).

The payer of the aforesaid income will deliver to Chief Commissioner or Commissioner of Income-tax one copy of the declaration (received from the recipient of income) on or before the 7th day of the month next following the month in which the declaration is furnished. If he fails to do so he will be liable to a penalty of an amount which shall not be less than one hundred rupees but which may extend to two hundred rupees for every day during which the default continues.

#### **Certificate of tax deducted [Section 203]**

The person who deducts tax has to issue a certificate in the prescribed form to the person from whose payments deduction has been made, showing therein the particulars of payment, the date of tax deducted at source and the date of its credit to the Central Government. It is on the basis of this certificate that the payee can claim credit for tax paid on his behalf and can claim refund, if any, due to him on the basis of tax liability for the relevant year.

#### **Consequence in the event of default [Section 201]**

Where any person, including the principal officer of a company,

- (a) who is required to deduct any sum in accordance with the provisions of this Act; or
- (b) referred to in sub-section (1A) of section 192, being an employer,

does not deduct, or does not pay, or after so deducting fails to pay, the whole or any part of the tax, as required by or under this Act, then, such person, shall, without prejudice to any other consequences which he may incur, be deemed to be an assessee in default in respect of such tax :

However, any person, including the principal officer of a company, who fails to deduct the whole or any part of the tax in accordance with the provisions of this Chapter on the sum paid to a resident or on the sum credited to the account of a resident shall not be deemed to be an assessee in default in respect of such tax if such payee.

- (i) has furnished his return of income under section 139;
- (ii) has taken into account such sum for computing income in such return of income; and
- (iii) has paid the tax due on the income declared by him in such return of income, and the person furnishes a certificate to this effect from an accountant in form 26A.

No penalty shall be charged under section 221 from such person, unless the Assessing Officer is satisfied that such person, without good and sufficient reasons, has failed to deduct and pay such tax.

No order shall be made deeming a person to be an assessee in default for failure to deduct the whole or any part of the tax from a person resident in India, at any time after the expiry of seven years from the end of the financial year in which payment is made or credit is given.

If a person responsible for deduction of tax at source fails to deduct the appropriate tax or, after making the due deduction fails to deposit it into the Government treasury, he shall be deemed to be an assessee in default and shall be liable to :

- (i) Payment of the whole or any part of the tax as due
- (ii) Interest at the rate of 1% per month or part of the month on the tax from the date on which such tax was deductible to the date on which such tax is deducted; and
- (iii) Interest at the rate of 1.5% per month or part of the month on the tax from the date on which such tax was deducted to the date on which such tax is actually paid;

However, in case any person, including the principal officer of a company fails to deduct the whole or any part of the tax on the sum paid to a resident or on the sum credited to the account of a resident but is not deemed to be an assessee in default, the interest shall be payable from the date on which such tax was deductible to the date of furnishing of return of income by such resident.

- (iv) Penalty which may be as high as the amount of the tax in default, however, no penalty shall be charged under Section 221 from such person unless the Assessing Officer is satisfied that such person has, without good and sufficient reasons, failed to deduct and pay the tax; and
- (v) Prosecution - where the amount of tax which the responsible person has failed to deduct or pay exceeds Rs. 1,00,000 he shall be punishable with rigorous imprisonment for a term not less than 6 months but which may be extended to 7 years and with fine. In any other case, he shall be punished with a rigorous imprisonment of a term of not less than 3 months but which may be extended to 3 years and with fine.

Where the amount of tax has not been deposited after it is deducted, the amount of tax together with the interest shall be a charge upon all the assets of the person.

The following table will give the list of forms of certificates to be issued and necessary form to be filed with Assessing Officer by the persons deducting the tax at source.

<b>Categories of payment</b>		<b>Form No. of Certificate</b>	<b>Form No. of return to be filed with Assessing Officer</b>
(1)		(2)	(3)
(a)	Salaries	12BA, 16, 16AA	24Q
(b)	Interest on Securities (Government)	16A	26Q
(c)	Interest on Securities (others)	16A	26Q
(d)	Interest other than Interest on Securities	16A	26Q
(e)	Dividends	16A	26Q
(f)	Winnings from Lotteries/Crossword puzzles	16A	26Q
(g)	Winnings from Horse Races	16A	26Q
(h)	Payments to contractors/Sub-contractors	16A	26Q
(i)	Insurance commission	16A	26Q
(j)	Non-resident sportsmen or sports association	16A	26Q
(k)	National Savings Scheme etc.	16A	26Q

(l)	Income on repurchase of units by mutual funds or UTI	16A	26Q
(m)	Commission, Remuneration or Reward on sale of lottery tickets	16A	26Q
(n)	Payment to non-resident	16A	27Q
(o)	Foreign company being unit holders of mutual fund	16A	27Q
(p)	Units held by offshore fund and income from foreign currency bonds	16A	27Q
(q)	Rent	16A	26Q
(r)	Commission (not being insurance commission) or brokerage	16A	26Q
(s)	Fee for professional or technical services	16A	26Q

### TAX COLLECTION AT SOURCE (TCS) [SECTION 206C]

Tax is to be collected at source in the following cases;-

#### Case 1 : Sale of :

I.	Alcoholic liquor for human consumption (other than Indian made foreign liquor)	TCS @ 1%.
II.	Indian made foreign liquor	TCS @ 1%
III.	Tendu leaves	TCS @ 5%
IV.	Timber obtained under the forest lease	TCS @ 2.5%
V.	Timber obtained by any mode other than under forest lease	TCS@ 2.5%
VI.	Any other forest produce not being timber or tendu leaves	TCS@ 2.5%
VII.	Scrap	TCS@ 1%
VIII.	Minerals, being coal or lignite or iron ore	TCS@ 1%

#### Case 2 : Grant of lease/license of :

Parking lot, toll plaza, mining and quarrying( other than mining and quarrying of miner oil, petroleum and natural gas TCS @ 2%.

#### Case 3 : - Sale of : -

Motor vehicle of the value exceeding Rs 10,00,000 whether payment is received in cheque or by any other mode. TCS @ 1%

#### Notes : -

1. In case 1, Tax is to be collected by seller from buyer. Seller include every person but does not include an individual or HUF( whose accounts are not required to be audited under section 44AB(a)/(b) during the financial year preceding the financial year in which sale is made).

Buyer does not include : -

- a) A public sector company, the Central Govt., a State Govt., and an Embassy, a High

Commission, Legation, Commission, Consulate and the trade representation, of a foreign state and a club; or

- b) A buyer in the retail sale of such goods purchased by him for personal consumption.
- 2. In case 1, tax has to be collected by the seller at the time of debiting the amount payable by the buyer to the account of buyer or at the time of receipt of such amount from the buyer in cash or issue of cheque/draft, or any other mode, whichever is earlier.
- 3. In case 1, Goods purchased for being used in manufacturing/processing is not subject to TCS. For this purpose buyer has to give declaration in duplicate to seller in form No. 27C. Declaration without PAN is not Valid.
- 4. In case 2, if licensee or lessee is a public sector company then TCS is not applicable.
- 5. In case 3, following points should be noted :
  - a) This case is applicable in case of sale of motor vehicles in retail sales and not in case of sales by manufacturers to dealers/distributors.
  - b) This case is not applicable where buyer is the Central/State Govt., an Embassy/High Commission/ Consulate/Trade representation of foreign Govt., local authority or a public sector company which is engaged in the business of carrying of passengers.

**SECTION 206CC [INSERTED VIDE FINANCE ACT, 2017 W.E.F. AY 2018-19]**

The provisions of this section are as under-

Collectee shall furnish his PAN to the person responsible for collecting such tax at source. If PAN is not intimated, tax shall be collected at twice the normal rate or at the rate of 5%, whichever is higher.

- i. Declaration filed under section 206(1A) shall not be valid unless the person filing the declaration furnishes his PAN in such declaration.
- ii. Lower tax collection certificate shall not be granted unless application in Form No. 13 by the collectee contains his PAN.
- iii. The collectee shall furnish his PAN to the collector and both shall indicate the same in all correspondence, bills and vouchers exchanged between them.
- iv. Where the PAN provided by the collectee is invalid or it does not belong to the collectee, it shall be deemed that PAN has not been furnished to the collector.

These provisions are not applicable to a non resident who does not have any permanent establishment in India.

**TIME LIMIT FOR THE PAYMENT OF TDS TO THE GOVERNMENT**

Sr. No.	Month	Non-Govt. Deductors	Government Deductors
1.	April to February	7th of the next month in which TDS is deducted	<ul style="list-style-type: none"> <li>• Same day in cases TDS deposited without challan no. ITNS 281.</li> <li>• 7th of the next month in which TDS is deducted in cases TDS deposited with challan</li> </ul>

2.	March	30th April of next financial year	<ul style="list-style-type: none"> <li>• Same day in cases TDS deposited without challan no. ITNS 281.</li> <li>• 7th of the next month in which TDS is deducted in cases TDS deposited with challan</li> </ul>
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**Note :** Any sum deducted u/s 194IA shall be paid to the credit of the central government within a period of 30 days (w.e.f. 01.06.2016) from the end of the month in which the deduction is made and shall be accompanied by a challan-cum-statement in Form No. 26QB.

The Due date to submit Form 24G extended from 10 days of the end of the relevant month to

- 30th day of April where the statement relates to the month of March and
- 15 days from the end of relevant month

It is furnished electronically under digital signature or electronically along with the verification of the statement.

### Issue of TDS Certificate

Every person deducting tax at source is required as per Section 203 to furnish a certificate to the payee to the effect that tax has been deducted along with certain other particulars. This certificate is usually called the TDS certificate. Even the banks deducting tax at the time of payment of pension are required to issue such certificates. In case of employees receiving salary income including pension, the certificate has to be issued in Form No.16. In all other cases, the TDS certificate is to be issued in Form 16B. The certificate is to be issued in the deductor's own stationery. However, there is no obligation to issue TDS certificate in case of tax at source is not deducted /deductible by virtue of claims of exemptions/ deductions.

### Due Date for Issue of Certificate

FORM 16 : 31 May of the Next Financial year in which tax is deducted.

FORM 16A : Within 15 days from due date for furnishing the statement of tax deducted under rule 31A

Quarter ended	Due date of Form 16A
30th June	15th August
30th September	15th November
31st December	15th February
31st March	15th June

**Form 16B :** Within 15 days from due date for furnishing the challan cum statement in Form 26QB

### Issue of Duplicate Certificate

Where the original TDS certificate is lost, the deductee can approach the deductor for issue of a duplicate TDS certificate. The deductor may issue a duplicate certificate in Form No. 16 or Form 16A as the case may be. However such a certificate has to be certified as duplicate by the deductor. Further, the deductor may, at his option, use digital signatures to authenticate such certificates. In case of issue of such certificates the deductor shall ensure that

- a) The provisions of sub-rule (2) of Rule 31 regarding specification of TAN, PAN of deductee book identification number; Challan identification number; receipt number of relevant quarterly statements etc. are complied with;
- b) Once the certificate is digitally signed, the contents of the certificates are not amendable to change; and

- c) The certificates have a control number and a log of such certificates is maintained by the deductor.

## TDS FORMS

Any person deducting any sum in accordance with the foregoing provisions of this Chapter shall pay within the prescribed time, the sum so deducted to the credit of the Central Government or as the Board directs. Further, quarterly TDS Return is required to be filed by the assessee who has deducted the TDS. TDS Returns include fields like TAN No., TDS Payment, amount deducted, type of payment, PAN No. etc.

Form No.	Particulars
Form 24Q	Statement for tax deducted at source from salaries
Form 26Q	Statement for tax deducted at source on all payments except salaries
Form 27Q	Statement for deduction of tax from interest, dividend, or any other sum payable to non-residents
Form 27EQ	Statement of collection of tax at source
Form 26QB	For section 194IA separate return is not required, challan cum return to be filed on Form 26QB to be deposited within a period of 30 days (w.e.f. 01.06.2016) from the end of the month in which the deduction is made.

The quarterly return statements should be accompanied by a signed verification in Form No. 27A. Form 27A is a control chart of quarterly TDS statements to be filed by deductors/collectors alongwith quarterly statements. It is a summary of TDS returns which contains control totals of 'amount paid' and 'income tax deducted at source'.

## TDS Return

A return of TDS is a comprehensive statement containing details of payment made and taxes deducted thereon along with other prescribed details. As per section 200(3) of the Act, the Due Date for filing TDS Return (both online as well as physical w.e.f. 01.06.2016) is as follows :

Quarter	Due Date for Form 24Q & Form 26Q	Form 27Q	Form 27EQ
April to June	31st July	31st July	15th July
July to Sept	31st Oct	31st Oct	15th Oct
Oct to Dec	31st Jan	31st Jan	15th Jan
Jan to March	31st May	31st May	15th May

**Note :** 'Nil' TDS return is not mandatory, however to facilitate the deductors and update data government has provided a facility for declaring nil TDS return.

The statement may be furnished in any of the following manners namely :

- Paper form
- Electronically, under digital signature in accordance with the procedures, formats and standards specified under sub-rule (5) of Rule 31A.
- Electronically, along with the verification of the statement in Form 27A or verified through an electronic process in accordance with the procedures, formats and standards specified under sub-rule (5) of Rule 31A.

It is to be noted that in case of the following quarterly, statements are to be delivered electronically;

- a) Every Government deductor,
- b) Corporate deductor,
- c) The deductor is a person required to get his accounts audited under sec. 44 AB in the immediately preceding financial year or
- d) The number of deductee's records in a statement for any quarter of the financial year is twenty or more;

Such quarterly statements are to be delivered electronically under digital signature or electronically with verification of statement in form 27A or verified through an electronic process in accordance with format and procedure specified in rule 31A(5). Further, a declaration in Form 27A is also to be submitted in paper format. Quarterly statements are also to be filed by such deductors in electronic format with the e-TDS Intermediary at any of the TIN Facilitation Centres, particulars of which are available at [www.incometaxindia.gov.in](http://www.incometaxindia.gov.in) and at <http://tin.nsd.com>

A person other than a deductor specified above may at his option deliver the quarterly statements electronically in computer media as provided above. However, it is not mandatory for it to do so.

It is mandatory for the deductor to quote the following in quarterly statements :

- TAN
- PAN of the deductor (except where deductor is an office of the government)
- PAN of all the deductees
- Particulars of tax paid to the Central Government including Book Identification Number or Challan Identification Number as the case may be.
- Particulars of amount paid or credited on which tax was not deducted in view of issue of certificate of no deduction of tax u/s 197 by the assessing officer to the payee.

**Refund of TDS**

In case of excess deduction of tax at source, claim of refund of such excess TDS can be made by the deductor. The excess amount is refundable as per procedure laid down for refund of TDS wherein the difference between the actual payment made by the deductor and the tax deductible at source, will be treated as the excess payment made.

In case such excess payment is discovered by the deductor during the financial year concerned, the present system permits credit of the excess payment in the quarterly statement of TDS of the next quarter during the financial year. In case, the deduction of such excess amount is made beyond the financial year concerned, such claim can be made to the Assessing Officer (TDS) concerned. However, no claim of refund can be made after two years from the end of financial year in which tax was deductible at source.

**TDS CHART FY 2019-20 "AY 2020-21"**

**CATEGORY A - WHEN RECIPIENT IS RESIDENT**

Nature of payment	TDS (SC : Nil, EC : Nil, SHEC : Nil)
Section 192 - Payment of salary : Normal slab rates are applicable + SC 15% / 10% (if net income exceeds Rs. 1 crore or 50 lakh as the case may be ), HEC @ 4%	

<b>Section 192A</b> - Payment of taxable accumulated balance of provident fund	10
<b>Section 193</b> - Interest on securities : a) Any debentures/securities for money issued by or on behalf of any local authority/statutory corporation, b) listed debentures of a company c) any security of the Central or State Government d) any other interest on securities (including interest on non-listed debentures)	10
<b>Section 194A</b> - Interest other than interest on securities	10
<b>Section 194B</b> - Winnings from lottery or crossword puzzle or card game or other game of any sort	30
<b>Section 194BB</b> - Winnings from horse races	30
<b>Section 194C</b> - Payment or credit to a resident contractor/sub-contractor a) payment/credit to an individual or a Hindu undivided family b) payment/credit to any person other than an individual or a Hindu undivided family	1 2
<b>Section 194D</b> Insurance commission a) payment/credit to an individual or a Hindu undivided family b) payment/credit to any person other than an individual or a Hindu undivided family	5
<b>Section 194DA</b> - Payment in respect of life insurance policy	5
<b>Section 194EE</b> - Payment in respect of deposits under National Savings Scheme, 1987	10
<b>Section 194F</b> - Payment on account of repurchase of units of MF or UTI	20
<b>Section 194G</b> - Commission on sale of lottery tickets	5
<b>Section 194H</b> - Commission or brokerage	5
<b>Section 194-I</b> – Rent a) rent of plant and machinery b) rent of land or building or furniture or fitting	2 10
<b>Section 194IA</b> - Payment/credit of consideration to a resident transferor for transfer of any immovable property (other than rural agricultural land)	1

<b>Section 194IB</b> - Payment of rent by an individual or HUF not subjected to tax audit under Section 44AB	5
<b>Section 194IC</b> - Payment under Joint Development Agreement to a resident individual or HUF who transfers land or building as per such agreement	10
<b>Section 194J</b> - Professional fees, technical fees, royalty or remuneration to a director (2% if payee is engaged in the business of call center)	10
<b>Section 194LA</b> - Payment of compensation on acquisition of certain immovable property	10
<b>Section 194LBA(1)</b> - Payment of the nature referred to in section 10(23FC) or section 10(23FC)(a) (with effect from June 1, 2016) or section 10(23FCA) by business trust to resident unit holders	10
<b>Section 194LBB</b> - Payment in respect of units of investment fund specified in section 115UB	10
<b>Section 194LBC(1)</b> - Payment in respect of an investment in a securitisation trust specified in clause (d) of the Explanation occurring after section 115TCA (with effect from June 1, 2016) -	
- if recipient is an individual or a Hindu undivided family	25
- if recipient is any other person	30

#### CATEGORY B - WHEN RECIPIENT IS NON-RESIDENT OR FOREIGN COMPANY

Aggregate payment or credit subject to TDS during the financial year 2019-20	If recipient is non-resident Individual/HUF/AOP/BOI/ Artificial juridical person			If recipient is non-resident co-operative society/ firm		If recipient is non-domestic company		
	Rs. 50 lakh or less	More than Rs. 50 lakh but not more than Rs. 1 crore	More than Rs. 1 crore	Rs. 1 crore or less	More than Rs. 1 crore	Rs. 1 crore or less	More than Rs. 1 crore but not more than Rs. 10 crore	More than Rs. 10 crore
Surcharge rate	SC : Nil	SC : 10%	SC : 15%	SC : Nil	SC : 12%	SC : Nil	SC : 2%	SC : 5%
<i>Nature of payment TDS (inclusive of SC : rate as applicable, HEC : 4%)</i>								

<b>Section 192</b> - Payment of salary	Normal Tax Rate plus SC, EC and SHEC	-	-	-	-	-	-	-
<b>Section 192A</b> - Payment of taxable accumulated balance of provident fund	10.40	11.44	11.96	-	-	-	-	
<b>Section 194B</b> - Winning from lottery or crossword puzzle or card game or other game of any sort	31.20	34.32	35.88	31.20	34.94	31.20	31.82	32.76
<b>Section 194BB</b> - Winning from horse races	31.20	34.32	35.88	31.20	34.94	31.20	31.82	32.76
<b>Section 194E</b> - Payment to a non- resident foreign citizen sportsman /entertainer or non-resident sports association	20.8	22.88	23.92	20.80	23.29	20.80	21.21	21.84
<b>Section 194EE</b> - Payment in respect of deposits under National Saving Scheme, 1987	10.40	11.44	11.96	NA	NA	NA	NA	NA
<b>Section 194F</b> - Re- purchase of units of MF or UTI	20.80	22.88	23.92	NA	NA	NA	NA	NA
<b>Section 194G</b> - Commission on sale of lottery tickets	5.20	5.72	5.98	5.20	5.82	5.20	5.30	5.46
<b>Section 194LB</b> - Payment/credit by way of interest by infrastructure debt fund	5.20	5.72	5.98	5.20	5.82	5.20	5.30	5.46
<b>Section 194LBA(2)</b> - Payment of the nature referred to in Section 10(23FC) [or (with effect from June 1, 2016) <b>section 10(23FC(a))</b> by <b>business trust to unit holders</b>	5.20	5.72	5.98	5.20	5.82	5.20	5.30	5.46

<b>Section 194LBA(3)</b> - Payment of the nature referred to in section 10(23FCA) by business trust to unit holders	31.20	34.32	35.88	31.20	34.94	41.60	42.43	43.68
<b>Section 194LBB</b> - Payment in respect of units of investment fund specified in Sec. 115UB	31.20	34.32	35.88	31.20	34.94	41.60	42.43	43.68
<b>Section 194LBC(2)</b> - Payment in respect of an investment in a securitisation trust specified in clause (d) of the Explanation occurring after section 115TCA (with effect from June 1, 2016)	31.20	34.32	35.88	31.20	34.94	41.60	42.43	43.68
<b>Section 194LC</b> - Payment/credit of interest by an Indian specified company on foreign currency approved loan/long-term infrastructure bonds (with effect from October 1, 2014, any bond) from outside India	5.20	5.72	5.98	5.20	5.82	5.20	5.30	5.46
<b>Section 194LD</b> - Interest on a rupee denominated bond of an Indian company or Government security (from June 1, 2013)	5.20	5.72	5.98	5.20	5.82	5.20	5.30	5.46
<b>Section 195</b> - Payment/credit of other sum to a non-resident :								
a) Income of foreign exchange assets payable to an Indian citizen	20.80	22.88	23.92	NA	NA	NA	NA	NA
b) income by way of long-term capital gains referred to in section 115E or section 112(1)(c)(iii)	10.40	11.44	11.96	10.40	11.64	10.40	10.60	10.92

c) short-term capital gains under section 111A	15.60	17.16	17.94	15.60	17.47	15.60	15.91	16.38
d) any other long-term capital gains [not being covered by section 10(33), 10(36)]	20.80	22.88	23.92	20.80	23.29	20.80	21.21	21.84
e) income by way of interest payable by Government/ Indian concern on money borrowed or debt incurred by Government or Indian concern in foreign currency not being interest referred to in section 194LB or Section 194LC	20.80	22.88	23.92	20.80	23.29	20.80	21.21	21.84
f) royalty [see Note 5]	10.40	11.44	11.96	10.40	11.64	10.40	10.60	10.92
g) royalty [not being royalty of the nature referred to in (f) supra] [see Note 6] –								
• where the agreement is made after March 31, 1961 but before April 1, 1976	10.40	11.44	11.96	10.40	11.64	52.00	53.04	54.6
• where the agreement is made on or after April 1, 1976	10.40	11.44	11.96	10.40	11.64	10.40	10.60	10.92
h) fees for technical services [see Note 7] –								
• where the agreement is made after February 29, 1964 but before April 1, 1976	10.40	11.44	11.96	10.40	11.64	52.00	53.04	54.6
• where the agreement is made on or after April 1, 1976	10.40	11.44	11.96	10.40	11.64	10.40	10.60	10.92
i) any other income	31.20	34.32	35.88	31.20	34.94	41.60	42.43	43.68

<b>Section 196B</b> - Payment/credit of income from units (including long-term capital gains on transfer of such units) to an offshore fund	10.40	11.44	11.96	10.40	11.64	10.40	10.60	10.92
<b>Section 196C</b> - Payment/credit of interest of foreign currency bonds or GDR (including long-term capital gains on transfer of such bonds) (not being dividend referred in section 115-O)	10.40	11.44	11.96	10.40	11.64	10.40	10.60	10.92
<b>Section 196D</b> - Payment/credit of income from securities (not being dividend, short-term or long-term capital gain) to Foreign Institutional Investors	20.80	22.88	23.92	20.80	23.29	20.80	21.21	21.84

**Notes :**

- 1) Under sections 192 tax is deductible from salary. The payer shall calculate salary taxable in the hands of recipient. The amount so determined is subject to tax deduction under sections 192. Under sections 192A, tax is deductible on taxable accumulated balance of provident fund. Under section 195, tax is deductible only if income is taxable in the hands of recipient in India. In any other case, gross payment is subject to tax deduction.
- 2) In Category B, tax is deductible at the above rates or the rates specified in Double Taxation Avoidance Agreements entered into by the Central Government under section 90 (whichever is lower) [section 2(37A)(iii)].
- 3) Tax is not deductible under section 192A, section 193, 194, 194A, 194D, 194DA, 194-I, or 194EE if the recipient makes a declaration in Form No. 15G/15H under the provisions of section 197A.
- 4) Under section 197 the recipient can apply the Assessing Officer in Form No. 13 to get a certificate of lower/no tax deduction. This benefit is, however, not available if tax is deductible under section 192A, section 194B, 194BB, 194E, 194EE, 194F, 194IA, 194LBA, 194LB, 194LC, 196B, 196C or 196D
- 5) Royalty payable by Government or an Indian concern in pursuance of an agreement made by non-resident with the Government or the Indian concern after March 31, 1976, where such royalty is in consideration for the transfer of all or any rights (including the granting of a licence) in respect of copyright in any book on a subject referred to in the first proviso to section 115A(1A) to the Indian concern or in respect of computer software referred to in the second proviso to section 115A(1A), to a person resident in India.
- 6) Not being royalty of the nature referred to above, payable by Government or an Indian concern in

pursuance of an agreement made by non-resident with the Government or the Indian concern and where such agreement is with an Indian concern, the agreement is approved by the Central Government or where it relates to matter included in the industrial policy, the agreement is in accordance with that policy.

- 7) Fees for technical services payable by Government or an Indian concern in pursuance of an agreement made by non-resident with the Government or the Indian concern and where such agreement is with an Indian concern, the agreement is approved by the Central Government or where it relates to matter included in the industrial policy, the agreement is in accordance with that policy.

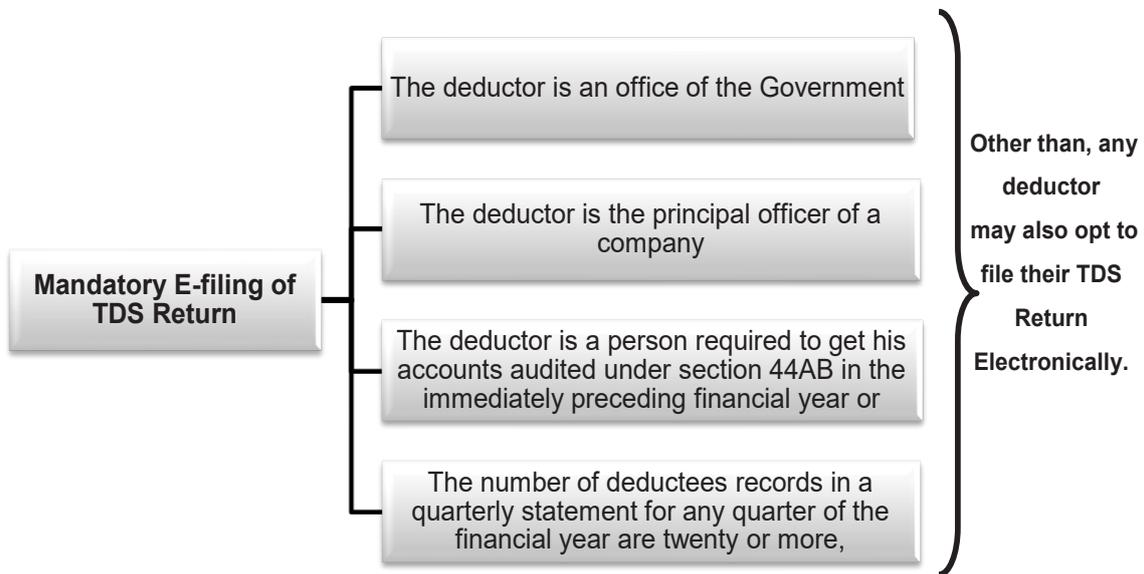
**MINIMUM THRESHOLD LIMIT UPTO WHICH TDS NOT APPLICABLE**

Sr. No.	Particular	Section	Threshold limit
1.	No deduction of tax at source from salaries	192	If net taxable income is less than maximum amount which is not chargeable to tax (Rs. 2,50,000 for an individual, Rs. 3,00,000 for Senior Citizens and Rs. 5,00,000 for Super Senior Citizens)
1A.	No TDS from payment of provident fund account of an employee	192A	If amount paid is less than Rs. 50,000
2.	No TDS from interest paid on debentures issued by a company in which public are substantially interested. Provident interest is paid by account payee cheque to resident individual or HUF	193	If amount paid or payable during the financial year does not exceed Rs. 5,000
3.	No TDS from interest on 8% Saving (Taxable) Bonds 2003 paid to a resident persons	193	If amount paid or payable during the financial year does not exceed Rs. 10,000
3A.	No TDS from interest on 6.5% Gold bonds, 1977 or 7% Gold bonds, 1980 paid to resident individual	193	If a declaration is made that the nominal value of such bonds did not exceed Rs. 10,000 at any time during the previous year
4.	No TDS from dividend paid by account payee cheque to resident persons	194	If amount paid or payable during the financial year does not exceed Rs. 2,500
5.	No TDS from interest other than on securities paid by a banking company or co-operative bank on time deposits	194A	If amount paid or payable during the financial year does not exceed Rs. 40,000. Rs. 50,000 in case of Senior Citizen.
6.	No TDS from interest on deposit with a post office under Senior Citizens Saving Scheme Rules, 2004	194A	If amount paid or payable during the financial year does not exceed Rs. 50,000
7.	No TDS from interest other than on securities (in any other case)	194A	If amount paid or payable during the financial year does not exceed Rs. 5,000
8.	No TDS from interest on compensation awarded by Motor Accident Claims Tribunal	194A	If amount paid or payable during the financial year does not exceed Rs. 50,000
9.	No TDS from Lottery / Cross Word Puzzles	194B	If amount paid or payable during the financial year does not exceed Rs. 10,000

10.	No TDS from winnings from horse races	194BB	If amount paid or payable during the financial year does not exceed Rs. 10,000
11.	No TDS from sum paid or payable to contractor	194C	a) If sum paid or payable to a contractor in a single payment does not exceed Rs. 30,000 b) If sum paid or payable to contractor in aggregate does not exceed Rs. 1,00,000 during the financial year
12.	No TDS from insurance commission paid or payable during the financial year	194D	If amount paid or payable during the financial year does not exceed Rs. 15,000
12A	No TDS from sum payable under a life insurance a police (including bonus) to a resident (w.e.f. 01-10-2014) person	194DA	If amount paid or payable during the financial year does not exceed Rs. 1 lakh
13.	No TDS from payments made out of deposits under NSS	194EE	If amount paid or payable during the financial year does not exceed Rs. 2,500
14.	No TDS from commission paid on lottery tickets	194G	If amount paid or payable during the financial year does not exceed Rs. 15,000
15.	No TDS from payment of commission or brokerage	194H	If amount paid or payable during the financial year does not exceed Rs. 15,000. Further no tax to be deducted from commission payable by BSNL/ MTNL to their PCO Franchisees.
16.	No TDS from payment of rent in respect of land & building, furniture or fittings or plant and machinery	194-I	If amount paid or payable during the financial year does not exceed Rs. 2,40,000
17.	No TDS from payment of consideration for purchase of an immovable property (other than agriculture land)	194-IA	If amount paid or payable during the financial year does not exceed Rs. 50 Lakhs
17A.	No TDS on payment of rent of any land or building or both by an individual/ HUF [whose books of account are not required to be audited under section 44AB] to resident person.	194-IB	If amount of rent does not exceed Rs. 50,000 for a month or part of a month.
18.	No TDS from payment of professional fees, technical fees, royalty and directors' remuneration	194J	If amount paid or payable during the financial year does not exceed Rs. 30,000
19.	No TDS from payment of compensation on compulsory acquisition of immovable property (other than Agricultural Land)	194LA	If amount paid or payable during the financial year does not exceed Rs. 2,50,000
20.	Furnishing of quarterly return in respect of payment of interest (other than interest on securities) to residents without deduction of tax	206A	If amount paid or payable during the financial year does not exceed :  • Rs.10,000 where payer is banking company or co-operative society;  • Rs.5,000 in other case

**E-TDS Return**

E-TDS return is prepared in the form Nos. 24Q, 26Q or 27Q in electronic media as per prescribed data structure either in a floppy or in a CD-ROM. The floppy or CD-ROM prepared should be accompanied by Form No. 27A should be signed and verified in the prescribed manner.. As per Section 206 of the Income Tax Act Corporate and Government deductors are compulsorily required to file their TDS return through electronic media. However, for other deductors filing of e-TDS return is optional and e-TDS return should be filed under Section 206 of the Income Tax Act in accordance with a scheme dated 26th August, 2003 for electronic filing of TDS return vide CBDT Circular No.8 dated 19.09.2003. The CBDT has appointed the Director General of Income Tax (Systems) as e-filing administrator for the purpose of electronic filing of returns of TDS Scheme, 2003. CBDT has also appointed National Securities Depository Limited (NSDL) as e-TDS intermediary. E-TDS return can be filed at any of the TIN-FC opened by the e-TDS intermediary for this purpose. The due date for filing quarterly TDS return both electronic and conventional form remains the same.



**Exemption to Non-Residents from requirement of furnishing PAN U/S 206AA**

Presently requirement of furnishing of PAN as per Section 206AA is also applicable to non-resident assessee also. Section 206AA has been amended to provide that provisions of this section shall not apply to non-resident, not being a company, or to a foreign company, subject to such conditions as may be prescribed.

**ADVANCE PAYMENT OF TAX**

The computation of advance tax liability, under different situations, is to be done as follows :

Section 207-219 of the Income Tax Act deals with the issues relating to advance payment of tax. In advance payment of tax, the assessee has to pay tax in a financial year on estimated income which is to be assessed in the subsequent assessment year. It follows the doctrine known as pay as you earn scheme.

It is obligatory for an assessee to pay advance tax where the advance tax payable is Rs. 10,000 or more (Section 208).

In order to reduce the compliance burden on senior citizens exemption from payment of advance tax section 207 has been amended to provide that resident individual -

- (1) not having any income chargeable under the head "Profits and gains of business or profession" and
- (2) of age 60 years or more need not pay advance tax and are allowed to discharge their tax liability (other than TDS) by payment of self-assessment tax.

#### Due Dates for Payment of Advance Tax

Particulars	In case of all assessee
On or before June 15 of the Previous year	Upto 15% of the Advance Tax due
On or before September 15 of the previous year	Upto 45% of the Advance Tax due as reduced by amount paid in earlier instalments
On or before December 15 of the previous year	Upto 75% of the Advance Tax due as reduced by amount paid in earlier instalments
On or before March 15 of the previous year	Upto 100% of the Advance Tax due as reduced by amount paid in earlier instalments

Any payment of advance tax payable made before March 31 shall be treated as advance tax paid during the financial year.

**Amendment to section 211** : With effect from April 1, 2017 an assessee (who declares his income in accordance with presumptive taxation regime under section 44ADA) shall also be liable to pay advance tax in one instalment on or before March 15 of the financial Year.

**Note** : The above provision also applies for advance tax in respect of presumptive income u/s 44AD w.e.f. AY 2017-18

In case of public holiday or bank holiday, date of payment automatically falls in the next working day and for that delay, interest is not charged under Sections 234B and 234C vide Circular No. 676 dated 14.01.1994.

Tax to be computed at the prevailing rate on the current income of the assessee, in a financial year.

#### Payment of advance tax in case of capital gains/casual income [Proviso to section 234C]

- (1) Advance tax is payable by an assessee on his/its total income, which includes capital gains and casual income like income from lotteries, crossword puzzles etc.
- (2) Since it is not possible for the assessee to estimate his capital gains, income from lotteries, etc., it has been provided that if any such income arises after the due date for any installment, then, the entire amount of tax payable (after considering tax deducted at source) on such capital gains or casual income should be paid in the remaining installments of advance tax which are due.
- (3) Where no such installment is due, the entire tax should be paid by 31st March of the relevant financial year.
- (4) No interest liability under section 234C would arise if the entire tax liability is so paid.

#### Adjustment of Advance Tax

Under Section 219, the total advance tax paid by an assessee other than for interest be adjusted against the total tax liability computed under regular assessment.

Under Section 234B of the Act where an assessee, who is liable to pay advance tax, under Section 208 has failed to pay such tax or where the advance tax paid under Section 210 is less than 90% of the assessed tax, he shall be liable to pay interest @ 1% for every month or part of the month.

Assessee has to pay advance tax even in respect of book profit tax under Section 115JB otherwise it is liable for interest under Sections 234B and 234C.

It is kind of mandatory payment of tax, assessed by the assessee himself on income before completion of the Financial Year.

### Role of Assessing Officer in relation to Advance Payment of Tax

An Assessing Officer (AO) can order payment of advance tax if the following conditions are satisfied :

1. •The assessee has already been assessed by way of regular assessment in respect of total income of any previous year.;
2. •Failure to pay advance tax by such assessee, inspite of legal obligation.
3. •The AO is of the opinion that such person is liable to pay advance tax on current year's income.
4. •The order must specify the amount of advance tax and installments in which advance tax has to be paid.
5. •Such order may be passed during the previous year but not later than last day of February.
6. •The order must be made in writing.

The assessee can pay advance tax at a rate lower than assessment made by the AO and the department cannot object to such assessment, but the assessee has to furnish his own estimate of lower current income in Form No. 28A - Punjab Tractors Ltd. v. CIT (2004) 137 Taxman 211 (Punjab & Haryana).

For higher estimate made by the assessee, Form 28A is not required to be furnished.

The AO will find out the current income on the following basis :

- (i) Total income of the latest previous year in respect of which the assessee has been assessed by way of regular assessment;
- (ii) The total income returned by the assessee for any previous year subsequent to the previous year for which regular assessment is made. whichever is higher;

AO can revise his order passed under Section 210(3) [Section 210(4)]

If after making the order under section 210(3), but before 1st March of the relevant financial year a return has been furnished by the assessee, (b) a regular assessment of the assessee is made, in respect of a later previous year, for a higher figure, then the Assessing officer may revise or amend his order.

On receipt of the order the assessee have to pay the advance tax accordingly.

**Illustration 1 :**

Calculate Advance Tax Payable by Arun from the following estimated incomes for the previous year 2019-20 :

- Business Income : Rs. 4,75,000;
- Rent from house property : Rs. 36,000 per month;
- Municipal taxes : Rs. 27,000;
- Winning from games : Rs. 70,000 (net of TDS);
- Life insurance premium paid for himself (sum assured : Rs. 5,00,000) : Rs. 30,000;

**Solution****Computation of Advance Tax payable by Arun for Previous Year 2019-20 (Assessment Year 2020-21)**

**Step 1 :** Compute Estimated Total Income for the year :

Particulars	Rs.	Rs.
<b>Income from house property :</b>		
Gross Annual Value [Rental Income (36,000 x 12)]	4,32,000	
Less : Municipal taxes paid by owner	(27,000)	
Net Annual Value (NAV)	4,05,000	
Less : Standard Deduction @ 30% of NAV	(1,21,500)	2,83,500
Profits and gains of Business or Profession		4,75,000
<b>Income from other sources :</b>		
Winning from games (gross) [70000 x 100/100 - 30%]		1,00,000
<b>Gross Total Income (GTI)</b>		<b>8,58,500</b>
Less : Deductions under Section 80C		(30,000)
<b>Total Income</b>		<b>8,28,500</b>

**Step 2 :** Computation Estimated of Tax Liability and Advance Tax Payable

Particulars	Rs.	Rs.
<b>Tax on :</b>		
Winning from Games @ 30% [1,00,000 x 30%]	30,000	
Balance Income @ Slab Rate [12,500 + 20% of (7,28,500 - 5,00,000)]	58,200	
Tax Payable		88,200
Add : Surcharge, if any		Nil
Add : Cess @ 4%		3,528

<i>Tax Liability Less : TDS</i>		91,728
Advance Tax Liability		(30,000)
Advance Tax		61,728
Advance Tax (Rounded off)		<b>61,730</b>

**Step 3 :** Advance tax instalments - Advance tax is payable as follows :

Upto	% (Rate)	Cumulative (Rs.)	Each instalment (Rs.)
15.06.2019	15	9,259 [61,730x15%]	9,259
15.09.2019	45	27,778 [61,730x45%]	18,519
15.12.2019	75	46,297 [61,730x75%]	18,519
15.03.2020	100	61,730 [61,730x100%]	15,433

### Illustration 2 :

Red Ltd. (an Indian company) has estimated its income for previous year 2019-20. Calculate advance tax payable by it from the following :

- Business Income : Rs. 10,80,000;
- Income from house property (after deduction under section 24) : Rs. 7,20,000;
- Long term capital gain (LTCG) on transfer of immovable property on 1st November, 2017 : Rs. 3,60,000;
- Interest on bank deposits (other than saving bank account) : Rs. 45,000.
- TDS on business income and interest was Rs. 60,000
- Deduction under section 80G is Rs.1,00,000.

### Solution

**Computation of advance tax payable by Red Ltd. for Previous Year 2019-20 (Assessment Year 2020-21) :**

**Step 1 :** Compute Estimated total income for the year :

Particulars	Rs.
Profits and gains of Business or Profession	10,80,000
Income from house property	7,20,000
LTCG	3,60,000
Income from other sources :	
Interest on bank deposits	45,000
Gross Total Income (GTI)	22,05,000
Less : Deductions under Section 80G	(1,00,000)
<b>Total Income</b>	<b>21,05,000</b>

**Step 2 : Computation of Estimated Tax Liability and Advance Tax Payable**

Particulars	Rs.	Rs.
<b>Tax on :</b>		
LTCG @ 20% (3,60,000 x 20%)	72,000	
Balance Income @ 30% [(21,05,000 - 3,60,000) x 30%]	5,23,500	5,95,500
Add : Surcharge, if any		Nil
Add : Cess @ 4%		23,820
Tax Liability		6,19,320
Less : TDS		(60,000)
<b>Advance Tax Liability</b>		<b>5,59,320</b>
<b>Advance Tax (rounded off)</b>		<b>5,59,320</b>

**Step 3 : Advance Tax Instalments - Advance Tax is payable as follows :**

**Note :** Advance Tax is payable by all Assessee in four installments during the previous year i.e. by 15th June (15%), 15th September (45%), 15th December (75%) and 15th March (100%). However, in case of LTCG arising after one or more installments, advance tax on installments prior to date of LTCG can be paid without including tax on LTCG and advance tax on installments after LTCG must be paid in the remaining installments on the amount of total tax liability including that on LTCG.

Therefore, in this case, advance tax payable by 1st and 2nd installment would be based on Tax excluding Tax on LTCG and advance tax payable by 3rd and 4th installment would be based on tax including tax on LTCG.

Tax excluding tax on LTCG : Rs. 5,23,500 + Cess @ 4% =Rs. 5,44,440 -TDS Rs. 60,000 = Rs.4,84,440

Upto	Cumulative %	Cumulative (Rs.)	Each installment (Rs.)
15.06.2019	15	72,666 [4,84,440x15%]	72,666
15.09.2019	45	2,17,998 [4,84,440x45%]	1,45,332
15.12.2019	75	4,19,490 [5,59,320x75%]	2,01,492
15.03.2020	100	5,59,320 [5,59,320x100%]	1,39,830

**SELF-ASSESSMENT TAX (SAT)**

Self assessment tax means tax paid by the assessee on the basis of self assessment before filing of return of Income. Self Assessment is simply a process where a person himself assesses his tax liability himself on the income earned during the particular previous year and submits Income Tax Return to the department. Every person, before furnishing return under sections 139(return of income), 142(1), 148 (issue of notice where income has escaped assessment) and 153A (Assessment in case of search or requisition) shall make self assessment of his income and pay the tax, if due on the basis of such assessment. The total tax payable is calculated on the total income of the assessee after considering the following amount :

- (i) the amount of tax already paid under any provision of this Act;
- (ii) any tax deducted or collected at source;
- (iii) any relief of tax or deduction of tax claimed under section 90 or section 91 on account of tax paid in a country outside India;

- (iv) any relief of tax claimed under section 90A on account of tax paid in any specified territory outside India referred to in that section; and
- (v) any tax credit claimed to be set off in accordance with the provisions of section 115JAA or section 115JD.

In case in delay in furnishing of return of income self assessment tax shall also include interest for delay and fee for delay under section 234F.

Such determined value of tax along with the interest payable under any provision of this Act for any delay in furnishing the return or any default or delay in payment of advance tax is paid before furnishing the return and the proof of payment of such tax is attached with the return. Such amount paid before furnishing of return is Known as Self Assessment Tax.

## RETURNS

### RETURN OF INCOME [(SECTION 139(1)]

The procedure under the Income-tax Act for making an assessment of income begins with the filing of a return of income. Section 139 of the Act contains the relevant provisions relating to the furnishing of a return of income. According to that section, it is statutorily obligatory for every person being a company or a firm or being a person other than a company or firm to furnish a return of his total income or the total income of any other person in respect of which he is assessable under the Income-tax Act, in all cases where his total income or the total income of any other person for which he is liable to be assessed before claiming any deduction under chapter VI-A exceeds, in any relevant previous year, the maximum amount which is not chargeable to income-tax. The return of income must be furnished by the assessee in the manner prescribed by the Board from time to time.

It should be obligatory for the firm to file return of income in every case. Further, in respect of individual, HUF, AOP, BOI, Artificial juridical Person, filing of return of income shall be compulsory if their total income before allowing deductions under sections 10A, 10B, 10BA or chapter VI-A exceeds the maximum amount which is not chargeable to income tax.

### Compulsory filing of Income Tax return in relation to Assets located outside India

It is mandatory to file a return of income where a person, being a resident other than not ordinarily resident in India and who during the previous year has any asset or is a beneficial owner of any asset or is a beneficiary of any asset (including any financial interest in any entity) located outside India or signing authority in any account located outside India.

In such a case, it is immaterial that the taxable income is less than the maximum amount not chargeable to tax.

The difference between beneficial ownership and beneficiary has been clarified by way of an explanation which suggests that “beneficial owner” in respect of an asset means an individual who has provided, directly or indirectly, consideration for the asset for the immediate or future benefit, direct or indirect, of himself or any other person and “beneficiary” in respect of an asset means an individual who derives benefit from the asset during the previous year and the consideration for such asset has been provided by any person other than such beneficiary.

A person shall be mandatorily required to file his return of income, –

- (i) if during the previous year has deposited an amount or aggregate of the amounts exceeding one crore rupees in one or more current account maintained with a banking company or a co-operative bank; or
- (ii) has incurred expenditure of an amount or aggregate of the amounts exceeding two lakh rupees for himself or any other person for travel to a foreign country; or

## 502 EP-TL

- (iii) has incurred expenditure of an amount or aggregate of the amounts exceeding one lakh rupees towards consumption of electricity; or
- (iv) fulfils such other prescribed conditions, as may be prescribed.

It is further provided that a person who is claiming such rollover benefits on investment in a house or a bond or other assets, under sections 54, 54B, 54D, 54EC, 54F, 54G, 54GA and 54GB of the Act, shall necessarily be required to furnish a return, if before claim of the rollover benefits, his total income is more than the maximum amount not chargeable to tax.

### Due date for filing return of income

The assessee is obliged to voluntarily file the return of income without waiting for the notice of the Assessing Officer calling for the filing of the return.

The due date for filing of the return by an assessee if his total income of any other person in respect of which he is assessable exceeds the maximum amount not chargeable to tax, shall be as follows :

- (a) 30th day of September of the Assessment Year, where the assessee is -
  - (i) a company,
  - (ii) a person, other than a company whose accounts are required to be audited under the Income-tax Act or any other law, for the time being in force,
  - (iii) a working partner of a firm whose accounts are required to be audited under this Act or under any law for the time being in force..
- (b) 30th day of November of the assessment year, in the case of an assessee who is required to furnish a report referred to in section 92E.
- (c) 31st day of July of the Assessment Year, in the case of any other assessee.

### E-filing of Return

Filing of Income Tax Returns is a legal obligation of every person who total for the previous year exceeds the exemption limit provided under the Income Tax Act, 1961. The Income Tax Department has introduced on line facility in addition to conventional method to file return of income. The process of electronically filing of Income Tax return through the mode of internet access is called e-filing of return. It is mandatory to file the income tax returns online for all the registered taxpayers, However, paper returns can be filed by those who are above 80 years of age and do not have any income from regular business or profession. The only obligation for the user of this facility is to have a PAN number. There are different forms from ITR- 1 to ITR-7 for e-filing of returns. There is a provision e-filing for digital signature by the assessee.

### Income Tax Return Forms notified Notification No. 16/2018, dated 3-4-2018

The CBDT has notified Income-tax Return Forms (ITR Forms) for the Assessment Year 2019-20 vide this Notification. The ITR Forms and its applicability have been detailed below:

ITR Form No	Applicability
1	A one page simplified ITR 1 (SAHAJ) can be filed by an individual who is resident other than not ordinarily resident, having income from salaries, one house property, income from other sources (interest etc.). and having total income upto Rs. 50 lakh.

2	Individuals and HUFs having not having income from business or profession shall be eligible to file ITR 2.
3	Individuals and HUFs having income under the head “Profits and gains of business or profession” have to file ITR 3.
4	ITR 4 (SUGAM) can be used by eligible assesseees having presumptive income from business or profession. Thus, eligible assesseees having only presumptive income under section 44AD, 44ADA or 44AE, under the head “Profits and gains of business or profession” have to file return in ITR 4. In addition, they may have salary income, income from house property and income from other sources (excluding winnings from lottery and income from race horses). Any person having agricultural income in excess of Rs. 5,000 cannot use ITR 4. Further, a person claiming relief of foreign tax paid under section 90, 90A or 91 cannot use this form. Also, this form cannot be used by a resident having any asset (including financial interest in any entity) located outside India or signing authority in any account located outside India and by a resident having income from any source outside India.
5	ITR 5 can be used by persons other than individual, HUF, company and person filing Form ITR 7.
6	ITR 6 can be used by companies other than companies claiming exemption under section 11.
7	ITR 7 can be used by persons including companies required to furnish return under sections 139(4A) or 139(4B) or 139(4C) or 139(4D) or 139(4E) or 139(4F).

All these ITR Forms are to be filed electronically. However, where return is furnished in ITR Form-1 (SAHAJ) or ITR-4 (SUGAM), the following persons have an option to file return in paper form:

an Individual of the age of 80 years or more at any time during the previous year; or

an Individual or HUF whose income does not exceed five lakh rupees and who has not claimed any refund in the Return of Income.

### Bulk Filing of Return

Finance Act, 2002 has introduced a new scheme of Bulk Filing of Return vide new Section 139(1A). According to the new provisions, any person, being an individual who is in receipt of income chargeable under the head “Salaries” may, at his option, furnish a return of his income for any previous year to his employer, in accordance with such scheme as may be specified by the Board in this behalf. The employer shall furnish all returns of income received by him on or before the due date, in such form (including on a floppy, diskette, magnetic cartridge tape, CD-ROM or any other computer readable media) and manner as may be specified in that scheme, and in such case, any employee who has filed a return of his income to his employer shall be deemed to have furnished a return of income under

Section 139(1) and the provisions of this Act shall apply accordingly.

However, the following returns of employees cannot be submitted under the above schemes :

- I. return of a year other than the current year;
- II. return without PAN;
- III. return under Block assessment;
- IV. return of an employee having more than one employer.

### Power to Central Government

Section 139(1C) empower the Central Government to exempt any class or classes of persons from the requirement of furnishing a return of income by issue notification in the Official Gazette.

#### Return of Loss [Section 139(3)]

The requirements of Income-tax Act making it obligatory for the assessee to file a return of his total income even in cases where the assessee has incurred a loss under the head 'profits and gains from business or profession' or loss from maintenance of race horses or under the head 'Capital gains'. However, loss under the head "Income from house property" under section 71B and unabsorbed depreciation under section 32 can be carried forward for set-off even though return of loss has not been filed before the due date. Unless the assessee files a return of loss in the manner and within the same time limits as required for a return of income, the assessee would not be entitled to carry forward the loss for being set off against income in the subsequent year.

#### Belated Return [Section 139(4)]

Any person who has not filed the return within the time allowed under section 139(1) may file a belated return

- at any time before the end of the relevant assessment year or
- before the completion of the assessment whichever is earlier.

**Example :** For the previous year 2019-20, Mr. X did not file the return of income on the due date. Can Mr. X file the return of income after the due date?

Correct answer. Yes, As per section 139(4), Mr. X can file a belated return. Mr. X may file the return of income at any time on or before 31st of March 2021 (anytime before the end of the relevant Assessment Year 2020-21).

#### Return of Income of charitable trust and institutions [Section 139(4A)]

Sub-section (4A) of Section 139 also makes it incumbent of "every person in receipt of income derived from property held under trust or other legal obligation wholly for charitable or religious purposes or in part only for such purposes or of income being voluntary contributions within the meaning of Section 2(24)(iia)" to furnish a return of income in case the total income exceeds the maximum amount not chargeable to tax.

Further, one who is assessable as a representative assessee for the receipt of income derived from property held under Trust or other legal obligation wholly for charitable or religious purposes or in part only for such purposes or of income being voluntary contributions shall furnish a return of income of the previous year in the prescribed form and get it verified in such manner as prescribed under Section 139(1), if the total income (without giving effect to the provisions of Sections 11 and 12) exceeds the amount not chargeable to tax.

#### Return of Income of Political Party [Section 139(4B)]

It is also incumbent on the political parties to file their return of income [if the income (without giving effect to the provisions of Section 13A) exceeds the maximum amount not chargeable to tax], duly signed by the Chief Executive Officer of the party

#### Return of Income of Specified Association/Institutions [Section 139(4C)]

Following persons are required to file the return :

- (a) Research association referred to in Section 10(21);
- (b) news agency referred to in Section 10(22B);

- (c) association or institution referred to in Section 10(23A);
- (d) institution referred to in Section 10(23B);
- (e) fund or institution referred to in sub-clause (iv) or trust or institution referred to in sub-clause (v) or any university or other educational institution referred to in sub-clause (iiiab) or sub-clause (iiiad) or sub-clause (vi) or any hospital or other medical institution referred to in sub-clause (iiiac) or sub-clause (iiiiae) or sub-clause (via) of clause (23C) of section 10;
- (ea) Mutual Fund referred to in clause (23D) of section 10;
- (eb) securitisation trust referred to in clause (23DA) of section 10;
- (ec) venture capital company or venture capital fund referred to in clause (23FB) of section 10;
- (f) trade union referred to in Section 10(24)(a) or 10(24)(b),
- (g) body or authority or Board or Trust or Commission in section 10(46)
- (h) infrastructure debt fund referred to in section 10(47) or Mutual Fund or Securitisation Trust or venture capital company or venture capital fund.

**Scope of Section 139(4C) is expanded to include an assessee who is qualified to exemption under section 10(23AAA),(23EC),(23ED),(23EE), (29A). [Amendment vide Finance Act, 2017 w.e.f. AY 2019-20]**

The above persons shall, if the total income, without giving effect to the provisions of Section 10, exceeds the maximum amount which is not chargeable to income-tax, furnish a return of such income of the previous year in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed and all the provisions of this Act shall, so far as may be, apply as if it were a return required to be furnished under Section 139(1)".

#### **Revised Return [Section 139(5)]**

An assessee who is required to file a return of income is entitled to revise the return of income originally filed by him to make such amendments, additions or changes as may be found necessary by him. Such a revised return may be filed by the assessee at any time

- before the expiry of the relevant assessment year
- before the completion of assessment whichever is earlier.

Presently, if any person having furnished the return u/s 139(1) or sub-section (4) discovers any omission or any wrong statement therein, he may furnish a revised return at any time before the end of the relevant A.Y. or before the completion of the assessment, whichever is earlier.

Revised return can be further revised upto any number of times, within the prescribed period.

#### **Defective Return [Section 139(9)]**

If the Assessing Officer considers that the return of income furnished by the assessee is defective, he may intimate the defect to the assessee and give him an opportunity to rectify the defect within 15 days from the date of such intimation or within such further period as may be allowed by the Assessing Officer on the request of the assessee. If the assessee fails to rectify the defect within the aforesaid period, the return shall be deemed to be invalid and further it shall be deemed that the assessee had failed to furnish the return. However, where the assessee rectifies the defect after the expiry of the aforesaid period but before the assessment is made, the Assessing Officer may condone the delay and treat the return as a valid return.

If the self assessment tax is not paid on or before the date of furnishing the return of income, return shall be considered as defective return.

A return of income shall be regarded as a defective return unless all the following conditions are fulfilled :

- (a) the annexures, statements and columns in the return of income relating to computation of income chargeable under each head of income, computation of gross total income and total income have been duly filled in;
- (b) the return is accompanied by a statement showing the computation of tax payable on the basis of return as well as the report of audit obtained under Section 4AB;
- (bb) the return is accompanied by the report of the audit referred to in section 44AB, or, where the report has been furnished prior to the furnishing of the return, by a copy of such report together with proof of furnishing the report;
- (c) the return is accompanied by proof of :
  - (i) the tax, if any, claimed to have deducted at source and the advance tax and tax on self-assessment, if any, claimed to have been paid;
  - (ii) the amount of compulsory deposit, if any, claimed to have been made (The scheme has been abolished w.e.f. 1.4.1985).

But a return shall not be called defective where it is not accompanied by proof of the tax, if any, claimed to have been deducted at source, if :

- (a) a certificate for tax deducted was not furnished under Section 203 to the person furnishing his return of income;
- (b) such certificate is produced within a period of two years specified under Sub-section (14) of Section 155”.
- (d) where the regular books of account are maintained by the assessee, the return is accompanied by copies of :
  - (i) manufacturing account, trading account, profit and loss account or income and expenditure account or any similar account and balance sheet;
  - (ii) in the case of proprietary business or profession, the personal account of the proprietor; in the case of a firm, association of persons or body of individuals, personal accounts of the partners or members; and in the case of a partner or member of a firm, association of persons or body of individuals, also his personal account in the firm, association of persons or body of individuals.
- (e) where the accounts of the assessee have been audited, the return is accompanied by copies of the audited profit and loss account and balance sheet and auditors' report; and where an audit of cost accounts of the assessee has been conducted under Section 233B of the Companies Act, 1956 also the report under that section.
- (f) where regular accounts are not maintained by the assessee, the return is accompanied by a statement indicating the amounts of turnover or gross receipts, gross profit, expenses and net profit of the business or profession and the basis of which such amounts have been computed, and also disclosing the amounts of total sundry debtors, sundry creditors, stock-in-trade and cash balance as at the end of the previous year.

**Note :** Not relevant now as the assessee has to furnish annexure less return of income from assessment year 2007-08 and onwards.

A return of income is regarded as defective unless the self assessment tax together with interest, if any, payable in accordance with section 140A has been paid on or before the date of furnishing of return.

Section 139(9) of the Act has been amended to provide that a return which is otherwise valid would not be treated defective merely because self assessment tax and interest payable in accordance with the provisions of section 140A, has not been paid on or before the date of furnishing of the return.

### **SIGNING OF RETURN [SECTION 140]**

The return of income must be verified :

- (a) In the case of an individual,
  - (i) by the individual himself;
  - (ii) where he is absent from India, by the individual himself or by some person duly authorised by him in this behalf;
  - (iii) where he is mentally incapacitated from attending to his affairs, by his guardian or any other person competent to act on his behalf; and
  - (iv) where, for any other reason, it is not possible for the individual to verify the return, by any person duly authorised by him in this behalf :

Provided that in a case referred to in Sub-clause (ii) or (iv), the person verifying the return holds a valid power of attorney from the individual to do so, which shall be attached to the return :

- (b) in the case of a H.U.F. by the Karta, and, where the karta is absent from India or mentally incapacitated from attending to his affairs, by any other adult member of such family;
- (c) in the case of a local authority, the Principal Officer thereof;
- (d) in the case of a firm, by managing partner thereof or where for any unavoidable circumstances such managing partner is not able to verify the return, or where there is no managing partner as such, by any partner thereof, not being a minor;
- (e) in the case of a limited liability partnership, by the designated partner thereof, or where for any unavoidable reason such designated partner is not able to verify the return, or where there is no designated partner as such, by any partner.
- (f) in the case of any other association, by any member of the association or Principal Officer thereof;
- (g) in the case of any other person, by that person or some person competent to act on his behalf;
- (h) in the case of a company; by the managing director thereof, or where for any unavoidable reason such managing director is not able to verify the return or where there is no managing director, by any director thereof.

Provided that where the company is not resident in India, the return may be verified by a person who holds a valid power of attorney from such company to do so, which shall be attached to the return :

Insolvency professional to verify the return of income where application for Corporate Insolvency has been admitted.

Provided further that –

- (a) where the company is being wound up, whether under the order of a court or otherwise, or where any person has been appointed as the receiver of any assets of the company, the return shall be verified by the liquidator referred to in Sub-section (1) of Section 178;

- (b) where the management of the company has been taken over by the Central Government or any State Government under any law, the return of the company shall be verified by the Principal Officer thereof;
- (i) in the case of a political party referred-to in Sub-section (4B) of Section 139, by the Chief Executive Officer of such party whether such Chief Executive Officer is known as secretary or by any other designation.

### **Scheme to facilitate submission of returns through tax return preparers [Section 139B] [W.E.F. 1-6-2006]**

W.e.f. 1.6.2006, a new section 139B have been inserted in the Act so as to provide that for the purpose of enabling any specified class or classes of persons to prepare and furnish returns of income, the Board may, by way of notification, frame a scheme providing that such persons may furnish their returns of income through a Tax return preparer authorized to act as such under the scheme. This scheme is not applicable for a company or a person who is required to undergo a 'tax audit' or 'audit under any other law'.

It has been further provided that the Scheme framed under the said section shall specify the manner in which the Tax return preparer shall assist the persons furnishing the return of income, and shall also affix his signature on such return.

A Tax return preparer may be an individual other than a person referred to in clause (ii) or clause (iii) or clause (iv) of sub-section (2) of section 288 or an employee of the specified class or classes of persons, who has been authorized to act as a Tax return preparer under this Scheme.

In other words, the following persons are not authorized to act as Tax return preparer :

- any officer of a scheduled bank in which the assessee maintains a current account or has regular dealings.
- A legal practitioner; or
- A chartered accountant.

### **Educational qualification for Tax Return Preparers(TRP) notified vide Notification No. 4/2018, dated 19-01-2018 :**

An individual, who holds a bachelor degree from a recognised Indian University or institution, or has passed the intermediate level examination conducted by the Institute of Chartered Accountants of India or the Institute of Company Secretaries of India or the Institute of Cost Accountants of India, shall be eligible to act as TRP.

The Scheme notified under the said section shall provide the manner in which a Tax return preparer shall be authorized, the educational and other qualifications to be possessed, and the training and other conditions required to be fulfilled, by a person to act as a Tax return preparer, the code of conduct for the Tax return preparer, the duties and obligations of the Tax return preparer, the manner in which the authorization may be withdrawn and any other matter which is required to be or may be specified.

## **FEE AND INTEREST**

### **Interest for belated payment of Income-Tax [Section 220(2)]**

An assessee is liable to pay interest @ 1% for every month or part thereof comprised in the period intervening between the expiry of 30 days w.e.f. serving of the notice of demand and actual payment of tax for the delay in making the payment of tax demanded beyond 30 days from the date of receipt of the demand notice.

Sub-section (2A) of Section 220, empowers the Board to reduce or waive the amount of interest payable by an assessee under the above section on the recommendation made by the Chief Commissioner or Commissioner in this behalf. The Board's order will be passed only upon satisfaction that :

- (a) the payment of such interest has caused or would cause genuine hardship to the assessee;
- (b) the default in the payment of the amount on which interest has been paid or was payable was due to circumstances beyond the control of the assessee; and
- (c) the assessee has co-operated in any enquiry relating to the assessment or any proceeding for recovery of any amount due from him.

Provided that the order accepting or rejecting the application of the assessee, either in full or in part, shall be passed within a period of twelve months from the end of the month in which the application is received. Further no order rejecting the application, either in full or in part, shall be passed unless the assessee has been given an opportunity of being heard.

Provided also that where any application is pending as on the 1st day of June, 2016, the order shall be passed on or before the 31st day of May, 2017.

### **Interest for default in furnishing Return of Income [Section 234A]**

In cases where a return on income is furnished after the due date or is not furnished at all, the assessee has to pay simple interest at the rate of 1% per cent for every month or part of the month of default on the amount of tax on the total income as determined under sub-section (1) of Section 143, and where a regular assessment is made, on the amount of the tax or the total income determined under regular assessment or reduced by an amount of (1) advance tax if paid; (2) any TDS/TCS; (3) any relief under Sections 90, 90A; (4) any deduction under Sections 91; (5) any tax credit under the provisions of Section 115JAA(6) Relief U/s 89.

The period for which the interest is payable commences from the date immediately following the due date for filing the return and ending on the date of furnishing of the return. Where the return is not furnished, the interest will be payable from the due date for filing the return till the date of completion of assessment.

### **Interest for default in payment of Advance Tax [Section 234B]**

Where the assessee, liable to pay advance tax, has not remitted the same or Where the advance tax paid is less than 90 per cent of assessed tax.

He has to pay simple interest on assessed tax means the tax on the total income determined under subsection(1) of section 143 and where a regular assessment is made, the tax on the total income determined under such regular assessment as reduced by the amount of (1) advance tax, if any paid; (2) any TDS/TCS; (3) any relief under Sections 90, 90A; (4) any deduction under Section 91; (5) any tax credit under provision of Section 115JAA (6) Relief U/s 89 @1% percent for every month or part of month from 1st day April next following such financial year to the date of determination of total income under section 143(1) and where a regular assessment is made, to the date of such regular assessment.

In cases where the assessee has paid tax on the basis of self assessment under Section 140A, before the date of completion of a regular assessment, the interest is calculated on above basis upto the date of payment of tax under Section 140A and, the thereafter, on the amount by which the advance tax and tax paid under Section 140A fall short of advance tax.

In the cases of enhancement or reduction of the amount on which interest was payable under Section 147 (income escaping assessment) or Section 153A;

Section 154 (rectification of mistake); Section 155 (other amendments on completed assessment of a partner in a firm; member of an AOP or body of individuals etc.); Section 250 (appeal); Section 254 (orders of the Appellate Tribunal); Section 260 (Decision of High Court or Supreme Court on the case stated; Section 262 (hearing before Supreme Court); Section 263 (revision of orders prejudicial to revenue); Section 264 (Revision of orders); or 245D(4) [order of the Settlement Commission, the interest shall be increased or reduced correspondingly. Where the interest has already been paid to the assessee, a notice of demand, calling for payment of such

amount, has to be served on the assessee by the Assessing Officer. Such notice of demand shall be deemed to be an order under Section 156 of the Act.

### Interest for deferment of Advance Tax [Section 234C]

(a) If the assessee who is liable to pay advance tax under Section 208 has failed to pay such tax or has underestimated the instalments of advance tax, he has to pay interest as follows :

- (i) If advance tax paid on or before 15 June is less than 15% of tax due on total income declared in the return or If advance tax paid on or before 15 September is less than 45% of tax due on total income declared in the return filed by the assessee or If advance tax paid on or before 15 December is less than 75% of tax due on total income declared in the return the assessee shall pay simple interest @ 1% per month for a period of three months on the amount of the shortfall from 15%, 45%, and 75% of the tax due on the returned income.
- (ii) If advance tax paid on or before March 15 is less than 100% of tax due on total income declared in the return, as reduced by tax deducted at source, simple interest is payable @ 1% per month on the amount of shortfall from the tax due on the returned income declared.

Provided that if the advance tax paid by the assessee on the current income, on or before the 15th day of June or the 15th day of September, is not less than 15% or, as the case may be, 45% of the tax due on the returned income, then, the assessee shall not be liable to pay any interest on the amount of the shortfall on those dates.

(b) an eligible assessee in respect of the eligible business referred to in section 44AD, who is liable to pay advance tax under section 208 has failed to pay such tax or the advance tax paid by the assessee on its current income on or before the 15th day of March is less than the tax due on the returned income, then, the assessee shall be liable to pay simple interest at the rate of 1% on the amount of the shortfall from the tax due on the returned income.

**Amendment to Section 234C(1)** : In respect of an assessee (who declares his income in accordance with presumptive taxation regime under section 44ADA), interest under this section shall be levied, if the advance tax paid on or before March 15, is less than the tax due on the returned income.

The following explanation shall be substituted w.e.f. 1.4.2007, namely :

*“Explanation : In this section “tax due on the returned income” means the tax chargeable on the total income declared in the return of income furnished by the assessee for the assessment year commencing on the 1st day of April immediately following the financial year in which the advance tax is paid or payable, as reduced by the amount of,- (1) any TDS/TCS (2) any relief of tax under Section 90 or 90A (3) any deduction under Section 91 (4) any tax credit u/s 115JAA.”*

Amendment to section 234C : With effect from AY 2019-20 any shortfall in payment of advance tax is on account of under estimation or failure in estimation of the income of the nature referred to in section 115BBDA, interest under section 234C shall not be levied subject to fulfilment of the fact that assessee has deposited the whole amount of tax in respect of such income as a part of remaining instalments of advance tax or if no instalment is due then tax is deposited before the end of financial year.

### Fees for Delay in Furnishing Return of Income [Section 234F]

Following are the provisions of this section-

- i. A fee of Rs. 5,000 shall be levied if Return of income is filed after the due date of return u/s 139(1) but on or before 31st December of the Assessment Year.
- ii. A fee of Rs. 10,000 shall be paid in case return is not filed up-to 31st December of the Assessment Year.

- iii. In cases where the total income does not exceed Rs 5,00,000, the fee amount shall not exceed Rs. 1,000.

Consequently provisions of Section 271F relating to penalty in respect of failure to furnish return of income shall not apply from assessment year 2019-20.

## COLLECTION AND RECOVERY OF TAX



### (a) Notice of Demand [Section 156] [Rules 15, 38, Forms 7, 28]

When any tax, interest penalty, fine or any other sum is payable in consequence of any order passed under this Act, the Assessing Officer shall serve upon the assessee a notice of demand in the prescribed form specifying the sum so payable.

Provided that where any sum is determined to be payable by the assessee or [the deductor or the collector under sub-section (1) of section 143 or sub-section (1) of section 200A or sub-section (1) of section 206CB], the intimation under those sub-sections shall be deemed to be a notice of demand for the purposes of this section.

### (b) Intimation of loss [Section 157]

When in the course of the assessment of the total income of any assessee, it is established that a loss has taken place which the assessee is entitled to have carried forward and set off against the income in subsequent years, the Assessing Officer shall notify to the assessee by an order in writing the amount of the loss as computed by him for the purposes of carry forward and set off.

### (c) Assessee in Default

The amount specified in the notice of demand shall be paid within 30 days of the service of the notice at the place and to the person mentioned in the notice. If the Assessing Officer has any reason to believe that it will be detrimental to revenue if the full period of 30 days is allowed he may, with the prior approval of the Joint Commissioner reduce the period as he thinks fit (Section 220).

If the amount specified in the notice of demand is not paid within the period mentioned in the notice, the assessee shall be liable to pay simple interest at one per cent for every month or part of a month comprised in the period commencing from the day immediately following the end of the 30 days or shorter period, as allowed, and ending with the date of payment of the tax. If the assessee is not in a position to pay the amount in the prescribed time, he may submit an application to the Assessing Officer before the expiry of the due date of the payment. On receipt of such application, the Assessing Officer may extend the time for payment or allow payment by instalments, subject to such conditions as he may think fit to impose. If the amount is not paid as mentioned above, the assessee shall be deemed to be in default and shall be liable to pay in addition to the amount of the arrears and the amount of interest, by way of penalty such amount as the Assessing Officer may direct. In the case of continuing default, he shall be liable to pay such further amount as the Assessing Officer may, from time to time, direct. However, the total amount of penalty shall not exceed the amount of tax in arrears.

Where an assessee is in default or is deemed to be in default in making a payment of tax, the Tax Recovery

## 512 EP-TL

Officer may draw up under his signature a statement in the prescribed form specifying the amount of arrears due from the assessee and shall proceed to recover from such assessee the amount specified in the certificate (being the statement referred to above) by one or more of the modes mentioned below, in accordance with the rules laid down in the Second Schedule.

- (A) (i) attachment and sale of the assessee's movable or immovable property;
  - (ii) arrest of the assessee and his detention in prison; and
  - (iii) appointing a receiver for the management of the assessee's movable and immovable properties (Section 222).
- (B) The Assessing Officer may also recover the tax by any one or more of the following modes of recovery :
  - (i) attachment of salary;
  - (ii) garnishee order from a court ;
  - (iii) sale of movable property (Section 226);
- (C) Through State Government (Section 227);
- (D) In pursuance of agreement with foreign countries (Section 228A);
- (E) By suit or under other law (Section 232).

**Note :** For details please refer to the relevant sections of the Act.

Notwithstanding anything contained in sub-section (2), the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner may reduce or waive the amount of interest paid or payable by an assessee under the said sub-section if he is satisfied that -

- (i) payment of such amount has caused or would cause genuine hardship to the assessee;
- (ii) default in the payment of the amount on which interest has been paid or was payable under the said sub-section was due to circumstances beyond the control of the assessee; and
- (iii) the assessee has co-operated in any inquiry relating to the assessment or any proceeding for the recovery of any amount due from him :

Provided that the order accepting or rejecting the application of the assessee, either in full or in part, shall be passed within a period of twelve months from the end of the month in which the application is received :

Provided further that no order rejecting the application, either in full or in part, shall be passed unless the assessee has been given an opportunity of being heard. Provided also that where any application is pending as on the 1st day of June, 2016, the order shall be passed on or before the 31st day of May, 2017.

### **REFUNDS (SECTION 237 TO SECTION 245)**

Refund means "to repay" or restore what was taken under the income-tax law. Refunds arise in those cases where the amount of tax paid by a person or on his behalf is greater than the amount with which he is properly chargeable for that year. Under the following circumstances the refunds may become due :

- (i) The tax deducted at source is higher than the amount of tax payable, as determined on regular assessment;
- (ii) The amount of advance tax paid or tax paid on the basis of self- assessment exceeds the tax payable as determined on regular assessment;
- (iii) The tax determined and paid on the basis of regular assessment gets reduced as a result of rectification of mistake which had crept in the assessment or is reduced in appeal or revision;

- (iv) The same income is taxed in India and in a foreign country and the assessee is entitled to double taxation relief.

For claiming refund it is necessary that the income in respect of which refund of tax is being claimed must have been included in his total income as per the return of Income.

Every claim for refund under this chapter shall be made in the prescribed Form (No. 30) within one year from the last day of the assessment year to which the claim is related. If the assessee has not filed the return of income he must file the return alongwith the certificate/s of tax deducted at source, challans for payment of tax, salary certificate and/ or tax paid in a foreign country. The dividend warrants and other certificates should be filed in original, duly signed by the assessee, to evidence the ownership of shares etc., from which the income is derived. If, for some reason, the original certificates are not traceable, duplicates issued by the concerned companies may be furnished. However, in such cases an indemnity bond stating that the original certificates are not traceable and no refund in respect of such warrants had already been claimed, should also accompany the claim. Indemnity bond should be on a stamp paper of the prescribed value depending upon the amount of tax deduction.

Where refund arises on completion of assessment on account of excess payments of advance tax or on self-assessment or it results on account of reduction in appeal, revision or rectification of mistakes, no formal application for refund is required. The Assessing Officer shall grant such refund on his own. However, where an assessment is set aside or cancelled by virtue of such an order and an order of fresh assessment is directed to be made, the refund if any, shall become due only on the making of fresh assessment. In cases where the assessment is annulled, the refund shall become due only of the amount of tax paid in excess of the tax chargeable on the total income returned by the assessee (Section 240).

However, the assessing officer is authorised to admit a belated refund claim subject to satisfying the following conditions :

- (a) the refund arising as a tax deducted at source under Section 192, 193, 194, 194A, 194B, 194C, 194D and 195 or as a result of excess advance tax payments under Section 208, does not exceed ' 10,000;
- (b) the returned income is not a loss, where the assessee claims the benefit of carry forward of the loss;
- (c) the refund claimed is not supplementary in nature i.e. a claim for additional amount of refund after the completion of the original assessment for the same year; and
- (d) the income of the assessee is not assessable in the hands of any other person under any provisions of the Act.

### Whom to apply for refund?

Claim for refund should be preferred to the Assessing Officer having jurisdiction to assess the assessee.

In bigger towns like Delhi, Bombay, Calcutta, Madras, separate Refund Circles have been opened to settle refund cases. However, these circles settle refund cases where income is restricted to 'Other Sources'.

### Who is entitled to refund?

Any one of the following persons can apply for the refund :

- (i) Owner of the income who has made excess payment;
- (ii) Where the income of a person is included in the hands of another, only the latter is entitled to refund;
- (iii) In case of death of the assessee, his legal representative;
- (iv) In case of insolvency of the assessee - the receiver;
- (v) In case of liquidation of a company - the liquidator of the company;

## 514 EP-TL

- (vi) In case of minor or incapable assessee - the guardian of the minor or incapable;
- (vii) In case of non-resident assessee - his agent provided he has been duly authorised by the principal; and
- (viii) In case of dissolved partnership firm - any partner provided he has been duly authorised by all other ex-partners of the firm.

### Issue of Refund

If the Assessing Officer is satisfied that the refund claim is complete and in order, he shall complete the assessment and issue a refund voucher payable at the Reserve Bank or the State Bank or any treasury. The refund voucher is encashable like any other cheque, within three months from the date of issue. If the assessee fails to encash it within the prescribed time (3 months from the date of issue), he should send it to the Assessing Officer who will cancel it and issue a fresh one. If the applicant is a resident and the amount of refund is small, the amount may be sent by money order at Government cost. Where the assessee is a non-resident, generally a Bank Draft is sent at his cost.

### Adjustment of Refund

All refunds may not be settled by actual payments. Wherever it is found that tax for some other years (either earlier or subsequent to the year to which the refund relates) are outstanding against the assessee, the refund due may be adjusted against the outstanding demand and the balance, if any, refunded to him. However, the amount can be adjusted only after giving an intimation in writing to the assessee of the action proposed to be taken for the purpose.

### Interest on Refunds

Section 244A, provides that where, in pursuance of any order passed under the Income-tax Act, refund of any amount becomes due to the assessee, he shall be entitled to receive, in addition to the said amount, simple interest thereon calculated in the following manner :

- (a) Where the refund is out of any tax collected at source under Section 206C or paid by way of advance tax or treated as paid under Section 199, during the financial year immediately preceding the assessment year, interest calculated at the rate of one half per cent for every month or part of a month comprised in the period from 1st day of April of the assessment year to the date on which the refund is granted. But, if the amount of refunds is less than ten per cent of the tax as determined on regular assessment, no interest shall be payable.
- (b) where the refund is out of any tax paid under section 140A, such interest shall be calculated at the rate of one-half per cent for every month or part of a month comprised in the period, from the date of furnishing of return of income or payment of tax, whichever is later, to the date on which the refund is granted **[Amendment vide Finance Act, 2016 w.e.f. 1st June, 2016]**.

However, no interest shall be payable if the amount of refund is less than ten percent of the tax as determined under Sub-section (1) of Section 143 or regular assessment.

- (c) In any other case, such interest has to be calculated at the rate of one half per cent for every month or part of a month comprised in the period or periods from the date or dates of payment of the tax or penalty to the date on which the refund is granted (The "date of payment of tax or penalty" means the date on and from which the amount of tax or penalty; specified in the demand notice under Section 156 is paid in excess of such demand).
- (d) Where a refund arises out of appeal effect being delayed beyond the time prescribed under sub-section (5) of section 153, the assessee shall be entitled to receive, in addition to the interest payable under sub-section (1) of section 244A, an additional interest on such refund amount calculated @ 3% per annum, for the period beginning from the date following the date of expiry of the time allowed under

sub-section (5) of section 153 to the date on which the refund is granted. It is clarified that in cases where extension is granted by the Principal Commissioner or Commissioner by invoking proviso to sub-section (5) of section 153, the period of additional interest, if any, shall begin from the expiry of such extended period [Amendment vide Finance Act, 2016 w.e.f. 1st June, 2016].

- (e) The assessee is not entitled to any interest on refund where a delay in payment thereof takes place for reasons attributable to the assessee. Any question as to the period to be excluded has to be decided by the Chief Commissioner or Commissioner whose decision thereon shall be final.
- (f) In the event of increase or reduction of the amount on which the interest is payable (as a consequence of an order 143(3); 144; 147; 154; 155; 250; 254; 260; 262; 263; 264; or 245D(4), interest payable is to be increased or reduced accordingly. In the case of subsequent reduction of the interest, the Assessing Officer has to serve a demand notice on the assessee requiring him to pay back such amount as has been paid in excess.

The provisions of this section shall apply in respect of assessments for the assessment year commencing on the 1st day of April, 1989 and subsequent years. However, in respect of assessment of fringe benefits, the provisions of this Sub-section shall have effect as if for the figures “1989”, the figures “2006” had been substituted.

**New Section 244A(1B)** : This section provides that where refund of any amount becomes due to the deductor, such person shall be entitled to receive, in addition to the refund, simple interest on such refund at rate of 0.5% per month or part of month. Interest will be available from the date on which claim for refund is made in the prescribed form to the date on which refund is granted. Where refund arises on account of giving effect to an appellate order under section 250/254/262, interest will be available from the date of deposit of TDS to the date on which refund is granted. However, interest shall not be allowed for the period for which the delay (in the proceedings resulting in the refund) is attributable to the deductor. [Amendment vide Finance Act, 2017 w.e.f. AY 2019-20]

However, where the proceedings resulting in the refund are delayed for reasons attributable to the assessee, whether wholly or partly, the period of delay so attributable to him shall be excluded as per the decision taken by the Chief Commissioner or Commissioner (his decision thereon shall be final).

**New Section 241A** : This section provides that for the returns furnished for assessment year 2017-18 (or any subsequent year), where refund is due to the assessee under section 143(1) and the assessing officer is of the opinion that the grant of refund may adversely effect the recovery of revenue, he may, for the reasons to be recorded in writing and with previous approval of the Principal Commissioner or Commissioner, withhold the refund up to the date on which the assessment is made. [Amendment vide Finance Act, 2017 w.e.f. AY 2019-20].

## CASE LAWS

### 1. Provision Mandating Quoting of Aadhaar for IT Returns & PAN is valid

#### **Binoy Viswam v. Union of India (2017)**

Recently, Section 139AA was incorporated to the Income Tax Act vide Finance Act, 2017 requiring mandatory quoting of Aadhaar or enrolment ID of Aadhaar application form for filing of income tax returns and making application for allotment of PAN (Permanent Account Number) with effect from July 1 this year. As per the provision, non-enrolment of Aadhaar by July 2017 would render the PAN of the defaulting individual invalid, attracting serious consequences under the Income Tax Rules.

A number of petitions were filed before the Top-Court challenging the vires of the above provision. The petitioners contended that the new provision “compelling” tax payers to link their Aadhaar Card to PAN would amount to violation of right to privacy. He further contended that as per the Supreme Court verdict in 2015, the Aadhaar “was not mandatory” for all the citizens. It was held that Aadhaar should be voluntary and no benefits can be denied for want of it. The petitioner, therefore, contended that the scheme itself, was

voluntary and the card is to be obtained only on the consent of the individual.

The bench concurred with the argument of the Government that the primary purpose of introducing this provision was to take care of the problem of multiple PAN cards obtained in fictitious names.

While accepting this contention, Justice A.K Sikri said that people who do not have Aadhaar Card are not bound to apply for it till the verdict of the Constitution Bench. It was clarified that “assessee who are not Aadhaar card holders and do not comply with the provision of Section 139(2), their PAN cards be not treated as invalid for the time being.” However, people who have Aadhaar must link it with PAN Card since it is necessary to prevent fake PAN cards.

In *Binoy Viswam v. Union of India*, a two-judge bench of the Supreme Court upheld the constitutional validity of the provisions of Section 139AA of the Income Tax Act which mandates quoting of Aadhaar for IT Returns & PAN.

### LESSON ROUND UP

- The Income-tax Act provides for collection and recovery of income-tax in the following ways, namely,
  - (i) deduction of tax at source in respect of income by way of salaries, interest on securities, interest other than interest on securities, winnings from lotteries and crossword puzzles, winnings from horse-race, insurance commission, dividends, payment to contractors or subcontractors and payments to non-residents;
  - (ii) advance payment of income-tax before the assessment by the assessee himself;
  - (iii) direct payment of income-tax by the assessee on self-assessment; and
  - (iv) after the assessment is made by the Assessing Officer.
- Sections 192 to 206 of the Income-tax Act lay down the provisions relating to deduction of tax at source.
- Section 197A provides that no deduction of tax at source is to be made from (i) interest on securities, (ii) dividends, and (iii) payments in respect of deposits under NSS, etc. if the following conditions are satisfied:
  - a) The recipient of such income is an individual and resident in India.
  - b) Such person furnishes a declaration in writing in duplicate, in the prescribed form and verified in the prescribed manner, to the payer of such income to the effect that the tax on his estimated total income of the previous year in which such income is to be included for computing his total income will be nil.
- Section 207-219 of the Income Tax Act deals with the provisions relating to advance payment of tax. In advance payment of tax, the assessee has to pay tax in a financial year under estimated income which is to be taxed in the subsequent assessment year. It follows the doctrine known as pay as you earn scheme. It is obligatory for an assessee to pay advance tax where the advance tax payable is Rs. 10,000 or more (Section 208).
- Filing of Return: The procedure under the Income-tax Act for making an assessment of income begins with the filing of a return of income. Section 139 of the Act contains the relevant provisions relating to the furnishing of a return of income.
- E-Filing of Return: The Income Tax Department has introduced on line facility in addition to conventional method to file return of income. The process of electronically filing of Income Tax return through the mode of internet access is called e-filing of return.

- Permanent Account Number: Every person, who has not been allotted any permanent account number, is obliged to obtain permanent account number, if;
  - a) if his total income assessable during the previous year exceeds the maximum amount which is not chargeable to tax or
  - b) any person carrying on business or profession whose total sales turnover or gross receipts are or is likely to exceed Rs. 5,00,000 in any previous year or
  - c) is required to furnish a return of income under Section 139.
- Refund means “to repay” or restore what was taken under the income-tax law. Refunds arise in those cases where the amount of tax paid by a person or on his behalf is greater than the amount with which he is properly chargeable for that year.

### SELF TEST QUESTIONS

*These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.*

#### Multiple Choice Questions “MCQs”

1. Mr. Anil who is a non-resident in India during the previous year has paid consultancy fees of Rs. 50 lakhs to X Ltd, a non-resident foreign company in connection to a project / liaison office in India. Under which section Mr. Anil is required to deduct tax at source on the above payment?
  - a) Section 194J of the Income tax Act, 1961
  - b) Section 195 of the Income tax Act, 1961
  - c) No TDS is required to be deducted
  - d) None of the above

Answer: (b)

2. Interest on deferment of advance tax is levied under section:
  - a) Section 234A of the Income tax act, 1961
  - b) Section 234B of the Income tax act, 1961
  - c) Section 234C of the Income tax act, 1961
  - d) Section 201A of the Income tax act, 1961

Answer: (c)

3. The TDS Certificate issued by an employer to his employees in case of salary income is
  - a) Form 16
  - b) Form 26
  - c) Form 26A
  - d) Form 26Q

Answer: (a)

4. Quoting of PAN is compulsory in which of the following cases:
  - a) Deposit exceeding Rs. 50,000 in Post Office Savings Bank
  - b) Payments to hotels of bills of Rs. 50,000 at any one time



# Lesson 10

## Assessment, Appeals & Revision

### LESSON OUTLINE

- Income Tax Authorities
- Assessment
- Types of Assessment
- Appeal Before the Commissioner (Appeals)
- Appealable order [Section 246A]
- Procedure for filing of appeal [Section 249(1)]
- Period of limitation to prefer an appeal [Section 249(2)]
- Payment of Tax before Filing Appeal [Section 249(4)]
- Procedure in appeal [Section 250]
- Powers of the Commissioner (Appeals)
- Revision by the Commissioner of Income Tax [Section 263 and 264]
- Revision of orders prejudicial to the interest of revenue [Section 263]
- Revision of order in the Interest of Assessee [Section 264]
- Circumstances in which no revision can be made [Section 264(4)]
- Appeal before Appellate Tribunal
- Appealable orders [Section 253(1) and (2)]
- Procedure for filing appeal [Section 253(3),(4)&(6)]
- Order of Appellate Tribunal [Section 254]
- Procedure of Appellate Tribunal [Section 255]
- Appeal Before High Court
- Appeal Before Supreme Court
- Penalties and Offence
- LESSON ROUND UP
- SELF TEST QUESTION

### LEARNING OBJECTIVES

The provisions of the Income-Tax Act contained in Sections 116 to 136 specify income tax authorities, the procedure relating to the appointment of the various income-tax authorities, their powers, functions, jurisdiction and control. The procedure under the Income-tax Act for making an assessment of income begins with the filing of a return of income. Section 139 of the Act contains the relevant provisions relating to the furnishing of a return of income. On the basis of return of income the income tax authority makes the assessment.

At the end of this lesson, you will learn;

- Various income-tax authorities, their powers, functions, jurisdiction and control.
- What are the types of assessment
- When can order for re-assessment be issued.
- How the mistake in return can be rectified and by whom.

The Income-tax Act provides for various remedies to an assessee on completion of the assessment. The main remedies available to an assessee on completion of the assessment are Appeals, Revision, and Rectification. All these remedies work in different areas. However, strictly speaking the remedies are not alternative to each other but at times more than one remedial proceeding may be used as complimentary to each other so as to achieve the best results.

The right to appeal arises where the taxpayer is aggrieved by the order passed by the income-tax authority. Where the Assessing Officer accepts the return filed by the taxpayer and passes an order making no modification, an appeal does not lie against that order as the taxpayer cannot be said to be aggrieved of that order.

At the end of this lesson, you will learn

- What are the provisions for filing of appeal.
- What is the procedure to file an application before the appellate authority.
- When order of appeal can be revised.
- What is the ground and quantum of penalty imposed.

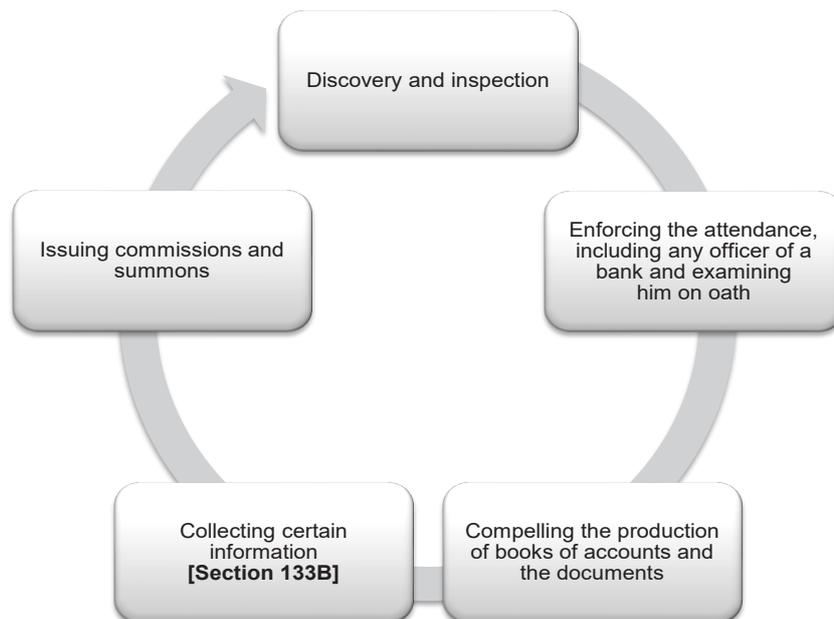
**INCOME-TAX AUTHORITIES (APPOINTMENT, JURISDICTION AND POWERS) [SECTION 116]**

The following are the income-tax authorities who are statutorily empowered to administer the law of Income-tax :

- (i) The Central Board of Direct Taxes, constituted under the Central Boards of Revenue Act, 1963;  
Principal Director General of Income-tax or Principal Chief Commissioners of Income-tax
- (ii) Directors-General of Income-tax or Chief Commissioners of Income-tax Principal Director of Income-tax or Principal Commissioners of Income-tax
- (iii) Directors of Income-tax or Commissioners of Income-tax or Commissioners of Income-tax (Appeals);  
Additional Directors of Income-tax or Additional Commissioners of Income-tax or Additional Commissioners of Income-tax (Appeals);  
Joint Directors of Income tax or Joint Commissioners of Income-tax.
- (iv) Deputy Directors of Income-tax or Deputy Commissioners of Income-tax or Deputy Commissioners of Income-tax (Appeals);
- (v) Assistant Directors of Income-tax or Assistant Commissioners of Income-tax;
- (vi) Income-tax Officers;
- (vii) Tax Recovery Officers;
- (viii) Inspectors of Income-tax.

The provisions of the Income-tax Act contained in Sections 116 to 136 specify income tax authorities, the procedure relating to the appointment of the various income-tax authorities, their powers, functions, jurisdiction and control. In addition to the various provisions contained in these sections, the Income-tax Department follows the system of functional allocation and distribution of work with a view to specialising and concentrating in the various areas of income- tax assessment, procedure, collection, recovery, refund, appeals, etc.

For all purposes of the Income-tax Act, the Income Tax authorities are vested with the various powers which are vested in a Court of Law under the Code of Civil Procedure while trying a suit in respect of any case. More particularly, the provisions of the Code of Civil Procedure and the powers granted to the tax authorities under the code would in respect of :



Every income-tax authority shall be deemed to be a Civil Court for the purposes of Section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973. The powers granted are generally quasi-judicial. In particular, the powers of income-tax authorities relate to discovery, production of evidence etc., searches and seizures, application of retained assets, power to call for information from various parties, authorities and bodies, powers of survey, powers relating to the inspection of the registers of companies etc. Further, all proceedings under the Income-tax Act before any income-tax authority must be deemed to be judicial proceedings within the meaning of Sections 193 and 228 and for purposes of Section 196 of the Indian Penal Code. For a detailed Study of the various powers, functions, jurisdiction, etc., of the different classes of income-tax authorities and the general scheme of administration of the Income-tax Act, students may refer to the relevant provisions of the Income-tax Act.

### **Appointment of Income-tax Authorities [Section 117]**

The Central Government may appoint such persons as it thinks fit to be income-tax authorities. Where an income-tax authority is authorised by the Board, it may appoint such executive or ministerial staff as may be necessary to assist it in the execution of its function.

### **Control of Income-tax Authorities [Section 118]**

The Board is empowered to control the income-tax authorities. It may notify that any income-tax authority will be sub-ordinate to such other income-tax authority or authorities as may be specified in the notification.

### **Instructions to Subordinate Authorities [Section 119]**

The Board is empowered to issue orders, instructions and directions to its subordinate authorities from time to time. The Board may also issue guideline, principles or procedures to be followed by its income tax authorities and if it is in the interest of public, then the same may be published and circulated. The Board also empowered to authorize any income tax authority to admit an application for any claim of exemption, deduction, refund or any other relief under this act and deal with the same if it was genuinely out of the taxpayer control.

### **Jurisdiction of Income-tax Authorities [Section 120]**

Income-tax authorities are required to exercise or perform such powers or functions as are assigned to them by the Board [Section 120(1)].

Any income-tax authority, being an authority higher in rank, may, if so directed by the Board exercise the powers and performs the functions of the income-tax authority lower in rank and any such direction issued by the Board shall be deemed to be a direction issued under Sub-section (1).

The Board may authorise any other income-tax authority to issue orders in writing for the exercise of the powers and performance of the functions by all or any of the income-tax authority who are subordinate to it [Section 120(2)]. While issuing such directions, the Board or any other income-tax authority authorised by it may take into account (i) territorial area, (ii) persons or classes of persons, (iii) incomes or classes of income, and (iv) cases or classes of cases [Section 120(3)].

## **THE CENTRAL BOARD OF DIRECT TAXES (CBDT)**

### **Appointment and Working of the Board**

The Central Board of Direct Taxes was a statutory body created under the Central Boards of Revenue Act, 1963 [Section 2(12)]. The Board in its working is closely associated with the Ministry of Finance. The Board consist of a chairman and six members, all of whom are ex-officio Special Secretary to the Government of India.

## Jurisdiction

It is the topmost executive authority in the sphere of direct taxes. Its powers of administration supervision and control extend over the whole department.

## Power

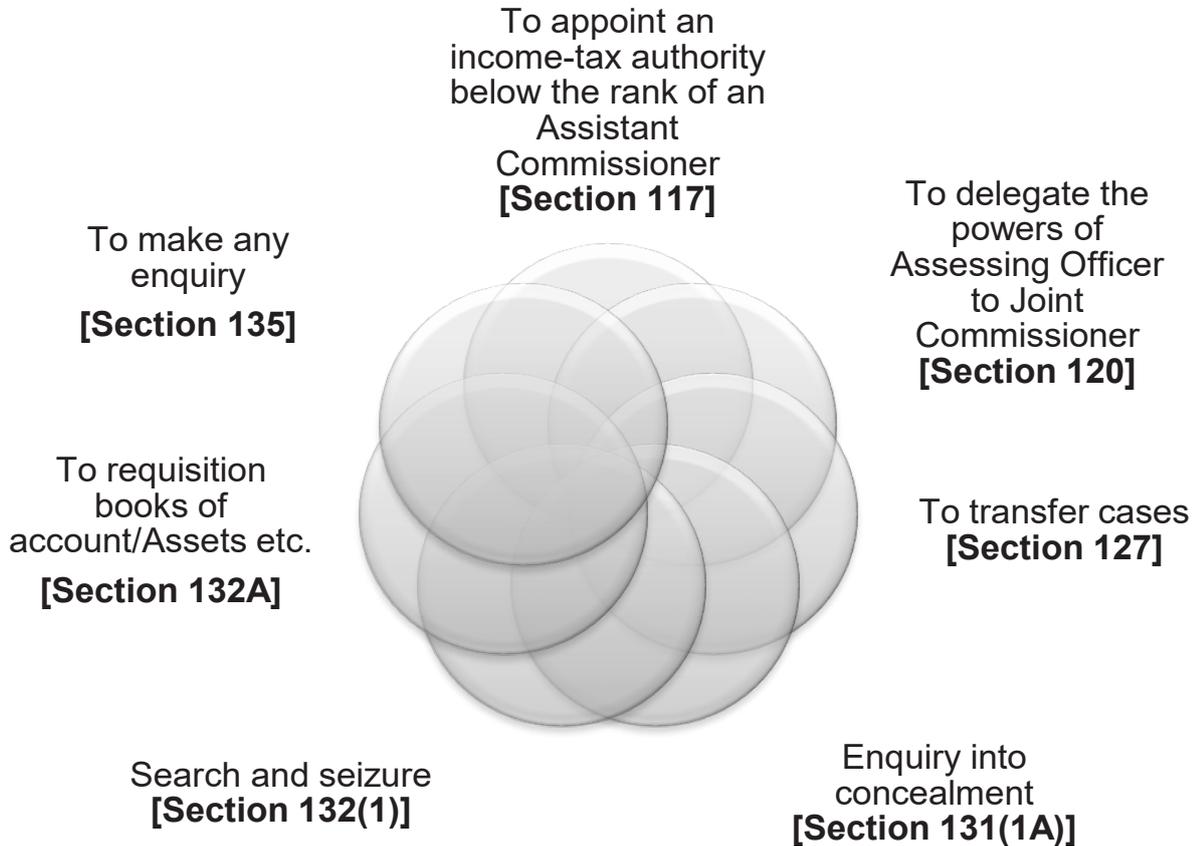
- (i) **Power to make Rules** : It has the power to make rules (under Section 295), subject to the approval of Central Government, for carrying out the purposes of this Act. The Rules may be made for whole or any part of India.
- (ii) **To issue instructions [Section 119(1)]**: It may issue orders, instructions and directions to income tax authorities for the proper administration of this act and such authorities and all other persons employed in the execution of the Act shall observe and follow the same. However, no such orders, instructions or directions shall be issued so as to :
  - require any income tax authority to make a particular assessment or to dispose of a particular case in a particular manner; or
  - interfere with the discretion of the Commissioner (Appeal) in the exercise of his appellate functions.
- (iii) **Power to issue orders, guidelines, procedures [Section 119(2)(a)]**: It may, if it considers it necessary or expedient so to do, for the purpose of proper and efficient management of the work of assessment and collection of revenue, issue, from time to time, general or special orders in respect of any class of income or fringe benefit or class of cases, setting forth directions or instructions (not being prejudicial to assessee) as to the guidelines, principles or procedures to be followed by its subordinates in execution of their duties. Any such orders may, if the Board is of the opinion that it is necessary in the public interest so to do, be published and circulated for general information.
- (iv) **Power to relax certain provisions [Section 119(2)(a)]**: The Board is empowered to relax the provision relating to the charge of interest for defaults in deduction of tax at source, or payment of such tax [under Section 201(1A)] or payment of advance tax (Section 211) or interest for defaults in furnishing return (Section 234A) or interest for defaults in payment of advance tax (under Section 234B or Section 234C) or assessment and recovery of tax etc. Other provisions, in appropriate cases, Board may relax the provisions of sections are 115P, 115S, 115WD, 115WE, 115WF, 115WG, 115WH, 115WJ, 115WK, 139, 143, 144, 147, 148, 154, 155, 158BFA, 211, 234E, 270A, 271, 271C, 271CA and 273.
 

The Board is also empowered to relax the provisions relating to the computation of total income and deductions to be made in computing total income in cases of genuine hardship. It can be done by a general or special order and for reasons to be specified therein.
- (v) **Power to admit belated refund application** : To avoid genuine hardship in any case or class of cases, the Board may authorise any income-tax authority, not being Commissioner (Appeals) to admit belated application or claim for any exemption, deduction, refund or any other relief [Section 119(2)(b)].
- (vi) **Power to decide jurisdiction** : The Board is empowered to decide jurisdictional matters of any income-tax authority and assign to them such functions as are to be performed by them (Section 120).

**Power to disclose information** : The Board may disclose information relating to any assessee, to any officer, authority, or body performing any functions under any tax law relating to the imposition of any tax, duty or cess or dealing in foreign exchange under Foreign Exchange Management Act, 1999,

if it considers such disclosure in public interest. The Board may also authorise any other income-tax authority to disclose such information (Section 138). The provision is intended to facilitate exchange of information about tax evaders. Principal Director-General or Director-General or Director of Income-Tax

The Principal Director – General has the following powers :



- (a) **To appoint an income-tax authority below the rank of an Assistant Commissioner [Section 117]** : If so authorised by the Central Government a Director-General or Director may appoint an income- tax authority below the rank of Assistant Commissioner.
- (b) **To delegate the powers of Assessing Officer to Joint Commissioner [Section 120]** : Where Director- General or Director is so authorised by the Board, he may delegate the powers and functions of the Assessing Officer to Joint Commissioner.
- (c) **To transfer cases [Section 127]** : The Director-General may transfer any case from one or more Assessing Officers subordinate to him to any other Assessing Officer also subordinate to him.
- (d) **Enquiry into concealment [Section 131(1A)]** : If the Director-General or Director or Deputy Director or Assistant Director (w.e.f. 1.6.1988) has reason to suspect that any income has been concealed, or is likely to be concealed, by any person or class of persons, within his jurisdiction, he is empowered to make any enquiry or investigation relating thereto notwithstanding that no proceedings with respect to such person or class of persons are pending before him [Section 131 (1A)].
- (e) **Search and seizure [Section 132(1)]** : Where the Director- General or Director or Chief Commissioner or Commissioner in consequence of information in his possession has reason to believe that (a) any person to whom notice has been issued in respect of discovery and inspection etc. [under Section 131(1)] or (b) any person to whom notice has been issued to produce accounts or documents [under

Section 142(1)], has failed to do so far he is not likely to produce such accounts or documents, or (c) any person is in possession of undisclosed income or property, he is empowered [under Section 132(1)] to authorise any Deputy Director, Deputy Commissioner, Assistant Director (Assistant Commissioner w.e.f.1.4.1989) or Assessing Officer to enter and search any building, place, vessel, vehicle or aircraft, where he has reason to suspect about their availability and seize any such books of accounts, other documents, money, bullion, jewellery or other valuable article or thing found as a result of such search.

The “reason to believe or reason to suspect” to for issuing warrant of authorization of search/seizure shall not be disclosed to any person or authority or Appellate Tribunal. Amendment to section 132(1) will take effect from April 1, 1962 and amendment to section 132(1A) and 132A(1) from October 1, 1975.

- (f) **To requisition books of account/Assets etc. [Section 132A]** : Where any books of account or documents have been taken into custody by any officer or authority under any other law (e.g. by Commissioner or Customs, Sales Tax Commissioner etc.) and the Director General or Director or the Chief Commissioner or Commissioner, in consequence of information in his possession, has reason to believe that (i) any person, required to produce such accounts/documents prior to their acquisition under any other law, has failed to do so, or (ii) such accounts or documents will be useful for any proceeding under income-tax law but such person would not produce them on their return by the officer or authority under any other law, or (iii) any assets represent income or property which has not been, or would not have been disclosed by any person from whose possession or control such assets have been taken into custody by any officer or authority under any other law, he may authorise any Deputy Director, Deputy Commissioner, Assistant Director, Assistant Commissioner or Income-tax Officer to require such officer or authority under any other law to deliver such books of account or documents or such assets to the requisitioning officer under income-tax law. On a requisition being made, such officer or authority under any other law is required to deliver such books of accounts or documents or assets to the requisitioning officer either forthwith or after such time when it is no longer necessary to retain them in his custody.

The “reason to believe or reason to suspect” to for issuing warrant of authorization of search/seizure shall not be disclosed to any person or authority or Appellate Tribunal. Amendment to section 132(1) will take effect from April 1, 1962 and amendment to section 132(1A) and 132A(1) from October 1, 1975.

- (g) **To make any enquiry [Section 135]** : The Director-General or Director is competent to make any enquiry under this Act.

## Chief Commissioner or Commissioner of Income-Tax

### Powers of Chief Commissioner or Commissioner of Income-Tax

To appoint an income-tax authority below the rank of Assistant Commissioner **[Section 117]**

To delegate the powers of Assessing Officer to Deputy Commissioner **[Section 120]**

To transfer case **[Section 127]**

Power regarding discovery, production of evidence etc. **[Section 131]**

Search and seizure **[Section 132]**

To requisition books of accounts etc. **[Section 132A]**

Power of survey **[Section 133A]**

To make any enquiry **[Section 135]**

Disclosure of information respecting assessee **[Section 138]**

To sanction reopening of the assessment after the expiry of four years **[Section 151(2)]**

To approve withholding of refund in certain cases **[Section 241]**

Set-off of refund against arrears of tax **[Section 245]**

To direct the Assessing Officer to prefer appeal to the Tribunal against A.A.C.'s order **[Section 253(2)]**

To revise any order passed by the Assessing Officer which is prejudicial to revenue **[Section 263]**

Revision of any order passed by a subordinate authority on application by the assessee or suo motu **[Section 264]**

The Chief Commissioner or Commissioner of Income tax has the following powers :

- (i) **To appoint an income-tax authority below the rank of Assistant Commissioner [Section 117]** : If so authorised by the Central Government, a Chief Commissioner or Commissioner may appoint an income-tax authority below the rank of Assistant Commissioner.
- (ii) **To delegate the powers of Assessing Officer to Deputy Commissioner [Section 120]** : Where Chief Commissioner or Commissioner is so authorised by the Board, he may delegate the powers and functions of the Assessing Officer to Joint Director or Joint Commissioner.
- (iii) **To transfer case [Section 127]** : The Chief Commissioner or Commissioner is empowered to transfer any case from any Assessing Officers to any other Assessing Officer or Assessing Officers.

- (iv) **Power regarding discovery, production of evidence etc. [Section 131]** : The Chief Commissioner or Commissioner has the same powers as are vested in a Court under the Code of Civil Procedure in respect of discovery and inspection, compelling production of books of accounts and other documents (relating to any period), issuing commissions enforcing the attendance of any person, including any officer of a banking company and examining him on oath.

The Commissioner may impound or retain any books of accounts or other documents produced before him for such time as he thinks fit [Section 131(3)]. Where such power is exercised by the Assessing Officer, he has to record reasons before impounding the books of accounts or documents. The Assessing Officer or Assistant Commissioner cannot retain the books of accounts/documents for a period exceeding 15 days without prior approval of the Chief Commissioner or Director-General or Commissioner [Section 131(3)].

- (v) **Search and seizure [Section 132]** : Like Director-General or Director, the Chief Commissioner or Commissioner of Income-tax has also got the powers of search and seizure.
- (vi) **To requisition books of accounts etc. [Section 132A]** : Like Director-General or Director of Income-tax, the Chief Commissioner or Commissioner is also vested with the power to requisition books of accounts.
- (vii) **Power of survey [Section 133A]** : An income-tax authority may enter, after sunrise and before sunset, any office, or any other place (where business or profession is carried on or where any books of accounts/ documents, cash, stocks or other valuable articles relating to business are kept), for the purpose of verifying whether tax has been deducted or collected at source in accordance with the relevant provisions. Provided that such place is within the limits of the area assigned to him, or any place in respect of which he is authorised for the purposes of this section by such income-tax authority who is assigned the area within which such place is situated,

He may also require the deductor or the collector or any other person who may at that time and place be attending in any manner to such work to afford him the necessary facility to inspect such books of account or other documents available at such place, and to furnish such information as he may require in relation to such matter.

The income-tax authority acting under this section may also place marks of identification, impound or retain in his custody books of account or other documents inspected by him, make inventory of articles verified or record the statement of any person. Provided that such impounding shall be done only after recording the reasons for doing so and the period of retention (without obtaining the approval of the Principal Chief Commissioner or the Chief Commissioner or the Principal Director General or the Director General or the Principal Commissioner or the Commissioner or the Principal Director or the Director thereof, as the case may be) shall not exceed a period of fifteen days (exclusive of holidays).

Where an assessee incurs an ostentatious expenditure on any function, ceremony, the income-tax authority is empowered to collect information about such expenditure from the assessee or any other person who is likely to possess information in this connection and may record their statement which may be used thereafter as an evidence. This may be done at time such function or ceremony is over.

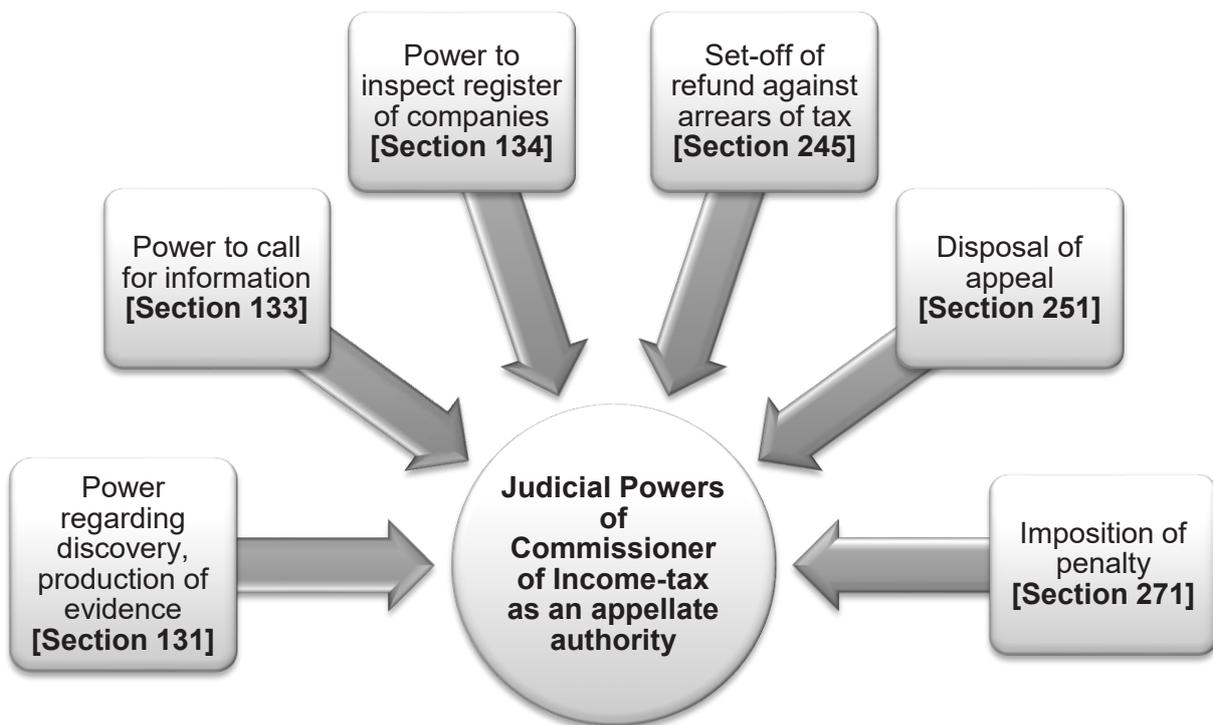
**Amendment to Section 133A(1)** : 'Any Place' to include any place at which an activity for charitable purpose is carried on. (w.e.f April 1, 2017)

- (viii) **To make any enquiry [Section 135]** : The Chief Commissioner or Commissioner is competent to make any enquiry under this Act.
- (ix) **Disclosure of information respecting assesseees [Section 138]** : Where a person makes an application to the Chief Commissioner or Commissioner in the prescribed form for any information relating to any assessee in respect of any assessment, he may furnish the information asked for in

respect of that assessment if he satisfied that such disclosure is in public interest.

- (x) **To sanction reopening of the assessment after the expiry of four years [Section 151(2)]** : The assessment of an income which has escaped assessment can be reopened after the expiry of four years from the end of the relevant assessment year only if the Chief Commissioner or Commissioner has sanctioned such reopening.
- (xi) **To approve withholding of refund in certain cases [Section 241]** : Where any proceeding is pending against the assessee and the Assessing Officer is of the opinion that the grant of the refund may adversely affect the revenue, the Chief Commissioner or Commissioner may authorise the Assessing Officer to withhold the refund till such time as the Chief Commissioner or Commissioner may determine.
- (xii) **Set-off of refund against arrears of tax [Section 245]** : The Chief Commissioner or Commissioner is empowered to set off the amount of refund or any part thereof due to any person against the arrears of the tax due from such person. Any intimation in writing to this effect should be given to such person.
- (xiii) **To direct the Assessing Officer to prefer appeal to the Tribunal against A.A.C.'s order [Section 253(2)]** : The Commissioner may, if he objects to any order passed by a Commissioner (Appeals), direct the Assessing Officer to appeal to the Appellate Tribunal against the order.
- (xiv) **To revise any order passed by the Assessing Officer which is prejudicial to revenue [Section 263]** : The Commissioner may revise any order passed by the Assessing Officer which is prejudicial to the interest or revenue.
- (xv) **Revision of any order passed by a subordinate authority on application by the assessee or suo motu [Section 264]** : The Commissioner may revise either on his own motion or on an application made by the assessee within the prescribed time for such revision, any order passed by an authority subordinate to him. He may pass such order thereon, not being an order prejudicial to the assessee as he may think fit.

### COMMISSIONER OF INCOME-TAX (APPEALS)



The Commissioner of Income-tax (Appeals) is an appellate authority. It is vested with the judicial powers :

- (1) **Power regarding discovery, production of evidence [Section 131]** : Like Chief Commissioner or Commissioner, the power regarding discovery, production of evidence etc., can also be exercised by the Commissioner (Appeals).
- (2) **Power to call for information [Section 133]** : The Commissioner of Income-tax (Appeals) may, for the purposes of this Act :
  - (a) require any firm to furnish him with a return of the names and addresses of the partners of the firm and their respective shares;
  - (b) require any Hindu Undivided Family to furnish him with a return of the names and addresses of the manager and the members of the family;
  - (c) require any person whom he has reason to believe to be a trustee, guardian or agent, to furnish him with a return of the names of the persons for or of whom he is trustee, guardian or agent, and of their addresses;
  - (d) require any assessee to furnish a statement of the names and addresses of all persons to whom he has paid in any previous year rent, interest, commission, royalty or brokerage, or any annuity together with particulars of such payments made;
  - (e) require any dealer, broker or agent or any person concerned in the management of a stock or Commodity Exchange to furnish a statement of the names and addresses of all persons to whom he or the Exchange has paid any sum in connection with the transfer, whether by way of sale, exchange or otherwise, of assets, or on whose behalf or from whom he or the Exchange has received any such sum, together with particulars of all such payments and receipts;
  - (f) require any person, including a banking company or any officer thereof, to furnish information in relation to such point or matter or to furnish statements of accounts and affairs verified in the specified manner, giving such information as may be required by him.

**Amendment to First Proviso to Section 133** : w.e.f. April 1, 2017 power in respect of inquiry or proceeding under the Act, may also be exercised by the Joint Director, Deputy Director and Assistant Director.

**Amendment to Second Proviso to Section 133** : w.e.f. April 1, 2017 Joint Director, Deputy Director may exercise the powers in respect of such inquiry, without seeking prior approval of higher authorities.

**Amendment to Section 133C** : Section 133C has been amended to empower CBDT to make a scheme for centralised issuance of notice calling for information and documents for the purpose of verification of information in its possession, processing of such documents and making outcome of thereof available to assessing officer for necessary action, if any.

- (3) **Power to inspect register of companies [Section 134]** : The Commissioner (Appeals) may inspect and, if necessary, take copies or cause copies to be taken, of any register of members, debenture holders or mortgagees of any company or of any entry in such register. The Commissioner (Appeals) may also authorize (in writing) any person subordinate to him to inspect and, if necessary, take copies or registers as aforesaid.
- (4) **Set-off of refund against arrears of tax [Section 245]** : The Commissioner (Appeals) is empowered to set off the amount of refund or any part thereof due to any person against the arrears of tax due from such person. Intimation in writing to this effect should be given to such person.
- (5) **Disposal of appeal [Section 251]** : In disposing of an appeal, the Commissioner (Appeals) has the following powers :

- (a) in an appeal against an order of assessment he may confirm, reduce, enhance or annul the assessment, or he may set aside the assessment and refer back to the Assessing Officer for making a fresh assessment in accordance with such directions as given by him.
- (b) in an appeal against an order imposing a penalty, he may confirm or cancel such order or vary it so as either to enhance or reduce the penalty.
- (c) in any other case, he may pass such order in appeals as he thinks fit.

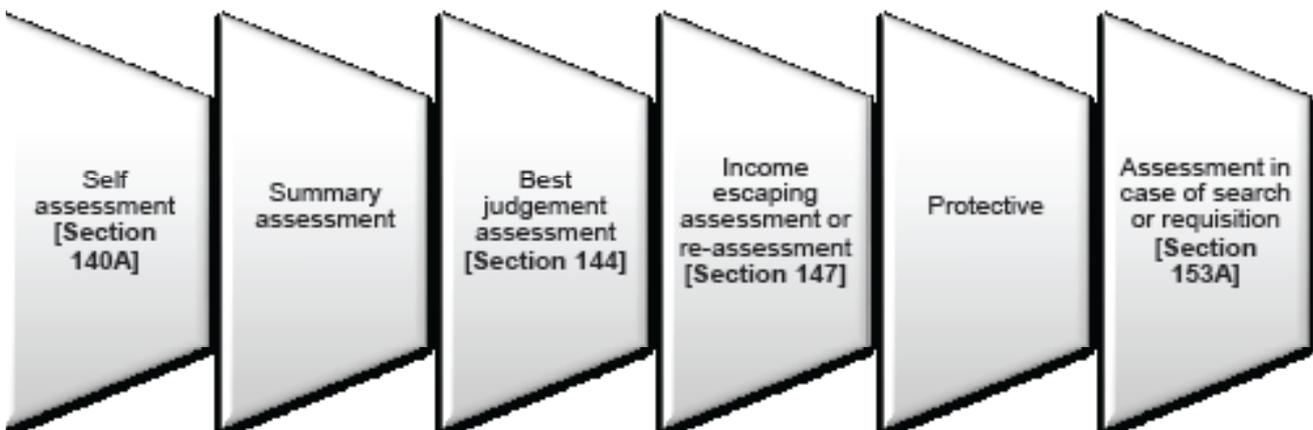
It may be noted that an assessment or a penalty cannot be enhanced or the amount of refund cannot be reduced unless the appellant had a reasonable opportunity of showing cause against such enhancement or reduction.

- (6) **Imposition of penalty [Section 271]** : The Commissioner (Appeals) may impose penalty for not producing the books of accounts or other documents [Section 142(1)] or for concealment of income (under Section 271).

## ASSESSMENT

Every assessee has to submit his income details to income tax department by filing his income tax return. Once the return of income is filed by an assessee, the very next step is the processing of the income tax return by the income tax department. While processing, department verifies and examines the correctness of the income details provided by assessee. This process of examining the income tax return by the Income Tax Department is called "Assessment" and includes re-assessment and best judgment assessment under section 144.

## TYPES OF ASSESSMENT



### (A) SELF ASSESSMENT [SECTION 140A]

Self assessment is the first step in the process of assessments. Self Assessment is simply a process where a person himself assesses his tax liability on the income earned during the particular previous year and submits Income Tax Return to the department. Every person, before furnishing return under sections 139(return of income), 142(1), 148 (issue of notice where income has escaped assessment) and 153A (Assessment in case of search or requisition) shall make self assessment of his income and pay the tax, if due on the basis of such assessment. The total tax payable is calculated on the total income of the assessee after considering the following amount :

- (i) the amount of tax already paid under any provision of this Act;
- (ii) any tax deducted or collected at source;
- (iii) any relief of tax or deduction of tax claimed under section 90 or section 91 on account of tax paid in a country outside India;

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- (iv) any relief of tax claimed under section 90A on account of tax paid in any specified territory outside India referred to in that section; and
- (v) any tax credit claimed to be set off in accordance with the provisions of section 115JAA or section 115JD.
- (vi) any relief u/s 89

In case in delay in furnishing of return of income, self assessment tax shall also include interest for delay and fee for delay in filing return under section 234F.

Hence, this is an assessment by the assessee himself called "Self Assessment" before filing of his income tax return, so that work of income tax department became easy.

### **(B) SUMMARY ASSESSMENT: CENTRALISED PROCESSING OF RETURN [SECTION 143(1)]**

Summary assessment is the assessment without calling the assessee and without human intervention. Assessment under section 143(1) is like preliminary checking of the income tax return. Under this assessment no detailed scrutiny of income tax return is carried out but total income or loss is computed after making the following adjustments (if any), namely

- i. any arithmetical error in the return; or
- ii. an incorrect claim, if such incorrect claim is apparent from any information in the return; or
- iii. disallowance of loss claimed, if return of the previous year for which set-off of loss is claimed was furnished beyond the due date specified under section 139(1); or
- iv. disallowance of expenditure indicated in the audit report but not taken into account in computing the total income in the return; or
- v. disallowance of deduction claimed u/s 10AA, 80IA to 80-IE, if the return is furnished beyond the due date specified under section 139(1); or
- vi. addition of income appearing in Form 26AS which has not been included in computing the total income in the return. However, no such adjustment shall be made unless an intimation is given to the assessee of such adjustment either in writing or in electronic mode.

After making the aforesaid adjustments, income tax department sends an intimation under section 143(1) in which comparative income tax computation [i.e. as provided by an assessee in income tax return and as computed u/s 143(1)], which serves as demand notice if there is a tax liability otherwise simply an intimation about processing of return of income.

**Time limit for intimation under section 143(1) :** No intimation for tax or interest due under section 143(1) shall be sent after the expiry of 1 year from the end of financial year in which return of income is made.

Example : For the assessment year 2020-21, Mr. Rajan files the ITR on 25th July 2020. Intimation under section 143(1) may be sent up to 31st March 2022.

Processing under section 143(1) be mandated before Assessment.

Under the existing provision of sub-section (1D) of section 143, processing of a return is not necessary where a notice has been issued to the assessee under sub-section (2) of the said section.

Amendment has been made in sub-section (1D) of the Act to provide that before making an assessment under sub-section (3) of section 143, a return shall be processed under sub-section (1) of section 143.

### **(C) SCRUTINY (REGULAR) ASSESSMENT [SECTION 143(2) & (3)]**

Where a return has been made under Section 139, or in response to a notice under Sub-section (1) of Section

142, the Assessing Officer shall, if he considers necessary or expedient to ensure that the assessee has not understated the income or has not computed excessive loss or has not underpaid the tax in any manner, serve on the assessee a notice requiring him, on a date to be specified therein, either to attend his office or to produce, or cause to be produced there, any evidence on which the assessee may rely in support of the return :

Provided that no notice under sub-section (2) shall be served on the assessee after the expiry of six months from the end of the Financial year in which the return is furnished.

On the day specified in the notice issued under Sub-section (2), or as soon afterwards as may be, after hearing such evidence as the assessee may produce and such other evidence as the Assessing Officer may require on specified points, and after taking into account all relevant material which he has gathered, the Assessing Officer shall, by an order in writing, make an assessment of the total income or loss of the assessee, and determine the sum payable by him or refund of any amount due to him on the basis of such assessment.

**E-Assessments** : The Finance Act, 2018 has inserted a new sub-section (3A) in Section 143 that the Central Govt. may make a scheme for the purpose of making assessment so as to impart greater efficiency, transparency and accountability by:

- (a) Eliminating the interface between the Assessing Officer and the assessee in the course of proceeding to the extent technologically feasible.
- (b) Optimising utilization of the resources through economies of scale and functional specialization.
- (c) Introducing a team-based assessment with dynamic jurisdiction.

As part of e-governance initiative to facilitate conduct of assessment proceedings electronically, Income-tax department has launched 'E-Proceeding' facility. Under this initiative, CBDT has made it mandatory for the tax officers to take recourse of electronic communications for all limited and complete scrutiny. The CBDT had issued the instructions and notice formats for conducting scrutiny assessments electronically. As per the instruction, except search related assessments, all scrutiny assessments shall be conducted only through the 'E-Proceeding' functionality available at e-filing website of Income-tax Department.

#### **(D) BEST JUDGMENT ASSESSMENT [SECTION 144]**

The Assessing Officer, after taking into account all relevant material which he has gathered, and after giving the assessee an opportunity of being heard, makes the assessment of the total income or loss to the best of his judgment and determine the sum payable by the assessee on the basis of such assessment in the following cases :

- If any person fails to make the return required under section 139(1) and has not made a return or a revised return under section 139(4) or 139(5), or
- When a person fails to comply with all the terms of a notice issued under section 142(1) or fails to comply with a direction issued under section 142(2A) for getting the accounts audited, or
- If any person having made a return, fails to comply with all the terms of a notice issued under section 143(2).

Prior to the proceedings the AO should issue a show cause notice to the assessee. However if the assessee has already issued notice under section 142(1)(i) and the assessee has not complied with the terms then AO can proceed further without issuing a show cause notice.

Further AO cannot assess the income below returned income and cannot assess losses higher than the returned losses. A refund cannot be granted under section 144.

The assessing officer can also reject the accounts book under section 145 and can make best judgment assessment under section 144 if :

- The accounts books are incorrect, false or incomplete.
- If the accounting method employed is such that the profit cannot be derived from it correctly.
- Where the method of accounting adopted by the assessee is not followed by him regularly or income has not been computed in accordance with notified standards.
- If the assessee has not followed the income computation and disclosure standards notified by the government.

### **(E) INCOME ESCAPING ASSESSMENT OR RE-ASSESSMENT [SECTION 147]**

If the Assessing Officer has reason to believe that any income chargeable to tax has escaped assessment for any assessment year, he may, subject to the provisions of sections 148 to 153,

- assess or reassess income which has escaped assessment or
- recompute the loss or the depreciation allowance or any other allowance, as the case may be for the relevant assessment year.

Section 147, the Assessing Officer shall serve on the assessee a notice requiring him to furnish, within such period, as may be specified in the notice, a return of his income or the income of any other person in respect of which he is assessable under this Act during the previous year corresponding to the relevant assessment year, in the prescribed form, and verified in the prescribed manner and setting forth such other particulars, as may be prescribed; and the provisions of this Act shall, so far as may be, apply accordingly as if such return were a return furnished as per the requirements of Section 139.

Provided that in case a summary assessment or reassessment has been made for the relevant assessment year, no action shall be taken under this section after the expiry of four years from the end of the relevant assessment year, unless any income chargeable to tax has escaped assessment for such assessment year by reason of the failure on the part of the assessee to make a return under section 139 or in response to a notice issued under sub-section (1) of section 142 or section 148 or to disclose fully and truly all material facts necessary for his assessment, for that assessment year :

Provided further that nothing contained in the first proviso shall apply in a case where any income in relation to any asset (including financial interest in any entity) located outside India, chargeable to tax, has escaped assessment for any assessment year :

Provided also that the Assessing Officer may assess or reassess such income, other than the income involving matters which are the subject matters of any appeal, reference or revision, which is chargeable to tax and has escaped assessment.

The following shall also be deemed to be cases where income chargeable to tax has escaped assessment, namely :

- (i) where no return of income has been furnished by the assessee although his total income or the total income of any other person in respect of which he is assessable under this Act during the previous year exceeded the maximum amount which is not chargeable to income-tax ;
- (ii) where a return of income has been furnished by the assessee but no assessment has been made and it is noticed by the Assessing Officer that the assessee has understated the income or has claimed excessive loss, deduction, allowance or relief in the return ;
- (iii) where the assessee has failed to furnish a report in respect of any international transaction which he was so required under section 92E ;
- (iv) where an assessment has been made, but ;

- income chargeable to tax has been under assessed ; or
  - such income has been assessed at too low a rate ; or
  - such income has been made the subject of excessive relief under this Act ; or
  - excessive loss or depreciation allowance or any other allowance under this Act has been computed ;
- (v) Where a return of income has not been furnished by the assessee or a return of income has been furnished by him and on the basis of information or document received from the prescribed income-tax authority, under sub-section (2) of section 133C, it is noticed by the Assessing Officer that the income of the assessee exceeds the maximum amount not chargeable to tax, or as the case may be, the assessee has understated the income or has claimed excessive loss, deduction, allowance or relief in the return.
- (vi) where a person is found to have any asset (including financial interest in any entity) located outside India.

The assessing officer before making the assessment under this section will have to issue notice u/s 148 to the assessee requiring him to file the return even if he has already filed the return under section 139 or 142(1). The AO is duty bound to provide the assessee the reasons recorded by him, if the assessee request for it. If on request the reasons are not supplied then AO cannot proceed the assessment. **The time limit for issue of notice under section 148 is as under :**

<b>Cases</b>	<b><i>Upto 4 years from the end of relevant assessment year</i></b>	<b><i>Beyond 4 years but upto 6 years from the end of the relevant assessment year.</i></b>
Where assessment order passed u/s 143(3) or 147	(i) Notice can be issued for any amount of escaped income.  (ii) Notice can be issued by Assistant Commissioner or Deputy Commissioner and by AO with the approval of Joint Commissioner.	(i) Notice can be issued only if escaped income is of ' 100,000 or more.  (ii) Notice can be issued by the AO only with the approval Chief Commissioner or Commissioner.
Where no assessment order has been passed u/s 143(3) or 147.	Notice can be issued by AO whatever be the amount.	Notice can be issued by the AO only with the approval Joint Commissioner only when the amount is likely to be Rs. 100,000 or more for that year.

However, the time lime of 6 years is not sufficient in cases where assets are located outside India because gathering information regarding such assets takes much more time on account of additional procedures and laws of foreign jurisdictions. Therefore, the time limit for issue of notice for reopening an assessment has been increased to 16 years, where the income in relation to any asset (including financial interest in any entity) located outside India, chargeable to tax, has escaped assessment.

### **Inquiry Before Assessment [Section 142]**

**1. Issue of notice to the assessee to submit return (if not submitted earlier) :** The provisions contained in section 142(1)(i) provides that in a case where a person has not made a return of his income before the end of the relevant assessment year, the Assessing Officer may serve a notice after the end of the relevant assessment year under said sub-section requiring such person to furnish his return of income.

The Assessing Officer may ask to produce, or cause to be produced, such accounts or documents and to furnish in writing and verified in the prescribed manner information in such form and on such points or matters (including a statement of all assets and liabilities of the assessee, whether included in the accounts or not).

However, the previous approval of the Joint Commissioner shall be obtained before requiring the assessee to furnish a statement of all assets and liabilities not included in the accounts. Further, the Assessing Officer shall not require the production of any accounts relating to a period more than three years prior to the previous year.

**2. Make Inquiry and give opportunity of being heard u/s 142(2) :** For the purpose of obtaining full information in respect of the income or loss of any person, the Assessing Officer may make such inquiry as he considers necessary.

**3. Give direction to get books of accounts audited u/s 142(2A) to (2D) :** Having regard to the nature and complexity of the accounts volume of the accounts, doubts about the correctness of the accounts, multiplicity of transaction in the accounts or specialised nature of Business activity of the assessee and the interests of the revenue, assessing officer is of the opinion that it is necessary to order audit then with the previous approval of the Chief Commissioner or Commissioner the Assessing Officer may direct an assessee to get his accounts audited by an accountant even if the accounts have earlier been audited.

The Assessing Officer shall not direct the assessee to get the accounts audited unless the assessee has been given a reasonable opportunity of being heard.

Every report under sub-section (2A) shall be furnished by the assessee to the Assessing Officer within the period as specified by the Assessing Officer.

However, the Assessing Officer may, suo motu, or on an application made in this behalf by the assessee and for any good and sufficient reason, extend the said period by such further period or periods as he thinks fit but shall not exceed 180 days from the date on which the direction under sub-section (2A) is received by the assessee.

The expenses of, and incidental to, such audit (including the remuneration of the Accountant) shall be determined by the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner in accordance with such guidelines as may be prescribed and the expenses so determined shall be paid by the Central Government.

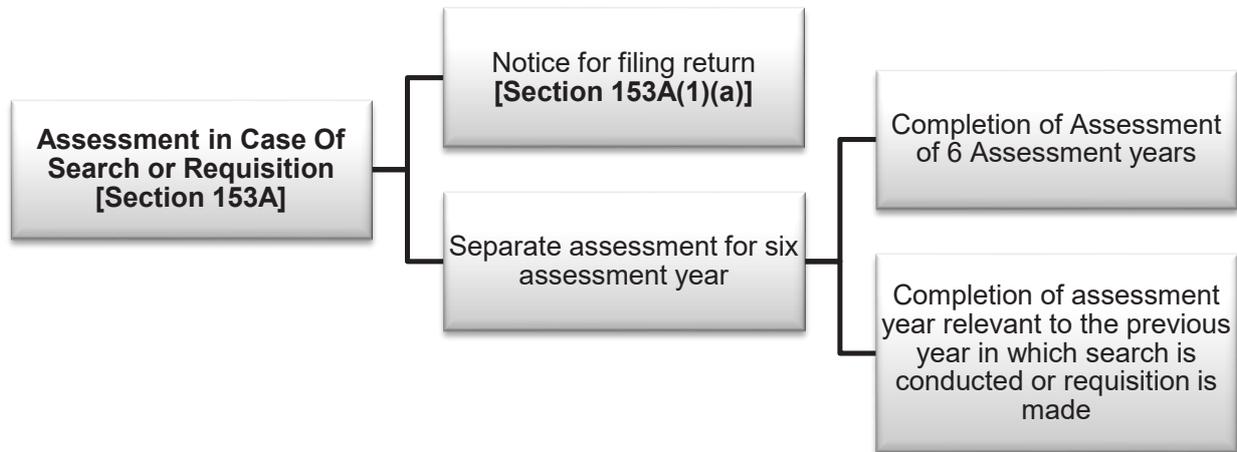
## **(F) PROTECTIVE ASSESSMENT**

Where it is not clear as to who has received the income and prima facie, it appears that the income may have been received either by A or by B or by both together, the Assessing Officer can commence proceedings against both A and B to determine the question as to who is responsible to pay the tax [Lalji Haridas v. I.T.O. (1961) 43 ITR p. 387 (S.C.)].

In protective assessment, the income tax authorities are merely making an assessment until the matter is decided as to who is really liable to pay tax. Further, a protective order of assessment of tax liability can be passed but not an order of penalty. However, it may be noted that protective order for recovery is not permissible.

## **(G) ASSESSMENT IN CASE OF SEARCH OR REQUISITION [SECTION 153A]**

Notwithstanding anything contained in sections 139, 147, 148, 149, 151 and 153 in case of a person where search is initiated under section 132 or books of accounts, other documents or any assets are requisitioned under section 132A after 31.05.2003 the Assessing Officer shall assesses or reassesses the total income of six assessment years immediately proceeding the assessment years relevant to the previous year in which such search is conducted or requisition is made.



### (a) Notice for filing return [Section 153A(1)(a)]

The time limit for completion of assessment /reassessment/re-computation shall be 18 months (12 months from AY 2020-21 onwards) from the end of the assessment year in which income was first assessable first time.

The concerned assessing officer can issue notice for 6 preceding assessment years and for “the relevant assessment year or years”. For this purpose “relevant assessment year” shall mean an assessment year preceding the assessment year relevant to the previous year in which search is conducted or requisition is made which falls beyond 6 assessment years but not later than 10 assessment years from the end of the assessment year relevant to the previous year in which search is conducted. However, for the “relevant assessment year” notice can be issued if-

- The assessing officer has in his possession books of accounts or other documents or evidence which reveal that the income which has escaped assessment amounts to (or likely to amount) to Rs. 50 lakhs (or more) in one year or in aggregate in the relevant 4 assessment years falling beyond 6 assessment years.
- Such income escaping assessment in the form of asset( for this purpose “asset” shall include immoveable property being land or building or both, shares and securities, loans and advances, deposits in bank account);
- The income escaping assessment or part thereof relates to such year or years; and
- Search under section 132 is initiated or requisition under section 132A is made on or after April 1, 2017.

Income tax authorities are not required to disclose reason for conducting search before any person, authority or Tribunal for such 6 assessment year as per amended section 132. However, this concession is not available in respect of “relevant assessment year or years” beyond such 6 assessment years.

### (b) Separate assessment for six assessment year

The Assessing Officer shall assess or reassess the total income of each of such six assessment year [Proviso 1 to section 153(1)].

#### (i) Time limit of completion of Assessment of 6 Assessment years [Section 153B(1 )(a)]

The Assessing officer shall make an order of assessment or re-assessment in respect of each assessment year falling within six assessment years under section 153A [Assessment in case of search or requisition] within a period of 21 months from the end of the financial year in which the last of the authorization for search under section 132 [search and seizure] or for requisition under section 132A [Powers to requisition books of accounts] was executed.

Where the search was executed and during the course of proceedings for the assessment or re-assessment, a reference under section 92CA(1) is made the period for making an order of assessment or reassessment shall be extended by 12 months.

**(ii) Time limit of completion of assessment of assessment year relevant to the previous year in which search is conducted or requisition is made [Section 153(1)(b)]**

Time limit of completion of assessment in respect of the assessment year relevant to the previous year in which search is conducted under section 132 or requisition is made under section 132A within a period of 21 months from the end of the financial year in which the last authorizations for search under section 132 or for requisition under section 132A was executed.

In case assessment has a reference to section 92CA(1), then the above period shall be extended by 12 months.

**Estimation of value of assets by Valuation Officer [Section 142A]**

- (1) The Assessing Officer may, for the purposes of assessment or reassessment, make a reference to a Valuation Officer to estimate the value, including fair market value, of any asset, property or investment and submit a copy of report to him.
- (2) The Assessing Officer may make a reference to the Valuation Officer under sub-section (1) whether or not he is satisfied about the correctness or completeness of the accounts of the assessee.
- (3) The Valuation Officer, on a reference made under sub-section (1), shall, for the purpose of estimating the value of the asset, property or investment, have all the powers that he has under section 38A of the Wealth-tax Act, 1957. (Wealth Tax has been abolished by Finance Act, 2015)
- (4) The Valuation Officer shall, estimate the value of the asset, property or investment after taking into account such evidence as the assessee may produce and any other evidence in his possession gathered, after giving an opportunity of being heard to the assessee.
- (5) The Valuation Officer may estimate the value of the asset, property or investment to the best of his judgment, if the assessee does not co-operate or comply with his directions.
- (6) The Valuation Officer shall send a copy of the report of the estimate made under sub-section (4) or sub-section (5), as the case may be, to the Assessing Officer and the assessee, within a period of six months from the end of the month in which a reference is made under sub-section (1).
- (7) The Assessing Officer may, on receipt of the report from the Valuation Officer, and after giving the assessee an opportunity of being heard, take into account such report in making the assessment or reassessment.

*Explanation.* – In this section, “Valuation Officer” has the same meaning as in clause (r) of section 2 of the Wealth-tax Act, 1957. (Wealth Tax has been abolished by Finance Act, 2015)

**Time limit for completion of Assessments and Re-assessments [Section 153]**

**(1) As per Section 153(1), the time limit for making assessment under section 143(3) [scrutiny assessment] and 144 [best judgment assessment] is:-**

- (a) Within 21 months from the end of the assessment year in which the income was first assessable. [For assessment year 2017-18 or before]
- (b) 18 months from the end of the assessment year in which the income was first assessable. [For assessment year 2018-19]

- (c) 12 months from the end of the assessment year in which the income was first assessable [Assessment year 2020-21 and onwards]

Note:- If reference is made to Transfer Pricing Officer (TPO), the period available for assessment shall be extended by 12 months.

**(2) As per Section 153(2), the time limit for making assessment under section 147 [ income escaping assessment ] is:-**

- (a) Within 9 months from the end of the financial year in which the notice under section 148 was served (if notice is served before 01-04-2019).
- (b) 12 months from the end of the financial year in which notice under section 148 is served (if notice is served on or after 01-04-2019).

Note:- If reference is made to Transfer Pricing Officer TPO, the period available for assessment shall be extended by 12 months.

**(3) Section 153(2A) deals with assessment where original assessment has been cancelled or set aside by the Appellate Authority under section 250 (Procedure in hearing), 254 (Order of Appellate Tribunal) or by Commissioner of Income Tax under section 263 (Revision of Orders, Prejudicial to Revenue), 264 (Revision of Orders in favour of Assessee) :** The Time limit for completion of Assessment/Re-Assessment is 12 months from end of the Financial Year in which –

- (a) Such order of set aside or cancelling the order is passed by the Appellate Authority under section 250 or 254 received by commissioner of Income Tax.
- (b) Order under section 263 or 264 was passed by the Commissioner of Income Tax.

However, if reference was made to Transfer Pricing Officer under section 92CA(1) during the course of proceeding such period shall be extended by 12 months for completion of assessment.

*Note :* The Commissioner (Appeals) cannot cancel or set aside the Assessment and refer the case to the Assessing Officer for fresh assessment. However, it can be set aside by ITAT or Commissioner under section 263 or 264.

(4) Where effect to an order under section 250 or section 254 or section 260 or section 262 or section 263 or section 264 is to be given by the Assessing Officer, wholly or partly, otherwise than by making a fresh assessment or reassessment, such effect shall be given within a period of three months from the end of the month in which order under section 250 or section 254 or section 260 or section 262 is received by the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner, as the case may be, the order under section 263 or section 264 is passed by the Principal Commissioner or Commissioner :

Provided that where it is not possible for the Assessing Officer to give effect to such order within the aforesaid period, for reasons beyond his control, the Principal Commissioner or Commissioner on receipt of such request in writing from the Assessing Officer, if satisfied, may allow an additional period of six months to give effect to the order. **[Amendment vide Finance Act, 2016]**

(5) Section 153(4) deals with the cases where any Proceeding initiated or order of assessment/re-assessment made under 153A(1) [relating to assessment of search cases] has been annulled in an appeal or in other legal proceedings and assessment/re-assessment relating to assessment year which was abaited has been revived :

In such case the time limit for completion of Assessment/Re-Assessment is 1 year from end of the month of such revival or within the time specified in section 153 or section 153B(1) [prescribe time limit for completion of assessment under section 153A] whichever is later.

### Rationalisation of Time Limit for Assessment, Reassessment and Recomputation and Assessment in Search Cases

Section 153/ 153B of the Act has been amended vide Finance Act, 2019 with the following changes in time limit from the existing time limits :

<b>Section reference</b>	<b>New time limit</b>
Regular assessment u/s 143/Best judgment assessment u/s 144	21 months from the end of the AY in which income was first assessable
Reassessment u/s 147	9 months from the end of the financial year in which notice for reassessment is served 12 months if notice u/s 148 served on or after 1.4.2019
An order of fresh assessment as a result of an order u/s 254 or 263 or 264 setting aside or cancelling an assessment	9 months from the end of the financial year in which such order is received by prescribed authorities 12 months If order passed on or after 1.4.2019
An order giving effect otherwise than making a fresh assessment or reassessment	3 months from the end of the month in which such order is received by prescribed authorities and additional period of six months, where it is not possible to pass such order by assessing officer for reasons beyond its control. For cases pending on 01.06.2016, time limit extended to 31.03.2017
Assessment, reassessment or recomputation to give effect to any finding or direction contained in the order of CIT, CIT(A), ITAT or any court	12 months from the end of the month in which such order is received. For cases pending on 01.06.2016, time limit extended to 31.03.2017 or 12 months from the end of the month in which the order is received, whichever is later.
Assessment is made on partner on firm in consequence of assessment made on firm u/s 147	12 months from the end of month in which the assessment order in case of the firm is passed
Reference made to TPO u/s 92CA	Additional time period of 12 months granted from end of normal time limit
Assessment u/s 153A	21 months from the end of the financial year in which the last of the authorisations for search u/s 132 or for requisition u/s 132A was executed 18 months w.e.f. 1.4.2018 12 months w.e.f. 1.4.2019
Assessment u/s 153C	21 months from the end of the financial year in which the last of the authorisation for search u/s 132 or requisition u/s 132A was executed. 18 months w.e.f. 1.4.2018 12 months w.e.f. 1.4.2019

### Computation of Period of limitation

In computing the period of limitation for this purpose, the time taken in the following cases shall be excluded :

- (i) the time taken in re-opening the whole or part of the proceeding or in giving an opportunity to the assessee to be re-heard under section 129;
- (ii) the period during which the assessment proceeding is stayed by an order or injunction of any court;
- (iii) the period commencing from the date on which the Assessing Officer directs the assessee to get his accounts audited under section 142(2A) and ending with the last date on which the assessee is required to furnish a report of such audit or where such direction is challenged before a court, ending with the date on which order is setting aside the date on which such direction is received by the commissioner;
- (iv) the period (not exceeding 60 days) commencing from the date on which the declaration under Section 158A(1) is received by the Assessing Officer and ending with the date on which the order thereunder is made by him;
- (v) where an application made before the Income-tax Settlement Commission is rejected by it, the period commencing from the date on which application is made and ending with the date on which the order is received by the Chief Commissioner or Commissioner.
- (vi) the period commencing from the date on which an application is made before the Authority for Advance Rulings under sub-section (1) of section 245Q and ending with the date on which the order rejecting the application is received by the Commissioner under sub-section (3) of section 245R, or
- (vii) the period commencing from the date on which an application is made before the Authority for Advance Rulings under sub-section (1) of section 245Q and ending with the date on which the advance ruling pronounced by it is received by the Commissioner under sub-section (7) of section 245R; or
- (viii) the period commencing from the date on which reference or first of the references for the exchange of information is made by the authority competent under an agreement referred to in section 90 or section 90A and ending with the date on which the information requested is last received by the commissioner or a period of one year whichever is less; or

The period commencing from the date on which the Assessing Officer makes a reference to the Valuation Officer under section 142A and ending with the date on which the report of the Valuation Officer is received by the Assessing Officer.

## APPEAL

***An appeal is a complaint to a superior authority of an injustice done by inferior authority. The party complaining is called "Appellant" and the other party is known as "Respondent"***

## INTRODUCTION

The right to appeal must be given by express enactment in the Act. Therefore, in case there is no provision in the Act for filing an appeal regarding a particular matter, no appeal shall lie. The right to appeal arises where the taxpayer is aggrieved by the order passed by the income-tax authority. However, where the Assessing Officer accepts the return filed by the tax payer and passes an order making no modification, an appeal does not lie against that order as the taxpayer cannot be said to be aggrieved of that order. Similarly, where an appellate authority accepts the contention of the taxpayer and allows the appeal, there is no further appeal by the assessee against that order.

The assessee may prefer an appeal against the orders of the Assessing Officer to the Commissioner (Appeals), in accordance with the relevant provisions under Section 246 and appeal against the order of the Commissioner (Appeals) can be preferred by the Assessee or the Commissioner of Income Tax and such appeal lies with the Appellate Tribunal.

The Finance (No.2) Act, 1998 has amended the provisions regarding remedy against order of Tribunal. Where

earlier the assessee or the CIT, if not satisfied with the order of Tribunal, could only request the Tribunal to refer that matter to the High Court. After 1.10.98 as provided by Finance (No.2) Act, 1998 the assessee or CIT if not satisfied with the order of the tribunal can appeal directly to the High Court, if High Court is satisfied that the case involve a substantial question of law and if the assessee or Commissioner of Income-tax is not satisfied with the order passed by the High Court they may file an appeal against the order of the High Court to the Supreme Court. However, it should be noted that in the case of question of fact tribunal is the final & binding authority and its decision is final.

### **APPEALS ORDERS BEFORE COMMISSIONER (APPEALS)**

Appealable order before Commissioner (Appeals) [Section 246A]

Any assessee or any deductor or any collector aggrieved by any of the following orders may appeal to the Commissioner (Appeals) :

- (a) against an order passed by a Joint Commissioner under Clause (ii) of Sub-section (3) of Section 115VP or an order against the assessee where he denies his liability to be assessed under the Income Tax Act, or an intimation under section 143 (1) or (1B) or section 200A(1) or section 206CB(1), where the assessee or deductor or collector objects to making of adjustment or any order of assessment under section 143(3) except an order passed in pursuance of directions of Dispute Resolution Panel or Section 144 where assessee object to the amount of income assessed or amount of tax determined or amount of loss computed or status under which he is assessed;
- (b) against an order of assessment, re-assessment or re-computation under Section 147 except an order passed in pursuance of directions of dispute resolution panel or Section 150;
- (ba) an order of assessment or reassessment under Section 153A except an order passed in pursuance of directions of dispute resolution panel;
- (bb) an order of assessment or re-assessment under section 92CD(3);
- (c) against an order of rectification of mistake under Section 154 or Section 155 having effect of enhancing assessment or reducing refund or order refusing to allow claim made by assessee under these sections;
- (d) against an order under Section 163 treating the assessee as the agent of a non-resident;
- (e) against an order under Section 170(2) or 170(3) relating to succession of business otherwise on death;
- (f) against an order made under Section 171;
- (g) against an order under Section 185;
- (h) against an order cancelling the registration of firm under section 186(1) or (2);
- (i) against an order under Section 237;
- (j) against an order under Section 201 or 206 (C)(A);
- (k) A person deemed to be an assessee in default for not collecting the whole or any part of tax or after collecting the tax, failing to pay the same, may appeal before Commissioner (Appeals) on or after April 1, 2007.
- (l) against an order imposing a penalty under Section 221, 271, 271A, 271AAA, 271AAB, 271F, 271FB, 272AA, Section 272, 272B, 272BB or Section 273;
- (m) an order of imposing or enhancing penalty under Section 275(1A);
- (n) against an order of assessment made by an assessing officer under clause (c) of Section 158BC, in respect of search initiated under Section 132 or books of account, other documents or any assets

requisitioned under Section 132A;

- (o) against an order imposing a penalty under Sub-section (2) of Section 158BFA;
- (p) against an order imposing penalty under Section 271B or Section 271BB;
- (q) against an order made by a Joint Commissioner imposing a penalty under Section 271C, Section 271CA, Section 271D or Section 271E;
- (r) against an order made by a Joint Commissioner imposing a penalty under Section 272AA and by a Joint Commissioner or Joint Director under Section 279A;
- (s) against an order imposing a penalty under Chapter XXI of Income tax Act;
- (t) against an order made by an Assessing Officer other than a Joint Commissioner under the provisions of this Act, in case of specified person or classes of persons.

Where a person has deducted and paid tax in accordance with Section 195 and 200 in respect of any sum (other than interest) chargeable under the Act he is entitled to prefer an appeal under Section 248 to be declared not liable to deduct tax. In other words, the right to appeal under Section 248 is conditional and can be exercised only if tax is deducted at source and paid to the Government.

Section 248 provides that where under an agreement or other arrangement, the tax deductible on any income (not being interest) under Section 195 is to be borne by the payer (i.e., "net of tax" arrangement) and such person having paid such tax to the credit of the Central Government, claims that no tax was required to be deducted on such income, he may appeal to the Commissioner (Appeals) for a declaration that no tax was deductible on such income.

### PROCEDURE FOR FILING OF APPEAL [SECTION 249(1)]

The appeal should be filed in the prescribed form and verified in the prescribed manner. In case of an appeal made to the Commissioner (Appeals) on or after the 1st day of October, 1998, it shall be accompanied by a fees irrespective of the date of initiation of the assessment proceedings. The rates of fees are as follows :

SI No	Assessed Income	Fees
1	Rs. 1,00,000 or less	Rs. 250
2	More than Rs. 1,00,000 but not more than Rs. 2,00,000	Rs. 500
3	More than Rs. 2,00,000	Rs. 1000
4	Any other case	Rs. 250

Form No. 35 is the prescribed form [under Rule 45(1)] of the appeal. The form of appeal, the grounds and the verification appended to the form should be signed [Rule 45(2)] as per provisions applicable to the signing of return under Section 140.

Form No.35 requires that the memorandum of appeal, statement of facts and the grounds of the appeal must be in duplicate and should be accompanied by a copy of the order appealed against and the notice of demand in original, if any.

### PERIOD OF LIMITATION TO PREFER AN APPEAL [SECTION 249(2)]

The appeal has to be presented within the period of limitation as given below :

**1. Appeal by person denying liability to deduct tax in respect of payments payable to non-resident or a foreign company [Section 249(2)(a)] :** Where the appeal relates to any tax deducted at source from payment made to a non-resident, (other than a company) or to a foreign company, any interest, other 'than interest on

securities or any other sum chargeable under the provisions of the Income Tax Act (not being salaries), within 30 days from the date of payment of tax deducted at source to the credit of the Central Government.

**2. Appeal against assessment to penalty [Section 249(2)(b)] :** Where the appeal relates to any assessment or penalty order the appeals have to be presented within 30 days of the date of service of the notice of demand relating to that assessment or penalty order.

**3. Other appeals [Section 249(2)(c)] :** In any other case, the appeal has to be presented within 30 days of the date on which intimation of the order sought to be appealed against is served on the appellant.

In computing the period of limitation for an appeal or an application, the day on which the order is served has to be excluded. If the assessee was not furnished with a copy of the order along with the notice of the order, or demand, the time required for obtaining a copy of such order is also to be excluded and the date will be extended by that period. It may be noted that even where the assessee has not been supplied with copy of the order concerned, the time taken in making an application which does not comply with all the legal requirements cannot be excluded under the provisions of Section 268. If the application for obtaining the copy of the order has not been properly stamped or has been made by a person not authorised to do so, the time which has elapsed between the making of the invalid application and putting the application in order would not be excluded in computing the period of limitation.

If any appeal is filed after the period of limitation, the Commissioner (Appeals) may admit the appeal after the said period if he is satisfied that the appellant had sufficient cause for not presenting the appeal within that period [Section 249(3)]. Such delayed appeals must be accompanied by a condonation petition showing and explaining the reason/cause of the appellant for not being able to file the appeal within the period of limitation and praying for condemnation of the delay. The power to condone the delay is discretionary and the discretion must be judiciously exercised. The discretion is to be exercised where sufficient cause for not presenting the appeal within the time is made out by the appellant. The period for filing an appeal cannot be extended simply because the appellant's case is hard and calls for sympathy or merely out of benevolence to the party seeking relief. The sufficient cause must be a cause which is beyond the control of the party seeking the condonation of the delay. Illness is sufficient cause, if it can be shown that the man was utterly disabled to attend to any duty. The cause for delay in filing the appeal which, by due care and attention could have been avoided cannot be a sufficient cause. Negligence on the part of the servants or agent entrusted with the filing of the appeal cannot be considered as a sufficient cause. The change of legal situation brought about by a decision of the Supreme Court may be valid ground for condoning delay. The words "sufficient cause" should receive a liberal interpretation so as to advance substantial justice where no negligence nor inaction nor want of bona fide is imputable to the applicant.

An appeal presented after the period of limitation is still an "appeal" and an order dismissing it as time barred is one passed in appeal [under Section 250 and not under Section 249(3)]. An appeal lies therefrom to the Appellate Tribunal and thereafter to the High Court on a question of law.

Provided further that where an application has been made under sub-section (1) of section 270AA, the period beginning from the date on which the application is made, to the date on which the order rejecting the application is served on the assessee, shall be excluded.

#### **PAYMENT OF TAX BEFORE FILING APPEAL [SECTION 249(4)]**

No appeal against any order passed by the Assessing Officer can be admitted by the Commissioner (Appeals) unless at the time of filing of the appeal the assessee has paid tax due on the income returned by him, or where the assessee has not furnished the return of income, he has paid an amount equal to the amount of advance tax which was payable by him. If the appellant wants exemption from the payment of such tax he has to make an application to the Commissioner (Appeals) who is empowered to waive this requirement in appropriate cases if he is satisfied that there are good and sufficient reasons for doing so. In such cases, the Commissioner (Appeals) is required to record such reasons in writing. It may be noted that Income-tax law requires only the

payment of tax before the filing of the appeal and not the payment of any penalty or any other sum payable by the assessee on the basis of the order appealed against.

**PROCEDURE IN APPEAL [SECTION 250]**

Commissioner (Appeals) shall fix a day and place for the hearing of the appeal and shall give notice of the same to the appellant and to the Assessing Officer against whose order the appeal is preferred.

The following shall have the right to be heard at the hearing of the appeal :

- (a) The appellant, either in person or by an authorised representative.
- (b) The Assessing Officer, either in person or by a representative.

The Commissioner (Appeals) shall have the power to adjourn the hearing of the appeals from time to time. He may, before disposing of any appeal, make such further enquiry as he deems fit, or may direct the Assessing Officer to make further enquiry and report as he deems fit, or may direct the Assessing Officer to make further enquiry and report the result of the same to the Commissioner (Appeals).

The Commissioner (Appeals) may, at the hearing of an appeal, allow the appellant to go into any ground of appeal not specified in the grounds of appeal if he is satisfied that the omission of that ground from the form of appeal was not willful or unreasonable. His order disposing of the appeal shall be in writing and shall state the points for determination, the decision thereon and the reasons for the decision. In every appeal, the Commissioner (Appeal), where it is possible, may hear and decide such appeal within a period of one year from the end of the financial year in which such appeal is filed before him Commissioner (Appeal) under Section 246A(1). On the disposal of the appeal, the Commissioner (Appeals) shall communicate the order passed by him to the assessee and to the Chief Commissioner or Commissioner.

Appeal by Income tax department shall be filed before appellate Tribunal, High court and Supreme Court only where the tax effect of appeal exceeds the following monetary limits:

Appeal in Income tax matter	Monetary Limit
Before ITAT	INR 20,00,000
Before High Court	INR 50,00,000
Before Supreme Court	INR 1,00,00,000

**POWERS OF THE COMMISSIONER (APPEALS) [SECTION 251]**

In disposing of an appeal, the Commissioner (Appeals) shall have the following powers :

1. In an appeal against an order of assessment, he may confirm, reduce, enhance or annul the assessment.
2. In an appeal against an order imposing a penalty, he may confirm or cancel such order or vary it so as to either enhance or reduce the penalty.
3. In any other case, he may pass such orders in the appeal as he deems fit.

The Commissioner (Appeals) shall not enhance an assessment or a penalty or reduce the amount of refund unless the appellant has had a reasonable opportunity of showing cause against such enhancement or reduction.

While disposing an appeal, the Commissioner (Appeals) may consider and decide the facts arising out of the proceedings which in respect of order appealed against were carried notwithstanding that such matter was not raised before the Commissioner (Appeals) by the appellant.

In an appeal against the order of assessment in respect of which the proceedings before the Settlement

Commission abates under the section 245HA, the Commissioner (appeals) can confirm, reduce, enhance or annul the assessment after taking into consideration of the following -

1. the material and other information produced by the assessee before the Settlement Commission
2. the results of the enquiry held by the Settlement Commission
3. the evidence recorded by the Settlement commission in the course of proceedings before it
4. such other material as may be brought on his record.

## REVISIONS

### REVISION BY THE COMMISSIONER OF INCOME TAX [SECTIONS 263 AND 264]

The right to file such appeals against the orders of the Assessing Officer is not available to the Department. It is for this reason that the Commissioner has been vested with revisional powers under Section 263, where the order of the Assessing Officer is erroneous in so far as it is prejudicial to the interests of the revenue. But such revisional power can be exercised only in respect of orders which are not the subject matter of appeals. The reason is that once an assessment order is appealed against, the Commissioner (Appeals) has got the powers to enhance the assessment under Section 263 and a right of appeal upto the Tribunal is provided to the assessee against the orders of the Assessing Officer. In the following cases Commissioner of Income-tax can revise an order passed by the Assessing Officer :

#### REVISION BY THE COMMISSIONER OF INCOME TAX

Revision of orders prejudicial to the interest of Revenue [Section 263]	Revision of order in the interest of Assessee [Section 264]	Circumstances in which no revision can be made [Section 264(4)]
<ul style="list-style-type: none"> <li>• Revision can be only of the order of Assessing Officer [Section 263(1)]</li> <li>• Order erroneous and prejudicial to the interest of revenue [Section 263(1)]</li> <li>• Assessee to be given an opportunity of being heard [Section 263(1)]</li> <li>• Time limit for making the revisional order [Sections 263(2) and (3)]</li> </ul>	<ul style="list-style-type: none"> <li>• Revision of order of subordinate authority only [Section 264(1) and Explanation 2]</li> <li>• Suo motu revision [Section 264(1) and (2)]</li> <li>• Revision on application of the assessee [Section 264(1), (3) &amp; (5)]</li> <li>• Nature of the order [Section 264]</li> </ul>	<ul style="list-style-type: none"> <li>• If the order is appealable to the Commissioner (Appeals), such order cannot be revised until the time within which such appeal may be made expires.</li> <li>• The order is appealable to the Commissioner or the Appellate Tribunal, revisional power cannot be exercised until the time within which such appeal may be made expires.</li> </ul>

### REVISION OF ORDERS PREJUDICIAL TO THE INTEREST OF REVENUE [SECTION 263]

The Department has no right of appeal to the Commissioner (Appeals) against any order passed by the Assessing Officer. Therefore, the Commissioner of Income-tax has been empowered to revise such orders of the Assessing Officer as are prejudicial to the interest of the revenue. Such power, however, is subject to certain conditions as given below :

#### 1. Revision can be only of the order of Assessing Officer [Section 263(1)]

The Commissioner of Income-tax can revise only the orders of Assessing Officer. For the purposes of this clause, an order passed by the Assessing Officer includes an order of assessment passed on or before or after 1.6.1988, including : (i) an assessment order made by the Assistant Commissioner or the Income Tax Officer on the basis of the directions issued by the Joint Commissioner under Section 144A, (ii) an order made by the Joint Commissioner in exercise of the powers or in performance of the functions of an Assessing Officer conferred

on, or assigned to him under the orders or directions issued by the Board or by the Chief Commissioner or Director General or Commissioner authorised by the Board in this behalf under Section 120 [Jurisdiction of Income Tax authorities].

An explanation to the above sub section has been inserted by Finance Act, 2015, w.e.f 1.6.15 that an order passed by the Assessing Officer shall be deemed to be erroneous in so far as it is prejudicial to the interests of the revenue, if, in the opinion of the Principal Commissioner or Commissioner, –

- (a) the order is passed without making inquiries or verification which should have been made;
- (b) the order is passed allowing any relief without inquiring into the claim;
- (c) the order has not been made in accordance with any order, direction or instruction issued by the Board under section 119; or
- (d) the order has not been passed in accordance with any decision which is prejudicial to the assessee, rendered by the jurisdictional High Court or Supreme Court in the case of the assessee or any other person.”.

In case the order referred to above has been the subject matter of any appeal filed on or before or after June 1, 1988 the powers of the Commissioner shall extend and shall always be deemed to have extended to such matters as had not been considered and decided in such appeal. The appellate orders passed by the Commissioner (Appeals) are outside the purview of the revisional powers vested in the Commissioner of Income-tax. But if the assessment order of the Assessing Officer is pending in an appeal before the appellate authority (as aforesaid), it can be revised by the Commissioner of Income-tax. So long the appeal is not disposed of, the order of the Assessing Officer will be considered as subsisting and operative. Therefore, it can be revised.

## 2. Order erroneous and prejudicial to the interest of revenue [Section 263(1)]

If the Commissioner of Income-tax considers that the order of the Assessing Officer is erroneous in so far as it is prejudicial to the interest of the revenue, such order can be revised after giving the assessee an opportunity of being heard.

The word “erroneous” includes cases where there has been a failure to make the necessary enquiries. The Commissioner of Income-tax may consider an order of the Assessing Officer to be erroneous not only if it contains some apparent error of reasoning or of law or of fact on the face of it but also because it is a stereotype order which simply accepts what the assessee has stated in his return and fails to make enquiries which are called for in the circumstances of the case. The Assessing Officer is not only an adjudicator but also an investigator. He cannot remain passive in the face of a return which is apparently in order but calls for further enquiry. It is his duty to ascertain the truth of the facts stated in return when the circumstances of the case are such as to provoke enquiry.

The words “prejudicial to the interests of revenue” appearing under Section 263(1) have not been defined in the Act, but they must mean that the order of the Assessing Officer is such, that it is not in accordance with law in consequence whereof the lawful revenue due to the State has not been realised or cannot be realised. The Allahabad High Courts’ decision in *Commissioner of Income-tax v. Sunder Lal* (1974, 96 ITR 310) was followed by it in *Commissioner of Income-tax v. Kashi Nath & Co.* 1988, 170 ITR 28) holding that the power of the Commissioner of income-tax under Section 263 of the Income Tax Act is quasi-judicial in character. He must give reasons in support of his conclusion that the assessment order is erroneous in so far as it is prejudicial to the interests of the Revenue. If he does not give the reasons, the order can be vitiated. For example, if the Commissioner is of the opinion that the Assessing Officer had allowed deductions in excess of what they were due in a particular case, such order is erroneous and prejudicial to the interests of the revenue. Hence, it may be revised by the Commissioner of Income Tax.

In *Malabar Industrial Co. Ltd. v. Commissioner Income Tax* (1992, 198 ITR 611) the Kerala High Court held that the words ‘prejudicial to the interests of the revenue’ are of wide import and they should not be limited to a

case where the order passed by the Income-tax Officer (now Assessing Officer) can be considered to be one prejudicial to the revenue administration as such. The question whether an order of the Income Tax Officer is prejudicial to the interests of revenue would depend on the facts of each case and there can be no universal formula applicable to finding out any such prejudicial error. The High Court followed the rule laid down by the Supreme Court in *Tara Devi Aggarwal v. CIT (1973, 88 ITR 523)* but dissented from the rule laid down by the Madras High Court in *Venkatakrishna Rice Co. v. CIT (1987, 163 ITR 129)*.

The Commissioner can revise an order passed by the Assessing Officer only if it is erroneous and prejudicial to the interests of the revenue; if the order sought to be revised is not prejudicial to the interest of the revenue the Commissioner has no jurisdiction to revise it. The failure of the Assessing Officer to deal with the claim of the assessee in the assessment order may be an error, but an erroneous order by itself is not enough to give jurisdiction to the Commissioner to revise it under Section 263. It must be further shown that the order was prejudicial to the interests of the revenue.

### **3. Assessee to be given an opportunity of being heard [Section 263(1)]**

The process of revision is completed in three stages : (i) the Commissioner may call for and examine the records of any proceeding under the Act which is within his administrative powers. If after examining the material and relevant facts on record, the Commissioner considers prima facie that any order of the Assessing Officer is erroneous and prejudicial to the interest of the revenue, he must, in the (ii) place, give the assessee an opportunity of being heard. The opportunity of being heard to be given to the assessee contemplates that the Commissioner must disclose to the assessee the grounds on which he desires to make a revision under Section 263. This is essential. If the assessee does not know on what points he is to be heard, he may not visualise what he has to say at the hearing and the opportunity of being heard may prove to be illusory. Further, the notice to show cause must be served on the assessee reasonably ahead of the date fixed for hearing, because the time allowed to the assessee to prepare the case should not be short but reasonable. The Commissioner is also required to examine the merits of the objection raised by the assessee. Without going into the merits of the claim of the assessee, it is not possible for the Commissioner to say that the order of the Assessing Officer has caused any prejudice to the interests of the revenue. He may also cause enquiry to be made by his subordinates. Before making his order, he must disclose to the assessee the material collected by him on enquiry if he wants to use the materials collected from such inquiry against the assessee. If the matter collected from the enquiry is only supporting material and does not constitute the basic grounds on which the revision order is to be passed, the failure of the Commissioner to disclose to the assessee the fact of the enquiry does not vitiate the revision order.

In the third stage, the Commissioner is required to pass the necessary order if he finally concludes that the order of the Assessing Officer is erroneous and prejudicial to the interests of the revenue. He can enhance or modify the assessment. He has also the power to cancel the assessment and direct a fresh assessment. The power of cancellation of the assessment with a direction to make a fresh assessment is called for only in cases where there is something totally or basically wrong with the assessment which is not capable of being remedied by amendments to the assessment order itself. Where the Commissioner comes to the conclusion that there is a defect in the assessment order in so far as the question of the levy of interest was not considered by the Assessing Officer, the Commissioner should direct the Assessing Officer to consider the question on merits and in accordance with law after giving the assessee an opportunity of being heard. It is not further necessary for him, nor would the circumstances of the case justify, that the whole assessment should be set aside. Setting aside the assessment has got far reaching consequences and such power should be exercised only where the circumstances call for a remedial action. The revisional order must be a speaking order giving reasons for such revisions otherwise the order may be vitiated. The power of suo-moto revision of the Commissioner of Income- tax under Section 263(1) is in the nature of supervisory jurisdiction and can be exercised only if the circumstances specified therein exist. Two circumstances must exist : (i) the order should be erroneous, and (ii) by virtue of the order being erroneous, prejudice must have been caused to the interests of the revenue. An order cannot be termed as erroneous unless it is not in accordance with law. If an Income-tax Officer

acting in accordance with law makes certain assessment, the same cannot be termed as erroneous by the Commissioner simply because according to him, the order should have been written more elaborately. In this case, the Tribunal was held justified in setting aside the order passed by the Commissioner under Section 263.

#### **4. Time limit for making the revisional order [Sections 263(2) and (3)]**

The revisional order can be passed within two years from the end of the financial year in which the order sought to be revised was passed [Section 263(2)]. Once the revisional order is made within the time limit of two years from the end of the relevant financial year it is a valid order even if it is served on the assessee after the expiry of two years.

In computing the time limit of two years, the time taken in giving an opportunity to the assessee to be reheard (under Section 129) and any period during which the proceeding (under Section 263) is stayed by an order or injunction of any court is excluded [Explanation to Section 263(2)]. Order under Section 263 can't be passed to reduce tax utility or in favour of assessee. However Appeal against Section 263 can be made to ITAT.

It may be noted that the limit of two years does not apply to a revisional order which had been passed in consequences of or to give effect to, any finding or direction contained in an order of the Appellate Tribunal, the High Court or the Supreme Court. Such revisional order may be passed at any time [Section 263(3)].

### **REVISION OF ORDER IN THE INTEREST OF ASSESSEE [SECTION 264]**

An aggrieved assessee has his normal right of appeal against the order of the Assessing Officer to Commissioner (Appeals) under Section 246A and thereafter to the Appellate Tribunal under Section 253. Further, each and every order of the Assessing Officer is not appealable to the appellate authorities under Sections 246A and 253. The assessee may seek justice in such cases by making an application under section 264 to the Commissioner of Income Tax. For example, revision lies to the Commissioner against the levy of penal interest for not furnishing the return of total income within the prescribed time against which no appeal has been provided.

The revisional order passed under Section 264 cannot be prejudicial to the interest of the assessee. The whole subject matter is discussed below -

#### **1. Revision of order of subordinate authority only [Section 264(1) and Explanation 2]**

The Principal Commissioner or Commissioner of Income Tax may revise any order of an authority subordinate to him. Deputy Commissioner, Income Tax Officers and Inspectors of Income Tax are subordinate to the Principal Commissioner or Commissioner according to Section 118.

#### **2. Suo motu revision [Section 264(1) and (2)]**

The Principal Commissioner or Commissioner may, suo motu call for the record of any proceeding under this Act in which any, order has been passed by any authority subordinate to him. He may make such enquiry and may pass such order as he thinks fit but such order cannot be prejudicial to the assessee [Section 264(1)]. He may act in such circumstances without notice to the assessee and without giving him an opportunity of being heard. Such exercise of the authority is a purely departmental affair and the assessee may know nothing about this. While acting suo motu, the Commissioner may revise the order of his subordinate authority within one year from the date of the order sought to be revised [Section 264(2)]. If the order has been made more than one year back, such order cannot be revised by him.

It is obligatory on the Principal Commissioner or Commissioner to pass an order under Section 264 within a period of one year from the end of financial year in which the application is made for revision. In computing the period of limitation, the time taken in giving an opportunity to the assessee to be re-heard (under Section 129) and any period during which any proceeding under this Section is stayed by an order or injunction of any court is excluded. Though an order has, to be passed within one year, an order in revision may be passed at any time in consequence of or to give effect to any findings or directions contained in an order of the Appellate Tribunal, High Court or the Supreme Court.

### 3. Revision on application of the assessee [Section 264(1), (3) & (5)]

The assessee is entitled to make an application to the Principal Commissioner or Commissioner of Income-tax for the revision of any order passed by an authority subordinate to him. Such an application can be made within one year from the date on which the order in question was communicated to him or from the date on which he otherwise came to know of it, whichever is earlier [Section 264(3)]. The Principal Commissioner or Commissioner is empowered to admit a belated application if he is satisfied that the assessee was prevented by sufficient cause from making the application within the prescribed time.

The application for revision by the assessee is always to be accompanied by a fee of '500 [Section 264(5)]. On receipt of the revision application, the Principal Commissioner or Commissioner may call for the record. He may make such enquiry and pass such order as he deems fit. Such an order should not be prejudicial to the assessee [Section 264(1)].

There are two important points of distinction between the cases : (i) where the Principal Commissioner or Commissioner makes suo motu revision; and (ii) where he makes a revision on the application of the assessee. While acting suo motu, he can pass the revisional order only within one year from the date of the order sought to be revised. There is no such time limit when the revisional order is passed on the basis of application filed by the assessee. Once the application is made within the period of limitation prescribed therefor, or after the condonation of delay, the order may be passed at any time thereafter. Secondly, while acting suo motu, the

Commissioner acts in the exercise of his administrative jurisdiction and, hence, he is not bound to give a hearing to the assessee. In fact the review is purely a departmental affair in such cases. On the other hand, when he is moved by the assessee for the said purposes, the jurisdiction conferred on him is a judicial one and, hence, he must give an opportunity to the assessee to put forward his case.

### 4. Nature of the order [Section 264]

The Principal Commissioner or Commissioner may pass such order as he thinks fit provided such order is not prejudicial to the assessee. This is so whether the Commissioner acts suo motu, or on the revision application of the assessee. An order of the Principal Commissioner or Commissioner passed in revision can be said to be prejudicial to the assessee only when he is, as a result of it, placed in a different and worse position than that in which he was placed by the order under review'. If the Principal Commissioner or Commissioner effects a reduction of income under one head and an increase under another but, on the whole reduces the assessment, his order cannot be said to be prejudicial to the assessee. Though the Principal Commissioner or Commissioner may not change the order of the subordinate authority to the prejudice of the assessee, he may not give the relief asked for by the assessee. An order of the Principal Commissioner or Commissioner declining to interfere with the order of the subordinate authority cannot be deemed to be an order prejudicial to the assessee (Explanation 1 to Section 264). The power to pass such orders as he deems fit is not an arbitrary one to be exercised according to his fancy. He must act according to the rules of reason and justice, not according to private opinion, according to law not humour. His discretion is not to be arbitrary, vague and fanciful, but legal and regular. It is a power coupled with duty to exercise it in the interest of justice to the assessee.

### **CIRCUMSTANCES IN WHICH NO REVISION CAN BE MADE [SECTION 264(4)]**

The Principal Commissioner or Commissioner of Income-tax cannot revise the order of his subordinate authority in the following cases :

- (i) If the order is appealable to the Commissioner (Appeals), such order cannot be revised until the time within which such appeal may be made expires. If an appeal has been made to the Commissioner (Appeals), the revisional power cannot be exercised while the appeal is pending but it may be exercised after the appeal has been disposed of. The Commissioner (Appeals) for the purpose of Section 264 is an authority subordinate to the Commissioner of Income-tax. Hence, the order of the Commissioner (Appeals) can be revised.

- (ii) If the order is appealable to the Commissioner (Appeals) or the Appellate Tribunal, revisional power cannot be exercised until the time within which such appeal may be made expires. But, in such cases, if the assessee waives his right of appeal, the Commissioner may revise the order even before the time for appeal has expired. But once the order has been made the subject of an appeal the revisional powers come to an end. An order can be said to be made the “subject of an appeal” only when it is the subject of an effective appeal. If the Commissioner (Appeals) or the Appellate Tribunal refuses to entertain an appeal on the ground that it is time barred, or grants permission to the appellant to withdraw the appeal, the order cannot be said to be the “subject of an appeal” and the assessee would be entitled to apply to the Commissioner for revision.

### Remedy against the Revisional Order

An order of the Commissioner passed under Section 264 is not appealable to the Tribunal. Nor does a reference lie against such an order to the High Court since a reference to the High Court lies only against an order passed by the Tribunal. Since the order of the Commissioner is judicial or quasi-judicial in character, it is within the ambit of the High Court’s jurisdiction under Article 226 of the Constitution and a petition for a writ of certiorari to quash an unjust or illegal order of the Commissioner is maintainable.

### APPELLATE TRIBUNAL [SECTION 252]

The Central Government shall constitute an Appellate Tribunal consisting of as many judicial and accountant members as it thinks fit to exercise the powers and discharge the functions conferred on the Appellate Tribunal by this Act. The ITAT is constituted and works under the Ministry of Law. It is thus a body outside the administrative control of the Central Board of Direct Taxes.

The Appellate Tribunal is not an Income-tax Authority in the sense of being an integral part of the department. On the contrary, by its constitution, powers and jurisdiction, not to speak of the manner of their recruitment, the Tribunal is an independent arbitral tribunal. The proceedings before it are advisory. It has also the trappings of a judicial body in the sense that it has to deal with the Department on the one side, and the assessee on the other in as much as they face each other as opposing parties. In such a situation the Tribunal has to decide only those issues which are properly raised before it by the one or the other party in the appeal or in the cross objections. Under the Act, the Tribunal has got to decide an appeal and not merely give it a disposal by dismissing it for default of appearance. This, however, does not mean that the Tribunal has got to take upon themselves the responsibility of finding facts or points of law which are not urged by the Department or the assessee, as the case may be. *CIT v. A. C. Paul (1983) 142 ITA 811 (Mad.)*.

The Tribunal is the final Authority and ordinarily, if after considering the matters in the proper perspective and after surveying all material which is available to it, the Tribunal arrives at some conclusion one way or the other, that conclusion would have to be respected, unless it can be regarded as impossible or perverse. *CIT v. Lalchand Bhabutmal Jain (1985) 151 ITR 360 (Bom.)*.

### APPEALABLE ORDERS [SECTION 253(1) AND (2)]

Any assessee aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order.

1. An order passed by Commissioner (Appeals) under Section 154 ordering a rectification of mistake, or under Section 250 in connection with the disposal of an appeal or Section 271 imposing a penalty for failure to furnish return etc. or section 270A [inserted vide Finance Act, 2016] or Sections 271 A or 272A.
2. An order passed by an assessing officer under Clause (c) of Section 158BC, in respect of search initiated under Section 132 or books of account other documents or any assets requisitioned under Section 132A, after the 30th day of June, 1995 but before the 1st day of January, 1997.

3. An order passed by a Principal Commissioner or Commissioner under Section 12AA relating to registration of trust or under Section 263 relating to revision of orders prejudicial to revenue or under Section 272A penalty for failure to answer question, sign statements, allow inspection etc., on or under Section 154 rectifying a mistake, or an order passed by a Chief Commissioner, or a Director General or a director under Section 272A.
4. An order passed by an Assessing Officer under Sub-section (1) of Section 115VZC.
5. An order passed by an Assessing Officer under section 143(3) or section 147 or section 153A or section 153C with the approval of the commissioner or an order passed under section 154 or section 155.
6. An order passed by an Assessing Officer under section 143(3) or section 147 or section 153A or section 153C with the approval of the Principal Commissioner or Commissioner as referred to section 144BA(12) or an order passed under section 154 or section 155 in respect of such order;
7. An order passed by the prescribed authority under sub-clause (vi) or sub-clause (via) of clause (23C) of section 10.
8. An orders passed by prescribed authority under section 10(23C)(iv) and 10(23C)(v) shall also be appealable before the Appellate Tribunal. **[Amendment vide Finance Act, 2017 w.e.f. April 1, 2017]**
9. An orders passed of penalty under section 271J as imposed by Commissioner (Appeals).

The Commissioner may, if he objects to any order passed by Commissioner (Appeals) under Section 154 or 250, direct the Assessing Officer to appeal to the Appellate Tribunal against the order.

#### **PROCEDURE FOR FILING APPEAL [SECTION 253(3), (4)&(6)]**

Every appeal to the Appellate Tribunal shall be filed within sixty days of the date on which the, order sought to be appealed against is communicated to the assessee or to the Commissioner, as the case may be.

The Assessing Officer or the assessee, as the case may be, on receipt of notice that an appeal against the order of the Commissioner (Appeals) has been preferred by the other party may, notwithstanding that he may not have appealed against such order or any part thereof, within thirty days of the receipt of notice, file a memorandum of cross-objections, verified in the prescribed manner, against any part of the order of the Commissioner (Appeals) and such memorandum shall be disposed of by the Appellate Tribunal as if it were an appeal presented within the specified period.

The Appellate Tribunal may admit an appeal or permit the filing of a memorandum of cross-objections after the expiry of the relevant period if it is satisfied that there was sufficient cause for not presenting it within that period.

An appeal to the Appellate Tribunal shall be in the prescribed form and shall be verified in the prescribed manner and shall, in case of an appeal made on or after the 1st day of October, 1998, irrespective of the date of initiation of the assessment proceedings be accompanied by a fine of :

- (a) Rs. 500 where the assessed income/loss is 1,00,000 rupees or less.
- (b) Rs. 1,500 where the assessed income/loss is more than one hundred thousand rupees but not more than two hundred thousand rupees.
- (c) One percent of the assessed income, subject to a maximum of ten thousand rupees where the assessed income is more than two hundred thousand rupees,
- (d) Rs. 500 in any other case, except in case of an appeal filed by the department or a memorandum of cross-objections.

An application for stay of demand has to be accompanied by a fee of Rs. 500.

In making an appeal to the Tribunal, the following documents shall be sent in triplicate.

- (a) The memorandum of appeal.
- (b) The grounds of appeal.
- (c) Copy of the order of the Commissioner (Appeals).
- (d) Copy of the grounds of appeal and statement of facts filed before the Commissioner (Appeals).
- (e) Copy of the order of the Assessing Officer.
- (f) Challan for payment of requisite fee.

Where the appellant desires to refer to any documents or evidence he is permitted to file the same with Tribunal in the form of a paper book within one month from the date of filing the appeal. Though the prescribed period in one month, it will be preferable to file the same along with the appeal. Where an appellate order by the Commissioner (Appeals) is passed as a consolidated order for a number of years, appeals to the Tribunal shall be filed separately for each year.

### **Procedure when in an appeal by revenue an identical question of law is pending before Supreme Court [Section 158AA]**

A new section 158AA is inserted in the Income-Tax Act by Finance Act, 2015 relating to procedure when in an appeal by revenue on an identical question of law is pending before Supreme Court. Sub-section (1) seeks to provide that where the Commissioner or Principal Commissioner is of the opinion that any question of law arising in the case of an assessee for any assessment year is identical with a question of law arising in his case for another assessment year which is pending before the Supreme Court, he may, instead of directing the Assessing Officer to file appeal to the Appellate Tribunal, direct the Assessing Officer to make an application to the Appellate Tribunal, stating that an appeal on the question of law arising in the relevant case may be filed when the decision on the question of law becomes final in the other case.

Sub-section (2) seeks to provide that the Commissioner or Principal Commissioner shall direct the Assessing Officer to make an application under subsection (1) only if an acceptance is received from the assessee to the effect that the question of law in the other case is identical to that arising in the relevant case; and in case no such acceptance is received, the Commissioner or Principal Commissioner shall proceed in accordance with the provisions contained in section 253 (2) or sec 253(2A).

Sub-section (3) seeks to provide that where the order of the Commissioner (Appeals) referred to in sub-section (1) is not in conformity with the final decision on the question of law in the other case, the Commissioner or Principal Commissioner may direct the Assessing Officer to appeal to the Appellate Tribunal against such order and, save as otherwise provided in this section, all other provisions of Part B of chapter XX shall apply accordingly.

### **ORDER OF APPELLATE TRIBUNAL [SECTION 254]**

The Appellate Tribunal may, after giving both the parties to appeal an opportunity of being heard, pass such orders thereon as it may think fit.

The Appellate Tribunal may, at any time within six months the end of month in which the order was passed [Amendment vide Finance Act, 2016], with a view to rectifying any mistake apparent from the record, amend any order passed by it and shall make such amendment if the mistake is brought to its notice by the assessee or the Assessing Officer. But, any amendment which has the effect of enhancing an assessment or reducing a refund or otherwise increasing the liability of the assessee shall not be made unless the Appellate Tribunal has given notice to the assessee of its intention to do so and has allowed the assessee a reasonable opportunity of being heard.

The Tribunal's decision would have binding effect within the jurisdiction and has a persuasive value outside its jurisdiction.

Sub-section (2A) provides that in every appeal, the Appellate Tribunal, where it is possible may hear and decide such appeal within a period of four years from the end of the financial year in which such appeal is filed under Section 253(1). Sub-section (2B) provides that the cost of any appeal to the Appellate Tribunal shall be at the discretion of the Tribunal.

Section 254(2A) pertaining to stay of demand by the Appellate Tribunal has been modified as follows :

1. Initially the Tribunal can pass an order of the stay only for a period not exceeding 180 days from the date of the order staying the demand.
2. The tribunal shall dispose of appeal within the aforesaid period.
3. If appeal is not disposed of within the aforesaid period, the period of stay may be extended. The total period of stay cannot be more than 365 days reckoned from the beginning of the period. Extension is possible only if delay is not attributable to assessee.
4. Appeal shall be disposed of by the Tribunal within the extended period.
5. If appeal is not disposed of within the extended period or periods, the order of stay shall stand vacated after the expiry of such period or periods.

The Appellate Tribunal shall send a copy of any orders passed under this section to the assessee and to the Commissioner. On question of fact, the order passed by the Appellate Tribunal on appeal shall be final. An order made by the Appellate Tribunal shall be sufficiently comprehensive and self-contained. It should be possible to ascertain from the order all the relevant facts and the questions arising on the appeal. It should also disclose what were the contentions of the parties and should state why and for what reasons those contentions were repelled.

Under Section 254(1), the Tribunal may, after giving both parties to the appeal an opportunity of being heard, pass such-orders thereon as it deems fit.

No limitation has been placed on the powers of the Commissioner (Appeals) or the Appellate Tribunal under Section 251 (1) or 254(1). The only limitation on their appellate jurisdiction is that they cannot go into the question of propriety of an ex-parte proceeding or a best judgment assessment. The quantum of assessment, the quantum of tax or the question of registration of a firm can always be gone into. *Vishnu Kumar Gupta v. CIT (1983) 143 ITR 169 (All)*. However, the power of stay is not likely to be exercised in a routine way or as a matter of course in view of the special nature of taxation and revenue laws. Only when a strong prima facie case is made out, the Tribunal will consider whether to stay the recovery proceedings. Stay will be granted only in deserving and appropriate cases and where the Tribunal is satisfied that the entire purpose of the appeal will be frustrated or rendered nugatory by allowing the recovery proceedings to continue during the dependency of the appeal before it.

Section 254(1) empowers the Appellate Tribunal to give its decision on the grounds urged and it can pass appropriate orders. It is not open to the Tribunal itself to raise a ground or permit the party who had not appealed to raise a ground which will work adversely on the appellants.

Under Section 254(2), the Appellate Tribunal has got ample power to rectify a mistake apparent from record suo motu. If the mistake is brought to the notice of the Tribunal by the parties to the appeal, the Tribunal is empowered to rectify the same. *Addl. CIT v. ITAT (1983) 139 ITR 615 (AP)*.

From the Assessment year 2009-10(w.e.f.1.10.2008),the third proviso to sub-section (2A) provides that if such appeal is not decided within the period allowed originally or the periods so extended or allowed ,the order of stay shall stand vacated after expiry of such period or periods.

The intention behind these provisions has been very clear that the Appellate tribunal cannot grant stay either under the original order or any other subsequent order, beyond the period of 365 days in aggregate.

If the Tribunal is unable to decide the appeal on the basis of materials before it, it may admit fresh evidence and decide the appeal. It may also keep the appeal pending and direct any one of the subordinate authorities to ascertain further facts.

### **PROCEDURE OF APPELLATE TRIBUNAL [SECTION 255]**

The powers and functions of the Appellate Tribunal may be exercised and discharged by benches constituted by the President of the Appellate Tribunal from amongst the members thereof. The bench shall consist of one judicial member and one accountant member.

The President or any other member of the Appellate Tribunal, authorised in this behalf by the Central Government, may, sitting singly, dispose of any case which has been allotted to the Bench of which he is a member and which pertains to an assessee whose, total income as computed by the Assessing Officer in the case does not exceed ' 50,00,000 [Amendment vide Finance Act, 2016]. The President may, for the disposal of any particular case, constitute a Special Bench consisting of three or more members, one of whom shall necessarily be a judicial member and one an accountant member.

If the members of a Bench differ in opinion on any point, the point shall be decided according to the opinion of the majority if there is a majority. But if the members are equally divided, they shall state the point or points on which they differ and the case shall be referred by the President of the Appellate Tribunal for hearing on such point or points by one or more of the other members of the Appellate Tribunal. Such point or points shall be decided according to the opinion of the majority of the members of the Appellate Tribunal who have heard the case including those who first heard it.

The Appellate Tribunal shall have the power to regulate its own procedure and the procedure of Benches thereof in all matters arising out of the exercise of its powers or of the discharge of its functions including the places at which the Benches shall hold their sittings.

The Appellate Tribunal shall have, for the purpose of discharging its functions, all the powers which are vested in the Income-tax authorities under Section 131, and any proceeding before the Appellate Tribunal shall be deemed to be a judicial proceeding and for the purpose of Section 196 of the Indian Penal Code, the Appellate Tribunal shall be deemed to be a Civil Court for all purposes of Section 195 and Chapter XXXV of the Code of Criminal Procedure.

The Appellate Tribunal is a final fact finding authority and if it arrives at its own conclusions or facts after the consideration of the evidence before it, the Court will not interfere. It is necessary, however, that every fact 'for' and 'against' the assessee must have been considered with due care and the Tribunal must have given its finding in a manner which would have clearly indicated what were the questions which arose for determination, what was the evidence pro and contra in regard to each one of them, and what were the findings reached on the evidence on record before it.

### **APPEAL TO HIGH COURT**

Sections 260A and 260B are inserted w.e.f. October 1, 1998. Section 260A provides that an appeal shall lie to the High Court from every order passed in appeal by the Appellate Tribunal if the High Court is satisfied that the case involves a substantial question of law.

The Chief Commissioner or the Commissioner or an assessee aggrieved by any order passed by the Appellate Tribunal may file an appeal to the High Court and such appeal shall be filed within 120 days of the date on which the order appealed against is received by the assessee or the Chief Commissioner or Commissioner and shall be filed in the form of memorandum of appeal precisely stating the substantial question of law involved.

If the High Court is satisfied that a substantial question of law is involved in any case, it shall formulate that

question. The appeal shall be heard only on the question so formulated, and the respondents shall at the hearing of the appeal, be allowed to argue that the case does not involve such question. However, the High Court may for reasons to be recorded, hear the appeal on any other substantial question of law not formulated by it, if it is satisfied that the case involves such question.

The High Court shall decide the question of law so formulated and deliver such judgment thereon containing the grounds on which such decision is founded and may award such cost as it deems fit.

The High Court may determine any issue which has not been determined by the Appellate Tribunal or has been wrongly determined by the Appellate Tribunal on such substantial question of law.

Where the High Court delivers a judgment in an appeal filed before it under Section 260A, effect shall be given to the order passed on the appeal by the Assessing Officer on the basis of a certified copy of judgment [Section 260(1A)].

Section 260B provides that an appeal filed under Section 260A shall be heard by a bench of not less than two judges of the High Court and shall be decided in accordance with the opinion such Judges or the majority, if any. Where, however, there is no such majority, the part of law upon which they differ shall be referred to one or more of the Judges of the High Court and shall be decided according to the opinion of the majority of the Judges who have heard the case including those who first heard it.

The High Court also has power to stay a proceeding for recovery of demand arising out of the assessment order pending disposal of appeal.

### **APPEAL TO THE SUPREME COURT [SECTION 261]**

The aggrieved party is entitled to appeal to the Supreme Court against the judgment delivered by the High Court on the reference application made to it by the Tribunal (under Section 256) against an order made under Section 254 before the 1st day of October, 1998 or an appeal made to High Court in respect of an order passed under Section 254 on or after that date provided the High Court certifies the case to be fit for appeal to the Supreme Court. The right of appeal is, therefore, conditional and may be availed of only if the High Court gives a certificate of such fitness.

The High Court could certify the case as a fit one for appeal and grant leave to the Supreme Court if a substantial question of law is involved or if the question is likely to come up in successive year or if the question is otherwise of great public or private importance.

An application of fitness for appeal to the Supreme Court has to be made within 60 days from the date of High Court's judgment (under Article 132 of the Schedule to the Limitation Act, 1963). The time required for taking a certified copy of the High Court's judgment is to be excluded in computing such period of limitation.

If the High Court refuses to certify a case to be fit for appeal to the Supreme Court, an application may be made to the Supreme Court (under Article 136 of the Constitution) for special leave to appeal against the decision of the High Court.

The provisions of the Code of Civil Procedure, 1908 relating to the appeal to the Supreme Court are applicable in the case of appeals under Section 261 in the same manner as they are applicable in the case of appeals from decrees of a High Court [Section 262(1)].

Where the judgment of the High Court is changed or reversed in the appeal, effect is given to the order of the Supreme Court [Section 262(3)]. The law declared by the Supreme Court is binding on all courts within the territory of India under Article 141 of the Constitution.

On the receipt of a copy of judgment, the Appellate Tribunal has to pass such orders as are necessary to dispose of the case conformably to such judgment.

To award the cost of an appeal is at the discretion the Supreme Court

[Section 262(2)]. It would be open to the Court not to award costs even to the party which has succeeded in the appeal before it. If the Supreme Court awards costs to a party and the party has not complied with the order, a petition may be made to the appropriate High Court for execution of the order of the Supreme Court (Section 266). The High Court may transmit the order for execution to any court subordinate to it (Section 266).

Section 257 enables the Appellate Tribunal to make a direct reference to the Supreme Court if the Tribunal is of the opinion that, on account of a conflict in the decision of High Court in respect of any particular question of law, it is expedient that a reference should be made directly to the highest court.

### SUMMARY OF APPEALS

#### 1. Appeal to CIT(Appeals) [Section 246A to Section 251]

- ❖ Appeal can be made by Assessee only (First Appeal Section 246A)
- ❖ Within 30 days of payment of TDS or service of notice of demand or order. Delay may be condoned on sufficient cause been shown.
- ❖ Appeal is to be made in duplicate in Form No. 35.
- ❖ Appeal should be disposed within 1 year from the end of the financial year in which appeal was made.

#### 2. Appeal to ITAT [Section 252-255]

- ❖ Appeal can be made by assessee or Department. (Second appeal Section 253)
- ❖ Appeal can also be made under following situations :
  - a) Appeal against revision order under section 263
  - b) Against the order passed with previous approval or CCIT under section 115VZC(1) or on the direction of the Dispute Resolution Panel
  - c) Appeal against the order passed by CIT refusing to grant registration under Section 12AA or refusing to grant approval under section 80G.
- ❖ Appeal should be made within 60 days of communication of order to Assessee or CIT. Delay may be condoned on sufficient cause being shown.
- ❖ Appeal shall be made in Triplicate in Form No. 36.
- ❖ Disposal of appeal to be made within 4 years from the end of the financial year in which such appeal was made.

#### 3. Appeal to High Court [Section 260A-260B]

- ❖ Appeal may be made by Assessee or Department.
- ❖ Appeal should be made within 120 days of receipt of order of ITAT. Delay may be condoned on sufficient cause being shown by appellant.
- ❖ Form of appeal shall be as per Code of Civil Procedure, 1908 and time limit for disposal of appeal shall also be as per Code of Civil Procedure, 1908.

#### 4. Appeal to Supreme Court : [Section 261-262]

- ❖ Appeal may be made be Assessee or Department.
- ❖ Appeal is to be made within 90 days from the date of receipt of order of High Court. (As per Code of Civil Procedure, 1908). Delay may be condoned as per Code of Civil Procedure, 1908.
- ❖ Form of appeal shall be as per Code of Civil Procedure, 1908 and time limit for disposal of appeal shall also be as per Code of Civil Procedure, 1908.

## OFFENCES AND PENALTIES

An assessee should note that compliance with legal formalities is less costly than the payment of penalties or interest on tax dues. There are several formalities to be complied with to avoid any penalty. In this connection, reference may be made to the following table summarizing the defaults and penalties therefor.

Chapters XVII and XXI of Income-tax Act, 1961, contain various provisions empowering an Income-tax Authority to levy penalty in case of certain defaults. The various types of penalties are briefly described in the table given below :

Section	Type of Default	Quantum of Penalty		Levied by (Authority)
		Minimum Penalty	Maximum Penalty	
1	2	3	4	5
140A(3)	Failure to pay the self assessment tax or interest and fee or part thereof or both under Section 140A(1)	Such amount as the Assessing Officer may impose	Tax in arrears	Assessing Officer
158BFA	Determination of undisclosed income of block period	Minimum 100% of tax leviable in respect of undisclosed income	Maximum 300% of tax leviable in respect of undisclosed income	Assessing Officer or Commissioner (Appeals)
221(1)	Failure to make payment of tax and interest payable under Section 220(2) within the prescribed time limit	Such amount as the Assessing Officer may impose	Tax in arrears	-do-
234E	Failure to file statement within time prescribed in section 200(3) or in proviso to section 206C(3)	Fees of Rs. 200 per day during which failure continues	Amount of tax deductible or collectible	---
234F	Failure to file income tax return within the time as mentioned under section 139	1. Fees of Rs. 5,000 if return is furnished on or before 31st December of Assessment Year 2. Fees of Rs. 10,000 in any other case <b>Note:</b> Fees of Rs. 1,000 if total income of the person does not exceed Rs. 5,00,000	----	---

270A	Penalty for under reporting and misreporting of Income	50% of tax payable on underreported income (200% in case of misreporting of income)	-----	Assessing Officer or Commissioner (Appeals)
271(1)(b)	Failure to comply with : (i) a notice under Sections 115WD(2); 115WE; 142(1); 143(2) or, (ii) a direction under Section 142(2A)  <b>Note:</b> This section shall not apply to and in relation to any assessment for the AY commencing on or after 1.4.2017	Rs. 10,000 per failure	Rs. 10,000 per failure	Assessing Officer
271(1)(c)	Concealment of the particulars of income or furnishing of inaccurate particulars of income.  <b>Note :</b> The provisions of this section shall not apply to and in relation to any assessment for the assessment year commencing on or after the 1st day of April, 2017	100% of tax sought to be evaded	300% of the amount of tax sought to be evaded	Assessing Officer or Commissioner (Appeals)
271(4)	Distribution of profit by registered firm otherwise than in accordance with partnership deed and as a result of which partner has returned income below the real income  <b>Note :</b> The provisions of this section shall not apply to and in relation to any assessment for the assessment year commencing on or after the 1st day of April, 2017	Upto 150% of difference between tax on partner's income assessed and tax on returned income in addition to tax payable	-do-	Assessing Officer or Commissioner (Appeals)
271A	Failure to keep, maintain or retain books of account etc. as required under Section 44AA	Rs. 25,000	Rs. 25,000	Assessing Officer or Commissioner (Appeals)

271AA	<p>Failure to keep and maintain information and document in respect of international transaction or specified domestic transaction or fails to report such transactions or maintains or furnishes an incorrect information or document.</p> <p>[If any person fails to furnish the information and the document as required under sub-section (4) of section 92D, the prescribed income-tax authority referred to in the said sub-section may direct that such person shall pay, by way of penalty, a sum of five hundred thousand rupees. Amendment vide Finance Act, 2016 w.e.f. 1st April, 2017]</p>	<p>A sum equal to 2% of the value of each international transaction or specified domestic transaction.</p> <p>Rs. 5,00,000</p>	-----  -----	-do-
271AAB	<p>Undisclosed income found during search where search has been initiated :</p> <p>on or before 1.7.2012</p> <p>on or after 1.7.2012 but before 15.12.2016</p> <p>on or after 15.12.2016</p>	<p>10% of undisclosed income.</p> <p>10%, 20% or 60% of undisclosed income, as the case may be.</p> <p>30% or 60% of undisclosed income, as the case may be.</p>	-----	Assessing Officer
271AAC	<p>Penalty where income includes any income referred to in Section 68, Section 69, Section 69A, Section 69B, Section 69C or Section 69D.</p>	<p>10% of tax payable on undisclosed income</p>	----	Assessing Officer
271B	<p>Failure to get accounts audited under Section 44AB or furnish audit report along with return of income</p>	<p>One-half per cent of Total Sales, Turnover or Gross Receipts</p>	Rs. 1,50,000	Assessing Officer
271BA	<p>Failure to furnish report under Section 92E</p>	<p>Rs. 1,00,000</p>	—	-do-

271C	Failure to deduct tax at source or failure to pay wholly or partly the tax u/s 115-O(2) or second proviso to Section 194-B	A sum equal to the amount of tax omitted to be deducted or paid	-do-	
271CA	Failure to collect tax at source	100% of tax sought to be collected	—	Imposed by the Joint Commissioner
271D	Taking any loan or deposit or specified sum in contravention of Section 269SS.  “Specified sum” means any sum of money receivable, whether as advance or otherwise, in relation to transfer of an immovable property, whether or not the transfer takes place.	A sum equal to the amount of loan or deposit or specified amount so taken or accepted		-do-
271DA	Receiving of an amount of Rs. 2,00,000 or more otherwise than an A/c payee cheque/ draft/ECS, in contravention of provisions of <b>Section 269ST</b>	A sum equal to the amount of such receipt. However, penalty shall not be imposed, if such person proves that there were good and sufficient reasons for the contravention.		Imposed by the Joint commissioner
271DB	Failure to provide facility for accepting payment through prescribed electronic modes of payment as referred to in section 269SU (w.e.f. 1.11.2019)	Rs. 5,000 rupees for every day of default		Imposed by the Joint Commissioner
271E	Repayment of deposit or specified advance in contravention of Section 269T. “Specified advance” means any sum of money in the nature of advance, by whatever name called, in relation to transfer of an immovable property, whether or not transfer takes place.	A sum equal to the amount of deposit or specified amount	-do-	

271FA	<p>Failure to Furnish Statement of Financial Transaction or Reportable Account in Section 285BA(2)</p> <p>Failure to Furnish Annual Information Return in Section 285BA(5)</p>	<p>Rs. 500 per day during which such failure continues</p> <p><b>Rs.</b> 1000 per day during the failure continues beginning immediately after the expiry of time period specified in the notice of furnishing return</p>		
271FAA	<p>Furnishing of inaccurate information in statement of financial transaction or reportable account.</p> <p>Failure to furnish annual information return within the period specified in notice u/s 285BA(5)</p>	<p>Rs. 50,000</p> <p>Failure to furnish annual information return within the period specified in notice u/s 285BA(5)</p>		prescribed income - tax authority
271FAB	<p>Section 9A provides that fund Rs. 5,00,000 management activity carried out by an eligible offshore investment fund through an eligible fund manager acting on behalf of such fund shall not constitute business connection in India (subject to certain conditions). The provision requires that eligible investment fund shall furnish within 90 days from the end of the financial year a statement, in respect of its activities in a financial year, in the prescribed form containing information relating to fulfilment of specified conditions and such other information or documents as may be prescribed. Penalty to be levied if investment fund failed to comply with the requirement.</p>	Rs. 5,00,000		
271FB	<p>Failure to furnish Fringe Benefit Return (FBT is not applicable from the AY 2010-11 onwards)</p>	Rs. 100 per day for the days of default		

271G	Failure to furnish information or document in respect of international transaction or specified domestic transaction under Section 92D(3).	A sum equal to 2% of the value of each international transaction or specified domestic transaction.		Transfer Pricing Officer as referred to in Section 92CA
271GA	<p>Section 285A provides for reporting by an Indian concern if following two conditions are satisfied :</p> <p>(a) Shares or interest in a foreign company or entity derive substantial value, directly or indirectly, from assets located in India; and</p> <p>(b) Such foreign company or entity holds such assets in India through or in such Indian concern. In this case, the Indian entity shall furnish the prescribed information for the purpose of determination of any income accruing or arising in India under Section 9(1)(i). In case of any failure, the Indian concern shall be liable to pay penalty.</p>	<p>(a) a sum equal to 2% of value of transaction in respect of which such failure has taken place, if such transaction had effect of, directly or indirectly, transferring right of management or control in relation to the Indian concern;</p> <p>(b) a sum of Rs. 5,000 in any other case.</p>		
271GB	<p>1. Failure to furnish report under section 286(2)</p> <p>2. Failure to produce the information and documents within the period allowed under section 271GB(6)</p> <p>3. Failure to furnish report or failure to produce information/ documents under section 286 even after serving order under section 271GB(1) or 271GB(2)</p> <p>4. Failure to inform about inaccuracy in report furnish under section 286(2) Or furnishing of inaccurate information or document in response to notice issued under section 286(6).</p>	<p>1. Rs. 5,000 per day upto 30 days and Rs. 15,000 per day beyond 30 days</p> <p>2. Rs. 5,000 for every day during which the failure continues.</p> <p>3. Rs. 50,000 for every day for which such failure continues beginning from the date of serving such order.</p> <p>Rs. 5,00,000</p>		

271H	<p>Fails to furnish statement within the time prescribed in sub-section (3) of section 200 or proviso to section 206C(3) or furnishes incorrect information.</p> <p>However, no penalty shall be payable if tax along with interest has been deposited and the statement has been furnished within one year from the time prescribed.</p>	Rs. 10,000	Rs. 1,00,000	Assessing Officer
271-I	As per section 195(6) of the Act, any person responsible for paying to a non-resident or to a foreign company, any sum (whether or not chargeable to tax), shall furnish the information relating to such payment in Form 15CA and 15CB. Penalty shall be levied in case of any failure.	Rs. 100,000		Assessing Officer
271J	Furnishing incorrect information in a report or certificate under the provisions of this Act (or rules made thereunder) by a Chartered Accountant or a Merchant Banker or a Registered Valuer	Rs. 10,000 for each such report or certificate. However, if the concerned person proves that there was reasonable cause for the aforesaid failure, then penalty shall not be imposable		The assessing officer of the commissioner (Appeals)
272A(1)	<p>Refusal or failure by legally binding person in respect of subject matter of assessment, to:</p> <p>(a) answer questions</p> <p>(b) sign statement</p> <p>(c) attend to give evidence or produce books of account, etc., in compliance with summons under section 131(1)</p> <p>(d) comply with notices u/s 142(1)/143(2) or failure to comply with direction issued u/s 142(2A).</p>	Rs. 10,000 for each failure/default		

272A(2)	Failure to comply with a notice issued under Section 94, to give notice of discontinuance of business/ profession under Section 176(3); fails to furnish returns/ statements specified in Sections 133, 206, 206C, or 285B; fails to allow inspection of (i) register mentioned in Section 134, or (ii) entry in such register, or (iii) allow copies thereof to be taken, fails to furnish return of income under Section 139(4A) or, fails to deliver declaration under Section 197A; fails to furnish certificate under Section 203 or section 206C, fails to deduct and pay tax under Section 226; fails to deduct or pay tax u/s 192(2C), fails to deliver a copy of declaration u/s 206C(1A); fails to deliver the copy of statement within the time specified u/s 200(3) or the proviso to 206C(3); fails to deliver within the time specified u/s 206A(1).  However, no penalty shall be payable where statement required u/s 200(3) or proviso to section 206C(3) on or after 1st July 2012.	Rs. 100 for every day of default		Joint Director or Joint Commissioner (Chief Commissioner or Commissioner in case of default under Section 197A)
272AA	Failure in compliance with Section 133B	Any amount subject to a maximum of Rs.1,000	Rs. 1,000	Joint Commissioner/ Asstt Director/ Assessing Officer
272B	Failure to comply with provisions relating to PAN or Aadhar as referred to in section 139A/139A(5)(c)/(5A)/(5C)	Rs. 10,000 for each default	—	—
272BB	Failure in compliance with Section 230A	Rs. 10,000 for each failure/default	—	Assessing Officer
272BBB	Failure to comply with Section 206CA (TCAN)	Rs.10,000	—	—

**Note :** : No penalty is imposable for any failure under sections 271(1)(b), 271A, 271AA, 271B, 271BA, 271BB, 271C, 271CA, 271D, 271E, 271F, 271FA, 271FAB, 271FB, 271G, 271GA, 271GB, 271H, 271-I, 272A(1)(c) or (d), 272A(2), 272AA(1), 272B, 272BB(1), 272BB(1A), 272BBB(1), 273(1)(b), 273(2)(b) and 273(2)(c) if the person or assessee proves that there was reasonable cause for such failure (section 273B).

Section 273AA provides that a person may make application to the Principal Commissioner/Commissioner for granting immunity from penalty, if (a) he has made an application for settlement under section 245C and the

proceedings for settlement have abated; and (b) penalty proceeding have been initiated under this Act. The application shall not be made after the imposition of penalty after abatement.

The order under sub-section (3), either accepting or rejecting the application in full or in part, shall be passed within a period of twelve months from the end of the month in which the application under the said sub-section is received by the Principal Commissioner or the Commissioner :

Provided that no order rejecting the application, either in full or in part, shall be passed unless the assessee has been given an opportunity of being heard.

Provided further that where any application is pending as on the 1st day of June, 2016, the order shall be passed on or before the 31st day of May, 2017.

**(Amendment vide Finance Act, 2016 w.e.f. 1st April, 2017)**

### Rationalisation of Penalty Provisions

The existing provisions relating to levy of penalty u/s 271(1)(c) due to concealment of income or furnishing of inaccurate particulars of income by the taxpayer is to be replaced by a new section 270A categorizing the defaults into two categories viz. under-reporting of income and misreporting of income.

<i>Under-reporting of Income</i>	<i>Mis-reporting of Income</i>
<ul style="list-style-type: none"> <li>the income assessed is greater than the income determined in the return processed under clause (a) of sub-section (1) of section 143;</li> </ul>	non-recording of investments in books of account;
<ul style="list-style-type: none"> <li>the income assessed is greater than the maximum amount not chargeable to tax, where no return of income has been furnished;</li> </ul>	claiming of expenditure not substantiated by evidence;
<ul style="list-style-type: none"> <li>the income reassessed is greater than the income assessed or reassessed immediately before such re-assessment;</li> </ul>	recording of false entry in books of account
<ul style="list-style-type: none"> <li>the amount of deemed total income assessed or reassessed as per the provisions of section</li> </ul>	misrepresentation or suppression of facts;
115JB or 115JC, as the case may be, is greater than the deemed total income determined in the return processed under clause (a) of sub-section (1) of section 143;	
<ul style="list-style-type: none"> <li>the amount of deemed total income assessed as per the provisions of section 115JB or 115JC is greater than the maximum amount not chargeable to tax, where no return of income has been filed;</li> </ul>	failure to record any receipt in books of account having a bearing on total income;
<ul style="list-style-type: none"> <li>the income assessed or reassessed has the effect of reducing the loss or converting such loss into income.</li> </ul>	failure to report any international transaction or deemed international transaction under Chapter X.
<ul style="list-style-type: none"> <li>if total income reassessed as per section 115JB or section 115JC (MAT or AMT) is greater than deemed total income assessed/ reassessed under MAT or the AMT immediately before such reassessment.</li> </ul>	

The rate of penalty shall be fifty per cent of the tax payable on under-reported income. However in a case where under reporting of income results from misreporting of income by the assessee, the person shall be liable for penalty at the rate of two hundred per cent of the tax payable on such misreported income.

These amendments effective from 1st day of April, 2017 and accordingly apply in relation to assessment year 2017-2018 and subsequent years. Consequential amendments had also been made in sections 119, 253, 271A, 271AA, 271AAB, 273A and 279 to provide reference to newly inserted section 270A.

## OFFENCES AND PROSECUTION

### Rigorous Imprisonment

Section	Nature of Default	Minimum Period	Maximum Period
275A	Dealing with seized assets in contravention of the order made by the officer conducting search	Any period up to 2 years and fine	2 years and fine
275B	Failure to comply with the provision of section 132(I)(iib)	Any period up to 2 years and fine	2 years and fine
276	Removal, concealment, transfer or delivery of property to tax recovery	Any period up to 2 years and fine	2 years and fine
276A	Failure to comply with the provisions of section 178(1) & (3) by liquidator of a company	Any period up to 2 years but not less than 6 months in absence of special and adequate reasons	2 years
276AB	Failure to comply with provisions of sections 269UC, 269UE and 269UL	6 months and fine	2 years and fine
276B	Failure to pay tax to the Government's treasury or failure to pay to the Government tax payable by him as required by section 115-0(2) or second proviso to section 194B	3 months and fine	7 years and fine
276BB	Failure to pay to the Government , tax collected u/s. 206C	3 months and fine	7 years and fine
276C(1)	Wilful attempt to evade tax penalty or interest imposable or <b>under reports his income</b> under the Act.	If tax evaded exceeds ₹ 25, 00,000, then for 6 months & fine; otherwise 3 months and fine.	If tax evaded exceeds ₹ 25,00,000, 7 years & fine; otherwise 2 years and fine.
276C(2)	Wilful attempt to evade the payment of any tax ,penalty or interest	3 months and fine	2 years and fine

276CC	Wilful failure to file return of income in time u/s 139(1), or in Response to notice u/s.142(1) or sec. 148(Non-Cognizable as per Sec.279A)	If tax evaded exceeds ₹ 25,00,000 & 6 months and fine In any other case, 3 months and fine.  Note : No prosecution if : (i) the return is filed before the expire of the assessment year; or (ii) the tax payable on regular assessment , as reduced by TDS and advance tax does not exceed ₹ 10,000	If tax evaded exceeds ₹ 25,00,000, 7 years & fine; otherwise 2 years and fine
276CCC	Wilful failure to furnish in due times the return of total income which is required to be furnished u/s. 158BC.	3 months and fine	3 months and fine
276D	Wilful failure to produce books of account and documents u/s. 142(1) or wilful failure to comply with a direction to get the accounts audited u/s. 142(2A)	Any period upto 1 year and fine	1 year and fine
277	Making a false statement in verification or delivering a false account or statement(non-cognizable as per Sec.279A)	If tax evaded exceeds ₹ 25, 00,000; 6 months & fine; otherwise 3 months and fine.	If tax evaded exceeds ₹ 25, 00,000, 7 years & fine; otherwise 2 years and fine.
278	Abetment to make a false statement or declaration. (non-cognizable as per, Sec. 279A)	If tax evaded exceeds ₹ 1, 00,000; 6 months; otherwise 3 months and fine.	If tax evaded exceeds ₹ 25, 00,000, 7 years; otherwise 2 years and fine
278A	Punishment for second and subsequent offences u/s 276B, 276C(1), 276CC, 277 or 278	6 months for every offence and fine	7 year for every offence and fine
280(1)	Disclosure of particulars by public servants in contravention of section 138(2) [Prosecution to be instituted with previous sanction of Central Government under section 280(2)]	Up to 6 months (simple/ rigorous) and fine	6 months and fine

#### No punishment if proved that there was reasonable cause for failure [Section 278AA]

If there is a reasonable cause, it can be offered as a defense against penalty, prosecution, etc. Any failure under section 276A, 276AB or 276B is not punishable if he proves that there was reasonable cause for such failure.

Reasonable cause can be reasonably said to be a cause which prevents a man of average intelligence and ordinary prudence, acting under normal circumstances, without negligence or inaction or want of bona fides.

'Reasonable cause' as applied to human action is that which would constrain people of average intelligence and ordinary prudence. It means an honest belief founded upon reasonable grounds, of the existence of a state of circumstances, which, assuming them to be true, would reasonably lead any ordinary prudent and cautious man, placed in the position of the person concerned, to come to the conclusion that the same was the right thing to do.

### Immunity from Penalty and Prosecution [Section 270AA]

Assessee may make an application to the Assessing Officer for grant of immunity from imposition of penalty u/s 270A and initiation of proceedings u/s 276C if :-

- Tax and interest payable as per assessment or reassessment order paid within the period specified in such notice of demand and no appeal preferred against assessment or reassessment order.
- Application shall be made within one month from the end of the month in which the order is received in the form and manner as may be prescribed.
- Order u/s 270AA shall be passed by AO after expiry of time allowed for filing of appeal before CIT(A).
- No immunity if penalty proceedings is initiated for misreporting of income.
- Order accepting or rejecting application to be made within a period of one month from the end of the month in which such application is received. In case of rejection, an opportunity of being heard to assessee. Order of AO shall be final.
- No appeal shall lie against assessment or reassessment order where application u/s 270AA has been accepted.
- In case if application is rejected, then the period beginning from the date on which such application is made to the date on which the order rejecting the application is served on the assessee shall be excluded for calculation of the time period available for filing appeal before CIT(A) against assessment or reassessment order.

Amendment effective from 01.04.2017 and accordingly apply in relation to assessment year 2017-2018 and subsequent years.

### Provision for Bank Guarantee [Section 281B]

- Section 281B of the Act has been amended so as to provide that Assessing Officer 'AO' shall revoke provisional attachment of property made under sub-section (1) of the aforesaid section in a case where the assessee furnishes a bank guarantee from a scheduled bank, for an amount not less than the fair market value of such provisionally attached property or for an amount which is sufficient to protect the interests of the revenue.
- To determine the FMV of the property, the AO may, make a reference to the Valuation Officer, who may be required to submit the report of the estimate of the property to the AO within a period of thirty days from the date of receipt of such reference.

## LESSON ROUND UP

- Types of Assessment
  - Self assessment (Section 140A)
  - Summary assessment (Section 143(1))

Regular assessment [Section 143(2) and 143(2)]

Best judgment assessment (Section 144)

Income escaping assessment or re-assessment (Section 147)

Protective assessment.

- Self assessment is the first step in the process of assessments. Self Assessment is simply a process where a person himself assesses his tax liability on the income earned during the particular previous year and submits Income Tax Return to the department.
- Under summary assessment, Assessing Officer completes the assessment without passing a regular assessment order. The Assessing Officer issue an acknowledgement/intimation under section 143(1) of tax payable or refundable as the case may be on the basis of Return of Income filed by the assessee under section 139 or in response to a notice issued under section 142(1).
- Where a return has been made under Section 139, or in response to a notice under sub-section (1) of Section 142, the Assessing Officer shall, if he considers necessary or expedient to ensure that the assessee has not understated the income or has not computed excessive loss or has not underpaid the tax in any manner, serve on the assessee a notice requiring him, on a date to be specified therein, either to attend his office or to produce, or cause to be produced there, any evidence on which the assessee may rely in support of the return.
- **Best Judgment Assessment** : The Assessing Officer, after taking into account all relevant material which he has gathered, and after giving the assessee an opportunity of being heard, makes the assessment of the total income or loss to the best of his judgment and determine the sum payable by the assessee on the basis of such assessment.
- **Income Escaping Assessment** : If the Assessing Officer has reason to believe that any income chargeable to tax has escaped assessment for any assessment year, he may, subject to the provisions of sections 148 to 153.
- The right to appeal must be given by express enactment in the Act. Therefore, in case there is no provision in the Act for filing an appeal regarding a particular matter, no appeal shall lie. The right to appeal arises where the taxpayer is aggrieved by the order passed by the income-tax authority.
- The assessee may prefer an appeal against the orders of the Assessing Officer to the Commissioner (Appeals), in accordance with the relevant provisions under Section 246 and appeal against the order of the Commissioner (Appeals) can be preferred by the Assessee or the Commissioner of Income Tax and such appeal lies with the Appellate Tribunal.
- The Central Government shall constitute an Appellate Tribunal consisting of as many judicial and accountant members as it thinks fit to exercise the powers and discharge the functions conferred on the Appellate Tribunal by this Act.
- Section 260A provides that an appeal shall lie to the High Court from every order passed in appeal by the Appellate Tribunal if the High Court is satisfied that the case involves a substantial question of law.
- The aggrieved party is entitled to appeal to the Supreme Court against the judgment delivered by the High Court.
- Chapters XVII and XXI of Income-tax Act, 1961, contain various provisions empowering an Income-tax Authority to levy penalty in case of certain defaults.

**SELF TEST QUESTIONS**

These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation

**Multiple Choice Questions (MCQs)**

1. The appeal against the order of Appellate Tribunal can be filed to High Court:

- a) for any matter in the order
- b) only if any question of fact is involved
- c) only if any substantial question of law is involved
- d) None of the above

Answer: c

2. An Appeal to High Court against the order of ITAT is to be filed within a period of ----- from the date on which the ITAT's order is communicated to the tax payer

- a) 30 Days
- b) 60 Days
- c) 90 Days
- d) 120 Days

Answer: d

3. Income Tax Authority below the rank of Deputy Commissioner of Income Tax:

- a) is appointed by the Central Board of Direct Taxes
- b) may be appointed by the Board/Director General/Chief Commissioner/Director/Commissioner if authorised by Board
- c) is appointed only by the Central Govt.
- d) None of the above

Answer: b

4. The assessee can object to the jurisdiction of Assessing Officer, if no return is filed:

- a) within 3 months of notice u/s 142(1) or 148 for filing the return of income or time allowed to show cause why best judgment assessment u/s 144 should not be made, whichever is earlier
- b) within one month of notice u/s 142(1) or 148 for filing the return of Income or time allowed to show cause u/s 144 whichever is earlier
- c) within the time allowed in notice u/s 142(1) or 148 for filing return of Income or time allowed to show cause u/s 144 whichever is earlier
- d) None of the above

Answer: c

5. Where total income assessed by the Assessing Officer was Rs. 4,50,000 and the assessee wishes to file an appeal to Income Tax Appellate Tribunal against the order of Commissioner (Appeals). The fee for filing such appeal shall be:

- a) Rs. 1,500



# Lesson 11

## Concept of Indirect Taxes at a Glance

### LESSON OUTLINE

- Background
- Constitutional Powers of Taxation
- Indirect Taxes in India – An Overview
- Pre GST Tax Structure and Deficiencies
- Administration of Indirect Taxation in India
- Existing Tax Structure
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

GST is a major milestone in indirect tax reforms in independent India. GST is a tax which will make India one unified common market. It is a destination based consumption tax. It is applicable all over India including Jammu & Kashmir. It adorns dual taxation model where Union and states levy and collect taxes simultaneously. It ensures seamless flow of input tax credit to a large extent. It has been designed to be fully automated and online. A giant portal called GSTN is being used to ensure working of the GST system which is the IT backbone of GST.

A high powered federal body called GST Council has been established under Article 279A of the Constitution of India to decide policy matters, formulate principles for administration and implementation of GST.

Constitutional amendment was necessary to enable Centre and states to levy GST simultaneously.

At the end of this lesson, you will be able to learn:

- Overview of Indirect Taxation
- Administration under indirect taxation regime
- What were the constitutional amendments required to roll out GST
- What is the existing system of Indirect Taxation
- Overview of previous Indirect Taxation regime

## BACKGROUND

Taxation is one of the essential and decisive elements in the working of machinery of a Nation. It forms a quintessential part of development of any country. The revenue that is collected in the form of taxes is used for providing goods and services for public utility such as infrastructure, transportation, facilities like rain shelters and common areas, sanitation and all other such amenities which are provided by the government of the country.

A tax can be said to be a non-penal, yet compulsory transfer of resources from the private to the public sector levied on the basis of a predetermined criteria. Taxes are collected for serving the primary purpose of providing sufficient revenues to the State and have become a mechanism through which the social and economic objectives of a welfare state could be achieved. Every amount that is collected is contributed towards providing better infrastructure facilities for public at large. The same is also utilized towards rural revival and social well-being of general public. Taxation system is instrumental in removing poverty and inequality from the society. On the other hand, tax reform is fundamental equipment in strategy development aiming at holistic growth of the society. Thus, the importance of an efficient tax system and reforms in tax system cannot be undermined.

There are two types of taxes levied in India, i.e., Direct tax, which is levied directly on income, profession, etc, of an individual and where the tax burden cannot be passed on to any other person. Indirect tax, on the other hand, is not paid on the direct income of an individual person but is levied indirectly on the ultimate consumer of goods and services for consumption of goods and services. Hence, the former is levied on the income while latter is levied on the goods and services. In indirect taxes, immediate burden is on one person and ultimate burden is on some other person i.e., the person who ultimately consumes.

Goods and Services Tax (GST) was rolled out in India with effect from 1st July, 2017. GST is one of the greatest tax reforms in India. It transforms the system of taxation and tax administration into a digital world by adopting the latest information technology. With the introduction of GST, India has joined the club of developed and progressing Nations which are already having a common tax on goods and services.

**Following are some of the distinctions between direct and indirect taxes :**

DIRECT TAXES	INDIRECT TAXES
These are mainly on income, wealth, profession etc. of persons	These are consumption based taxes on goods and services
Tax payer pays taxes directly to government	Tax payer pays taxes indirectly through intermediaries like importers , suppliers etc.
Direct taxes become payable after the benefit/ income reaches the tax payer	Indirect taxes are payable even before the goods/ services reach the tax payer.
Income tax, corporation tax are main sources of direct tax	Customs and GST are major indirect taxes in India.
Individuals, HUFs, firms and companies are the Tax payers.	End-consumer of the goods and services bear the final burden of tax.

## CONSTITUTIONAL POWERS OF TAXATION

Constitution of India is the supreme law of India. It lays down the framework defining fundamental political principles, establishes the structure, procedures, powers and duties of government institutions and sets out fundamental rights, directive principles and the duties of citizens. Constitution of India thus lays down the foundation brick for arranging the powers, duties and the supremacy to legislate all laws of India. The authority to levy a tax is hence derived from the Constitution of India.

Article 246 of the Indian Constitution, lays down three types of lists and distributes legislative powers including taxation, between the Parliament of India and the State Legislatures. It lays down the subject

matters with respect to which only the Parliament can make rules, where the State Legislatures can exclusively lay down the rules and a Concurrent List whereby both the Parliament as well as State Legislatures can legislate. Thus the Constitution of India allocates the power to levy various taxes between the Centre and the states.

Broadly, the previous indirect tax regime consisted of Central and State laws. For the Central Government, Central Excise, Customs and Service tax were the three main components of indirect taxes. While for State Government, Value Added Tax (VAT) and CST were the major taxes along with Octroi, Entertainment Tax etc. Taxation of goods and services was governed under separate legislatures. In respect of goods, the Centre had the powers to levy tax on the manufacture of goods (except alcoholic liquor for human consumption, opium, narcotics etc.) while the states had the powers to levy tax on the sale of goods. In the case of inter-state sales, the Centre had the power to levy a tax (the Central Sales Tax) but, the tax was collected and retained entirely by the states. As far as services were concerned, it was the Centre alone that was empowered to levy service tax governed by the Finance Act.

Introduction of the Value Added Tax (VAT) was considered to be a major step and an essential breakthrough in the field of indirect taxes. Although primarily VAT was successful, there were certain shortcomings in the structure of VAT. The reasons for such shortcomings was that there was a mosaic of taxes being levied on goods and services, such as luxury tax, entertainment tax, etc., which were not subsumed in the VAT thereby marginalizing the benefits of comprehensive tax credit mechanism. Further to this, many other taxes were levied by both the Central Government and the State Government on production, manufacture and distributive trade, where no set-off was available in the form of input tax credit. These taxes added to the cost of goods and services and led to tax on tax i.e., cascading of taxes and the erstwhile indirect tax regime was ineffective to remove this cascading effect of taxes.

These taxes were being levied and collected exclusively under their respective entries in Union and State lists as demarcated by Article 246.

Goods & Services Tax regime of indirect taxes brought a single tax which was levied on supply of goods or services or both with concurrent jurisdiction of Centre and states. This led to bringing about amendments in the Constitution so that they may simultaneously levy and collect Goods & Services Tax.

The Constitution of India has been amended by the **Constitution (One Hundred and First Amendment) Act, 2016** for this purpose.

To bring out GST laws governing goods and services, Article 246A has been inserted to enable levy of tax on goods and services simultaneously both by Centre and states/ union territories.

## CONSTITUTION AMENDMENT ACT, 2016

### Article 246A

Article 246A was inserted by Constitution (101st) Amendment Act, 2016, especially for the Goods & Services Tax. Article 246A provides that:

- (1) Notwithstanding anything contained in Article 246 and Article 254, Parliament, and subject to clause (2), the Legislature of every State, have power to make laws with respect to goods and services tax imposed by the Union or by such State.
- (2) Parliament has exclusive power to make laws with respect to goods and services tax where the supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.

*Explanation* : Provisions of Article 246A, shall, in respect of goods and service tax referred to in Article 279A (5), will be effective from the date recommended by the Goods and Services Tax Council.

Article 246 deals with subject matter of laws made by Parliament and by the legislatures of the States and Article 254 with Inconsistency between laws made by Parliament and laws made by the Legislatures of States.

#### **Amendment to Article 248**

Article 248 contains the Residuary Powers of legislation. Article 248(1) reads as follows –

**Article 248(1)** : Subject to Article 246A, Parliament has exclusive power to make any law with respect to any matter not enumerated in the Concurrent List or State List.

**Article 248(2)** : Such power shall include the power of making any law imposing a tax not mentioned in either of those Lists.

#### **Amendment to Article 249**

**Article 249** deals with the power of Parliament to legislate with respect to a matter in the State List in the national interest. After amendment Article 249(1) reads as follows –

**Article 249(1)** : Notwithstanding anything in the foregoing provisions of this Chapter, if the Council of States has declared by resolution supported by not less than two-thirds of the members present and voting that it is necessary or expedient in the national interest that Parliament should make laws with respect to goods and services tax provided under Article 246A or any matter enumerated in the State List specified in the resolution, it shall be lawful for Parliament to make laws for the whole or any part of the territory of India with respect to that matter while the resolution remains in force.

#### **Amendment to Article 250**

**Article 250** deals with the power of Parliament to legislate with respect to any matter in the State List if a Proclamation of emergency is in operation. After amendment Article 250(1) reads as follows -

**Article 250(1)** - Notwithstanding anything in this Chapter, Parliament shall, while a Proclamation of Emergency is in operation, have power to make laws for the whole or any part of the territory of India with respect to goods and services tax provided under Article 246A or any of the matters enumerated in the State List.

#### **Amendment to Article 268**

**Article 268** deals with duties levied by the Union but collected and appropriated by the states. The amendment proposes deletion of some words. After amendment, Article 268 reads as follows –

**Article 268(1)** : Such stamp duties as are mentioned in the Union List shall be levied by the Government of India but shall be collected –

In the case where such duties are leviable within any Union territory, by the Government of India, and

In other cases, by the States within which such duties are respectively leviable.

**Article 268(2)** : The proceeds in any financial year of any such duty leviable within any State shall not form part of the Consolidated Fund of India, but shall be assigned to that State.

#### **Amendment to Article 269**

**Article 269** deals with taxes levied and collected by the Union but assigned to the states.

The amended Article 269 (1) reads as follows –

**Article 269(1)** - Taxes on the sale or purchase of goods and taxes on the consignment of goods except as provided in Article 269A shall be levied and collected by the Government of India but shall be assigned and shall

be deemed to have been assigned to the States on or after the 1st day of April, 1996 in the manner provided in clause (2).

### Article 269A

The newly inserted Article 269A provides for levy and collection of goods and services tax in course of inter-state trade or commerce.

Article 269A(1) provides that goods and services tax on **supplies** in the course of inter-State trade or commerce shall be levied and collected by the Government of India and such tax shall be apportioned between the Union and the States in the manner as may be provided by Parliament by law on the recommendations of the Goods and Services Tax Council.

The explanation to this clause provides that supply of goods, or of services, or both in the course of import into the territory of India shall be deemed to be supply of goods, or of services, or both in the course of inter-state trade or commerce.

*Note:* Integrated Goods & Services Tax Act, 2017 was passed by Parliament on the basis of Article 269A

Article 269A (2) provides that the amount apportioned under clause (1) shall not form part of the Consolidated Fund of India.

Article 269A(3) provides that where an amount collected as tax levied under clause (1) has been used for payment of the tax levied by a State under Article 246A, such amount shall not form part of the Consolidated Fund of India.

Article 269A (4) provides that where an amount collected as tax levied by a State under article 246A has been used for payment of the tax levied under clause (1), such amount shall not form part of the Consolidated Fund of the State.

Article 269A(5) provides that the Parliament may, by law, formulate the principles for determining the place of supply, and when a supply of goods, or of services, or both takes places in the course of inter-state trade or commerce.

### Amendment to Article 270

Article 270 deals with distribution of revenues between the Union and states. After amendment Article 270 (1) reads as follows –

Article 270(1) - All taxes and duties referred to in the Union List, except the duties and taxes referred to in Articles 268, 269 and 269A, respectively, surcharge on taxes and duties referred to in Article 271 and any cess levied for specific purposes under any law made by Parliament shall be levied and collected by the Government of India and shall be distributed between the Union and the States in the manner provided in clause (2).

The newly inserted clauses are –

Article 270(1A) – The tax collected by the Union under clause (1) of Article 246A shall also be distributed between the Union and the States in the manner provided in clause (2).

Article 270(1B) - The tax levied and collected by the Union under clause (2) of article 246A and article 269A, which has been used for payment of the tax levied by the Union under clause (1) of article 246A, and the amount apportioned to the Union under clause (1) of article 269A, shall also be distributed between the Union and the States in the manner provided in clause (2).

### Amendment to Article 271

Article 271 deals with surcharge on certain duties and taxes for the purpose of the Union. After amendment, Article 271 reads as follows-

Article 271 - Notwithstanding anything in Articles 269 and 270, Parliament may at any time increase any of

the duties or taxes referred to in those Articles, except the goods and services tax under Article 246A, by a surcharge for the purposes of the Union and the whole proceeds of any such surcharge shall form part of the Consolidated Fund of India.

## **GOODS AND SERVICES TAX COUNCIL**

Section 12 of the Act proposed to insert a new Article 279A after Article 279 which deals with Goods and Services Tax Council.

Consequently, Article 279A was inserted by the Constitution (101st) Amendment Act, 2016 with effect from September 12, 2016

### **Article 279A**

(1) The President shall, within sixty days from the date of commencement of the Constitution (One Hundred and First Amendment) Act, 2016, by order, constitute a Council to be called the Goods and Services Tax Council.

(2) The Goods and Services Tax Council shall consist of the following members, namely :

- (a) the Union Finance Minister..... Chairperson;
- (b) the Union Minister of State in charge of Revenue or Finance..... Member;
- (c) the Minister in charge of Finance or Taxation or any other Minister nominated by each State Government.....Members.

(3) The Members of the Goods and Services Tax Council referred to in sub-clause (c) of clause (2) shall, as soon as may be, choose one amongst themselves to be the Vice-Chairperson of the Council for such period as they may decide.

(4) The Goods and Services Tax Council shall make recommendations to the Union and the States on –

- (a) the taxes, cesses and surcharges levied by the Union, the States and the local bodies which may be subsumed in the goods and services tax;
- (b) the goods and services that may be subjected to, or exempted from the goods and services tax;
- (c) model Goods and Services Tax Laws, principles of levy, apportionment of Goods and Services Tax levied on supplies in the course of inter-State trade or commerce under article 269A and the principles that govern the place of supply;
- (d) the threshold limit of turnover below which goods and services may be exempted from goods and services tax;
- (e) the rates including floor rates with bands of goods and services tax;
- (f) any special rate or rates for a specified period, to raise additional resources during any natural calamity or disaster;
- (g) special provision with respect to the States of Arunachal Pradesh, Assam, Jammu and Kashmir, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, Himachal Pradesh and Uttarakhand; and
- (h) any other matter relating to the goods and services tax, as the Council may decide.

(5) The Goods and Services Tax Council shall recommend the date on which the goods and services tax be levied on petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas and aviation turbine fuel.

(6) While discharging the functions conferred by this article, the Goods and Services Tax Council shall be guided by the need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services.

(7) One-half of the total number of Members of the Goods and Services Tax Council shall constitute the quorum at its meetings.

(8) The Goods and Services Tax Council shall determine the procedure in the performance of its functions.

(9) Every decision of the Goods and Services Tax Council shall be taken at a meeting, by a majority of not less than three-fourths of the weighted votes of the members present and voting, in accordance with the following principles, namely : –

- (a) the vote of the Central Government shall have a weightage of one-third of the total votes cast, and
- (b) the votes of all the State Governments taken together shall have a weightage of two-thirds of the total votes cast, in that meeting.

(10) No act or proceedings of the Goods and Services Tax Council shall be invalid merely by reason of –

- (a) any vacancy in, or any defect in, the constitution of the Council; or
- (b) any defect in the appointment of a person as a Member of the Council; or
- (c) any procedural irregularity of the Council not affecting the merits of the case.

(11) The Goods and Services Tax Council shall establish a mechanism to adjudicate any dispute —

- (a) between the Government of India and one or more States; or
- (b) between the Government of India and any State or States on one side and one or more other States on the other side; or
- (c) between two or more States, arising out of the recommendations of the Council or implementation thereof.

The GST Council has been constituted under Article 279A to make recommendations to the Union and States on the taxes, cesses and surcharges levied by the Centre, the States and the local bodies which are subsumed in the GST.

It brings about certainty and breaks trade barriers and entry barriers among the states of India including Jammu & Kashmir.

Thus, Article 279A (1) provides that the President shall, within 60 days from the date of the commencement of the Act, by order, constitute a Council to be called the Goods and Services Tax Council. Article 279A(2) provides the constitution of GST Council as under -

1. Union Finance Minister – Chairperson;
2. The Union Minister of State in charge of Revenue or Finance- Member;
3. The Minister in charge of Finance or Taxation or any other Minister nominated by each State Government – Members.

The members shall, as soon as may be, choose one amongst themselves to be the Vice Chairperson of the Council for such period as they may decide.

The mechanism of GST Council would ensure harmonization on different aspects of GST between the Centre and the states as well as among states. It has been provided in the Constitution (101st Amendment) Act, 2016 that the GST Council, in discharge of its various functions, shall be guided by the need for a harmonized structure of GST and for the development of a harmonized national market for goods and services.

### Amendment of Article 286

Article 286 deals with the restrictions as to imposition of tax on the sale or purchase of the goods. After amendment, Article 286 reads as follows:

Article 286 (1) - No law of a State shall impose, or authorize the imposition of, a tax on the supply of goods or of services or both, where such supply takes place –

1. outside the State; or
2. in the course of the import of the goods or services or both into, or export of the goods or services or both out of, the territory of India.

Article 286 (2) - Parliament may by law formulate principles for determining when a supply of goods or services or both takes place in any of the ways mentioned in clause (1).

### Amendment of Article 366

Article 366 defines some words. Clause (12A) is proposed to be inserted after clause (12). The newly inserted clause (12A) defines the term 'goods and services tax' as any tax on supply of goods, or services or both except taxes on the supply of the alcoholic liquor for human consumption.

Clauses (26A) and (26B) have been inserted after clause (26). Clause (26A) defines the term 'services' as anything other than goods.

Clause (26B) defines the term 'State', with reference to articles 246A, 268, 269, 269A and 279A including a Union territory with Legislature.

### Amendment of Article 368

Article 368 deals with the power of Parliament to amend Constitution and procedure therefor.

### Amendment of Sixth schedule

Sixth schedule deals with the provisions as to the administration of tribal areas in the States of Assam, Meghalaya, Tripura and Mizoram.

Para 8 of the schedule deals with powers of the Regional Councils to assess and collect land revenue and impose taxes. Clause (e) after clause (3) (d) has been inserted. After this para, 8(3) reads as follows –

(3) The District Council for an autonomous district shall have the power to levy and collect all or any of the following taxes within such district, that is to say -

- (a) taxes on professions, trades, callings and employments;
- (b) taxes on animals, vehicles and boats;
- (c) taxes on the entry of goods into a market for sale therein, and tolls on passengers and goods carried in ferries;
- (d) taxes for the maintenance of schools, dispensaries or roads.; and
- (e) taxes on entertainment and amusements.

### Amendment of Seventh Schedule

Seventh Schedule deals with three types of Lists viz., Union List, State List and Concurrent List.

84. Duties of excise on the following goods manufactured or produced in India, namely –

1. Petroleum crude;
2. High speed diesel;
3. Motor spirit (commonly known as petrol);
4. Natural gas;
5. Aviation turbine fuel; and
6. Tobacco and tobacco products.

*Note:* On the above 6 items central excise duty is continued to be levied. On 1 to 5 only Central excise duty is levied and no GST. But on item No. 6 both GST and Central excise duty are imposed.

Entries 92 (Taxes on the sale or purchase of newspapers and on advertisements published therein) and 92C have been omitted.

Existing Entry 54 in the State List substituted as under :

**New Entry 54:** Taxes on the sale of petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas, aviation turbine fuel and alcoholic liquor for human consumption, but not including sale in the course of inter-State trade or commerce or sale in the course of international trade or commerce of such goods.

*Note:* On the above petroleum products imported, IGST is payable

Entry 62 in the State List substituted:

**62:** Taxes on entertainments and amusements to the extent levied and collected by a Panchayat or a Municipality or a Regional Council or a District Council.

*Note:* only taxes on entertainments and amusements collected by local bodies are taxable under Entry No. 62. All others have been subsumed under GST.

The following entries have been deleted

1. Entry No. 52 – Taxes on the entry of goods into a local area for consumption, use or sale therein.
2. Entry No. 55 - Taxes on advertisements other than advertisements published in the newspapers and advertisements broadcast by radio or television.

## COMPENSATION TO STATES FOR DEFICIT IN TAX COLLECTIONS

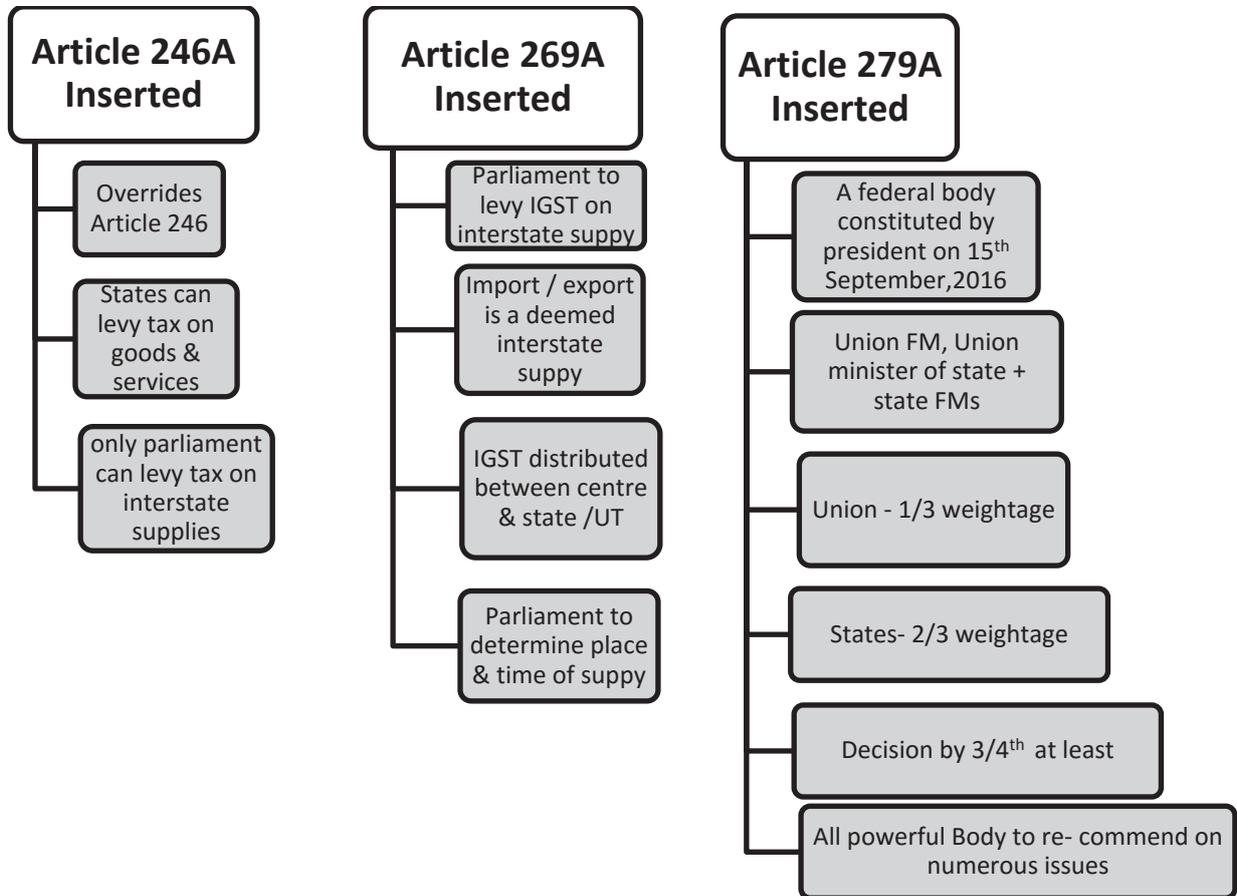
The amendment provides that Parliament shall, by law, on the recommendations of the GST Council, provide for compensation to the States for loss of revenue arising on account of implementation of the goods and service tax for a period of five years.

Parliament has passed the law to compensate states for revenue deficit. The Act is 'GST (Compensation to States) Act, 2017. Under this Act some additional tax is collected as GST compensation cess on specified goods and the amount is distributed among those states incurring revenue loss due to introduction of GST.

## POWER TO REMOVE DIFFICULTIES

Section 20 gives powers to the President to remove difficulties. If any difficulty arises in giving effect to the provisions of the Constitution as amended by this Act (including any difficulty in relation to the transition from the provisions of the Constitution as they stood immediately before the date of assent of the President to this Act to the provisions of the Constitutions as amended by this Act), the President may, by order, make such provisions, including any adaptation or modification of any provision of the Constitution as amended by this Act or law, as appear to the President to be necessary or expedient for the purpose of removing the difficulty. No such order

shall be made after the expiry of three years from the date of such assent. Every order shall, as soon as may be after it is made, be laid before each House of Parliament.



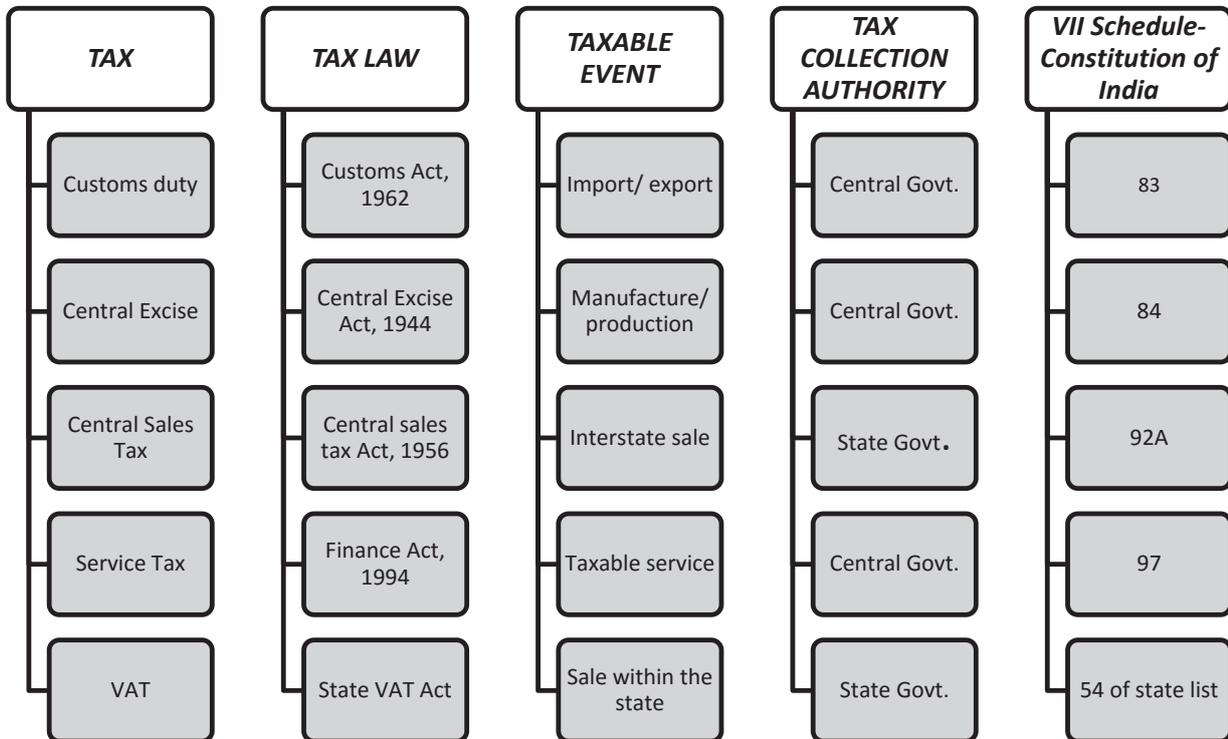
**INDIRECT TAXES IN INDIA – AN OVERVIEW**

In the erstwhile regime of indirect taxes, goods were subject to tax by both i.e., the Centre as well as the States. Up to the manufacture stage, Central Government was collecting excise duty except for on alcohol for human consumption, narcotics and narcotic drugs, etc. on which state excise was being imposed. Even after the implementation of GST, states continue to levy tax of state excise duty and sales tax on liquors. States have exclusive powers to collect tax on both intra state and interstate sales.

Service tax was levied and collected by Union Government exclusively. There were plenty of taxes collected by State governments on various subjects like luxury tax, purchase tax, entry tax and so on.

Till 1987, Central Excise was collected on the gross value which resulted in cascading effect. MODVAT scheme was introduced to reduce cascading effect. MODVAT Scheme was replaced by CENVAT Credit scheme was extended to service tax later on. Further, Centre was able to convince the states to introduce VAT on local sales. The process continued from 2003 to 2008 by which all the states in India became VAT states. In 2003, Haryana was the only state to introduce VAT. In 2005, majority of the states introduced VAT, the rest followed in the later years.

The following diagram summarizes the erstwhile indirect taxation in India :



### Basic summary of Goods & Services Tax

- The first country to implement Goods & Services Tax was France in as early as 1954.
- India has the highest tax slab in the world i.e., 28%, next only to Argentina which is at 27%
- Almost 160 countries around the world follow this scheme of indirect taxation
- Indian GST has four rate structure, viz. 5%, 12%, 18% and 28% with cess on sin goods and luxury items
- There is a special rate of 3% on precious metals like gold
- GST is covered under five legislations i.e., Central GST Act, State GST Act, Integrated GST Act, Union Territory GST Act and GST (Compensation to States) Act
- Integrated GST, Compensation cess and Central GST are charged by Central Government
- All taxation policies and their implementation are based on the recommendations of the GST Council
- The taxable event under GST is supply
- GST Bill was introduced under 122nd Constitutional Amendment Bill, but passed under 101st Amendment Act, 2016
- Assam was the first state to ratify GST Bill but Telangana was the first state to pass State GST Bill
- GST Council was constituted with its headquarters in Delhi. The Union Finance Minister is the Chairperson
- State Finance Ministers are members of GST Council

- 1st July will be observed as the GST day
- The threshold limit under GST is Rs. 40 Lakhs, for some special category states it is Rs. 20 Lakhs
- There is a special purpose vehicle called GSTN which caters the IT needs of GST. GSTN comes under Companies Act, 2013 with combined stake of Central and State Governments is 49%. The rest is contributed by LIC Finance with 11% and ICICI Bank, HDFC, HDFC Bank and NSE Strategic Investment Corporation with 10% each.
- The GST Council recommended a uniform policy on e way bill which is being implemented all over the country. This totally eliminates the checkpost system breaking the entry barriers and reducing bottlenecks in transportation.
- GST Council has also reviewed the rate structure of GST on goods and services. It also recommended reduction of rates on cases of merit.

### PRE GST TAX STRUCTURE & DEFICIENCIES

There are various economic factors internal as well as external due to which reforms in tax system become necessary. Issue of reforms in Indian tax system has always been a priority for all the administrative machinery even at the highest policy forums in the country. Integration of domestic economy with world economy makes it desirable.

Previous structure of indirect taxation in India had some challenges which needed to be addressed. Some of the challenges under the previous indirect tax structure could be attributed to:

- Central Excise wherein there were variable rates under Excise Duty such as 2% without CENVAT, 6%, 10%, 18%, 24%, 27%, coupled with multiple valuation system and various exemptions
- VAT where different states were charging VAT at different rates, which were resulting in imbalance of trade between the states
- Also, under VAT, there was a lack of uniformity in terms of registration, due date of payment, return filing assessment procedures, refund mechanism, appellate process etc., thus complicating the compliance mechanism. For example: A business establishment having offices in different states were required to follow the laws of the respective states.
- In respect of taxation of goods, CENVAT was confined to the manufacturing stage and did not extend to the distribution chain beyond the factory gate. As such, CENVAT paid on goods could not be adjusted against State VAT payable on subsequent sale of goods. This was true both for CENVAT collected on domestically produced goods as well as that collected as additional duty of customs on imported goods.
- CENVAT comprised of several components in the nature of cesses and surcharges such as the National Calamity Contingency Duty (NCCD), education and secondary and higher education cess, additional duty of excise on tobacco and tobacco products etc. This multiplicity of duties complicated the tax structure and often used to obstruct the smooth flow of tax credit.
- While input tax credit of CENVAT or additional duty of customs paid on goods was available to service providers paying Service Tax, they were unable to neutralize the State VAT or other State taxes paid on their purchase of goods.
- State VAT was payable on the value of goods inclusive of CENVAT paid at the manufacturing stage and thus the VAT liability of a dealer always used to get inflated without compensatory set-off.

- Inter-State sale of goods was liable to the Central Sales Tax (CST) levied by the Centre and collected by the states. This was an origin-based tax and could not be set-off against VAT in many situations.
- State VAT and CST were not directly applicable to the import of goods on which Special Additional Duties (SAD) of customs were levied at a uniform rate of 4% by the Centre. Input tax credit of such duties was available only to those entities who were manufacturing excisable goods. Other importers had to claim refund of this duty as and when they pay VAT on subsequent sales.
- VAT dealers were unable to set-off any Service Tax that they paid on procurement of taxable input services.
- State Governments also levied and collected a variety of other indirect taxes such as luxury tax, entertainment tax, entry tax etc. for which no set-off was available.



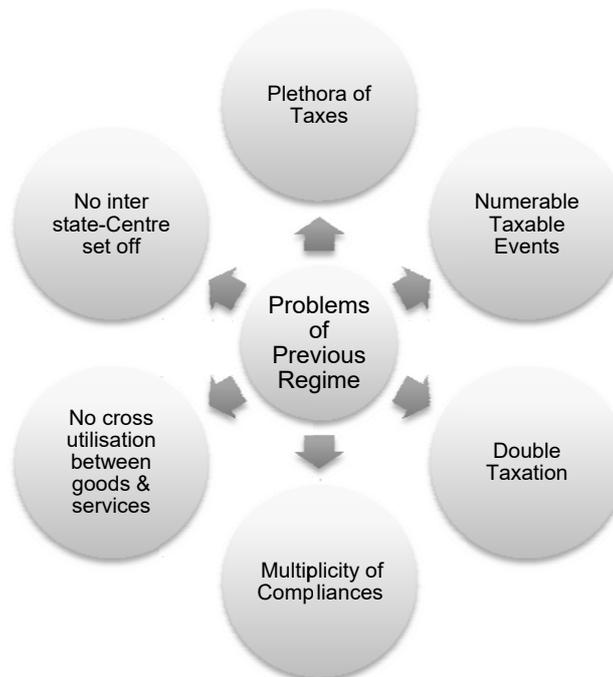
Following can be summarized as major reasons for implementation of a new indirect tax regime:

- (a) *Plethora of taxes* : There were various indirect taxes in India in existence prior to introduction of GST. There was a three tier system of tax collection in India :
  - i. Taxes levied by Central Government i.e. Customs Duties, Central Excise Duties, Service tax, additional duties of Excise etc.
  - ii. State Excise, VAT, CST, Entry tax, entertainment tax, luxury tax etc. are levied by the State Governments
  - iii. Local Bodies levy taxes like: entertainment tax, Octroi, property tax, local body tax, etc.
- (b) *Plenty of Taxable Events* : Taxes were levied at various stages on various taxable events by different authorities on the same subject matter or transaction. For example, Excise duty was levied at central level on manufacture. Service tax was levied on transport and other incidental services again by Central Government. Sales tax (VAT/CST) was collected by the State Government on sale. Entry tax was collected by State Government on the entry of goods in the state. Octroi was collected by municipal authorities when the goods enter the municipal area. The same goods were being subjected to varieties of taxes on variety of taxable events like entry, transport, manufacture, sale and so on. Most of the taxes were having cascading effect as there was no benefit of input tax credit.
- (c) *Double taxation* : On a single transaction, multiple taxes were being imposed, often by different authorities. For e.g. for a stay in a hotel in Delhi, you had to pay luxury tax as well as service tax. Service tax was collected by Central Government and applicable local taxes by State Government.

- (d) *Multiplicity of compliances* : Payment of tax to various authorities, different due dates, assessment, refund process at various levels made the taxation system more complex and led to an increase in compliance cost.

Further, there was inbuilt cascading effect of taxes due to:

- (i) *Lack of Cross-utilization facility between goods and services* : Taxes paid on procurement of input purchases were not allowed to be set off against output tax payable on services and vice versa.
- (ii) *Non-availability of set off arrangement against other State or Central Government levies* : CST paid in one state was not available as set off against sales tax payable in another state. Similarly, central taxes were not available as credit to set off against the taxes payable at the state level and vice versa. E.g., Excise duty and service tax paid on goods could not be used to pay VAT or CST. In the same way, VAT Credit (ITC) could not be used to pay excise duty or service tax.



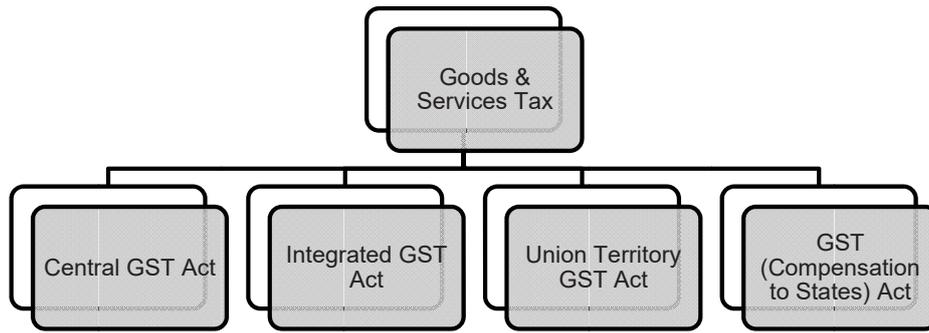
## ADMINISTRATION OF INDIRECT TAXATION IN INDIA

### Framework of GST

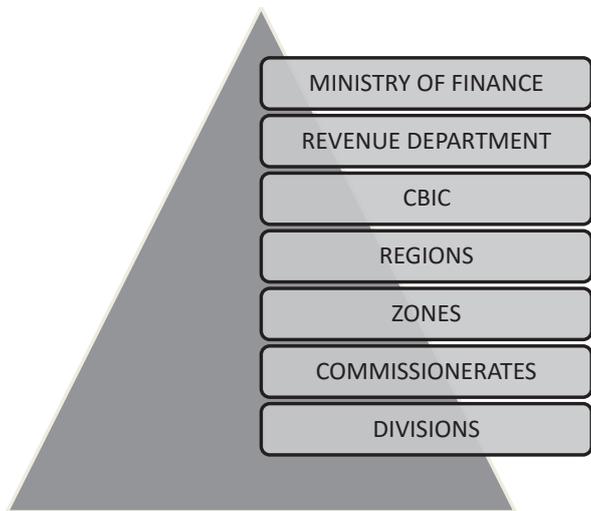
India is a federal country where both the Centre and the states have been assigned the powers to levy and collect taxes through respective legislations. Both the levels of Government i.e., at Centre and at the State level, have distinct responsibilities to perform according to the division of powers prescribed in the Constitution. A dual GST is thus implemented keeping in mind the Constitutional requirement of fiscal federalism.

Along with the amendment in the Constitution, to empower the Centre and the states to levy and collect the GST, four legislations were given assent by the President on April 12, 2017, which include:

- The Central GST Act, 2017
- The Integrated GST Act, 2017
- The GST (Compensation to States) Act, 2017 and
- The Union Territory GST Act, 2017



**ADMINISTRATIVE MECHANISM AT THE CENTRAL LEVEL**



AUTHORITY	HEADED BY
MINISTRY OF FINANCE	Union Finance Minister
REVENUE DEPARTMENT	Revenue Secretary
CBIC (Central Board of Indirect Taxes & Customs)	Chairman and Members
REGIONS	Principal Chief Commissioners
ZONES	Chief Commissioners
COMMISSIONERATES	Commissioners/ Principal Commissioners
DIVISIONS	Divisional officers/ deputy commissioner etc.

GST Council is the apex body for making recommendations on various issues relating to policy making, formulation of principles, implementation of policies under Goods and Services Tax regime.

Administration and Procedural Aspects of Goods and Services tax are administered by the Central Board of Indirect Taxes & Customs (CBIC) which is under the control of the Department of Revenue, Ministry of Finance.

**EXISTING TAX STRUCTURE**

**Passage of GST in India**

Goods & Services Tax is prevalent in almost 160 countries around the world and France was the first country to introduce the same in 1954. The journey to introduction of GST in India has been long and is a result of

larger sections of the society, particularly, trade and industry and the foreign establishments who have business interests in India.

To address the anomalies in the previous Indirect tax system, the Vajpayee government proposed comprehensive taxation on goods and services in July 17, 2000. It entrusted the job to a committee set up and headed by the then West Bengal Finance Minister to design a GST model.

When the Government of India set up the Empowered Committee of State Finance Ministers with the Hon'ble State Finance Ministers of West Bengal, Karnataka, Madhya Pradesh, Maharashtra, Punjab, Uttar Pradesh, Gujarat, Delhi and Meghalaya as members, it had the following objectives:

- to monitor the implementation of uniform floor rates of sales tax by States and Union Territories;
- to monitor the phasing out of the sales-tax based incentive schemes;
- to decide milestones and methods of States to switch over to VAT; and
- to monitor reforms in the Central Sales Tax system existing in the country.

Subsequently, Hon'ble State Finance Ministers of Assam, Tamil Nadu, Jammu & Kashmir, Jharkhand and Rajasthan were also notified as the members of the Empowered Committee.

On August 12, 2004, the Government of India decided to reconstitute the Empowered Committee with all the Hon'ble State Finance/Taxation Ministers as its members. Later on, it was decided to register the body as a Society under the Societies Registration Act, 1860. GST has been in the pipeline for a long time, for its implementation.

Here is a brief flash back mentioning the key milestones of the journey of GST in India:

- (i) **2003:** The Kelkar Task Force on Indirect Tax had suggested a comprehensive Goods and Services Tax based on VAT principle.
- (ii) **February, 2007:** An announcement was made by the then Hon'ble Union Finance Minister in the Central Budget (2007- 08) to the effect that GST would be introduced with effect from April 01, 2010.
- (iii) **September, 2009:** The Empowered Committee (EC) decided to constitute a Working Group consisting of Principal Secretaries / Secretaries (Finance / Taxation) and Commissioners of Trade Taxes of all States/UTs to give their recommendations on:
  - the commodities and services that should be kept in the exempted list;
  - the rules and principles of taxing the transactions of services including the transactions in inter-State services; and
  - finalization of the model suggested for inter-state transaction/movement of goods including stock transfers in consultation with the State Bank of India and some other nationalized banks.
- (iv) **November, 2009:** Based on inputs from Government(s) of Centre and States, Empowered Committee released its First Discussion Paper on GST.
- (v) **March, 2011:** The Constitution (One Hundred and Fifteenth Amendment) Bill, 2011 to give concurrent taxing powers to the Union and States was introduced in Lok Sabha. The Bill suggested the creation of Goods and Services Tax Council and a Goods and Services Tax Dispute Settlement Authority. The Bill was lapsed in 2014 and was replaced with the Constitution (122nd Amendment) Bill, 2014.
- (vi) **November, 2012:** A "Committee on GST Design", consisting of the officials of the Government of India, State Governments and Empowered Committee (EC) was constituted.
- (vii) **January, 2013:** The Empowered Committee deliberated on the proposed design including the Constitution (115th) Amendment Bill and submitted the report. Based on this Report, the EC

recommended certain changes in the Constitution Amendment Bill and decided to constitute three below mentioned Committees of Officers to discuss and Report on various aspects of GST:

- Committee on Place of Supply Rules and Revenue Neutral Rates;
  - Committee on dual control, threshold and exemptions;
  - Committee on IGST and GST on imports.
- (viii) **March, 2013:** A not for profit, non-Government, private limited company was incorporated in the name of Goods and Services Tax Network (GSTN) as special purpose vehicle setup by the Government primarily to provide IT infrastructure and services to the Central and State Government(s), tax payers and other stakeholders for implementation of GST.
- (ix) **August, 2013:** The Parliamentary Standing Committee submitted its Report to the Lok Sabha. The recommendations of the Empowered Committee and the recommendations of the Parliamentary Standing Committee were examined by the Ministry in consultation with the Legislative Department. Most of the recommendations made by the Empowered Committee and the Parliamentary Standing Committee were accepted and the Draft Amendment Bill was suitably revised.
- (x) **September, 2013:** The final draft Constitutional Amendment Bill incorporating the above stated changes was sent to the Empowered Committee (EC) for consideration.
- (xi) **November, 2013:** The EC once again made certain recommendations on the Bill after its meeting in Shillong. Certain recommendations of which were incorporated in the draft Constitution (115th Amendment) Bill and the revised draft was again sent to EC for its consideration.
- (xii) **June, 2014:** The draft Constitution Amendment Bill in March, 2014 was sent to the Empowered Committee after approval of the new Government.
- (xiii) **December, 2014:** The Constitution (One Hundred and Twenty-Second Amendment) Bill, 2014 seeking to amend the Constitution to introduce GST and subsume state Value Added Tax, Octroi and entry tax, luxury tax, etc. was introduced in the Lok Sabha on December 19, 2014 by the Hon'ble Minister of Finance, Mr. Arun Jaitley.
- (xiv) **May, 2015:** Constitution Amendment (122nd) Bill was passed by Lok Sabha on May 06, 2015.
- (xv) **May, 2015:** In Rajya Sabha, Bill was referred to a 21-member Select Committee of Rajya Sabha.
- (xvi) **July, 2015:** Select Committee submitted its report to Rajya Sabha on July 22, 2015.
- (xvii) **June, 2016:** On June 14, 2016, the Ministry of Finance released draft model law on GST in public domain for views and suggestion.
- (xviii) **August, 2016:** On August 03, 2016, the Constitution (122nd Amendment) Bill, 2014 was passed by Rajya Sabha with certain amendments.
- (xix) **August, 2016:** The changes made by Rajya Sabha were unanimously passed by Lok Sabha, on August 08, 2016.
- (xx) **September, 2016:** The Bill was adopted by majority of State Legislatures wherein approval of at least 50% of the State Assemblies was required
- (xxi) **September, 2016:** Final assent of Hon'ble President of India was given on 8th September, 2016
- (xxii) **April, 2017:** Parliament passed the following four bills:
- Central Goods and Services Tax (CGST) Bill
  - Integrated Goods and Services Tax (IGST) Bill

- Union Territory Goods and Services Tax (UTGST) Bill
- Goods and Services Tax (Compensation to States) Bill

(xxiii) **April, 2017:** President's assent was given to four key legislations on Goods and Services tax.

(xxiv) **July, 2017:** GST became a reality

The current status of GST Laws Passed in India is as under:

The law	Purpose
The Central Goods and Services Tax Act, 2017 (CGST Act)	To levy, collect CGST on intra-state supplies and for other matters
The Integrated Goods and Services Tax Act, 2017 (IGST Act)	To levy, collect IGST on inter-state supplies and for other matters
The Union Territory Goods and Services Tax Act, 2017 (UTGST Act)	To levy, collect UTGST on intra-UT supplies and for other matters
GST (Compensation to States) Tax Act, 2017	To compensate states for the loss of revenue if any due to introduction of GST
The States Goods and Services Tax Act, 2017 (SGST Act)	To levy, collect SGST on intra-state supplies and for other matters

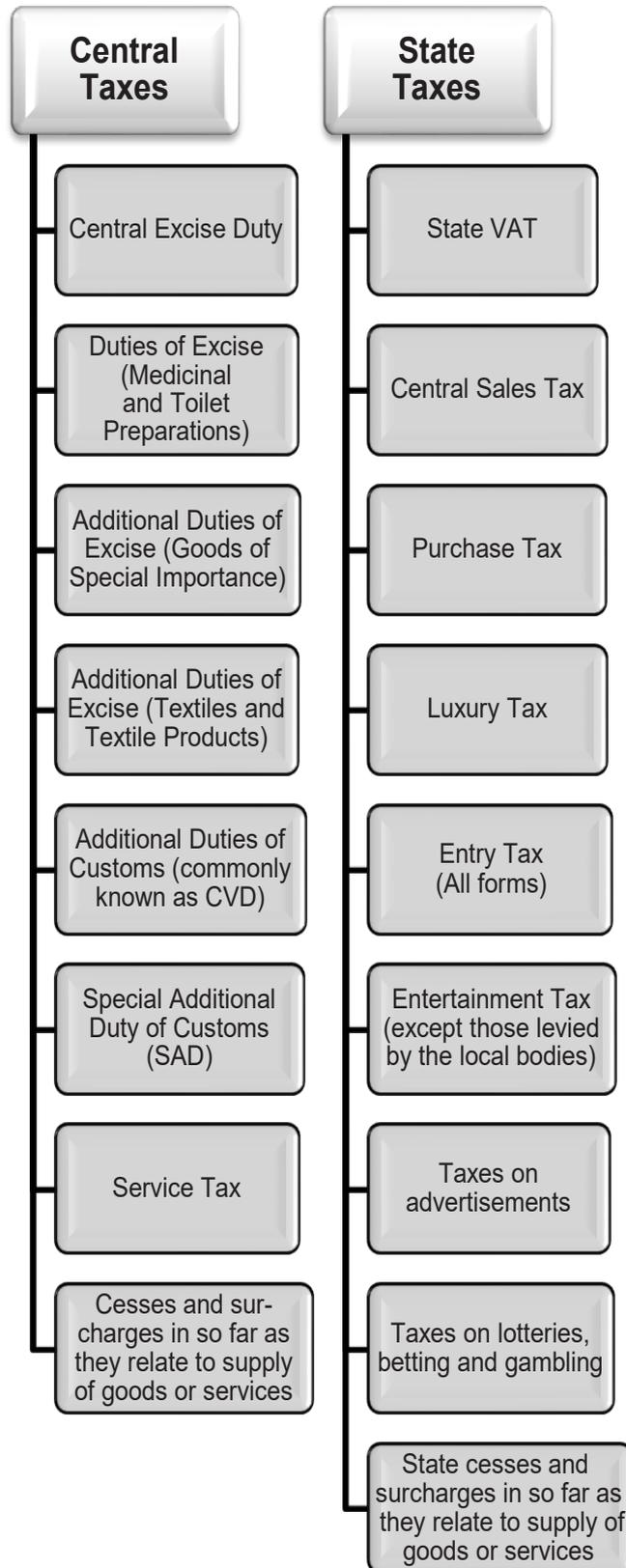
### GST in India

GST is one of the biggest taxation reforms of independent India with the objective of integrating State economies. GST, the most historic indirect tax reform, is implemented with the aim of enhancing the overall growth of the Nation along with supporting the Make in India initiative. It aims at creating a single, unified Indian market throughout the Nation. It is a comprehensive destination based indirect tax levy on goods as well as services at the national level. Its main objective is to consolidate multiple indirect tax levies into a single tax thus subsuming an array of tax levies, overcoming the limitations of previous indirect tax structure, and creating efficiencies in tax administration.

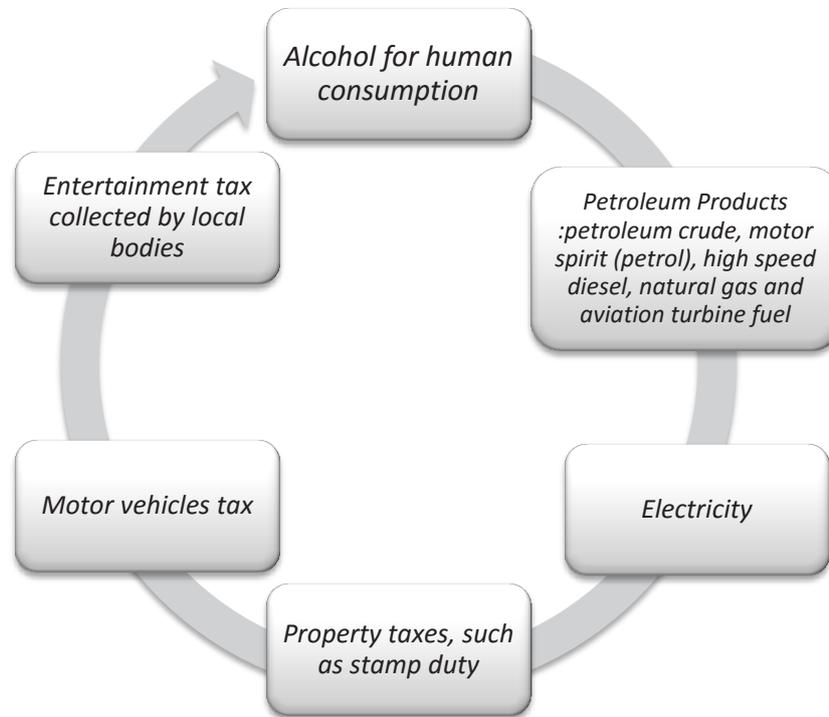
GST is a consumption based tax which is levied on the basis of "Destination principle." The concept relates to taxing the supply of goods or services at the point of consumption. It is a comprehensive tax regime covering both goods and services, and is collected on value-added at each stage of the supply chain. Further, GST paid on the procurement of goods and services can be set off against that payable on the supply of goods or services. Simply put, Goods and Services Tax is a tax levied on goods and services imposed at each point of supply. GST is a national level tax based on value added principle just like State level VAT which was levied as tax on sale of intra-state goods.

The essence of GST is in removing the cascading effects i.e., tax on tax of both Central and State taxes by allowing setting-off of taxes throughout the value chain, right from the original producer and service provider's point up to the consumer level. GST is a major improvement over existing system of VAT and disjointed Service Tax ushering a collective gain for industry, trade and common consumers as well as for the Central Government and the State Governments at large. GST, as a well-designed value added tax on all goods and services, is the most elegant method to eliminate distortions and to tax consumption.

The following taxes have been subsumed under GST:



The following subject matters kept outside the purview of GST. As such these are taxed under the existing laws of centre and states as the case may be.



Tobacco and tobacco products would be subject to GST. In addition, the Centre would have the power to levy Central Excise duty on these products.

### Models of GST

The principles of GST are largely common in almost all the countries. However, there are significant differences in the implementation of the same depending on continued existence of exemptions and special arrangements to meet specific policy objectives. The point of difference also arises from differences of approaches in the defining the jurisdiction of consumption and hence of the taxation. Moreover, there are a number of variations in the application of GST along with different interpretation of the same or similar concepts; different approaches to time of supply and its interaction with place of supply; different definitions of services and intangibles and inconsistent treatment of mixed supplies, around the world.

Different countries follow different model of GST based upon their own legislative and administrative structure and their requirements. Some of these models are:

- Australian Model wherein, tax is collected by the Centre and distributed to the States
- Canadian Model wherein there are three variants of taxes
- Kelkar-Shah Model based on Canada Model wherein taxes are collected by the Centre however, two different rates of tax are to be levied by the Centre and the States and
- Bagchi-Poddar Model which envisages a combination of Central Excise, Service Tax and VAT to make it a common base of GST to be levied both by the Centre and the States separately.

Mostly all over the world, many countries follow a unified GST regime. However, considering the federal nature of Indian Constitution, dual model of GST was required, proposed and levied. In dual model of GST, where the power to levy taxes is subjectively distributed between Centre and States, GST is levied by both, the Centre as well as the States and there are separate levies in the form of Central Goods and Services Tax (CGST), State

Goods and Services Tax (SGST) and Integrated Goods and Services Tax (IGST) enabling the tax credit across these three variants of taxes. Currently, Brazil and Canada also follow dual GST model.

The Indian GST system has its own uniqueness in many ways. Apart from India, Brazil is the only country in the world which follows a similar dual GST System. In India, GST has been rolled out as a uniform taxation system all across the Nation by removing entry barriers between states.

In Canada, though GST scheme closely resembles that of India, it failed to achieve consensus among states. As a result the GST was made optional not mandatory. States are free to adopt or reject GST. In India, GST is uniformly applicable all over India including the State of Jammu and Kashmir.

### LESSON ROUND UP

- There are two types of taxes i.e., Direct tax and Indirect Tax
- Previous Indirect tax laws consisted of various taxes at Central and State level including VAT, Excise, Service Tax and like
- Previous structure of indirect taxation in India had some challenges which needed to be addressed
- Goods & Services Tax regime of indirect taxes brought a single tax which was levied on supply of goods or services or both with concurrent jurisdiction of Centre and states
- Various Constitutional amendments became necessary to enable centre and states to levy GST simultaneously
- A high powered federal body called GST Council has been established under Article 279A of the Constitution of India
- A GST Council consisting of representatives from the Centre as well as State has been formulated under the GST Law of indirect taxes. The Council will make recommendations to the Union and the States on Goods and Service Tax laws, on any other matter relating to GST
- Various new Articles were inserted and old ones omitted and GST was brought in by Constitution (101st) Amendment Act, 2016

### SELF TEST QUESTIONS

#### Elaborative QUESTIONS

- Q1. Throw some light on the shortcomings of pre GST indirect tax regime in India.
- Q2. What is the constitution of GST Council in India and its functions?
- Q3. Briefly discuss the Model of GST followed in India.
- Q4. Discuss the administrative machinery of GST in India.
- Q5. Highlight the salient features of Indian GST.

### SUGGESTED READINGS

1. Goods & Services Tax, Laws, Concepts and Impact Analysis-Bloomsbury – Dr. Sanjiv Agarwal & Sanjeev Malhotra
2. GST Ready Reckoner- Taxmann – V.S. Datey
3. A complete guide to Goods & Services Tax Ready Reckoner in Q & A Format- Bloomsbury – Dr. Sanjiv Agarwal & Sanjeev Malhotra



# Lesson 12

## Basics of Goods and Services Tax

### LESSON OUTLINE

- Basic concepts and overview of GST
- GST Model
- Constitutional Framework of GST
- Taxable Event
- Concept of supply including composite and mixed supply
- Levy and collection of Tax
- Composition Scheme & Reverse Charge
- Exemptions under GST
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

GST is a consumption based tax levied on the basis of the “Destination principle.” It is an inclusive tax regime covering both goods and services, to be collected on value-added at each stage of the supply chain. One of the main reasons to go the GST way was to facilitate seamless credit across the entire supply chain and across all states under a common tax base.

GST regime shall enhance transparency in the indirect tax framework and is expected to bring down the rate of inflation. It will also be a boost to investment inflows, e-commerce and “Make in India” initiative. It shall uplift the less developed states and will lower compliance cost leading to overall efficiency in the indirect – tax structure of the country.

## BASIC CONCEPTS AND OVERVIEW OF GOODS AND SERVICES TAX

GST is a single, unified tax on every value-add, right from manufacture to sale / consumption of goods / services. Hence, with the advent of GST, the legacy taxes on manufacture (Excise), Inter-state sales (CST), Intra-state sales (VAT) and Service Tax have been subsumed. There has been a paradigm shift in the way the tax is being levied. We have now moved from source based to destination-based taxation, with GST coming into foray. Hence GST is also labelled as a destination-based / consumption-based tax.

GST also does away with the cascading effects of taxation, by providing a comprehensive and continuous chain of tax credits, end to end and taxing only the value-added at every stage. The final tax is borne by the end consumer, as all the parties in the interim can extinguish their respective collections against their respective liabilities and the tax already paid by them (Input Tax Credit).

A numerical example of the same below helps understand the concept better:

<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%;">Tax Collected from B</td> <td style="text-align: right;">18000</td> </tr> <tr> <td>Tax paid to Govt</td> <td style="text-align: right;">-18000</td> </tr> <tr> <td><b>Tax Incidence</b></td> <td style="text-align: right;"><b>NIL</b></td> </tr> </table>	Tax Collected from B	18000	Tax paid to Govt	-18000	<b>Tax Incidence</b>	<b>NIL</b>	<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%;">Tax Collected from C</td> <td style="text-align: right;">21600</td> </tr> <tr> <td>Tax paid to A</td> <td style="text-align: right;">-18000</td> </tr> <tr> <td>Tax Paid to Govt</td> <td style="text-align: right;">3600</td> </tr> <tr> <td><b>Tax Incidence</b></td> <td style="text-align: right;"><b>NIL</b></td> </tr> </table>	Tax Collected from C	21600	Tax paid to A	-18000	Tax Paid to Govt	3600	<b>Tax Incidence</b>	<b>NIL</b>	<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%;">Tax Paid to B</td> <td style="text-align: right;">-21600</td> </tr> <tr> <td><b>Final Tax Incidence</b></td> <td style="text-align: right;"><b>-21600</b></td> </tr> </table>	Tax Paid to B	-21600	<b>Final Tax Incidence</b>	<b>-21600</b>
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Tax Paid to Govt	3600																			
<b>Tax Incidence</b>	<b>NIL</b>																			
Tax Paid to B	-21600																			
<b>Final Tax Incidence</b>	<b>-21600</b>																			

Value Added                      20%

<b>Party A (Wholeseller)</b>	<b>Party B (Retailer)</b>	<b>Party C (Consumer)</b>												
<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%;">Value of Supply</td> <td style="text-align: right;">100000</td> </tr> <tr> <td>GST</td> <td style="text-align: right;">18000</td> </tr> <tr> <td><b>Invoice Value</b></td> <td style="text-align: right;"><b>118000</b></td> </tr> </table>	Value of Supply	100000	GST	18000	<b>Invoice Value</b>	<b>118000</b>	<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%;">Value of Supply</td> <td style="text-align: right;">120000</td> </tr> <tr> <td>GST</td> <td style="text-align: right;">21600</td> </tr> <tr> <td><b>Invoice Value</b></td> <td style="text-align: right;"><b>141600</b></td> </tr> </table>	Value of Supply	120000	GST	21600	<b>Invoice Value</b>	<b>141600</b>	
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<b>Invoice Value</b>	<b>118000</b>													
Value of Supply	120000													
GST	21600													
<b>Invoice Value</b>	<b>141600</b>													

### Note:

- a) There is no tax incidence on any interim party, i.e., neither on the wholeseller nor the retailer
- b) The reason is simple, the tax that each of them have paid, can be set off against their respective output tax liabilities (Input Tax Credit)
- c) The final incidence is only on the end consumer, clearly reiterating the manner in which the cascading effects of the legacy taxation methodologies have been done away with.

## GST MODEL

India has adopted a dual GST model, i.e., where the tax is imposed concurrently by the Centre and the States. For an intra-state sale, the GST is equally divided between the Centre and the State (CGST + SGST), and for inter-state sales, the GST is collected by the Centre (IGST).

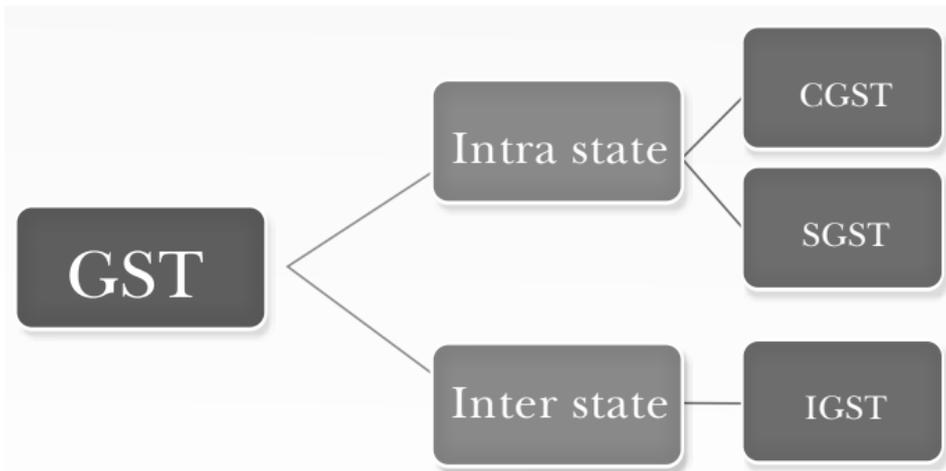
GST, therefore is a destination-based tax applicable on all transactions, involving supply of goods / services for a consideration, and comprises of **Central Goods & Services Tax (CGST)**, levied by the Central Government, and **State Goods and Services Tax (SGST)**, levied by the State Government OR **Union Territory Goods and Services Tax (UTGST)** levied by Union Territories, on Intra-state supplies of taxable goods & services.

Inter-state supplies of taxable goods / services are subject to Integrated Goods & Services Tax (IGST), which is levied by the Central Government and is equal to CGST + SGST.

The CGST is levied under the CGST Act, 2017. UTGST is levied under the UTGST Act, 2017 and this is applicable to Union Territories, i.e., Andaman & Nicobar Islands, Lakshadweep, Dadra & Nagar Haveli, Daman & Diu, Chandigarh and other territory. SGST is levied under the respective state legislations.

Jammu & Kashmir & Ladakh has been made union territories but for the time being J&K SGST Act is applicable.

Dadra & Nagar Haveli & Daman & Diu are to be merged into a single Union Territory.

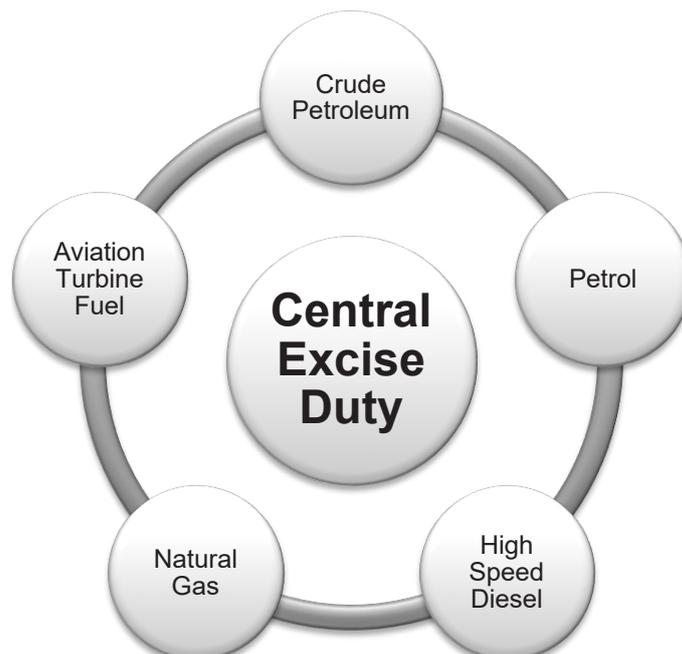


**CONSTITUTIONAL FRAMEWORK OF GOODS & SERVICES TAX**

Power to levy Goods and Services Tax (GST), has been conferred by Article 246A of the Constitution. This was introduced, by the Constitution (101st Amendment) Act, 2016.

**Presently not taxable under GST**

In respect of the following goods, the provisions around chargeability of GST would apply from the date when recommended by the GST Council.



Therefore, Central Excise Duty continues to be levied on manufacture of Tobacco, Petroleum Crude, High Speed Diesel, Petrol, Natural Gas and Aviation Turbine Fuel.

State Excise Duty continues to be levied on manufacture of alcohol. Tobacco attracts both Excise and GST.

### Outside the scope of GST

Petroleum Products and Alcoholic Liquor for human consumption is kept outside the ambit of GST. Additionally, though, electricity has not been explicitly excluded from GST but it is considered as Nil rated in GST and continues to be charged with pre-GST taxes, i.e., electricity duty by the State Governments.

There are certain activities which are items not covered under GST. They are beyond the scope of GST, i.e., GST will not apply on them. These are classified under Schedule III of the GST Act as “Neither goods nor services”.

#### 1. Services by an employee to the employer in relation to his employment

Related parties include employer-employee which raised many concerns whether employment now attracted GST. This clarification has been brought in to clarify whether GST is not applicable on employment. An employee will still pay income tax on salary earned .

#### 2. Court/Tribunal Services including District Court, High Court and Supreme Court

Courts will not charge GST to pass judgement.

#### 3. Duties performed by:

- The Members of Parliament, State Legislature, Panchayats, Municipalities and other local authorities
- Any person who holds a post under the provisions of the Constitution
- Chairperson/Member/Director in a body established by the government or a local body and who is not an employee of the same

#### 4. Services of a funeral, burial, crematorium or mortuary including transportation of the deceased

There are no taxes on funeral services for any religion.

#### 5. Sale of land and sale of building

Construction of a new building is subject to GST (being works contract).

#### 6. Actionable claims (other than lottery, betting and gambling)

Actionable Claims' means claims which can be enforced only by a legal action or a suit, example a book debt, bill of exchange, promissory note. A book debt (debtor) is not goods because it can be transferred as per Transfer of Property Act but cannot be sold. Bill of exchange, promissory note can be transferred under Negotiable Instruments Act by delivery or endorsement but cannot be sold.

Actionable claims are neither products nor services. They can be considered as something in lieu of money. So GST will not apply on these.

Lottery, betting and gambling attract 28% GST.

#### 7. Supply of goods from a place in the non-taxable territory to another place in the non-taxable territory without such goods entering into India\*.

#### 8. Supply in Customs port before Home consumption\*:

- (a) Supply of warehoused goods to any person before clearance for home consumption;
- (b) Supply of goods by the consignee to any other person, by an endorsement of documents of title to the

goods, after the goods have been dispatched from the port of origin located outside India but before clearance for home consumption.

## TAXABLE EVENT

The crux of any taxation system is the incidence, i.e., the point at which the liability to charge tax arises, and that event is nomenclated as the taxable event.

Goods and Services Tax, with its introduction and in the process of subsuming the other Acts, has overcome many shortcomings of the legacy system too, one of them being, the definition of taxable event. The multitude of tax laws that prevailed earlier, that is Central Excise, Sales Tax, Service Tax, VAT etc., were prone to ambiguity and controversies which has been overcome to a great extent by the comprehensive approach and definition as laid down by GST.

The taxable event in GST is the Supply of goods or services rather than sale, manufacture, production of goods and provision of services.

GST has kept it not only simple, but also robust, by stating that the entire value of supply of goods / services are taxed in an integrated manner.

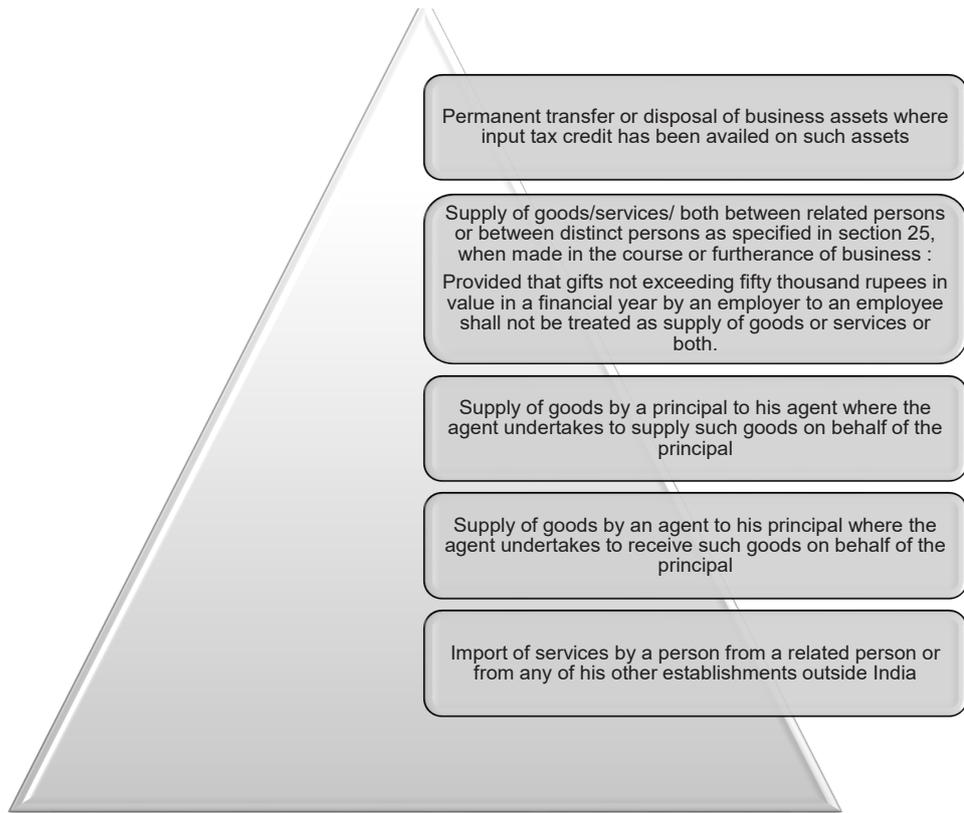
## CONCEPT OF SUPPLY

Supply is the point of taxation or the taxable event under Goods & Services Tax. The term supply is characterised by the following necessary traits:

- Supply should be of goods or services
- Anything which is not goods / services (like money, securities etc.) is not supply
- It must be reiterated that only movable property is construed as goods
- Barter and exchanges would be leviable to GST
- Licences, leases, rentals with or without transfer of the right to use are considered as supply and leviable to GST
- Supply should be made for a consideration which could be in the form of money or otherwise
- Supply includes the flow of money from a 3rd party in lieu of OR on behalf of the recipient
- Deposit is not consideration unless specifically applied to by the supplier
- Supply should be made in the course of OR for the furtherance of business
- Any supply made for personal consumption OR in personal capacity does not attract GST
- Supply should be made by a taxable person
- Supply between both non-taxable parties is not leviable to GST
- Supply could be made to a non-taxable person also
- A taxable person is one who is registered OR is liable to be registered under the Act

### Schedule I:

There are a few transactions which, even without consideration are construed as supply, also known as deemed supplies as specified in Schedule I:



**Schedule II:**

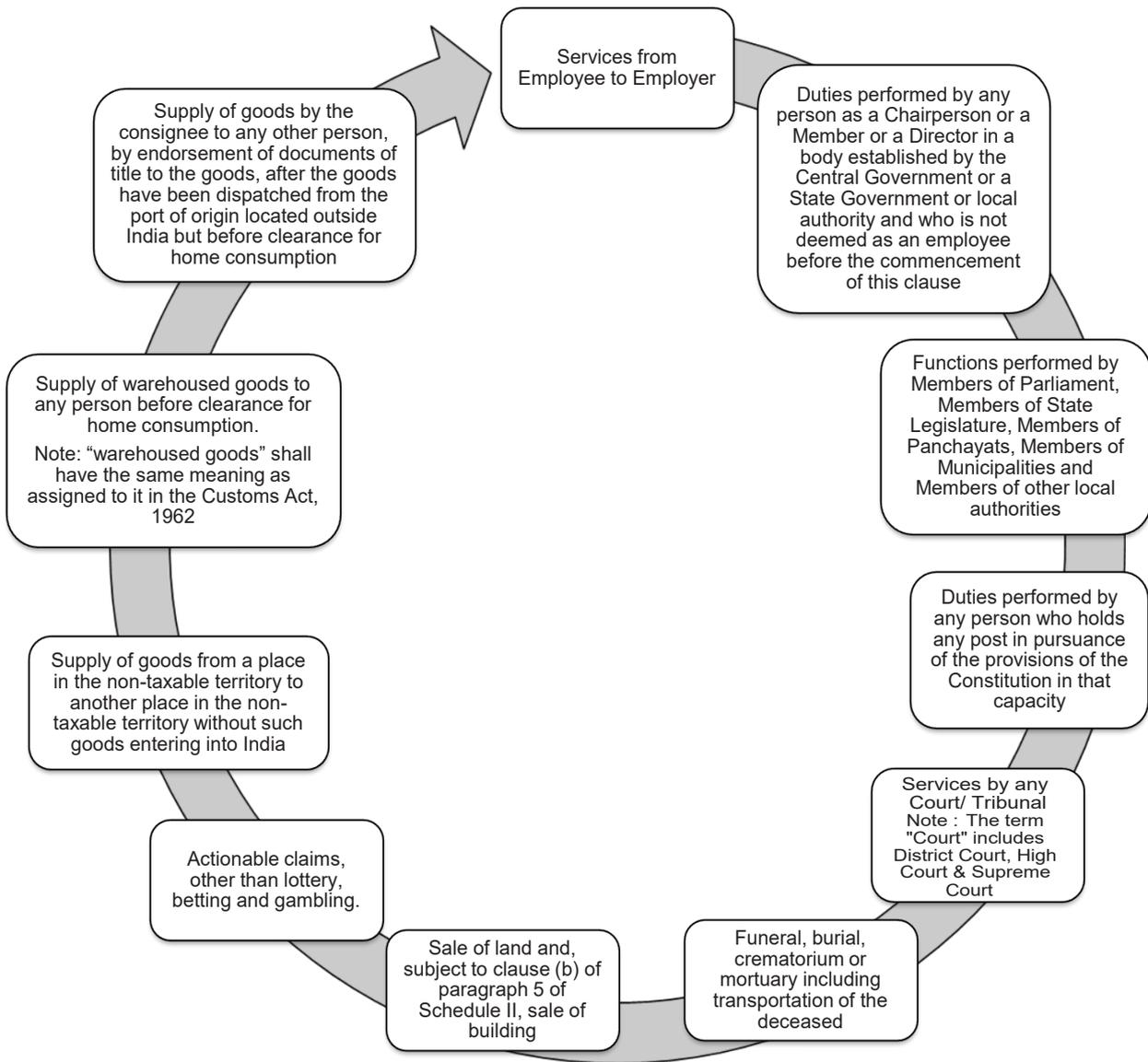
Schedule II of the Central Goods & Services Tax Act, 2017 lists activities or transactions which are to be treated as supply of goods or supply of services.

Form of Supply	Description
Supply of Goods	Transfer of title in goods
Supply of Goods	Transfer of title in goods under an agreement where property in goods passes at a future date on payment of full consideration
Supply of Goods	<p>Permanent transfer or disposal of goods forming part of business assets by or under the directions of the person carrying on the business whether or not for consideration</p> <p>Any goods forming a part of business assets will be deemed to be transferred in furtherance of business, before any person ceases to be a taxable person</p> <p>Exception</p> <ul style="list-style-type: none"> <li>• The business is transferred as a going concern</li> <li>• The business is carried on by a personal representative who is deemed to be a taxable person</li> </ul>
Supply of Goods	Supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration.

<b>Supply of Services</b>	Any transfer of right in goods or undivided share in goods without transfer of title
<b>Supply of Services</b>	Any lease, tenancy, easement, licence to occupy land Any lease or letting out of the building including a commercial, industrial or residential complex for business or commerce, either wholly or partly
<b>Supply of Services</b>	Any treatment or process which is applied to another person's goods
<b>Supply of Services</b>	Where, by or under the direction of a person carrying on a business, goods held assets or used for the purpose of business are put for any private use or made available to any person for any use other than for the purpose of business, at the direction of the person carrying on the business, whether or not for a consideration.
<b>Supply of Services</b>	Renting of immovable property
<b>Supply of Services</b>	Construction of a complex, building, civil structure or a part thereof, including a complex or building intended for sale to a buyer, wholly or partly, except where the entire consideration has been received after issuance of completion certificate, where required, by the competent authority or after its first occupation, whichever is earlier
<b>Supply of Services</b>	Temporary transfer or permitting the use or enjoyment of any intellectual property right
<b>Supply of Services</b>	Development design, programming, customisation, adaptation, upgradation, enhancement, implementation of information technology software
<b>Supply of Services</b>	Agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act
<b>Supply of Services</b>	Transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration
<b>Supply of Services</b>	Works Contract as defined under Section 2(119) Supply of goods, as a part of any service or in any manner, being food or any other article for human consumption or any drink (other than alcoholic liquor for human consumption), where such supply or service is for cash deferred payment or other valuable consideration

**Schedule III:**

There are a few activities which are specifically not to be considered as Supply. Schedule III to CGST Act, 2017 lists down the following activities which shall be treated neither as supply of goods nor supply of services.



For example, as per Schedule III, the services by an employee to an employer are not chargeable to GST, and the gifts made by employer to any employee up to INR 50,000 in any Financial Year shall not be treated as supply, however if more than INR 50,000 shall be subject to GST.

**Composite & Mixed Supply**

Often goods or services or both together are supplied in combination and that's when it may not be simple enough to distinguish supplies and identify them separately, as each of them may attract a different rate of tax but is sold as one package.

**Composite Supply**

Section 2(30) defines "composite supply" as a supply made by a taxable person to a recipient consisting of two or more taxable supplies of goods or services or both, or any combination thereof, which are naturally

bundled and supplied in conjunction with each other in the ordinary course of business, one of which is a principal supply;

The features of a composite supply are:

- a) Two or more taxable supplies of goods / services / both which are supplied in conjunction with each other
- b) They are naturally bundled
- c) A single price is charged for the supply
- d) One of the supplies within the package is identifiable as a principal supply

**Example:**

On buying a LED Television, along with it, the remote control, the wires and all the accessories that go with it along with the warranty and the maintenance services are provided.

It is evident here that the LED Television is the principal supply and the others (remote / wires / warranty are all ancillaries).

**Taxability**

The composite supply will be charged at the rate which is applicable to the principal supply.

<b>Composite Supply</b>	
	<b>INR</b>
LED Television supplied with remote, wires and 1 Yr Warranty with AMC	100000
GST (LED TV) @ 28%	28000
<b>Invoice Value</b>	<b>128000</b>

Here rates have been mentioned only for illustration purpose. Actual Rates may vary.

**Mixed Supply**

Under Section 2(74) of CGST Act, 2017, “mixed supply” means two or more individual supplies of goods or services, or any combination thereof, made in conjunction with each other by a taxable person for a single price where such supply does not constitute a composite supply. The features of a mixed supply are:

- a) Two or more taxable supplies of goods / services / both which are supplied in conjunction with each other
- b) They are deliberately bundled
- c) A single price is charged for the supply
- d) None of the supplies within the package is identifiable as a principal supply

**Example:**

One buys a consolidated package of beauty products (that is shampoo, comb, conditioner, nail polish, lipstick and tooth powder).

It is evident here that the products can all be independently supplied and any one of them cannot be singled out as a principal supply and these are deliberately bundled and sold together.

**Taxability**

The mixed supply will be charged at the rate applicable to the supply that attracts the highest rate of tax from within the consolidated package.

<b>Mixed Supply</b>	
	<b>INR</b>
Bottles of Shampoo (GST @ 28%)	2000
Bottles of Conditioners (GST @ 28%)	1500
Comb (GST @ 5%)	200
Hair Dryer (GST @ 28%)	1250
Lipstick set (GST @ 28%)	1750
Nail Polish (GST @ 28%)	800
Tooth Powder (GST @ 12%)	500
Consolidated Value of Supply	8000
GST (highest rate 28%)	2240
Invoice Value	10240

Here rates have been mentioned only for illustration purpose. Actual GST rates may vary.

### LEVY & COLLECTION OF TAX

GST is levied at the point of supply, that is at the time and place of supply and that's when the liability to charge GST arises.

As explained under Section 15 to Central Goods & Services tax Act, 2017, such GST would be levied on the transaction value.

#### **Rates (Goods)**

Rates are broadly 0.25%, 3%, 5%, 12%, 18% and 28% and that is split into CGST and SGST equally for Intra-state sales and fully leviable as IGST for Inter-state sale.

#### **Rates (Services)**

Rates are broadly 5%, 12%, 18% and 28% and that is split in to CGST and SGST equally for Intra-state sales and fully leviable as IGST for Inter-state sale.

### COMPOSITION SCHEME

Section 10 of the CGST Act, 2017 contains the provisions regarding composition levy. The objective of the scheme is to bring about simplicity and to reduce compliance cost for the small taxpayers. Small tax payers, who have an annual turnover of less than Rs. 1.5 crore (applicable from 1st April 2019 onwards) in the preceding Financial Year (FY) are eligible to opt for this scheme i.e., Composition Levy.

For the states namely (i) Arunachal Pradesh (ii) Manipur, (iii) Meghalaya, (iv) Mizoram, (v) Nagaland, (vi) Sikkim, (vii) Tripura, (viii) Uttarakhand aggregate turnover limit shall be Rs. 75 lakh.

The aggregate turnover would mean the sum of:

- i) Taxable supplies
- ii) Exempt supplies
- iii) Zero-rated supplies
- iv) Inter-state supplies

The Reverse Charge Mechanism supplies are not included here, as these would be added to the turnover of the unregistered supplier.

**Conditions & Restrictions**

- 1) The supplier who opts for Composition Levy cannot raise tax invoice
- 2) Therefore, they need not collect any tax on supply
- 3) Hence, the recipient of such supplies can't claim any Input Tax Credit (ITC) on supplies from such suppliers who have opted for Composition Levy
- 4) Similarly, even they themselves cannot claim any ITC on the inward taxable supplies
- 5) A person opting for the scheme shall mention on the invoices issued that he has opted for such scheme
- 6) He shall also mention "composition taxable person" on every notice board displayed at the place of business
- 7) The following cannot opt for composition levy:
  - a. Supplier of services (except restaurant services)
  - b. Supplier of exempt goods
  - c. Supplier of Inter-state supplies
  - d. E-commerce operators
  - e. Manufacturers of ice-cream, pan masala and tobacco
  - f. casual taxable person and non-resident taxable person

**Rates**

The tax rate prescribed for different categories of registered persons under the scheme is as follows :

S. NO.	REGISTERED PERSON	CGST RATE	SGST RATE	TOTAL TAX RATE
1.	Manufacturers (other than manufacturers of goods as may be notified by the Government i.e. ice cream, pan masala and tabacco)	0.5%	0.5%	1%
2.	Restaurant Services i.e., suppliers of food/ drink for human consumption (other than alcoholic liquour for human consumption)	2.5%	2.5%	5%
3.	Traders or any other supplier eligible for composition levy	0.5%	0.5%	1%

Turnover in case of traders has been defined as 'Turnover of taxable supplies of goods and services'. Thus, for traders, exempted supplies would not be added in the turnover for the purpose of levy of 1% Composition levy.

**Benefit for marginal supply of services along with the supply of goods or restaurant services.**

Fundamentally, the composition scheme can be availed in respect of goods and only one service namely, restaurant service. However, there are cases where a manufacturer/ trader is also engaged in supply of services other than restaurant service though the percentage of such supply of services is very small as compared to the supplies of goods. There may also be cases where a restaurant service provider is also engaged in supplying a small percentage of other services.

With a view to enable such taxpayers to avail of the benefit of composition scheme, second proviso to section

**604 EP-TL**

10(1) permits marginal supply of services [other than restaurant services] for a specified value along with the supply of goods and/or restaurant service, as the case may be. This specified value is the value not exceeding:

(a) 10% of the turnover in a State/Union territory in the preceding financial year

Or

(b) Rs. 5 Lacs

whichever is higher.

**For example:** Mr. Ram is engaged in supply of goods. His aggregate turnover in preceding FY is Rs. 80 lakh. Since his aggregate turnover in the preceding FY does not exceed Rs. 1.5 crore, he is eligible for composition scheme in current FY. Further, in current FY, he can supply services [other than restaurant services] upto a value not exceeding:

(a) 10% of Rs. 80 Lacs i.e. Rs. 8 Lacs

Or

(b) Rs. 5 Lacs

whichever is higher. Thus, he can supply services upto a value of Rs. 8 lakh in current FY. If the value of services supplied exceeds Rs. 8 lakh, he becomes ineligible for the composition scheme and has to opt out of the composition scheme

**New scheme of composition : Section 10(2A)**

As we have already seen that primarily, the composition scheme is available in respect of goods and only one service namely, restaurant service. Further with the supply of goods and/or restaurant service. However, a person engaged exclusively in supply of services other than restaurant service is not eligible for the composition scheme.

In order to provide benefit to such suppliers, a scheme to pay tax at the concessional rate has been formulated primarily for small service providers like salon stylist, tailors etc. who are not otherwise eligible for composition scheme.

*Sec 10(2A) : Composition scheme for service providers*

Notwithstanding anything to the contrary contained in this Act, but subject to the provisions of sub-sections (3) and (4) of section 9, a registered person, not eligible to opt to pay tax under sub-section (1) and sub-section (2), whose aggregate turnover in the preceding financial year did not exceed fifty lakh rupees, may opt to pay, in lieu of the tax payable by him under sub-section (1) of section 9, an amount of tax calculated at such rate as may be prescribed, but not exceeding three per cent. of the turnover in State or turnover in Union territory, if he is not--

- (a) engaged in making any supply of goods or services which are not leviable to tax under this Act;
- (b) engaged in making any inter-State outward supplies of goods or services;
- (c) engaged in making any supply of goods or services through an electronic commerce operator who is required to collect tax at source under section 52;
- (d) a manufacturer of such goods or supplier of such services as may be notified by the Government on the recommendations of the Council; and
- (e) a casual taxable person or a non-resident taxable person:

Provided that where more than one registered person are having the same Permanent Account Number issued under the Income-tax Act, 1961 , the registered person shall not be eligible to opt for the scheme under this sub-section unless all such registered persons opt to pay tax under this sub-section.”;

In computing aggregate turnover in order to determine eligibility of a registered person to pay tax under any of the composition schemes, the expression “aggregate turnover” shall include the value of supplies made by such person from the 1st day of April of a financial year up to the date when he becomes liable for registration under this Act, but shall not include the value of exempt supply of services provided by way of extending deposits, loans or advances in so far as the consideration is represented by way of interest or discount.

For the purposes of determining the tax payable by a person under this section, the expression “turnover in State or turnover in Union territory” shall not include the value of following supplies, namely supplies from the first day of April of a financial year up to the date when such person becomes liable for registration under this Act; and exempt supply of services provided by way of extending deposits, loans or advances in so far as the consideration is represented by way of interest or discount.’

The GST under Composition Scheme is not collected from the recipients / customers; this is simply a facility for hassle free compliance under GST. The composition levy if opted is applicable under one PAN, and then it is applicable for all businesses under that PAN, or none. This implies, that it is not allowed for some businesses under normal levy and some under composition levy.

Once the turnover breaches the threshold, the composition levy is switched off and the normal levy is applicable.

**Illustration 1**

P, a trader who has a revenue of INR 50,00,000 inclusive of GST @ 5% has purchases amounting to INR 40,00,000 (GST @ 5% extra). Book-keeping and GST compliance costs are INR 250,000 and other administrative costs are INR 50,000. He now wants to switch to Composition Levy. You are requested to advise in your capacity as a GST consultant.

Normal Levy		Composition Levy	
Revenue	50,00,000	Revenue	50,00,000
Less: GST	2,38,095	Less: GST	NIL
Net Revenue	47,61,905	Net Revenue	50,00,000
Less: Purchases	40,00,000	Less : Purchases	42,00,000
Book Keeping	2,50,000	Book Keeping	1,00,000
Other Costs	50,000	Other Costs	50,000
		GST Liability	50,000
<b>Profit</b>	<b>4,61,905</b>	<b>Profit</b>	<b>6,00,000</b>
Payable	2,38,095	<b>GST Liability</b>	<b>50,000</b>
ITC	2,00,000	(1% of Turnover)	
<b>GST Liability</b>	<b>38,095</b>		
<b>Cash Flow</b>	<b>4,23,810</b>	<b>Cash Flow</b>	<b>6,00,000</b>

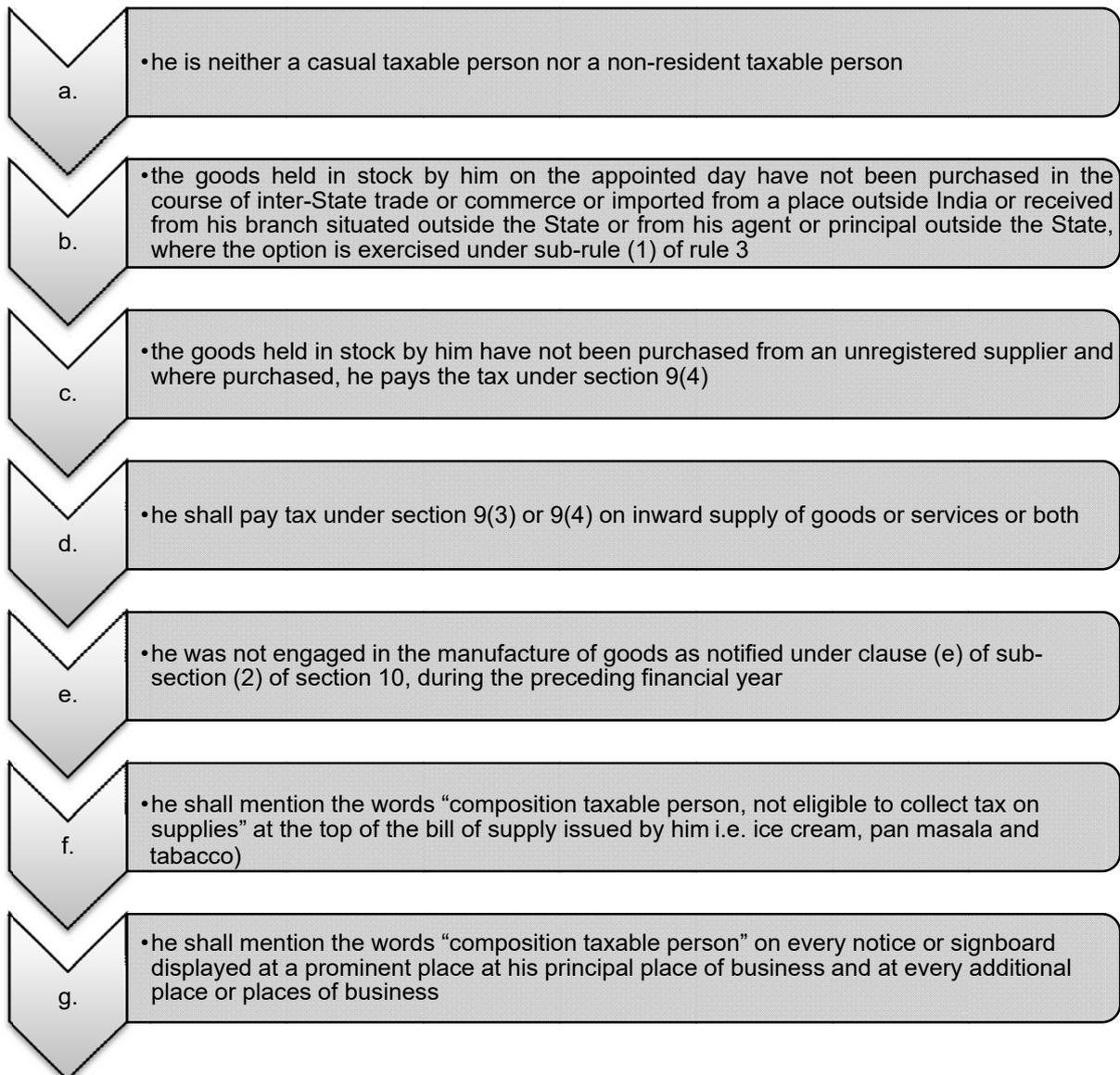
Notes:

1. GST liability wouldn't exist if he opts for composition levy and the trader can now charge the full amount which he was charging inclusive of GST earlier
2. For normal levy, the GST included in sales is  $50,00,000 * 5 / 105$
3. The ITC is available in case of normal levy and not composition levy
4. Hence, the taxes (input) are a part of purchase costs and the output is @ 1% of the turnover in case of Composition Levy

Since the book keeping costs are substantially lower in case of composition levy, the profits and cash flows are higher and hence the trader should be advised to switch to Composition Levy.

**Composition Rules [Chapter II, CGST Rules, 2017]**

Chapter II of Central Goods & Services Tax Rules, 2017 specify Composition Rules which lay down the conditions and restrictions of composition levy. The person exercising the option to pay tax under section 10 shall comply with the following conditions, namely :



**Intimation for composition levy [Rule 3]**

(1) Any person who has been granted registration on a provisional basis under clause (b) of sub-rule (1) of rule 24 and who opts to pay tax under section 10, shall electronically file an intimation in FORM GST CMP-01, duly signed or verified through electronic verification code, on the common portal, either directly or through a Facilitation Centre notified by the Commissioner, prior to the appointed day, but not later than thirty days after the said day, or such further period as may be extended by the Commissioner in this behalf:

Provided that where the intimation in FORM GST CMP-01 is filed after the appointed day, the registered person shall not collect any tax from the appointed day but shall issue bill of supply for supplies made after the said day.

(2) Any person who applies for registration under sub-rule (1) of rule 8 may give an option to pay tax under section 10 in Part B of FORM GST REG-01, which shall be considered as an intimation to pay tax under the said section.

(3) Any registered person who opts to pay tax under section 10 shall electronically file an intimation in FORM GST CMP-02, duly signed or verified through electronic verification code, on the common portal, either directly or through a Facilitation Centre notified by the Commissioner, prior to the commencement of the financial year for which the option to pay tax under the aforesaid section is exercised and shall furnish the statement in FORM GST ITC-03 in accordance with the provisions of sub-rule (4) of rule 44 within a period of (60) sixty days from the commencement of the relevant financial year.

(3A) Notwithstanding anything contained in sub-rules (1), (2) and (3), a person who has been granted registration on a provisional basis under rule 24 or who has been granted certificate of registration under sub-rule (1) of rule 10 may opt to pay tax under section 10 with effect from the first day of the month immediately succeeding the month in which he files an intimation in FORM GST CMP-02, on the common portal either directly or through a Facilitation Centre notified by the Commissioner, on or before the 31st day of March, 2018, and shall furnish the statement in FORM GST ITC-03 in accordance with the provisions of sub-rule (4) of rule 44 within a period of one hundred and eighty days from the day on which such person commences to pay tax under section 10:

Provided that the said persons shall not be allowed to furnish the declaration in FORM GST TRAN-1 after the statement in FORM GST ITC-03 has been furnished.

(4) Any person who files an intimation under sub-rule (1) to pay tax under section 10 shall furnish the details of stock, including the inward supply of goods received from unregistered persons, held by him on the day preceding the date from which he opts to pay tax under the said section, electronically, in FORM GST CMP-03, on the common portal, either directly or through a Facilitation Centre notified by the Commissioner, within a period of 180 days from the date on which the option for composition levy is exercised or within such further period as may be extended by the Commissioner in this behalf.

(5) Any intimation under sub-rule (1) or sub-rule (3) or sub-rule (3A) in respect of any place of business in any State or Union territory shall be deemed to be an intimation in respect of all other places of business registered on the same Permanent Account Number.

**Effective date for composition levy [Rule 4]**

(1) The option to pay tax under section 10 shall be effective from the beginning of the financial year, where the intimation is filed under sub-rule (3) of rule 3 and the appointed day where the intimation is filed under sub-rule (1) of the said rule.

(2) The intimation under sub-rule (2) of rule 3, shall be considered only after the grant of registration to the applicant and his option to pay tax under section 10 shall be effective from the date fixed under sub-rule (2) or (3) of rule 10.

**Validity of composition levy [Rule 6]**

(1) The option exercised by a registered person to pay tax under section 10 shall remain valid so long as he satisfies all the conditions mentioned in the said section and under these rules.

(2) The person referred to in sub-rule (1) shall be liable to pay tax under sub-section (1) of section 9 from the day he ceases to satisfy any of the conditions mentioned in section 10 or the provisions of this Chapter and shall issue tax invoice for every taxable supply made thereafter and he shall also file an intimation for withdrawal from the scheme in FORM GST CMP-04 within seven days of the occurrence of such event.

(3) The registered person who intends to withdraw from the composition scheme shall, before the date of such withdrawal, file an application in FORM GST CMP04, duly signed or verified through electronic verification code, electronically on the common portal.

(4) Where the proper officer has reasons to believe that the registered person was not eligible to pay tax under section 10 or has contravened the provisions of the Act or provisions of this Chapter, he may issue a notice to such person in FORM GST CMP-05 to show cause within fifteen days of the receipt of such notice as to why the option to pay tax under section 10 shall not be denied.

(5) Upon receipt of the reply to the show cause notice issued under sub-rule (4) from the registered person in FORM GST CMP-06, the proper officer shall issue an order in FORM GST CMP-07 within a period of thirty days of the receipt of such reply, either accepting the reply, or denying the option to pay tax under section 10 from the date of the option or from the date of the event concerning such contravention, as the case may be.

(6) Every person who has furnished an intimation under sub-rule (2) or filed an application for withdrawal under sub-rule (3) or a person in respect of whom an order of withdrawal of option has been passed in FORM GST CMP-07 under subrule (5), may electronically furnish at the common portal, either directly or through a Facilitation Centre notified by the Commissioner, a statement in FORM GST ITC01 containing details of the stock of inputs and inputs contained in semi-finished or finished goods held in stock by him on the date on which the option is withdrawn or denied, within a period of thirty days from the date from which the option is withdrawn or from the date of the order passed in FORM GST CMP-07, as the case may be.

(7) Any intimation or application for withdrawal under sub-rule (2) or (3) or denial of the option to pay tax under section 10 in accordance with sub-rule (5) in respect of any place of business in any State or Union territory, shall be deemed to be an intimation in respect of all other places of business registered on the same Permanent Account Number.

Chapter II of Central Goods & Services Tax Rules, 2017 specify Composition Rules which lay down the forms to be submitted by a person opting to be a Composition Dealer under Section 10 of the Act. The following is the list of forms specified in relation to a Composition Dealer.

S. No.	Form No.	Description	Due date
1.	GST CMP-01	Intimation to pay tax under section 10 (Only for persons registered under the existing law migrating on the appointed day)	Prior to appointed date or within 30 days of the appointed date or such further period as may be extended by the Commissioner in this behalf.
2.	GST CMP-02	Intimation to pay tax under section 10 (For persons registered under the Act)	Prior to commencement of financial year for which the scheme is opted for
3.	GST CMP-03	Intimation of details of stock and inward supplies from unregistered person	Within 90 days of exercise of option

4.	GST CMP-04	Intimation/Application for withdrawal from composition scheme	Within 7 days of occurrence of event
5.	GST CMP-05	Show cause notice on contravention of rules or act by proper officer	On contravention
6.	GST CMP-06	Reply to the notice to show cause	Within 15 days from service of such Notice
7.	GST CMP-07	Order for acceptance / rejection of reply to show cause notice	Within 30 days

### LIABILITY TO PAY GST

The liability to pay GST would depend on the mechanism the transaction aligns to, as under:

#### a) Forward Charge Mechanism

Forward charge or direct charge is the mechanism where the supplier of goods/services is liable to pay tax. For instance, if a Company Secretary provided a service to his client, the service tax will be payable by the Company Secretary. Here the supplier is registered under GST, he issues a tax invoice, collects the GST and pays it to the Government.

#### b) Reverse Charge Mechanism

Generally, the supplier of goods or services is liable to pay GST. However, in specified cases like imports and other notified supplies, the liability may be cast on the recipient under the reverse charge mechanism. Reverse Charge means the liability to pay tax is on the recipient of supply of goods or services instead of the supplier of such goods or services in respect of notified categories of supply. Here the supplier is not registered under GST, hence, he cannot issue a tax invoice, and therefore the recipient pays the GST on the supply on behalf of the supplier, directly to the Government.

It must be noted although, that Input Tax Credit can be availed in both the above scenarios, subject to the fulfilment of conditions for availing Input Tax Credit.

In case of E-commerce, the E-commerce operators, who are mandatorily required to register with GST, collect tax at source at a specified percentage and pay the same to the Government.

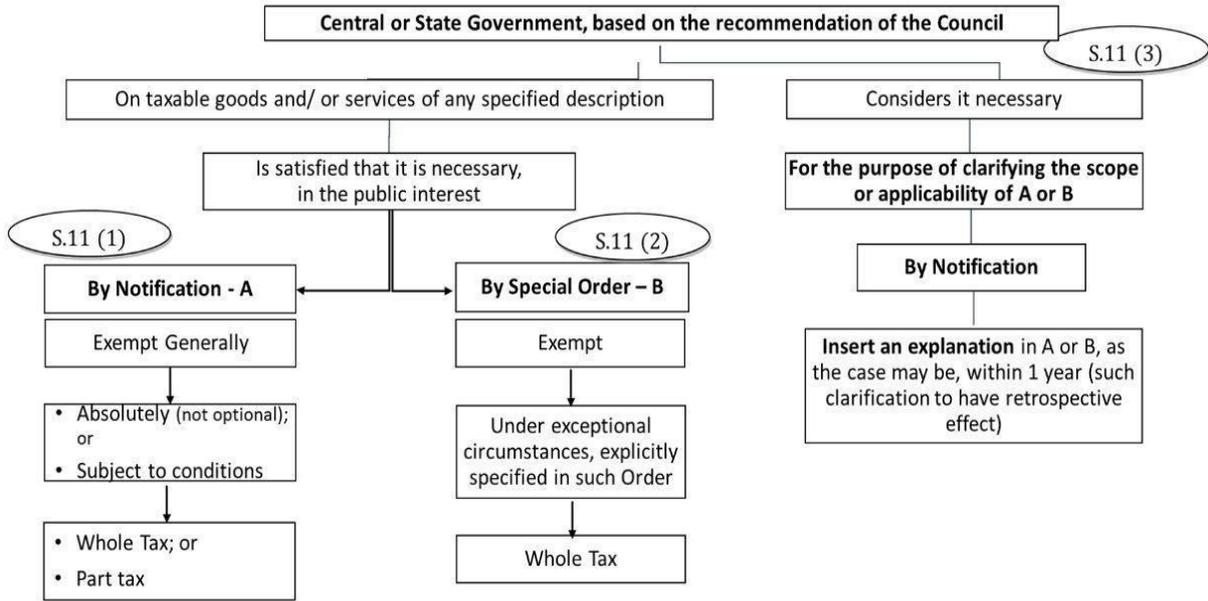
### EXEMPTIONS UNDER GOODS & SERVICES TAX

Governments offer exemptions which are based on goods and services consumed by low income people, people living in disadvantaged regions and so on. Central Government has the power to grant exemption on goods and / or services in the public interest generally or by special order.

General exemption is granted by **notification** and is available to all persons. It may be absolute or conditional. Such exemption may be total or partial.

Specific, also known as ad hoc exemption is granted to persons under circumstances of an exceptional nature by a **special order** communicated to the party seeking exemption. Example: charitable, educational, scientific, research, defence purpose etc.

Central Government also has the power to interpret by an explanation the provisions of the notification or order at a later date but within one year which has retrospective effect.



**Power to grant exemption from tax [Section 11 of CGST Act, 2017]**

(1) Where the Government is satisfied that it is necessary in the public interest so to do, it may, on the recommendations of the Council, by notification, exempt generally, either absolutely or subject to such conditions as may be specified therein, goods or services or both of any specified description from the whole or any part of the tax leviable thereon with effect from such date as may be specified in such notification.

(2) Where the Government is satisfied that it is necessary in the public interest so to do, it may, on the recommendations of the Council, by special order in each case, under circumstances of an exceptional nature to be stated in such order, exempt from payment of tax any goods or services or both on which tax is leviable.

(3) The Government may, if it considers necessary or expedient so to do for the purpose of clarifying the scope or applicability of any notification issued under sub-section (1) or order issued under sub-section (2), insert an explanation in such notification or order, as the case may be, by notification at any time within one year of issue of the notification under sub-section (1) or order under sub-section (2), and every such explanation shall have effect as if it had always been the part of the first such notification or order, as the case may be.

*Explanation.* – For the purposes of this section, where an exemption in respect of any goods or services or both from the whole or part of the tax leviable thereon has been granted absolutely, the registered person supplying such goods or services or both shall not collect the tax, in excess of the effective rate, on such supply of goods or services or both.

**Distinctions between General Exemption and Specific (Special Order) Exemption**

GENERAL EXEMPTION SECTION 11(1)	EXEMPTION BY SPECIAL ORDER SECTION 11(2)
This is granted by a notification	This is granted by a special order
This is goods/ services specific. Any supplier supplying these notified goods or services can enjoy the exemption	This is person specific and purpose specific. The goods are generally chargeable but exempted in special circumstances and hence not available to all persons generally

It may be absolute or conditional. If absolute, the supplier has to avail it and he can collect tax only at effective rates.	No such distinction
It may be partial or total	It is always total

Both the exemptions are granted in the public interest and both can be explained within one year of issue by the government. All the exemptions are based on the recommendations of the GST Council.

Section 6 of the IGST Act, 2017 also contains similar provisions and exemption of IGST is granted on interstate supply.

### Exemptions under GST

Exempt supply has been defined as supply of any goods / services / both, which attract a NIL rate of tax, or which may be wholly exempt from tax, and therefore includes non-taxable supplies.

Essential goods / services, have been exempted, some of the key ones are:

- a) Unbranded atta / besan / maida
- b) Milk
- c) Eggs
- d) Curd
- e) Fresh vegetables
- f) Health care &
- g) Education
- h) Services by the Government (except Post Office, transport of goods / passengers etc.)
- i) Services by RBI
- j) Services by ESIC / EPFO
- k) Services by IRDA, SEBI

### Difference between Nil Rated, Exempt, Zero Rated and Non-GST supplies

Supply Name	Description
Zero Rated	Exports Supplies made to SEZ or SEZ Developers.
Nil Rated	Supplies that have a declared rate of 0% GST. Example: Salt, grains, jaggery etc.
Exempt	Supplies are taxable but do not attract GST and for which ITC cannot be claimed. Example: Fresh milk, Fresh fruits, Curd, Bread etc.
Non-GST	These supplies do not come under the purview of GST law. Example: Alcohol for human consumption, Petrol etc.

**LESSON ROUND UP**

- GST does away with the cascading effects of taxation, by providing a comprehensive and continuous chain of tax credits, end to end and taxing only the value-add at every stage
- India has adopted a dual GST model, i.e., where the tax is imposed concurrently by the Centre and the States. For an intra-state sale, the GST is equally divided between the Centre and the State (CGST + SGST), and for inter-state sales, the GST is collected by the Centre (IGST)
- The exemptions from GST are those that have been kept out of scope and have been notified separately
- The taxable event is supply of goods / services for a consideration, during the course of business / for furtherance of business by a taxable person, and exceptions to this have been set out in the separate schedules
- Key differences between a composite & mixed supply are that the supplies within a composite supply are naturally bundled whereas within a mixed supply are deliberately bundled and that in the composite supply, the principal supply is discernible, whereas that isn't the case in a mixed supply

**SELF TEST QUESTIONS**

**ELABORATIVE QUESTIONS**

- Q1. What is the meaning of Supply under Goods & Services Tax?
- Q2. What constitutes Mixed Supply under Goods & Services Tax?
- Q3. Briefly explain the Composition Scheme under Goods & Services Tax
- Q4. Distinguish between General and Specific Exemptions.

**SUGGESTED READINGS**

1. Goods & Services Tax, Laws, Concepts and Impact Analysis-Bloomsbury – Dr. Sanjiv Agarwal & Sanjeev Malhotra
2. GST Ready Reckoner- Taxmann – V.S. Datey
3. A complete guide to Goods & Services Tax Ready Reckoner in Q & A Format- Bloomsbury – Dr. Sanjiv Agarwal & Sanjeev Malhotra

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# Lesson 13

## Concept of Time, Value and Place of Taxable Supply

### LESSON OUTLINE

- Basic concepts relating to nature of supply of goods and services
- Place of Supply of goods and services
- Provisions relating to Time of supply
- Value of Taxable Supply of goods and services
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

Supply is the taxable event under GST. The scope of supply has been given under Section 7 of the CGST Act, 2017. Taxable event means an event or situation which gives rise to tax liability.

Time of supply signifies the point of levy and value of supply determines value on which GST is payable.

At the end of this lesson, you will be able to learn –

- Various concepts relating to supply of goods and services
- The nature of supply as to intra and interstate
- Place of Supply
- Time of supply and
- Value of supply and the related Rules

## CONCEPT OF SUPPLY

### Nature of Supply [Section 7 to 9 of Integrated Goods & Services Tax Act, 2017]

Goods and Services Tax (GST) envisages two types of supply, intra state and interstate. The following table illustrates the principles to be applied for determining whether a supply is intra state or interstate. Students may note that it is important to know whether a given supply is interstate or intra-state as the tax or taxes payable are different in each case. For example, IGST is payable for interstate supply and CGST+SGST is payable for intra-state supply.

Section 7 of the IGST Act deals with the situations where a supply is categorized as inter-state supply. Such situations are tabulated as under –

Transaction Type	Goods	Services	Nature of supply
<b>Domestic</b>			
Supply of goods and/ or services where location of the supplier and the place of supply are in	two different States; two different Union territories; or a State and a Union territory		Interstate
<b>Imports</b>			
Supply of Imported goods till they cross the customs frontiers of India [For ex. High Sea Sales]			Interstate
Supply of service imported into the territory of India			
<b>Exports and other scenarios</b>			
(1) supplier located in India and the place of supply is outside India (2) to or by a Special Economic Zone developer or a Special Economic Zone (SEZ) unit (3) in the taxable territory, not being an intra-State supply and not covered elsewhere in this section			I N T E R S T A T E S U P P L Y

Section 8 of the IGST Act deals with the situations where a supply is categorized as intra-state supply. Such situations are tabulated as under –

Intra State Supply			
Supply of	Goods	Services	Nature of Supply
Where location of the supplier and the place of supply are in	same State or same Union Territory		Intra State

Essentially, if the location of supplier and the place of supply is within the same state, it is an Intra-State supply, and if these are in different states, then that is Inter-State supply.

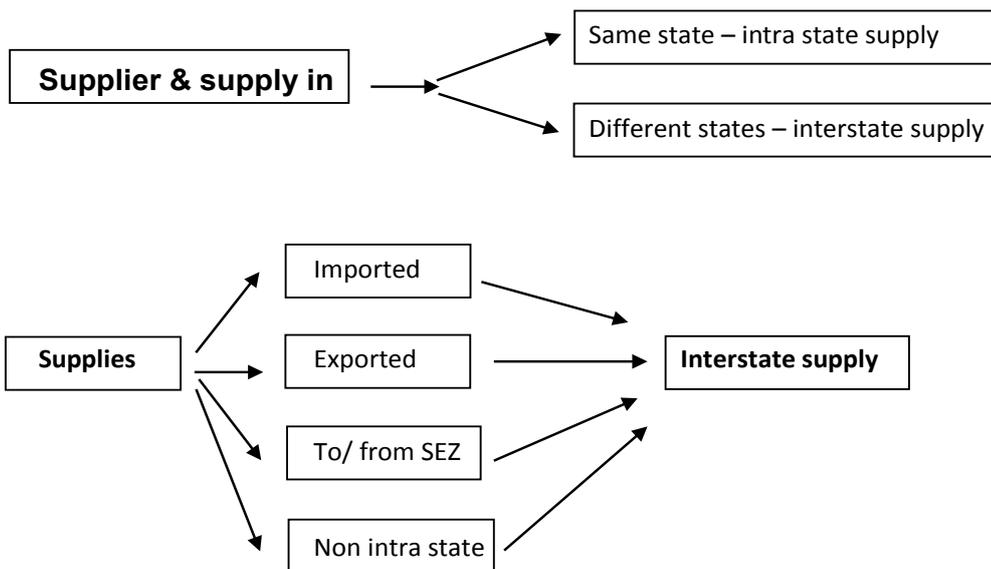
**What is not intra-state supply?**

- (i) Supplies to and by SEZ [even if the location of supplier and recipient are in the same state or union territory]
- (ii) Supply of imported goods till they cross the customs frontiers of India [for example High Sea Sales]
- (iii) Supplies made to a foreign tourist taking the goods out of India

Earlier, purchases made by foreign tourists in India were chargeable to VAT/ CST. Now under GST regime, IGST paid on goods taken out of India by a foreign tourist will be treated at par with exports and tax paid, if any, shall be refunded under the IGST Act, 2017. This practice is to conform to global taxation policies.

The following supplies will be treated as interstate supplies:

- (i) Supplies received in Domestic Tariff Area from SEZ unit located in Noida.
- (ii) Supplies made to SEZ developer in Kandla from Ahmedabad.
- (iii) Goods imported from France
- (iv) Goods sold by the importer located in Noida to a person located in Ludhiana before the bill of entry for clearance from the customs area is filed by the importer.
- (v) Supplier is in Delhi and supply is made in Switzerland
- (vi) Supplier is within Rajasthan and supply is made in Punjab, place of supply being Punjab
- (vii) Supplier is in Chandigarh (UT) and supply is made in Himachal Pradesh



**Supply in Territorial Waters [Section 9 IGST Act, 2017]**

Notwithstanding anything contained in this Act, –

- (a) where the location of the supplier is in the territorial waters, the location of such supplier; or
- (b) where the place of supply is in the territorial waters, the place of supply,

shall, for the purposes of this Act, be deemed to be in the coastal State or Union territory where the nearest point of the appropriate baseline is located.

The expression territorial waters have not been defined under the GST law. It should be understood as the area upto 12 nautical miles from base line of sea coast into the sea.

*Note:* 1 nautical mile = 1.853 Km

If the supplier is in territorial waters, the location of supplier or if the supply is in territorial waters, the place of supplies shall be taken as the coastal state or Union Territory closest to the base line.

*Example 1:* Suppose there is a supply from the territorial waters where the supplier is located and the nearest base line is at Kandla, Gujarat state, then the place of supply is said to be in Gujarat.

*Example 2:* Some goods were supplied to a fishing trawler located in territorial waters near Yanam, a part of Union Territory of Puducherry. Since the nearest base line is at Yanam, place of supply shall be the Union Territory of Puducherry. If the supplier is located in Puducherry, it shall be an intra-state supply. If the supplier is located in Chennai, it is an interstate supply.

**PLACE OF SUPPLY**

As such, the expression 'place of supply' has not been defined in Act, however, the collective reading of various provision makes us understand the purpose and relevance thereof in the GST law. The prime purpose of place of supply is to determine whether a supply is intra-state or inter-state and consequentially to determine whether IGST to be charged or CGST+SGST or UTGST to be charged. It is also relevant for the to determine which state/ Union Territory will get the tax revenue.

**Place of Supply of Goods [Section 10 of IGST Act, 2017]**

Section 10 prescribes the provisions for determining the place of supply of goods in domestic transactions. The five rules, each covering a unique scenario, are as under:

	<b>SITUATION</b>	<b>PLACE OF SUPPLY OF GOODS</b>
A	Supply involves movement of goods	Termination of goods for delivery (Illustration 1)
B	Delivery on the direction of third party	Principal place of business of third party (Illustration 2)
C	Does not involve movement of goods	Location of goods at the time of delivery (Illustration 3)
D	Installation/ assembly	Place of assembly or installation (Illustration 4)
E	Supply on board a conveyance	Location where goods are taken on board (Illustration 5)

Where place of supply cannot be determined, it is determined as per Rules.

**Illustration 1**

Mr. X of Mumbai sells refrigerators to M/s Y of Ahmedabad.

The place of supply would be Gujarat. Since the location of supplier (Maharashtra) and the place of supply

(Gujarat) are in different states, IGST would be charged, being inter-state supply.

### Illustration 2

A having registered place of business at Pune, placed an order on B Ltd. in New Delhi, for delivering a parcel to C who was at Nasik.

In this case, the place of supply would be Maharashtra [for transaction between B Ltd. and A]. Since the location of supplier (New Delhi) and place of supply (Maharashtra) are different, IGST would be charged.

However, the place of supply for a second leg of the transaction i.e. between A and C Ltd. would be determined under Scenario 'A', which shall be Maharashtra, considering that the movement of goods terminates at Nasik. Here, since the location of supplier (Pune/ Maharashtra) and place of supply (Nasik/ Maharashtra) are in the same state, CGST + SGST would be charged.

### Illustration 3

Srinivasan from Bangalore travelled to Chennai for a vacation and purchased a laptop from Croma at Chennai.

In this case, the place of supply would be Tamil Nadu and since the location of supplier and place of supply are same, CGST + SGST would be charged, being an intra-state supply.

### Illustration 4

Surya Narayan from Jamshedpur ordered a machine to be installed in his factory at Jamshedpur. The supplier, from Kolkata, sourced the parts from various states across the country after which the machine was successfully installed at his factory at Jamshedpur.

In this case, the place of supply would be Jamshedpur (Jharkhand). Since the location of the supplier (West Bengal) and the place of supply (Jharkhand) are different, IGST would be charged.

### Illustration 5

Howrah – New Delhi Rajdhani Express supplies food which was taken on board at Mugalsarai in Uttar Pradesh. The place of supply of food for a transaction between the supplier of food and the railways would be Uttar Pradesh.

However, the place of supply of food for a transaction between railways and the passengers would be determined under Section 12 of the IGST Act as such supply would be treated as ancillary to the supply of passenger transportation service.

### Place of supply in case of import/ export [Section 11 of IGST Act, 2017]

In case of import of goods, place of supply is location of importer

In case of export of goods, place of supply is the location outside India.

### Place of supply of services [Section 12 & 13 of IGST Act, 2017]

Section 12: Where both Supplier and Recipient are located in India

SERVICES	PLACE OF SUPPLY	
	Recent is Registered	Recipient is Unregistered
<b>Section 12(2):</b> General Principle	Location of Recipient	location of recipient if address on records exists or location of supplier, in other cases
<b>Section 12(3):</b> Exception/Special cases – a) Directly related to immovable property (b) Lodging accommodation (c) Accommodation for functions (d) Ancillary services to the above	Place of supply would be the location where the immovable property is situated. If the immovable property is located at more than one state, value shall be taken proportionately as per contract or as per Rules.	
<b>Section 12(4):</b> Beauty parlor, fitness, restaurant and catering services plastic cosmetic surgery etc.	Place of performance of service	
<b>Section 12(5):</b> Training & Performance Appraisal	Location of recipient	Location of performance
<b>Section 12(6):</b> Admission to cultural, artistic, sporting, educational, entertainment, amusement event etc. and ancillary services	Place where the event is held or where the park or such place is located	
<b>Section 12(7):</b> (a) Organization of events above including conferences, fair exhibition etc. (b) Ancillary Services, or assigning of sponsorship of such events	Location of such person.	– Location of event – Location of recipient if the event is held outside India
	If the event is held in more than one state or union territory, place of supply shall be determined for respective value assigned to each state or union territory on proportionate basis.	
SERVICES	STATUS OF RECIPIENT	
	Registered	Unregistered
<b>Section 12(8):</b> Transport of goods, including Courier/mail	Location of recipient	Location where goods are handed over for transportation.
	where the transportation of goods is to a place outside India, the place of supply shall be the place of destination of such goods	

<b>Section 12(9):</b> Transportation of passengers	Location of recipient	Place where the passenger embarks on (gets into) the conveyance for a continuous journey.
<b>Section 12(10):</b> On board a conveyance while in transit. Conveyance may be a ship, air craft, train, vehicle etc.	Location of first, scheduled point of departure of that conveyance for the journey.	
<b>Section 12(12):</b> Banking & Financial services and Stock broking services	Location of recipient if address exists on records of supplier or else, location of supplier.	
<b>Section 12(13):</b> Insurance services	Location of recipient	Location of recipient of services as on the records of the supplier.
<b>Section 12(11):</b> Telecommunication services including data transfer, broad casting, cable TV services etc.		
(a) fixed telecom line	Place of fixing/installation	
(b) post paid mobile, internet services	Billing address of recipient	
(c) Prepaid through agent	Address of Agent, place of payment/sale of voucher coupon etc.	
(d) In other cases	Address of recipient as per records. If address is not available, place of supplier of services	
Where leased circuit is installed in more than one state/ union territory, place of supply shall be determined for respective value assigned to each state or union territory on proportionate basis as per contract.		

### Analysis

- Mr. A is a Company Secretary registered at Mumbai and travels to Bangalore for business purpose and stays at a hotel there.  
In this case, the place of supply would be Bangalore/ Karnataka i.e. place of immovable property.
- XYZ Consultants (registered at Bangalore) provides training to its client's employees at Mumbai. The clients are registered at Chennai.  
In this case, if the client (recipient) is registered, the place of supply would be the location of recipient, that is Chennai (Tamil Nadu) and consequently IGST would be charged as the location of Supplier (State of Karnataka) and the Place of Supply (State of Tamil Nadu) are different. (Training & Performance Appraisal Services)
- In the above example, if the client was unregistered, the place of supply would have been Mumbai / Maharashtra and again IGST would be charged. (Training & Performance Appraisal Services)
- Radha is a resident of Mumbai and travelled to Bangalore for a vacation and booked tickets for an event at the water park.  
In this case, the place of supply would be Bangalore/ Karnataka (Admission to events).
- Mr. X based in Ahmedabad, solicits the services of an event management company based in New

Delhi, for his daughter's marriage. They plan for a destination wedding at a palace in Udaipur.

In this case, if Mr. X is registered, the place of supply would be Ahmedabad (Gujarat) and IGST would be charged, but if he is unregistered the place of supply would be Udaipur (Rajasthan) and IGST would be charged.

6. Nagendra Kumar is relocating from Bangalore to Chennai and calls for packers and movers for packing and relocation and shipping of household effects.

In this case the place of supply would be Bangalore (transportation services). Assuming the packers are also from Bangalore, CGST + SGST would be applicable.

7. Tarun books a round trip for AHM – PNQ – BLR – PNQ – AHM, with a stopover at Bangalore. The tickets are booked with a Bangalore based airline.

In this case, this would be treated as a continuous journey with a stopover. For the first leg, the place of supply would be Ahmedabad and since the Location of Supplier (BLR) and the Place of Supply (AHM) are different, IGST would be charged. For the second leg of the journey, the place of supply would be Bangalore, and since the Location of Supplier (BLR) and the place of supply are same, CGST + IGST would be charged. (Passenger Transportation Services).

8. Nikhil, from Kolkata, gets a job at Mumbai and he gets a landline connection done at Mumbai.

In this case, the place of supply would be Mumbai. If he would have taken a post-paid connection, and provided the Billing Address of Kolkata, the place of supply would have been Kolkata.

9. Priya, an unregistered person, from New Delhi, has an account with a Bank at New Delhi. She is on a vacation in Nainital, and visits a bank for getting a Demand Draft made.

In this case, since the address of the recipient will be available in the records of the supplier, the place of supply would be New Delhi.

In case she went to a branch at Nainital for availing currency exchange services which isn't linked to her account in New Delhi, the address of the recipient would not be available in the records of the supplier, and hence the place of supply would be Nainital.

### Section 13 – Where location of supplier or location of recipient is outside India

**Section 13(2) General scenario [where the situation does not fall in any of the cases spelt in Section 13(3) to Section 13(12) - Location of recipient.** However, place of supply shall be the location of supplier, if location of recipient is not available

#### Section 13(3)

- Where, service is in relation to goods required to be made physically available to the supplier - Location of actual performance
- Where, service is in relation to an individual and requires physical presence of such individual – Location of actual performance
- Where the service in relation to goods is provided from a remote location through electronic means – Location where the goods are actually situated.

**Section 13(4) Services in relation to Immovable Property:** Location of such property

**Section 13(5) Admission to/organization of events etc.:** Location of event

**Section 13(6) Services covered under Section 13(3), Section 13(4) and Section 13(5) provided at multiple locations and one or more location falls in taxable territory - Location falling in taxable territory**

**Section 13(7) Multi locations involving more than one State/UT:** Proportional to value in each State/UT

**Section 13(8) Banking, intermediary services and Hiring of means of transport including Yatch but excluding aircraft or vessel -** Location of supplier

**Section 13(9) Goods transport other than mail/courier:** Destination of Goods

**Section 13(10) Passenger transport services:** Location of embarkment

**Section 13(11) Services on board a conveyance:** First scheduled point of departure

**Section 13 (12) on line info, database etc.:** Location of recipient

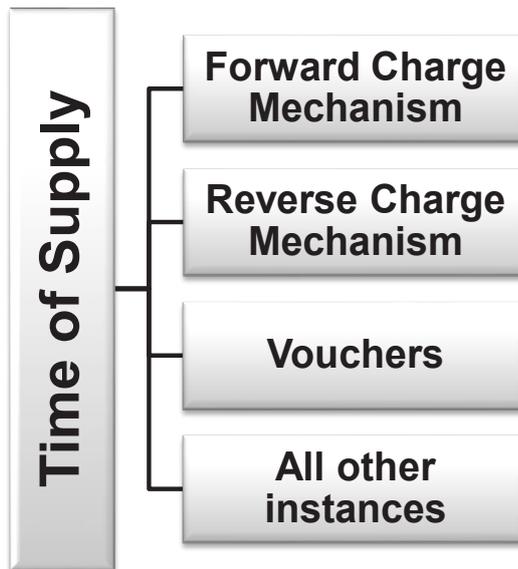
In case of advertisements over internet, the advertisement service shall be deemed to have been provided all over India. Thus, the value of such service will be apportioned amongst all States and UTs, of India. The amount attributable to the value of advertisement service disseminated in a State/UT shall be calculated on the basis of the internet subscribers in such State/UT.

**TIME OF SUPPLY**

**Concept of Time:** Time is the essence of levy. Tax is imposed when the supply is made. Hence it is important to determine the time of supply. Once time of supply is determined, levy is fixed and to be discharged on the due date.

Time of Supply means the point in time when goods have been deemed to be supplied or services have been deemed to be provided. The time of supply enables us to determine the rate of tax, value, and due dates for payment of taxes. Under GST, the liability to pay tax arises at the time of supply. CGST Act, 2017 states provisions to determine time of supply of goods under section 12 and time of supply of services under section 13 of the Act.

The provisions relating to the time of supply of goods and services are broadly centered around the following categories, as explained by the diagram below:



**Time of Supply of Goods [Section 12 of CGST Act, 2017]**

**Forward Charge Mechanism**

The provisions with respect to time of supply of goods under the forward charge mechanism can be depicted as

under, the time of supply would be the earliest of the following dates below, but this must be read in conjunction with the other key points mentioned below:

Date of Issue of Invoice	
Due date for Issue of Invoice	
Date of receipt of payment	

The due date of the invoice can be deciphered from Section 31(1) of the Act which mentions that the Invoice must be issued

- a. On / before the time of removal of the goods, where the supply involves movement of the goods
- b. On / before the delivery of the goods to the recipient, where the supply doesn't involve the movement of the goods
- c. On / before the issuance of the statement of account, in case of a continuous supply of goods
- d. On / before the time of supply subject to a maximum of 6 months from the date of removal, whichever is earlier, where the goods are supplied on "approval for sale / return" basis

The date of receipt of payment would be considered to be the earlier of

- a. Date of credit in the entity's bank account, as reflected in the bank statement
- b. Date on which the payment is recorded in the books of accounts of the supplier

**Note:** Date of receipt of Payment is currently not relevant for determining time of supply in case of goods as Notification No. 66/ 2017-CT dated 15-11-2017 has prescribed the time of supply for goods as specified in section 12(2)(a) of the CGST Act i.e. Date of issue of Invoice or the last date for issuance of invoice as per Section 31 CGST Act.

Section 31(4) of the Act provides that in case of continuous supply of goods, where successive statements of accounts or successive payments are involved, the invoice shall be issued before or at the time each such statement is issued or, as the case may be, each such payment is received.

Further, it has been provided, if there is an excess payment received, up to INR 1000/-; the supplier can choose to take the date of the invoice issued with respect to such excess amount, as the time of supply of goods for such excess value.

### Illustration 6

ABC Ltd. supplied goods to XYZ Ltd., under a contract for the goods to be delivered to the factory of XYZ Ltd. The goods were removed from the factory of ABC Ltd. on 9th September, 2018 and the goods were delivered to the factory of XYZ on 15th September, 2018.

The invoice was issued on 18th September, 2018 and the payment was credited to ABC's a/c on 20th October, 2018 although the entry in the books was made on 19th September, 2018 when the cheque was received.

Please advise on the time of supply.

In the above case, the relevant dates are as under:

- Date of issue of invoice: 18th September, 2018
- Due date for issue of invoice: 9th September, 2018 (as the supply involved movement of goods)
- Date of receipt of payment: 19th September, 2018 (earlier of the entry in the books and the credit in the bank a/c) [Date of payment not relevant in terms of Notification No. 66/2017 - CT dated 15.11.2017]

Hence, the time of supply will be 9th September, 2018.

### Illustration 7

A supplier delivers consignments of bricks on a continuous supply basis to various contractors. With respect to one of the supplies, the following details are available:

Invoice Date	Statement of Account (Due Date)	Receipt of Payment Date	Time of Supply
1st November	5th November	1st November	1st November
11th December	5th December	11th December	5th December
1st January	5th January	1st January	1st January

### Illustration 8

X Ltd. receives payment of INR 100,000 against the invoice value of INR 99,000. Advise the treatment on the excess payment.

In this case, in respect of INR 1000, the time of supply can be taken to be the date of the invoice to be issued in future for the said excess receipt.

### Reverse Charge Mechanism

The time of supply under the “reverse charge mechanism” is the earliest of the following:

- a) Date of receipt of goods
- b) 30 days from the date of invoice
- c) Date of payment, which is the earlier of the date of debit in the bank account as reflected in the bank statement and the date of recording the payment in the books of account, by the recipient

Reverse charge in case of goods may arise either under Section 9(3) or Section 9(4) of the CGST Act. Section 9(3) empowers the issuance of notification by the Government under which the tax will be paid by the recipient of goods as per reverse charge mechanism. Notification no. 4/2017-Central Tax (Rate) dated 28.06.2017 as amended from time to time provides the list of goods which will be subject to reverse charge mechanism subject to the category of supplier and recipient specified therein. These goods include cashew nuts (not shelled or peeled), bidi wrapper leaves (tendu), tobacco leaves, raw cotton, silk yarn, supply of lottery etc.

### Illustration 9

Mr.A, an agriculturist supplies raw cotton (under reverse charge) to Mr. B who manufactures cotton shirts. The date wise turnout of events is given below:

01.04.2019- Mr.B approaches Mr.A and places an order for 1 ton of cotton

## 624 EP-TL

10.05.2019- Mr.B receives the goods

15.05.2019- Mr.A issues an invoice

20.05.2019- Mr.B makes a payment by cheque and accordingly records it in his books of accounts.

25.05.2019- The payment gets debited from Mr.B' s bank account

In this case, the time of supply shall be the earlier of the following dates:

- a. the date of receipt of goods i.e. 10.05.2019
- b. the date of payment as recorded in the books of Mr. B i.e. 20.05.2019 or the date when the payment gets debited in the books of the recipient i.e. 25.05.2019 whichever is earlier
- c. the date immediately following thirty days from the date of issue of invoice, i.e. 15.05.2019 + 30 days + 1day =15.06.2019

Therefore, the time of supply will be 10.05.2019.

### Vouchers

The time of supply vis-à-vis vouchers is determined as under:

- a) Where the supply is identifiable at the time of the issue of the voucher, the date of issue of the voucher would be construed as the time of supply
- b) Where the supply is not identifiable at the time of issue of the voucher, the date of redemption of the voucher would be construed as the time of supply

Vouchers are instruments that can be exchanged as payment for goods / services, of the designated value therein. Hence, per definition, these are instruments, that the potential suppliers, are obliged to accept as consideration in lieu of the goods / services so supplied, in part or full. These vouchers set out clearly, the terms & conditions of use, validity, goods / services covered, identity of the potential suppliers etc.

### Illustration 10

ABC Ltd., enters in to an arrangement with "Hush Puppies", buys the vouchers, these vouchers were issued on 14th December, 2018. The Company then distributes these vouchers with denomination INR 4,000/- to all its employees on 24th December, 2018 valid until 31st January, 2019, so that they can use these vouchers for buying shoes of their choice. The employees make the most of it and redeem these vouchers on the New Year's, i.e., on 1st January, 2019.

In this case, the supply is identifiable at the point of issue of the voucher and hence the time of supply would be construed as 14th December, 2018.

### Illustration 11

Nisha buys a voucher from Shoppers Stop for INR 10,000 and gifts it to Tarun on 14th February. The voucher was valid until 29th February. Tarun redeems the vouchers at the nearby Shoppers Stop store on 29th February.

In this case, the supply was not identifiable at the point of issue of the voucher as Tarun was open to purchase anything from Shoppers' Stop, therefore the time of supply would be construed as the date of redemption of the voucher, that is 29th February.

### All other instances

In all other instances, the time of supply as per Section 12(5) is fixed as under:

- a) Due-date for filing periodic returns or

- b) In other cases, the date of payment of GST

**Time of supply of services [Section 13 of CGST Act, 2017]**

Section 13 covers the time of supply for services, as mentioned above, under Forward Charge Mechanism, Reverse Charge Mechanism, Vouchers and all other instances.

**Forward Charge Mechanism**

- In cases where the invoice has been issued on time, as per Section 31, earlier of the date of invoice and the date of receipt of payment
  - o Date of receipt of payment would be the earlier of the date of credit in the bank account or the date of entry in the books of account, whichever is earlier
- In cases where the invoice has not been issued on time, per Section 31, earlier of the date of provision of service and the date of receipt of payment
  - o Date of receipt of payment would be the earlier of the date of credit in the bank account or the date of entry in the books of account, whichever is earlier

Section 31 mandates that the time limit for issue of invoice is that the invoice must be issued either before the provision of service, or within 30 days from the date of supply of service (45 days for BFSI companies & NBFC's). Additionally, where the supply involves continuous supply of services, the invoice must be issued on / before the due date of payment (where the contract specifies the date) OR on / before the date of actual receipt of payment (where the due date is not ascertainable from the Contract) OR on / before the date of completion of milestone event where the payment is linked to completion of a milestone event.

**Illustration 12**

Determine the time of supply from the following particulars:

15th October	The marriage hall was fixed and the advance of INR 25000 was paid (amount agreed was INR 100,000)
20th October	Invoice issued for INR 25000
30th November	The marriage ceremony took place in the hall
14th December	The invoice was issued for balance INR 75000 indicating & adjusting the advance paid earlier
31st December	The balance payment was received

In the above case, the invoice was issued within the prescribed time (that is within 30 days of the event) and hence the time of supply would be the earlier of:

- a) The date of invoice: which is 14th December and
- b) The date of receipt of payment: which is 31st December

Therefore, for the amount of INR 75000, the time of supply would be 14th December. For the advance of INR 25000, the date of payment precedes the invoice and hence the time of supply for that amount would be 15th October.

As per Section 13(2), if there is an excess payment received, up to INR 1000/-; the supplier can choose to take the date of the invoice issued with respect to such excess amount, as the time of supply of services for such excess value.

**Reverse Charge Mechanism**

The time of supply of services under the reverse charge mechanism would be the earliest of:

- a) 60 days from the date of invoice &

- b) Date of payment, which is the earlier of the date of debit in the bank account as reflected in the bank statement and the date of recording the payment in the books of account, by the recipient

In case of transactions between 'associated enterprises' where the supplier of service is located outside India, the date of recording the supply in the books of the recipient or the date of payment whichever is earlier, will be the time of supply.

### Illustration 13

Mr. A provides legal services as an advocate to Mr. B which fall under reverse charge basis.

10.04.2019 – The services are provided to Mr.B

12.04.2019 – Mr. A issues an invoice to Mr.B

10.07.2019 – The payment is made by Mr.B through a cheque and recorded in his books of accounts

15.07.2019 – The payment gets debited from Mr. B's bank account

In this case, the time of supply shall be earlier of the following dates:

The date of payment i.e. 10.07.2019 (earlier of 10.07.2019 and 15.07.2019)

The date immediately following sixty days from the date of issue of invoice i.e. 12.06.2019 (12.04.2019+60days+1day).

Therefore, the time of supply shall be 12.06.2019.

### Vouchers

The term, "vouchers" has been explained earlier in the chapter. The time of supply of vouchers that are exchangeable for services, is as under:

- a) if the supply is identifiable at the point of issue, the date of issue of voucher
- b) the date of redemption of voucher in all other cases

### All other instances

In all other instances, the time of supply per Section 13(5) is fixed as under:

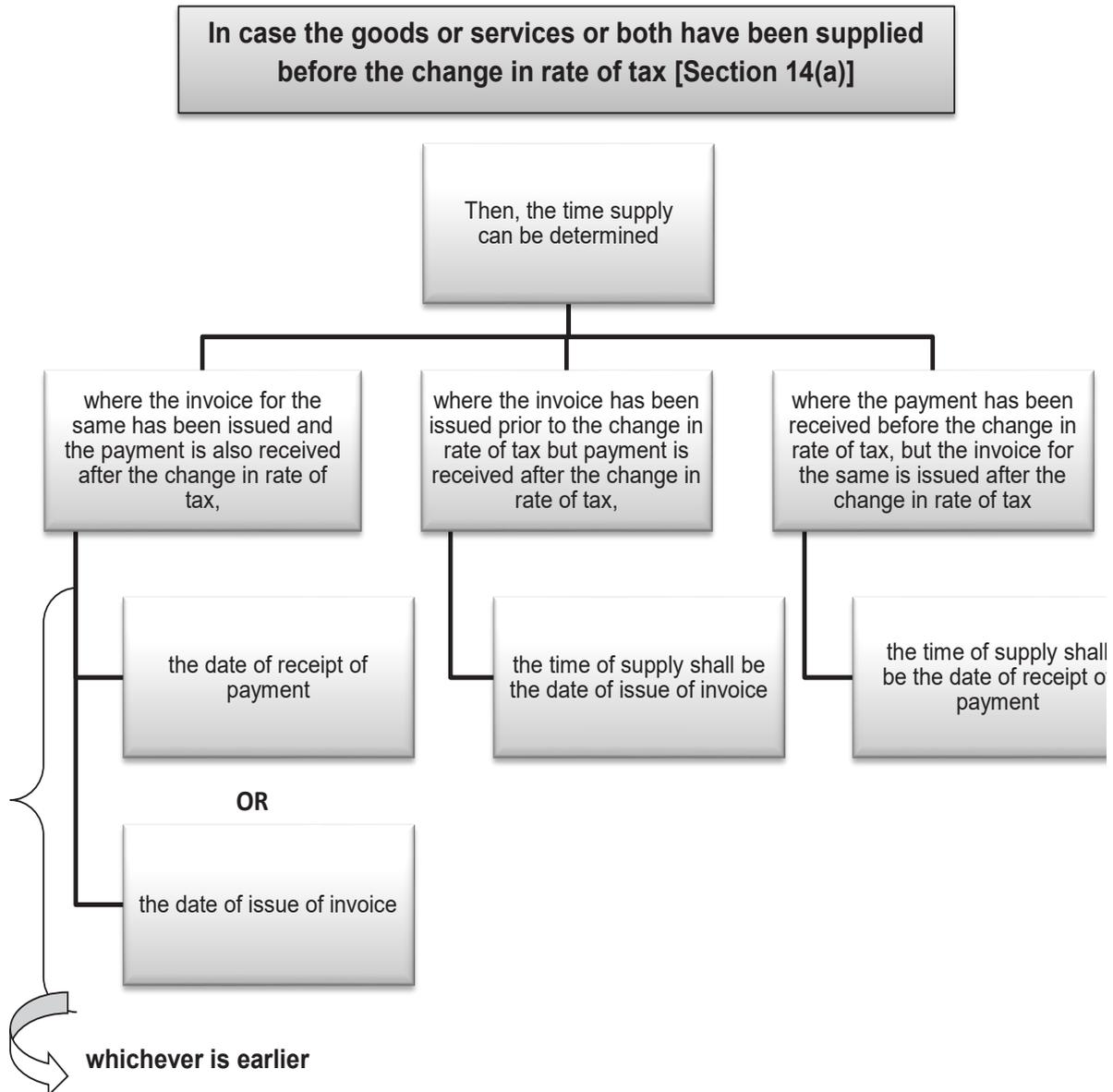
- a) Due-date for filing periodic returns or
- b) In other cases, the date of payment of GST

### Time of Supply in case of change in rate of tax [Section 14 of CGST Act, 2017]

Section 14 of the CGST Act, 2017 defines the time of supply, where there is a change in the rate of tax in respect of goods or services or both.

**Section 14(a):** In case the goods or services or both have been supplied before the change in rate of tax, the time of supply can be determined as follows:

- 1) where the invoice for the same has been issued and the payment is also received after the change in rate of tax, the time of supply shall be the date of receipt of payment or the date of issue of invoice, whichever is earlier; or
- 2) where the invoice has been issued prior to the change in rate of tax but payment is received after the change in rate of tax, the time of supply shall be the date of issue of invoice; or
- 3) where the payment has been received before the change in rate of tax, but the invoice for the same is issued after the change in rate of tax, the time of supply shall be the date of receipt of payment.

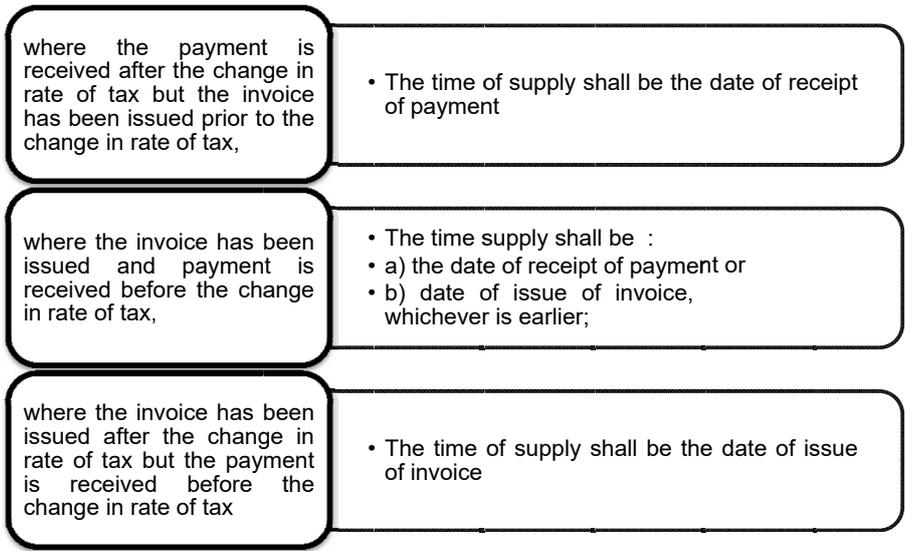


**Section 14(b):** In case the goods or services or both have been supplied after the change in rate of tax, the time of supply can be determined as follows:

- 1) where the payment is received after the change in rate of tax but the invoice has been issued prior to the change in rate of tax, the time of supply shall be the date of receipt of payment; or
- 2) where the invoice has been issued and payment is received before the change in rate of tax, the time of supply shall be the date of receipt of payment or date of issue of invoice, whichever is earlier; or
- 3) where the invoice has been issued after the change in rate of tax but the payment is received before the change in rate of tax, the time of supply shall be the date of issue of invoice:

Provided that the date of receipt of payment shall be the date of credit in the bank account if such credit in the bank account is after four working days from the date of change in the rate of tax.

In case the goods or services or both have been supplied after the change in rate of tax, the time of supply can be determined as follows



**Illustration 14**

Supply was made on 10th May, 2018. From the following particulars, find out the rate of GST applicable.

Event	Date of event	Rate applicable
Change of rate	31st May, 2018	Rate changed from 18% to 12%
Issue of Invoice	5th June, 2018	12%
Payment received	6th July, 2018	12%

Applicable rate is 12%. i.e. which is applicable on earlier of the two events, date of invoice and date of receipt of payment which in this case would be 5th June, 2018.

**Illustration 15**

Supply was made on 10th May, 2018. From the following particulars, find out the rate of GST applicable.

Event	Date of event	Rate applicable
Change of rate	30th June, 2018	Rate changed from 18% to 12%
Issue of Invoice	5th June, 2018	18%
Payment received	6th July, 2018	12%

*Answer:* Applicable rate is 18%. i.e. date of invoice i.e. 5th June, 2018 because it is earlier than the date of receipt of payment.

*Note:* When supply is made before change in rate, the principle of 'whichever is earlier' is followed. Similarly, where supply is made after the change in rate, 'whichever is later' principle is followed.

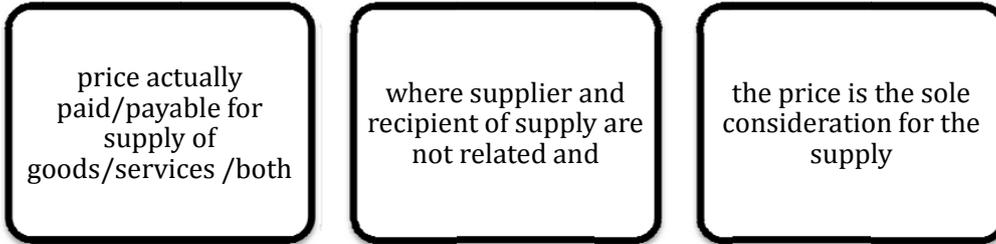
**VALUE OF TAXABLE SUPPLY [SECTION 15 OF CGST ACT, 2017]**

Students must have understood the concept of supply, place of supply and time of supply. Once, it is established that the underlying transaction constitutes supply in terms of Section 7 of the CGST Act, a person is liable to pay tax unless the transaction is exempted. Whether to pay CGST+SGST/UTGST or IGST, is determined by the place of supply. When to pay the tax is determined by the time of supply. Upon reaching this stage, it is essential to know the quantum of tax to be paid. Value of supply and rate of applicable tax are pre-requisites to calculate the tax liability. In this section, we will study the facets of Valuation, transaction value, inclusions and exclusions there from.

Section 15 of the CGST Act when read in conjunction with Chapter IV: Determination of Value of Supply of the CGST rules, states that the value of taxable supply under GST is the transaction value. Transaction value is defined as the price actually paid or payable for the said supply of goods or services or both, where the supplier and the recipient of the supply are not related, and the price is the sole consideration for the supply. [Section 15(1)]

Section 15 is equally applicable to interstate supplies under IGST.

**Transaction value means**



**Inclusions in determination of Value of Supply [Section 15(2)]**

- (a) any taxes, duties, cess, fees and charges levied under any law for the time being in force other than this Act, the State Goods and Services Tax Act, the Union Territory Goods and Services Tax Act and the Goods and Services Tax (Compensation to States) Act, if charged separately by the supplier;
- (b) any amount that the supplier is liable to pay in relation to such supply but which has been incurred by the recipient of the supply and not included in the price actually paid or payable for the goods or services or both;
- (c) incidental expenses, including commission and packing, charged by the supplier to the recipient of a supply and any amount charged for anything done by the supplier in respect of the supply of goods or services or both at the time of, or before delivery of goods or supply of services;
- (d) interest or late fee or penalty for delayed payment of any consideration for any supply; and
- (e) subsidies directly linked to the price excluding subsidies provided by the Central Government and State Governments

**Exclusions in determination of Value of Supply [Section 15(3)]**

- (a) Any discount which is given before or at the time of the supply if such discount has been duly recorded in the invoice issued in respect of such supply; and
- (b) any discount given after the supply has been affected, if –
  - (i) such discount was known and agreed at the time of supply, that is, established in terms of an agreement entered into at or before the time of such supply and specifically linked to relevant invoices; and
  - (ii) input tax credit as is attributable to the discount on the basis of document issued by the supplier has been reversed by the recipient of the supply.

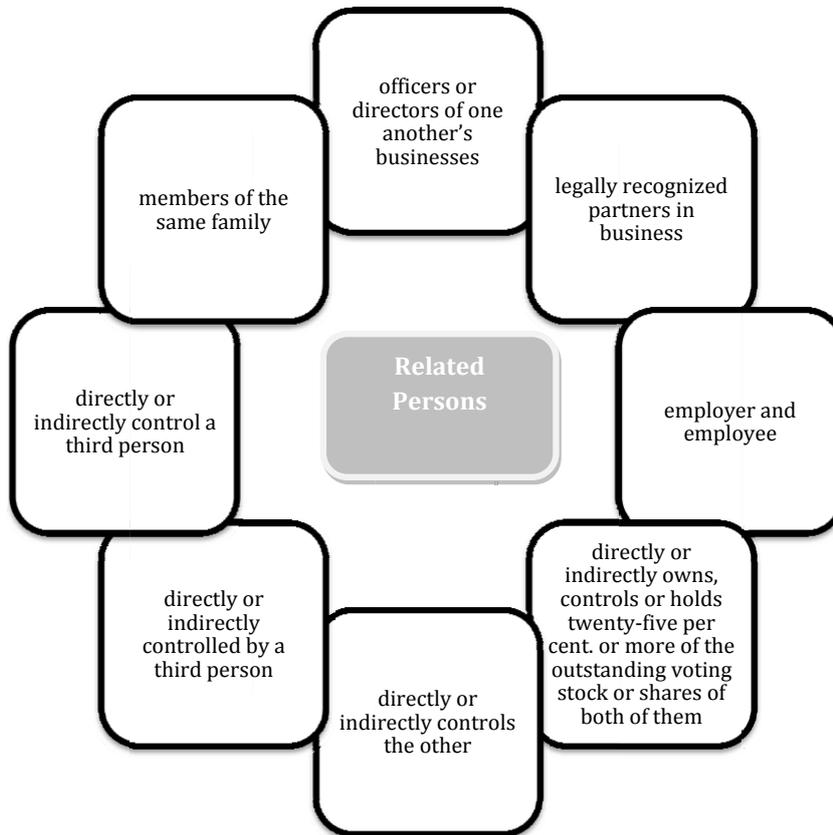
Where the value of the supply of goods or services or both cannot be determined under sub-section (1), the same shall be determined in such manner as may be prescribed. [Section 15(4)]

Notwithstanding anything contained in sub-section (1) or sub-section (4), the value of such supplies as may be notified by the Government on the recommendations of the Council shall be determined in such manner as may be prescribed. [Section 15(5)]

For the purposes of this Act persons shall be deemed to be “related persons” if–

- (i) such persons are officers or directors of one another’s businesses;
- (ii) such persons are legally recognized partners in business;
- (iii) such persons are employer and employee;
- (iv) any person directly or indirectly owns, controls or holds twenty-five per cent. or more of the outstanding voting stock or shares of both of them;
- (v) one of them directly or indirectly controls the other;
- (vi) both of them are directly or indirectly controlled by a third person;
- (vii) together they directly or indirectly control a third person; or
- (viii) they are members of the same family;

The term “person” also includes legal persons and persons who are associated in the business of one another in that one is the sole agent or sole distributor or sole concessionaire, howsoever described, of the other, shall be deemed to be related



**VALUATION RULES : CHAPTER IV, CGST RULES, 2017**

**Rule 27: Value of supply of goods or services where the consideration is not wholly in money**

Where the supply of goods or services is for a consideration not wholly in money, the value of the supply shall–

- (a) be the open market value of such supply;
- (b) if the open market value is not available under clause (a), be the sum total of consideration in money

and any such further amount in money as is equivalent to the consideration not in money, if such amount is known at the time of supply;

- (c) if the value of supply is not determinable under clause (a) or clause (b), be the value of supply of goods or services or both of like kind and quality;
- (d) if the value is not determinable under clause (a) or clause (b) or clause (c), be the sum total of consideration in money and such further amount in money that is equivalent to consideration not in money as determined by the application of rule 30 or rule 31 in that order.

**For example :**

- (1) Where a new phone is supplied for twenty thousand rupees along with the exchange of an old phone and if the price of the new phone without exchange is twenty-four thousand rupees, the open market value of the new phone is twenty-four thousand rupees.
- (2) Where a laptop is supplied for forty thousand rupees along with the barter of a printer that is manufactured by the recipient and the value of the printer known at the time of supply is four thousand rupees but the open market value of the laptop is not known, the value of the supply of the laptop is forty-four thousand rupees.

**Analysis:** Where, the consideration for a supply is not wholly in money [which means there is portion of consideration payable in kind], open market value of the underlying goods or services shall be the value for the purpose of calculating tax liability. However, where, open market value is also not available, then one may monetize the consideration which is in kind and add in the consideration in money to arrive at the value of supply. In case, the methodologies cannot be applied, then, one may find the value of goods or services of like kind or quality and adopt such value. In any of the above methodologies are not applicable, Rule 30 and Rule 31 be applied to arrive at the value of additional consideration not in money to finally arrive at the value of supply.

**Rule 28: Value of supply of goods or services or both between distinct or related persons, other than through an agent**

The value of the supply of goods or services or both between distinct persons as specified in sub-section (4) and (5) of section 25 or where the supplier and recipient are related, other than where the supply is made through an agent, shall

- (a) be the open market value of such supply;
- (b) if the open market value is not available, be the value of supply of goods or services of like kind and quality;
- (c) if the value is not determinable under clause (a) or (b), be the value as determined by the application of rule 30 or rule 31, in that order

Provided that where the goods are intended for further supply as such by the recipient, the value shall, at the option of the supplier, be an amount equivalent to ninety percent of the price charged for the supply of goods of like kind and quality by the recipient to his customer not being a related person:

Provided further that where the recipient is eligible for full input tax credit, the value declared in the invoice shall be deemed to be the open market value of the goods or services.

**Analysis:** Where the supplier and recipient are related or distinct, the statute book refuses to accept the transaction value as there is every possibility of collusion to reduce the value. Thus, Rule 28 provides for adoption of open market value of the same supply or if not available, open market value of the goods of like kind and quality. Where the recipient intends to make further supply of goods or services, the provision permits the supplier to value the goods at 90% of the price intended to be charged by the recipient while making further supply. It is also provided that where the recipient is eligible to avail full input tax credit, the value, whatever, is declared by the supplier, shall be accepted as the correct value.

**Rule 29: Value of supply of goods made or received through an agent**

The value of supply of goods between the principal and his agent shall

- (a) be the open market value of the goods being supplied, or at the option of the supplier, be ninety percent. of the price charged for the supply of goods of like kind and quality by the recipient to his customer not being a related person, where the goods are intended for further supply by the said recipient.

**For example:** A principal supplies groundnut to his agent and the agent is supplying groundnuts of like kind and quality in subsequent supplies at a price of five thousand rupees per quintal on the day of the supply. Another independent supplier is supplying groundnuts of like kind and quality to the said agent at the price of four thousand five hundred and fifty rupees per quintal. The value of the supply made by the principal shall be four thousand five hundred and fifty rupees per quintal or where he exercises the option, the value shall be 90 per cent of five thousand rupees i.e., four thousand five hundred rupees per quintal.

- (b) where the value of a supply is not determinable under clause (a), the same shall be determined by the application of rule 30 or rule 31 in that order.

**Rule 30: Value of supply of goods or services or both based on cost**

Where the value of a supply of goods or services or both is not determinable by any of the preceding rules of this Chapter, the value shall be one hundred and ten percent of the cost of production or manufacture or the cost of acquisition of such goods or the cost of provision of such services.

**Rule 31: Residual method for determination of value of supply of goods or services or both**

Where the value of supply of goods or services or both cannot be determined under rules 27 to 30, the same shall be determined using reasonable means consistent with the principles and the general provisions of section 15 and the provisions of this Chapter:

Provided that in the case of supply of services, the supplier may opt for this rule, ignoring rule 30.

**Rule 31A: Value of supply in case of lottery, betting, gambling and horse racing**

(1) Notwithstanding anything contained in the provisions of this Chapter, the value in respect of supplies specified below shall be determined in the manner provided hereinafter.

(2) (a) The value of supply of lottery run by State Governments shall be deemed to be 100/112 of the face value of ticket or of the price as notified in the Official Gazette by the organising State, whichever is higher.

(b) The value of supply of lottery authorised by State Governments shall be deemed to be 100/128 of the face value of ticket or of the price as notified in the Official Gazette by the organising State, whichever is higher.

*Explanation:* – For the purposes of this sub-rule, the expressions-

- (a) “lottery run by State Governments” means a lottery not allowed to be sold in any State other than the organizing State;
- (b) “lottery authorised by State Governments” means a lottery which is authorised to be sold in State(s) other than the organising State also; and
- (c) “Organising State” has the same meaning as assigned to it in clause (f) of sub-rule (1) of rule 2 of the Lotteries (Regulation) Rules, 2010.

(3) The value of supply of actionable claim in the form of chance to win in betting, gambling or horse racing in a race club shall be 100% of the face value of the bet or the amount paid into the totalisator.

**Rule 32: Determination of value in respect of certain supplies**

- (1) Notwithstanding anything contained in the provisions of this Chapter, the value in respect of supplies specified below shall, at the option of the supplier, be determined in the manner provided hereinafter
- (2) The value of supply of services in relation to the purchase or sale of foreign currency, including money changing, shall be determined by the supplier of services in the following manner, namely: -
  - (a) for a currency, when exchanged from, or to, Indian Rupees, the value shall be equal to the difference in the buying rate or the selling rate, as the case may be, and the Reserve Bank of India reference rate for that currency at that time, multiplied by the total units of currency:

Provided that in case where the Reserve Bank of India reference rate for a currency is not available, the value shall be one per cent of the gross amount of Indian Rupees provided or received by the person changing the money:

Provided further that in case where neither of the currencies exchanged is Indian Rupees, the value shall be equal to one per cent of the lesser of the two amounts the person changing the money would have received by converting any of the two currencies into Indian Rupee on that day at the reference rate provided by the Reserve Bank of India.

Provided also that a person supplying the services may exercise the option to ascertain the value in terms of clause (b) for a financial year and such option shall not be withdrawn during the remaining part of that financial year.

- (b) at the option of the supplier of services, the value in relation to the supply of foreign currency, including money changing, shall be deemed to be
    - (i) one per cent. of the gross amount of currency exchanged for an amount up to one lakh rupees, subject to a minimum amount of two hundred and fifty rupees;
    - (ii) one thousand rupees and half of a per cent of the gross amount of currency exchanged for an amount exceeding one lakh rupees and up to ten lakh rupees; and
    - (iii) five thousand and five hundred rupees and one tenth of a per cent of the gross amount of currency exchanged for an amount exceeding ten lakh rupees, subject to a maximum amount of sixty thousand rupees.
- (3) The value of the supply of services in relation to booking of tickets for travel by air provided by an air travel agent shall be deemed to be an amount calculated at the rate of five percent of the basic fare in the case of domestic bookings, and at the rate of ten per cent of the basic fare in the case of international bookings of passage for travel by air.

*Explanation.* - For the purposes of this sub-rule, the expression "basic fare" means that part of the air fare on which commission is normally paid to the air travel agent by the airlines.

- (4) The value of supply of services in relation to life insurance business shall be, -
  - (a) the gross premium charged from a policy holder reduced by the amount allocated for investment, or savings on behalf of the policy holder, if such an amount is intimated to the policy holder at the time of supply of service;
  - (b) in case of single premium annuity policies other than (a), ten per cent. of single premium charged from the policy holder; or
  - (c) in all other cases, twenty-five per cent. of the premium charged from the policy holder in the first year and twelve and a half per cent. of the premium charged from the policy holder in subsequent years:

Provided that nothing contained in this sub-rule shall apply where the entire premium paid by the policy holder is only towards the risk cover in life insurance

- (5) Where a taxable supply is provided by a person dealing in buying and selling of second hand goods i.e., used goods as such or after such minor processing which does not change the nature of the goods and where no input tax credit has been availed on the purchase of such goods, the value of supply shall be the difference between the selling price and the purchase price and where the value of such supply is negative, it shall be ignored:

Provided that the purchase value of goods repossessed from a defaulting borrower, who is not registered, for the purpose of recovery of a loan or debt shall be deemed to be the purchase price of such goods by the defaulting borrower reduced by five percentage points for every quarter or part thereof, between the date of purchase and the date of disposal by the person making such repossession.

- (6) The value of a token, or a voucher, or a coupon, or a stamp (other than postage stamp) which is redeemable against a supply of goods or services or both shall be equal to the money value of the goods or services or both redeemable against such token, voucher, coupon, or stamp.
- (7) The value of taxable services provided by such class of service providers as may be notified by the Government, on the recommendations of the Council, as referred to in paragraph 2 of Schedule I of the said Act between distinct persons as referred to in section 25, where input tax credit is available, shall be deemed to be NIL.

### **Rule 33: Value of supply of services in case of pure agent**

Notwithstanding anything contained in the provisions of this Chapter, the expenditure or costs incurred by a supplier as a pure agent of the recipient of supply shall be excluded from the value of supply, if all the following conditions are satisfied, namely, -

- (i) the supplier acts as a pure agent of the recipient of the supply, when he makes the payment to the third party on authorization by such recipient;
- (ii) the payment made by the pure agent on behalf of the recipient of supply has been separately indicated in the invoice issued by the pure agent to the recipient of service; and
- (iii) the supplies procured by the pure agent from the third party as a pure agent of the recipient of supply are in addition to the services he supplies on his own account.

*Explanation.* - For the purposes of this rule, the expression "pure agent" means a person who

- (a) enters into a contractual agreement with the recipient of supply to act as his pure agent to incur expenditure or costs in the course of supply of goods or services or both;
- (b) neither intends to hold nor holds any title to the goods or services or both so procured or supplied as pure agent of the recipient of supply;
- (c) does not use for his own interest such goods or services so procured; and
- (d) receives only the actual amount incurred to procure such goods or services in addition to the amount received for supply he provides on his own account.

**For example:** Corporate services Firm A is engaged to handle the legal work pertaining to the incorporation of Company B. Other than its service fees, A also recovers from B, registration fee and approval fee for the name of the company paid to the Registrar of Companies. The fees charged by the Registrar of Companies for the registration and approval of the name are compulsorily levied on B. A is merely acting as a pure agent in the payment of those fees. Therefore, A's recovery of such expenses is a disbursement and not part of the value of supply made by A to B.

**Rule 34: Rate of exchange of currency, other than Indian rupees, for determination of value**

- (1) The rate of exchange for determination of value of taxable goods shall be the applicable rate of exchange as notified by the Board under section 14 of the Customs Act, 1962 for the date of time of supply of such goods in terms of section 12 of the Act.
- (2) The rate of exchange for determination of value of taxable services shall be the applicable rate of exchange determined as per the generally accepted accounting principles for the date of time of supply of such services in terms of section 13 of the Act.

**Rule 35: Value of supply inclusive of integrated tax, Central tax, State tax, Union territory tax**

Where the value of supply is inclusive of integrated tax or, as the case may be, central tax, State tax, Union territory tax, the tax amount shall be determined in the following manner, namely, –

$$\text{Tax amount} = (\text{Value inclusive of taxes} \times \text{tax rate in \% of IGST or, as the case may be, CGST, SGST or UTGST}) \div (100 + \text{sum of tax rates, as applicable, in \%})$$

*Explanation.* - For the purposes of the provisions of this Chapter, the expressions

- (a) “open market value” of a supply of goods or services or both means the full value in money, excluding the integrated tax, central tax, State tax, Union territory tax and the cess payable by a person in a transaction, where the supplier and the recipient of the supply are not related and the price is the sole consideration, to obtain such supply at the same time when the supply being valued is made;
- (b) “supply of goods or services or both of like kind and quality” means any other supply of goods or services or both made under similar circumstances that, in respect of the characteristics, quality, quantity, functional components, materials, and the reputation of the goods or services or both first mentioned, is the same as, or closely or substantially resembles, that supply of goods or services or both.

**Illustration 16**

Nisha Enterprises had made supplies of INR 750,000 to Tee Kay Services. There was a tax levied by Municipal Authorities on such sale of INR 75,000/-. CGST and SGST chargeable on the supply was 37500/-. Packing charges, not included in the price above amounted to INR 15,000.

Nisha Enterprises received a subsidy of INR 30000/- from an NGO on the sale of such goods, and the price mentioned above is after taking in to account the subsidy.

Discount offered is @ 1% and that’s mentioned on the Invoice.

Determine the Value of Supply.

	Price Charged	7,50,000
Add:	Tax charged by Municipal Authorities	75,000
	Packing Charges	15,000
	Subsidy from NGO	30,000
	Total after all inclusions	8,70,000
Less:	Discount @ 1%	7,500

**Notes**

1. CGST and SGST is not included in the determination of value of supply, rather taxed post determination on the same
2. Subsidy since received from a non-governmental body is added back to determine the value of supply
3. Discount on basic price is an exclusion

### LESSON ROUND UP

- When the location of supplier and the place of supply is within the same state, it is an Intra-State Supply, and if these are in different states, then that is Inter-State supply
- To conform with international standards, IGST paid on goods taken out of India by a foreign tourist will be refunded under IGST Act, 2017
- Place of supply is important to determine the nature of sale (inter-state, intra-state, import or export) and the State where state component of GST will accrue
- Point of taxation means the point in time when goods have been deemed to be supplied or services have been deemed to be provided
- Vouchers are instruments that can be exchanged as payment for goods / services, of the designated value therein
- Section 31 mandates that the time limit for issue of invoice is that the invoice must be issued either before the provision of service, or within 30 days from the date of supply of service (45 days for BFSI companies & NBFCs)
- Section 15 of the CGST Act, 2017 when read in conjunction with Determination of Value of Supply of the CGST rules, states that the value of taxable supply under GST is the transaction value
- The term “person” also includes legal persons and persons who are associated in the business of one another in that one is the sole agent or sole distributor or sole concessionaire, howsoever described, of the other, shall be deemed to be related

### SELF TEST QUESTIONS

#### ELABORATIVE QUESTIONS

1. Explain the relevance of ‘time of supply’ in determining tax liability by a registered person? How do you determine time of supply for services under forward charge and reverse charge mechanism?
2. “Exports and Imports have been categorized as Inter-state supplies in the GST law” Discuss this statement by citing the relevant provisions under IGST Act, 2017.
3. Discuss the treatment of discounts in determining the value of supplies.
4. Define the term “Pure Agent” and discuss the taxability of transactions effected by a person in the capacity as “Pure Agent”
5. Discuss the valuation methodology for transactions effected between related or distinct persons.

### SUGGESTED READINGS

1. Goods & Services Tax, Laws, Concepts and Impact Analysis-Bloomsbury – Dr. Sanjiv Agarwal & Sanjeev Malhotra
2. GST Ready Reckoner- Taxmann – V.S. Datey
3. A complete guide to Goods & Services Tax Ready Reckoner in Q & A Format- Bloomsbury – Dr. Sanjiv Agarwal & Sanjeev Malhotra
4. Students may also visit “<http://cbic.gov.in/>” for regular updates on GST law.





# Lesson 14

## Input Tax Credit and Computation of GST Liability

### LESSON OUTLINE

- Input Tax Credit
- Apportionment of Credit and Blocked Credits
- Goods sent to Job Worker
- Input Service Distributor
- Computation of GST Liability
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

Tax paid for inputs, that is, for inward taxable supplies, is called input tax and the recipient is entitled to the credit of the same, which is called Input Tax Credit (ITC). When a tax at output level is nil, it is called exemption. When a tax at both input and output level is nil, it is called zero tax.

ITC is available on inward supplies and it is available even when goods are sent on job work. Input Service Distributor (ISD) is also allowed to distribute ITC on input services to its other registered units on certain terms and conditions.

At the end of this lesson, you will learn about:

- Input tax credit
- Apportionment of Credit and Blocked Credits
- Goods sent to Job Worker
- Distribution of ITC by ISD
- Computation of GST and matters incidental thereto

## INPUT TAX CREDIT

Taxes paid on inward supply of inputs, capital goods and services are called input taxes. These may be Integrated GST, Central GST, State GST or Union Territory GST. Taxes paid under reverse charge mechanism are also input taxes.

The credit of the above taxes is called input tax credit, that is, the taxes paid on inputs are available as a set off against the taxes payable on outward taxable supplies.

CGST Act, 2017 contains the provisions relating to ITC, its availment, utilization and conditions and restrictions attached therewith.

Definitions of input tax and input tax credit:

**Section 2(62)** “input tax” in relation to a registered person, means the Central tax, State tax, Integrated tax or Union Territory tax charged on any supply of goods or services or both made to him and includes –

- (a) the integrated goods and services tax charged on import of goods;
- (b) the tax payable under the provisions of sub-sections (3) and (4) of section 9;
- (c) the tax payable under the provisions of sub-sections (3) and (4) of section 5 of the Integrated Goods and Services Tax Act;
- (d) the tax payable under the provisions of sub-sections (3) and (4) of section 9 of the respective State Goods and Services Tax Act; or
- (e) the tax payable under the provisions of sub-sections (3) and (4) of section 7 of the Union Territory Goods and Services Tax Act,

but does not include the tax paid under the composition levy;

**Section 2(63)** “input tax credit” means the credit of input tax;

Input Tax Credit (ITC) is considered as a cornerstone of GST. In the previous tax regime, there was non-availability of credit at various points in supply chain, leading to a cascading effect of tax i.e., tax on tax and therefore increasing the cost of goods and services. This flaw has been removed under GST and a seamless flow of credit throughout the value chain is therefore available consequently doing away with the cascading effect of taxes.

To avail the benefit of ITC, it is required that the person availing such benefit is registered under GST. An unregistered person is not eligible to take the benefit of ITC. Section 155, of the CGST Act, 2017 states that where any person claims that he is eligible for input tax credit under this Act, the burden of proving such claim shall lie on such person.

**Section 49(5)** of the CGST Act, 2017 provides for utilization of ITC in Electronic credit ledger for payment of GST.

## ELIGIBILITY AND CONDITIONS FOR TAKING INPUT TAX CREDIT [Section 16]

(1) Every registered person shall,

- subject to such conditions and restrictions as may be prescribed and, in the manner, as specified in section 49,
- be entitled to take credit of input tax charged on,
- any supply of goods or services or both to him,
- which are used or intended to be used in the course or furtherance of his business, and
- the said amount shall be credited to the electronic credit ledger of such person.

(2) Notwithstanding anything contained in this section, no registered person shall be entitled to the credit of any input tax in respect of any supply of goods or services or both to him unless,

- (a) he is in possession of a tax invoice or debit note issued by a supplier registered under this Act, or such other **tax paying documents** as may be prescribed;

ITC can be availed on the basis of any of the following documents:

- i) Invoice issued by the supplier of goods and/or services
- ii) Invoice issued by the recipient receiving goods and/or services from unregistered supplier along with proof of payment of tax, in case of reverse charge
- iii) Debit note issued by the supplier
- iv) Bill of entry or similar document prescribed under the Customs Act, 1962
- v) Revised invoice
- vi) Document issued by the input service distributor

The documents basis which ITC is being taken should contain at least the following details:

- Amount of tax charged
- Description of goods or services
- Total value of supply of goods and/or services
- GSTIN of the supplier and recipient
- Place of supply in case of inter-State supply

The documents basis which ITC is being taken should have all the relevant particulars as prescribed in rule 46 of the CGST Rules.

The documents basis which ITC is being taken should have all the relevant particulars as prescribed in rule 46 of the CGST Rules.

- (b) he has received the goods or services or both.

To be eligible for ITC he must be in possession of a tax invoice or debit note issued by a supplier registered under this Act, or such other tax paying documents and received the goods or services or both.

The registered person need not receive the goods himself. It is sufficient even if the goods are delivered to some other person on his direction.

*Similarly, services may also be provided to a third party by the service provider (supplier) on the direction of the service recipient (registered person). In this case also, though the service recipient (registered person) does not receive the service, by virtue of explanation to section 16(2)(b) it is deemed that the registered person (service recipient) has received the service.*

In other words, service provided to any person on the direction of and on account of the registered person, is deemed to have been received by such registered person. So, ITC will be available to the registered person, on whose direction the services are provided to a third person.

*Explanation.* – For the purposes of this clause, it shall be deemed that the registered person has received the goods or, as the case may be, services –

- (i) where the goods are delivered by the supplier to a recipient or any other person on the direction of such registered person, whether acting as an agent or otherwise, before or during movement of goods, either by way of transfer of documents of title to goods or otherwise;

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- (ii) where the services are provided by the supplier to any person on the direction of and on account of such registered person.
- (c) subject to the provisions of section 41 or 43A, the tax charged in respect of such supply has been actually paid to the Government, either in cash or through utilization of input tax credit admissible in respect of the said supply; and
- (d) he has furnished the return under section 39:

### **ITC in case of goods received in lots or installments:**

Provided that where the goods against an invoice

- are received in lots or installments,
- the registered person shall be entitled to take credit upon receipt of the last lot or installment.

### **Failure to pay tax within stipulated time**

Provided further that where a recipient :

- fails to pay to the supplier of goods or services or both, other than the supplies on which tax is payable on reverse charge basis,
- the amount towards the value of supply along with tax payable thereon
- within a period of one hundred and eighty days from the date of issue of invoice by the supplier,
- an amount equal to the input tax credit availed by the recipient shall be added to his output tax liability, along with interest thereon, in such manner as may be prescribed.

Provided also that the recipient shall be entitled to avail of the credit of input tax on payment made by him of the amount towards the value of supply of goods or services or both along with tax payable thereon.

### **Depreciation claimed on Tax Component, ITC not allowed**

(3) Where the registered person has claimed depreciation on the tax component of the cost of capital goods and plant and machinery under the provisions of the Income-tax Act, 1961, the input tax credit on the said tax component shall not be allowed.

### **Due date to claim ITC**

(4) A registered person shall not be entitled to take input tax credit in respect of any invoice or debit note for supply of goods or services or both after

- the due date of furnishing of the return under section 39 for the month of September following the end of financial year to which such invoice or invoice relating to such debit note pertains or
- furnishing of the relevant annual return

whichever is earlier.

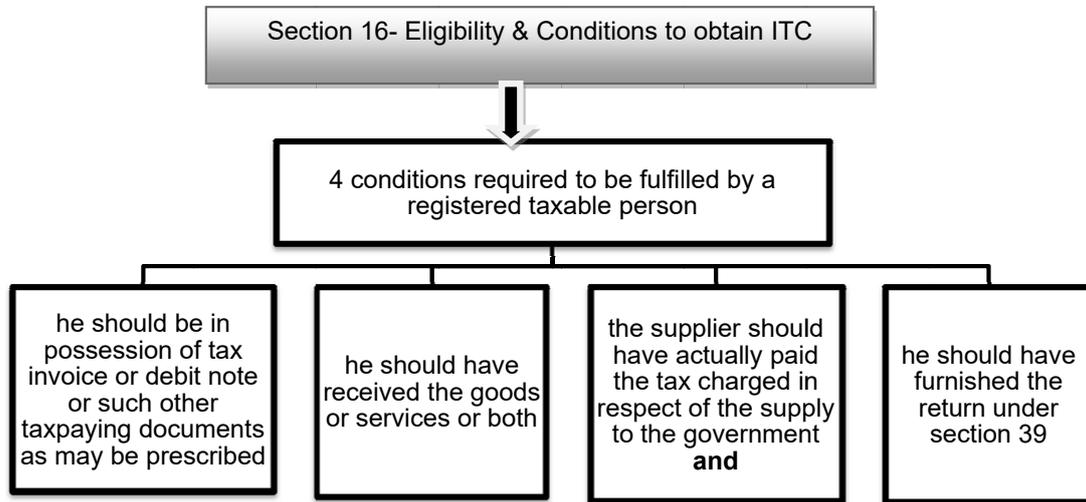
*Provided that the registered person shall be entitled to take input tax credit after the due date of furnishing of the return under section 39 for the month of September, 2018 till the due date of furnishing of the return under the said section for the month of March, 2019 in respect of any invoice or invoice relating to such debit note for supply of goods or services or both made during the financial year 2017-18, the details of which have been uploaded by the supplier under sub-section (1) of section 37 till the due date for furnishing the details under sub-section (1) of said section for the month of March, 2019*

Every registered person is eligible to take credit of GST charged to him for his inward supply of goods/ services if he uses such supplies in the course or furtherance of his business.

Such credit is called input tax credit and the same is to be credited to his electronic credit ledger.

Payment of tax and filing of return is also necessary to claim ITC. However, Section 41 allows ITC on provisional basis.

*Note: In a financial year, the return for September is to be filed by 20th of October under Section 39 of CGST Act, 2017.*



### Illustration 1

Mr. A orders 30000 tonnes of goods which are to be delivered by the supplier via 3 lots of 10000 each. The lots are sent under a single invoice with the first lot and the payment is made by the recipient for Value of Supply plus GST and the supplier has also deposited the tax with the Government.

The 3 lots are supplied in May, June and July 2019. The ITC is available to Mr. A only after the receipt of the 3rd lot. The reason is simple, one of the conditions to avail ITC is the receipt of goods which is completed only after the last lot is delivered.

### Illustration 2

For an Invoice dated 31st July 2019, the same pertains to the financial year 2019-20.

Hence the return for month of September following the end of the financial year to which such invoice relates is due on 20th October, 2020.

Let's say that the annual return is filed on 12th August, 2020.

The ITC therefore needs to be claimed within 12th August, 2020, which is the earlier of the two dates.

### Unmatched credit capped at '20 per cent':

Rule 36(4) has been inserted vide notification 49/2019-CT dated 9 Oct 2019 and it applies to all returns filed after 9 Oct 2019, that is, to Sept returns as well. This sub-rule states that (i) eligible credits appearing in GSTR 2A will be allowed (total credits minus ineligible credits under 17(2), 17(5), etc.) and (ii) additional unmatched ad hoc credit of 20 per cent of the eligible credits.

Experts explain the concern of trade is not entirely wrong but equally forceful are arguments in support of the Government's position in view of the differences in the language of DVAT Act and CGST Act. However, for the present, 120 per cent of eligible credits appearing in GSTR 2A after excluding ineligible credits will be allowed. And any claim of higher amount of credit could come in for scrutiny under section 61 with possibility of demand to reverse such excess amounts.

Restricting credit to only those amounts appearing in GSTR 2A is NOT in the only way to establish condition precedent in section 16(2)(c) and absence from GSTR 2A is NOT an indicator of non-payment of tax by respective supplier. Question remains whether such a rule is an acceptable solution, perhaps not. But the Government seems determined but its enforcement should not be against bona fide claims without allowing for the statutory time under section 37 to pass before taking returns for scrutiny.

### **Apportionment of credit and blocked credits [Section 17]**

Goods and Services Tax aims at providing seamless flow of credit throughout the supply chain.

However, below is a list of few situations as mentioned in section 17 of Central GST Act, 2017 where input tax credit will not be available:

Apportionment of ITC [Sub-sections (1) and (2) of section 17 read with rule 42 and rule 43 of CGST Rules]

(1) Where the goods or services or both are used by the registered person partly for the purpose of any business and partly for other purposes, the amount of credit shall be restricted to so much of the input tax as is attributable to the purposes of his business.

(2) Where the goods or services or both are used by the registered person partly for effecting taxable supplies including zero-rated supplies under this Act or under the Integrated Goods and Services Tax Act and partly for effecting exempt supplies under the said Acts, the amount of credit shall be restricted to so much of the input tax as is attributable to the said taxable supplies including zero-rated supplies

(3) The value of exempt supply under sub-section (2) shall be such as may be prescribed, and shall include supplies on which the recipient is liable to pay tax on reverse charge basis, transactions in securities, sale of land and, subject to clause (b) of paragraph 5 of Schedule II, sale of building.

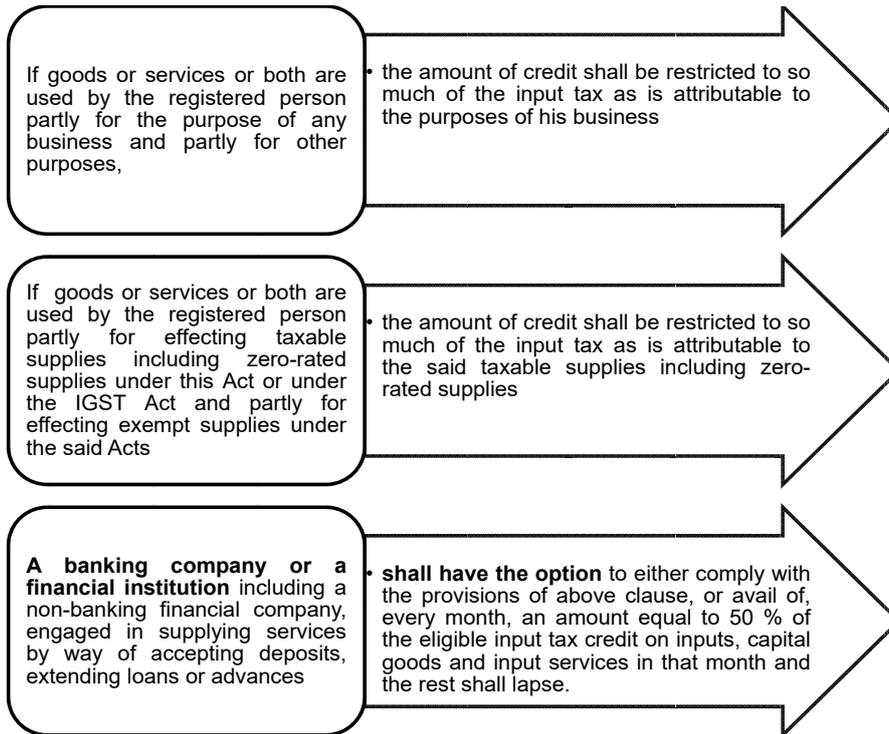
*Explanation.* – For the purposes of this sub-section, the expression “value of exempt supply” shall not include the value of activities or transactions specified in Schedule III, except those specified in paragraph 5 of the said Schedule. i.e. sale of land & sale of building. Therefore, while in all other items of Schedule III, I.T.C. will not be required to be reversed. However, in case of sale of land and building, I.T.C. will need to be reversed.

(4) A banking company or a financial institution including a non-banking financial company, engaged in supplying services by way of accepting deposits, extending loans or advances shall have the option to either comply with the provisions of sub-section (2), or avail of, every month, an amount equal to 50 % of the eligible input tax credit on inputs, capital goods and input services in that month and the rest shall lapse:

Provided that the option once exercised shall not be withdrawn during the remaining part of the financial year:

Provided further that the restriction of 50% shall not apply to the tax paid on supplies made by one registered person to another registered person having the same Permanent Account Number.

Input Tax Credit is available only on those goods and services used for business. Exports and supplies to SEZ fall under the category of zero-rated supplies. ITC is available on zero rated supplies and taxable supplies but not on exempt supplies.



Note :

The value of exempt supply shall be such as may be prescribed, and shall include supplies on which the recipient is liable to pay tax on reverse charge basis, transactions in securities, sale of land and, subject to clause (b) of paragraph 5 of Schedule II, sale of building.

In Point (3), the option once exercised shall not be withdrawn during the remaining part of the financial year.

In Point (3), the restriction of 50% shall not apply to the tax paid on supplies made by one registered person to another registered person having the same Permanent Account Number.

### Illustration 3

Input X is used to produce and supply output Y which is exempt. No ITC is available on input X because it was used for exempt supply.

In the above example if the output Y is exported or supplied to an SEZ unit, ITC is available on Input X as the out-ward supply is zero rated.

### Blocked Credits [Section 17(5)]

Notwithstanding anything contained in sub-section (1) of section 16 and subsection (1) of section 18, input tax credit shall not be available in respect of the following, namely:

- (a) Motor vehicles and other conveyances and related services (insurance, servicing and repair and maintenance)

motor vehicles for transportation of persons having approved seating capacity of not more than thirteen persons (including the driver), **except** when they are used for making the following taxable supplies, namely:—

- (A) further supply of such motor vehicles; or

- (B) transportation of passengers; or
- (C) imparting training on driving such motor vehicles;

(aa) vessels and aircraft **except** when they are used –

- (i) for making the following taxable supplies, namely: –
  - (A) further supply of such vessels or aircraft; or
  - (B) transportation of passengers; or
  - (C) imparting training on navigating such vessels; or
  - (D) imparting training on flying such aircraft;

(ii) for transportation of goods;

(ab) services of general insurance, servicing, repair and maintenance in so far as they relate to motor vehicles, vessels or aircraft referred to in clause (a) or clause (aa):

Provided that the input tax credit in respect of such services shall be available –

- (i) where the motor vehicles, vessels or aircraft referred to in clause (a) or clause (aa) are used for the purposes specified therein;
- (ii) where received by a taxable person engaged –
  - (I) in the manufacture of such motor vehicles, vessels or aircraft; or
  - (II) in the supply of general insurance services in respect of such motor vehicles, vessels or aircraft insured by him;

(b) the following supply of goods or services or both –

**Food & beverages, outdoor catering, health services and other services**

- (i) food and beverages, outdoor catering, beauty treatment, health services, cosmetic and plastic surgery, leasing, renting or hiring of motor vehicles, vessels or aircraft referred to in clause (a) or clause (aa) **except when used for the purposes specified therein, life insurance and health insurance:**

Provided that the input tax credit in respect of such goods or services or both shall be available where an inward supply of such goods or services or both is used by a registered person for making an outward taxable supply of the same category of goods or services or both or as an element of a taxable composite or mixed supply;

- (ii) membership of a club, health and fitness centre; and
- (iii) travel benefits extended to employees on vacation such as leave or home travel concession:

Provided that the input tax credit in respect of such goods or services or both shall be available, where it is obligatory for an employer to provide the same to its employees under any law for the time being in force.

**Works contract services for construction of immovable property [Clause (c) of section 17(5)]**

- (c) works contract services when supplied for construction of an immovable property (**other than plant and machinery**) except where it is an input service for further supply of works contract service;

**Self-construction of immovable property [Clause (d) of section 17(5)]**

- (d) goods or services or both received by a taxable person for construction of an immovable property

**(other than plant or machinery)** on his own account including when such goods or services or both are used in the course or furtherance of business.

*Explanation.* – For the purposes of clauses (c) and (d), the expression “construction” includes reconstruction, renovation, additions or alterations or repairs, to the extent of capitalization, to the said immovable property;

- (e) goods or services or both on which tax has been paid under section 10; (Composition Supply Scheme)
- (f) goods or services or both received by a non-resident taxable person except on goods imported by him;
- (g) goods or services or both used for personal consumption;
- (h) goods lost, stolen, destroyed, written off or disposed of by way of gift or free samples

However, where the activity of distribution of gifts or free samples falls within the scope of “supply” on account of the provisions contained in Schedule I of the said Act, the supplier would be eligible to avail the ITC.

#### **ITC in the hands of the supplier in respect of sales promotional schemes**

*Circular No. 92/11/2019 GST dated 28.03.2019 has clarified the entitlement of ITC in the hands of supplier in respect of various sales promotional schemes as under :*

##### *A. Samples and free gifts*

*Samples which are supplied free of cost, without any consideration, do not qualify as “supply” under GST, except where the activity falls within the ambit of Schedule I of the CGST Act.*

*ITC shall not be available to the supplier on the inputs, input services and capital goods to the extent they are used in relation to the gifts or free samples distributed without any consideration. However, where the activity of distribution of gifts or free samples falls within the scope of “supply” on account of the provisions contained in Schedule I of the said Act, the supplier would be eligible to avail the ITC.*

##### *B. Buy one get one free offer*

*This is not an individual supply of free goods, but a case of two or more individual supplies where a single price is being charged for the entire supply. It can at best be treated as supplying two goods for the price of one.*

*Taxability of such supply will be dependent upon as to whether the supply is a composite supply or a mixed supply and the rate of tax shall be determined as per the provisions of section 8.*

*ITC shall be available to the supplier for the inputs, input services and capital goods used in relation to supply of goods or services or both as part of such offers.*

##### *C. Discounts including ‘Buy more, save more’ offers*

*Discounts offered by the suppliers to customers (including staggered discount under “Buy more, save more” scheme and post supply / volume discounts established before or at the time of supply) shall be excluded to determine the value of supply provided they satisfy the parameters laid down in sub-section (3) of section 15, including the reversal of ITC by the recipient of the supply as is attributable to the discount on the basis of document (s) issued by the supplier.*

*However, the supplier shall be entitled to avail the ITC for such inputs, input services and capital goods used in relation to the supply of goods or services or both on such discounts.*

##### *A. Secondary discounts*

*These are the discounts which are not known at the time of supply or are offered after the supply is already over. Such discounts shall not be excluded while determining the value of supply. There is no impact on availability or otherwise of ITC in the hands of supplier in this case.*

- (i) any tax paid in accordance with the provisions of sections 74, 129 and 130. (Recovery Sections)

Section 17(6) The Government may prescribe the manner in which the credit referred to in sub-sections (1) and (2) may be attributed.

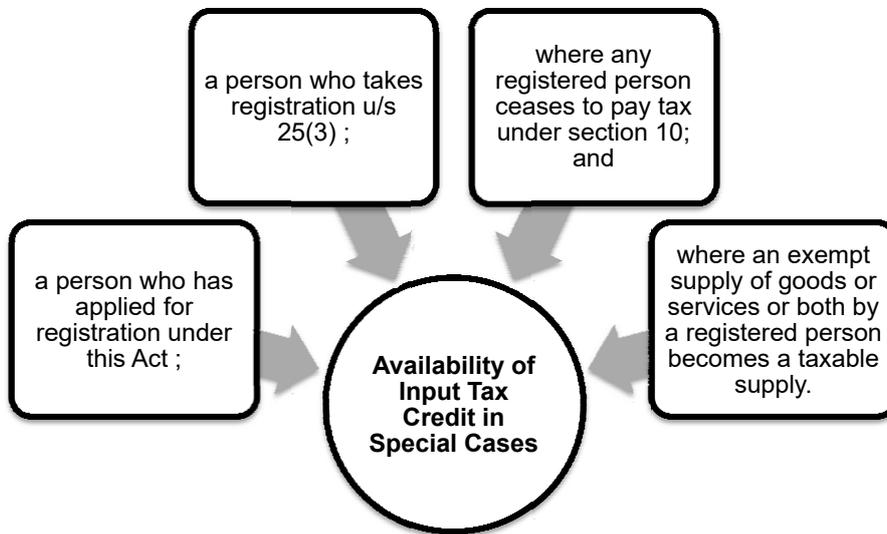
*Explanation.* – For the purposes of this Chapter and Chapter VI, the expression “plant and machinery” means apparatus, equipment, and machinery fixed to earth by foundation or structural support that are used for making outward supply of goods or services or both and includes such foundation and structural supports but excludes

- (i) land, building or any other civil structures;
- (ii) telecommunication towers; and
- (iii) pipelines laid outside the factory premises

*Explanation* – As per section 2(28) of the Motor Vehicles Act, 1988, “motor vehicle” or “vehicle” means any mechanically propelled vehicle adapted for use upon roads whether the power of propulsion is transmitted thereto from an external or internal source and includes a chassis to which a body has not been attached and a trailer; but does not include a vehicle running upon fixed rails or a vehicle of a special type adapted for use only in a factory or in any other enclosed premises or a vehicle having less than four wheels fitted with engine capacity of not exceeding twenty-five cubic centimetres.

**Availability of Input Tax Credit in Special Cases [Section 18]**

This section deals with eligibility of credit in special cases.



(1) Subject to such conditions and restrictions as may be prescribed –

- (a) a person who has applied for registration under this Act within thirty days from the date on which he becomes liable to registration and has been granted such registration shall be entitled to take credit of input tax in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the day immediately preceding the date from which he becomes liable to pay tax under the provisions of this Act;
- (b) a person who takes registration under sub-section (3) of section 25 shall be entitled to take credit of

input tax in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the day immediately preceding the date of grant of registration;

- (c) where any registered person ceases to pay tax under section 10, he shall be entitled to take credit of input tax in respect of inputs held in stock, inputs contained in semi-finished or finished goods held in stock and on capital goods on the day immediately preceding the date from which he becomes liable to pay tax under section 9:

Provided that the credit on capital goods shall be reduced by such percentage points as may be prescribed;

- (d) where an exempt supply of goods or services or both by a registered person becomes a taxable supply, such person shall be entitled to take credit of input tax in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock relating to such exempt supply and on capital goods exclusively used for such exempt supply on the day immediately preceding the date from which such supply becomes taxable:

Provided that the credit on capital goods shall be reduced by such percentage points as may be prescribed.

#### **Time Limit to claim ITC**

(2) A registered person shall not be entitled to take input tax credit under sub-section (1) in respect of any supply of goods or services or both to him after the expiry of one year from the date of issue of tax invoice relating to such supply.

*Note: Here, the maximum time limit for availing ITC is one year. Invoices more than one year old are not eligible for taking credit.*

#### **ITC in case of sale, merger, demerger, amalgamation, lease or transfer of the business**

(3) Where there is a change in the constitution of a registered person on account of sale, merger, demerger, amalgamation, lease or transfer of the business with the specific provisions for transfer of liabilities, or due to the death of the sole proprietor, the said registered person shall be allowed to transfer the input tax credit which remains unutilised in his electronic credit ledger to such sold, merged, demerged, amalgamated, leased or transferred business in such manner as may be prescribed.

#### **Reversal of ITC on switching to composition levy or exit from tax-paying status [Section 18(4) read with rule 44 of CGST Rules]**

(4) Where any registered person who has availed of input tax credit opts to pay tax under section 10 or, where the goods or services or both supplied by him become wholly exempt, he shall pay an amount, by way of debit in the electronic credit ledger or electronic cash ledger, equivalent to the credit of input tax in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock and on capital goods, reduced by such percentage points as may be prescribed, on the day immediately preceding the date of exercising of such option or, as the case may be, the date of such exemption:

Provided that after payment of such amount, the balance of input tax credit, if any, lying in his electronic credit ledger shall lapse.

(5) The amount of credit under sub-section (1) and the amount payable under sub-section (4) shall be calculated in such manner as may be prescribed.

#### **Amount payable on supply of capital goods or plant and machinery on which ITC has been taken [Section 18(6) read with rule 40(2) & rule 44(6) of CGST Rules]**

(6) In case of supply of capital goods or plant and machinery, on which input tax credit has been taken, the registered person shall pay an amount.

**650 EP-TL**

- equal to the input tax credit taken on the said capital goods or plant and machinery reduced by 5% per quarter of a year or part thereof from the date of issue of invoice for such goods [i.e., ITC pertaining to remaining useful life of the capital goods (in quarters)]\* OR
- the tax on the transaction value of such capital goods or plant and machinery determined under section 15,

whichever is higher:

Provided that where refractory bricks, moulds and dies, jigs and fixtures are supplied as scrap, the taxable person may pay tax on the transaction value of such goods determined under section 15.

The table below summarizes the entitlement of Input Tax Credit (ITC):

Case	Persons eligible	Goods entitled as on	Conditions
1.	Person who has applied for registration within 30 days from the date on which he becomes liable to registration, and has been granted such registration	He can claim the ITC on inputs held in the form of Raw Materials / WIP / Finished Goods as on the day immediately preceding the date from which he becomes liable to pay tax	ITC must be availed within 1 year from the date of issue of tax invoice by the supplier
2.	Person who isn't liable to register per se, but obtains voluntary registration	He can claim the ITC on inputs held in the form of Raw Materials/ WIP/ Finished Goods as on the day immediately preceding the date of registration	ITC must be availed within 1 year from the date of issue of tax invoice by the supplier
3.	Registered person who ceases to be under composition levy and switches to the regular scheme	He can claim the ITC on inputs held in the form of Raw Materials/ WIP / Finished Goods & Capital Goods as on the day immediately preceding the date from which he becomes liable to pay tax under the regular scheme	ITC on Capital Goods will be reduced by 5% per quarter of year / part thereof of usage from the date of invoice.
4.	Registered person whose exempt supplies become taxable	He can claim the ITC on inputs held in the form of Raw Materials/WIP/ Finished Goods & Capital Goods relating to such exempt supply as on the day immediately preceding the date from which the supply becomes taxable	ITC on Capital Goods will be reduced by 5% per quarter of year / part thereof of usage from the date of invoice.

**Illustration 4**

Mr. B becomes liable to pay tax on 1st August and has obtained registration on 17th August.

He will hence be entitled to take ITC effective 31st July on inputs (Raw Materials/Finished Goods & Capital Work in Process); except on Capital Goods.

It must be noted that if the application is not made within 30 days, then he will be able to claim ITC effective the date of grant of such registration.

**Illustration 5**

Mr. Z applies for voluntary registration on 1st September and is granted such registration on 9th September. He will hence be entitled to take ITC effective 8th September on inputs (Raw Material/Work in Process/Finished Goods); except on Capital Goods.

**Illustration 6**

Mr. C acquired a Capital Asset on 1st April, 2018 and used it for production of exempt supplies only. Now, in November 2019, his supplies become taxable. The cost of the asset was INR 250,000 and GST 18% was charged on it.

Hence the ITC applicable is INR 250,000\*18%, which is INR 45,000.

Now, number of quarters of usage that have elapsed between April 2018 to November 2019 are: seven.

Hence, there would be a reduction of 5% per quarter for 7 quarters, that is 35%.

Therefore, ITC available would be as under.

Total ITC	45000
Less: Redn for 7 quarters	15750
Net ITC available	29250

Note that this ITC would be available from the date immediately preceding the date from which the supply becomes taxable.

Rule 40(2) of CGST RULES, 2017, states that the amount of credit shall be calculated by reducing the input tax @ 5% for every quarter or part thereof. It shall be calculated from the date of issue of invoice for the capital goods

**Illustration 7**

X Ltd. purchased a machine for Rs. 100,000 and brought it on 1.8.2019 and paid 12% IGST. He availed input tax credit and used the capital goods in his business. On 5.11.2020 he resold it as second-hand machine for 65,000. Find out the amount of tax payable/ ITC reversible in the above case.

Input Tax	12000
Less: 5% per quarter of usage	3600
<b>Net ITC available</b>	<b>8400</b>
Transaction Value	65000
<b>Tax on Transaction Value</b>	<b>7800</b>

Notes:

- 6 quarters have elapsed and therefore 6\*5%, that is 30% would be the reduction for usage
- Tax on Transaction Value @ GST would be computed and compared to the Net ITC available
- The higher of the two would be payable for disposal of Capital Goods
- If the supply is intrastate, it should be payable in two equal parts (4200) to Centre and the concerned State (that is CGST + SGST).
- If it is an interstate supply, Rs. 8,400 is payable as IGST.
- An invoice has to be issued to the recipient with the details of tax amount.

**Transfer of ITC on account of change in constitution of registered person [Section 18(3) read with rule 41 of CGST Rules]**

In case of sale, merger, demerger, amalgamation, transfer or change in ownership of business etc., the ITC that remains unutilized in the electronic credit ledger of the registered person can be transferred to the new entity, provided there is a specific provision for transfer of liabilities in such change of constitution. Circular No. 96/15/2019 GST dated 28.03.2019 has clarified that transfer or change in the ownership of business includes transfer or change in the ownership due to death of the sole proprietor. In the case of demerger, ITC will be apportioned in the ratio of the value of assets of the new units as specified in the demerger scheme. Here, “value of assets” means the value of the entire assets of the business irrespective of whether ITC has been availed thereon or not.

The registered person should furnish the details of change in constitution on the common portal and submit a certificate from practicing Chartered Account/Cost Accountant certifying that the change in constitution has been done with a specific provision for transfer of liabilities. Upon acceptance of such details by the transferee on the common portal, the unutilized ITC gets credited to his electronic credit ledger. The transferee should record the inputs and capital goods so transferred in his books of account.

**Transfer of ITC on obtaining separate registrations for multiple places of business within a State/ Union Territory [Rule 41A of CGST Rules]**

Section 25 enables a taxpayer to obtain separate registrations for multiple places of business in a State/ Union territory. The registered person (transferor), having separate registrations for multiple places of business within a State/Union Territory, can transfer the unutilised ITC (wholly or partly) lying in his electronic credit ledger to any or all of the newly registered place(s) of business in the ratio of the value of assets held by them at the time of registration. Here, the ‘value of assets’ means the value of the entire assets of the business irrespective of whether ITC has been availed thereon or not.

- The registered person should furnish the prescribed details on the common portal within a period of 30 days from obtaining such separate registrations. Upon acceptance of such details by the newly registered person (transferee) on the common portal, the unutilised ITC gets credited to his electronic credit ledger.

## GOODS SENT TO JOB WORKER

A large number of industries depend upon outside support for completing manufacturing activity.

**Section 2(68):** “Job Work” means any treatment or process undertaken by a person on goods belonging to another registered person and the expression “job worker” shall be construed accordingly.

The person who undertakes the job of treatment or process for another person is called job worker. The owner of the goods who engages the job worker is called Principal. Inputs and capital goods can be sent to a job worker and the Principal can avail ITC on them. The goods can be sent directly from the job worker’s place without bringing them to the premises of the Principal.

Inputs should be brought back to the Principal OR alternatively sold from the job worker’s premises on behalf of the Principal:

- within one year in case of normal goods
- and within 3 years in case of capital goods

The period of 1 year and 3 years may, on sufficient cause being shown, be extended by the commissioner for a further period not exceeding 1 year and 2 years respectively.

If the goods are not sold / brought back within the stipulated time, the supply between the Principal and the job worker is treated as “deemed supply” and tax is payable thereon by the Principal.

Moulds and dies, jigs and fixtures, or tools sent out to a job worker for job work need not be brought within 3 years’ time (Capital Goods excludes moulds and dies, jigs and fixtures, or tools.)

Section 143 of CGST Act, 2017 states that a Principal under intimation and subject to such conditions as may be prescribed can send inputs or capital goods to a job worker without payment of tax for further process or treatment and from there subsequently to another job worker(s) and shall either bring back such inputs/capital goods after completion of job work or otherwise, within 1 year/3 years of their being sent out, or supply such inputs/capital goods after completion of job work or otherwise within 1 year / 3 years of their being sent out, from the place of business of a job worker on payment of tax within India or with or without payment of tax for export.

Provided that the principal shall not supply the goods from the place of business of a job worker in accordance with the provisions of this clause unless the said principal declares the place of business of the job worker as his additional place of business except in a case –

- (i) where the job worker is registered under section 25; or
- (ii) where the principal is engaged in the supply of such goods as may be notified by the Commissioner.

“Provided further that the period of one year and three years may, on sufficient cause being shown, be extended by the Commissioner for a further period not exceeding one year and two years respectively.”

The responsibility for keeping proper accounts for the inputs or capital goods shall lie with the Principal.

Any waste and scrap generated during the job work may be supplied by the job worker directly from his place of business on payment of tax, if such job worker is registered, or by the Principal, if the job worker is not registered.

For the purposes of job work, input includes intermediate goods arising from any treatment or process carried out on the inputs by the Principal or the job worker.

### **Taking ITC in respect of inputs and capital goods sent for job work [Section 19]**

Section 19 of the CGST Act, 2017 states that the Principal shall, subject to such conditions and restrictions as may be prescribed, be allowed input tax credit on inputs sent to a job worker for job work.

Although Section 16 of the CGST Act, 2017 specifically states that ITC will be provided only when goods are actually received, but under Job work this condition is exempted and ITC can be availed even if inputs or capital goods are directly sent to the job worker without being first brought to the place of business of Principal.

Taking ITC in respect of inputs and capital goods sent on job work:

- (1) The Principal shall, subject to such conditions and restrictions as may be prescribed, be allowed input tax credit on inputs sent to a job worker for job work.
- (2) Notwithstanding anything contained in clause (b) of sub-section (2) of section 16, the Principal shall be entitled to take credit of input tax on inputs even if the inputs are directly sent to a job worker for job work without being first brought to his place of business.
- (3) Where the normal goods sent for job work are not received back by the principal after completion of job work or otherwise or are not supplied from the place of business of the job worker in accordance with clause (a) or clause (b) of sub-section (1) of section 143 within one year of being sent out, it shall be deemed that such inputs had been supplied by the principal to the job worker on the day when the said inputs were sent out:

***Provided that where the inputs are sent directly to a job worker, the period of one year shall be counted from the date of receipt of inputs by the job worker.***

- (4) The principal shall, subject to such conditions and restrictions as may be prescribed, be allowed input tax credit on capital goods sent to a job worker for job work.
- (5) Notwithstanding anything contained in clause (b) of sub-section (2) of section 16, the principal shall be entitled to take credit of input tax on capital goods even if the capital goods are directly sent to a job worker for job work without being first brought to his place of business.
- (6) Where the capital goods sent for job work are not received back by the principal within a period of three years of being sent out, it shall be deemed that such capital goods had been supplied by the principal to the job worker on the day when the said capital goods were sent out.

Provided that where the capital goods are sent directly to a job worker, the period of three years shall be counted from the date of receipt of capital goods by the job worker.

- (7) Nothing contained in sub-section (3) or sub-section (6) shall apply to moulds and dies, jigs and fixtures, or tools sent out to a job worker for job work.

*Explanation.* –For the purpose of this section, “principal” means the person referred to in section 143.

Essentially, it's imperative to note that the Principal can claim ITC in Inputs / Capital Goods and can send these to the Job Worker for further processing without payment of GST under the cover of a prescribed challan but where these are not either sold by the job worker OR returned by the job worker within 1 Or 3 Years as above, then the supply between them is construed as Deemed Supply and tax with interest has to be discharged by the supplier.

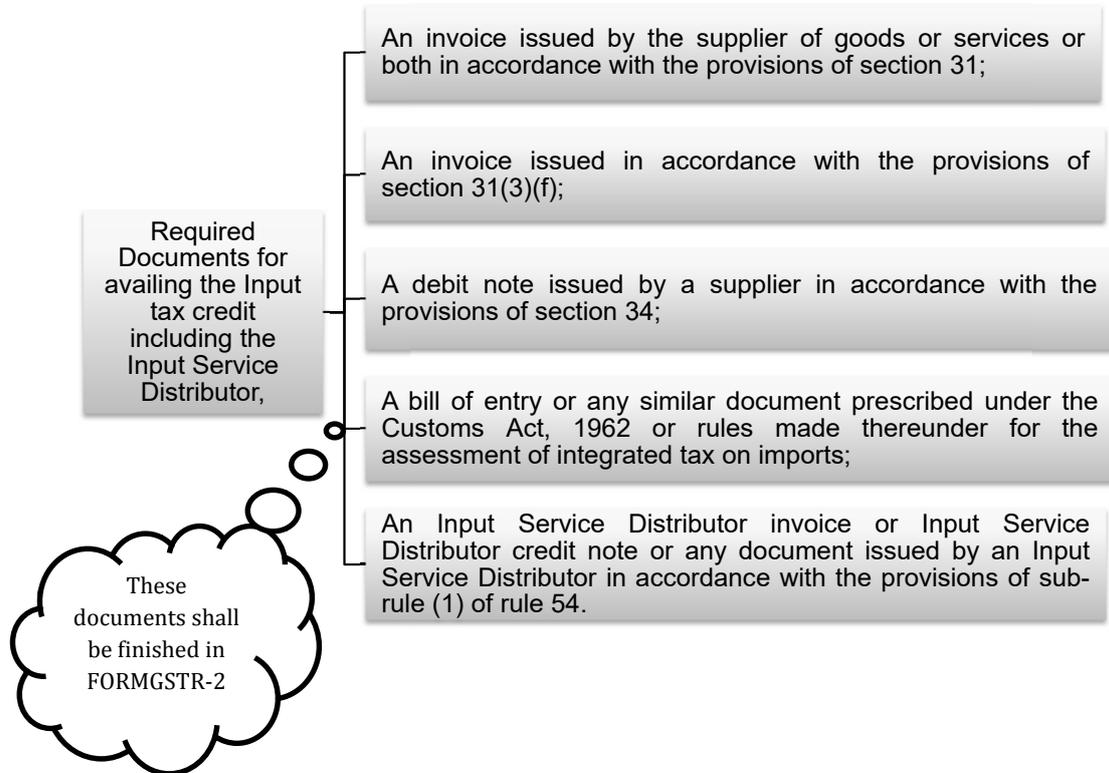
## **Input Tax Credit Rules**

### **Rule 36: Documentary requirements and conditions for claiming input tax credit**

- (1) The input tax credit shall be availed by a registered person, including the Input Service Distributor, on the basis of any of the following documents, namely, -
  - (a) an invoice issued by the supplier of goods or services or both in accordance with the provisions of section 31;
  - (b) an invoice issued in accordance with the provisions of clause (f) of sub-section (3) of section 31, subject to the payment of tax;
  - (c) a debit note issued by a supplier in accordance with the provisions of section 34;
  - (d) a bill of entry or any similar document prescribed under the Customs Act, 1962 or rules made thereunder for the assessment of integrated tax on imports;
  - (e) an Input Service Distributor invoice or Input Service Distributor credit note or any document issued by an Input Service Distributor in accordance with the provisions of sub-rule (1) of rule 54.
- (2) Input tax credit shall be availed by a registered person only if all the applicable particulars as specified in the provisions of Chapter VI are contained in the said document, and the relevant information, as contained in the said document, is furnished in Form GSTR-2 by such person.

Provided that if the said document does not contain all the specified particulars but contains the details of the amount of tax charged, description of goods or services, total value of supply of goods or services or both, GSTIN of the supplier and recipient and place of supply in case of inter-State supply, input tax credit may be availed by such registered person.

- (3) No input tax credit shall be availed by a registered person in respect of any tax that has been paid in pursuance of any order where any demand has been confirmed on account of any fraud, willful misstatement or suppression of facts.



### Illustration 8

ABC Ltd., sends T Shirts to its job workers for fixing the collar, in batches and a batch was sent on 14th July, 2017. The collars were fixed and the T-shirts were sent back to the Principal on 31st May, 2019.

In this case, since the goods were not returned to the Principal by the job worker after completion of the work within one year of it being sent back, the supply between the principal and the job worker would be a deemed supply, and hence tax would be need to be paid along with applicable interest.

Also, in such a case, when the goods are returned by the job worker to the Principal, that again would be construed as a separate supply.

### INPUT SERVICE DISTRIBUTOR

A company may have a number of units and the GST paid by it on input services received can be distributed to the beneficiary units on the basis of their previous year turnover. The office of the company which distributes the credit is called input service distributor.

**Section 2(61):** "Input Service Distributor" means an office of the supplier of goods or services or both which receives tax invoices issued under Section 31 towards the receipt of input services and issues a prescribed document for the purposes of distributing the credit of central tax, State tax, integrated tax or Union territory tax paid on the said services to a supplier of taxable goods or services or both having the same Permanent Account Number as that of the said office

### **Manner of distribution of credit by Input Service Distributor [Section 20]**

(1) The Input Service Distributor shall distribute the credit of central tax as central tax or integrated tax and integrated tax as integrated tax or central tax, by way of issue of a document containing the amount of input tax credit being distributed in such manner as may be prescribed.

(2) The Input Service Distributor may distribute the credit subject to the following conditions, namely: –

- (a) the credit can be distributed to the recipients of credit against a document containing such details as may be prescribed;
- (b) the amount of the credit distributed shall not exceed the amount of credit available for distribution
- (c) the credit of tax paid on input services attributable to a recipient of credit shall be distributed only to that recipient;
- (d) the credit of tax paid on input services attributable to more than one recipient of credit shall be distributed amongst such recipients to whom the input service is attributable and such distribution shall be pro rata on the basis of the turnover in a State or turnover in a Union territory of such recipient, during the relevant period, to the aggregate of the turnover of all such recipients to whom such input service is attributable and which are operational in the current year, during the said relevant period;
- (e) the credit of tax paid on input services attributable to all recipients of credit shall be distributed amongst such recipients and such distribution shall be pro rata on the basis of the turnover in a State or turnover in a Union territory of such recipient, during the relevant period, to the aggregate of the turnover of all recipients and which are operational in the current year, during the said relevant period.

*Explanation.* – For the purposes of this section, – (a) the “relevant period” shall be –

- (i) if the recipients of credit have turnover in their States or Union territories in the financial year preceding the year during which credit is to be distributed, the said financial year; or
- (ii) if some or all recipients of the credit do not have any turnover in their States or Union territories in the financial year preceding the year during which the credit is to be distributed, the last quarter for which details of such turnover of all the recipients are available, previous to the month during which credit is to be distributed;

(b) the expression “recipient of credit” means the supplier of goods or services or both having the same Permanent Account Number as that of the Input Service Distributor;

(c) the term “turnover”, in relation to any registered person engaged in the supply of taxable goods as well as goods not taxable under this Act, means the value of turnover, reduced by the amount of any duty or tax levied under entries 84 and 92A of List I of the Seventh Schedule to the Constitution and entries 51 and 54 of List II of the said Schedule.

### **Manner of distribution of credit by Input Service Distributor [Section 21]**

Where the Input Service Distributor distributes the credit in contravention of the provisions contained in section 20 resulting in excess distribution of credit to one or more recipients of credit, the excess credit so distributed shall be recovered from such recipients along with interest, and the provisions of section 73 or section 74, as the case may be, shall, mutatis mutandis, apply for determination of amount to be recovered.

### **Utilization of ITC**

Input Tax Credit (ITC) is credited to a person’s electronic credit ledger. The person may use this to pay his output tax liability.

**Section 49A****Utilisation of input tax credit subject to certain conditions**

*Notwithstanding anything contained in section 49, the input tax credit on account of central tax, State tax or Union territory tax shall be utilised towards payment of integrated tax, central tax, State tax or Union territory tax, as the case may be, only after the input tax credit available on account of integrated tax has first been utilised fully towards such payment.*

**Section 49B****Order of utilisation of input tax credit**

*Notwithstanding anything contained in this Chapter and subject to the provisions of clause (e) and clause (f) of sub-section (5) of section 49, the Government may, on the recommendations of the Council, prescribe the order and manner of utilisation of the input tax credit on account of integrated tax, central tax, State tax or Union territory tax, as the case may be, towards payment of any such tax.*

**Chapter IX: Payment of Tax of the CGST Rules****Rule 88A: Order of utilization of input tax credit**

*Input tax credit on account of integrated tax shall first be utilised towards payment of integrated tax, and the amount remaining, if any, may be utilised towards the payment of central tax and State tax or Union territory tax, as the case may be, in any order.*

*Provided that the input tax credit on account of central tax, State tax or Union territory tax shall be utilised towards payment of integrated tax, central tax, State tax or Union territory tax, as the case may be, only after the input tax credit available on account of integrated tax has first been utilised fully.*

Order of utilization of input tax credit is as under:

Input tax credit on account of	Output liability on account of Integrated tax	Output liability on account of Central tax	Output liability on account of State tax/ Union Territory tax
Integrated tax	(I)	(II) – In any order and in any proportion	
(III) Input tax credit on account of Integrated tax to be completed exhausted mandatorily			
Central tax	(V)	(IV)	Not permitted
State tax/ Union Territory tax	(VII)	Not permitted	(VI)

Therefore, it is clear that there is no offset available between the CGST and the SGST.

**Illustrations 9**

ABC Ltd. is engaged in the manufacture of electrical appliances and following details are available, advice ITC eligibility of the following :

Item	GST Paid
Electrical Transformers utilized in the manufacturing process	INR 250,000
Trucks used for transporting materials	INR 125,000
Cakes and Pastries for consumption within factory	INR 12,500

**Treatment**

- (1) The ITC on electrical transformers would be fully available as these are used in the course of business/ furtherance of business
- (2) The ITC on trucks used for transporting vehicles would be available as these are used in the course of business/furtherance of business
- (3) ITC on food and beverages is a blocked credit unless the inward taxable supplies are consumed to make outward taxable supplies in the same category whereas the above is for consumption and hence disallowed

**Illustration 10**

Mr. X has procured a machinery for INR 25,00,000 and paid GST of INR 450,000 (18% GST). He has capitalized the invoice value and will claim depreciation of the entire Invoice Value. Please advise on the availability of ITC.

If the depreciation is claimed on the ITC component, ITC cannot be availed and hence Mr. X will not be able to avail ITC in this case.

**Illustration 11**

Mr. B procured stocks worth INR 50,00,000 inclusive of GST but these goods were lost to dacoity, however, he now wants to avail ITC as he has anyways paid the entire Invoice.

ITC can only be availed if the goods / services so availed are consumed to make outward taxable supplies or if they are required during the course of business / furtherance of business. In this case, the goods were lost and hence no ITC can be availed.

**Illustration 12**

Mr. Z, a supplier of goods, pays GST under regular scheme. Mr. Z is an inter-state supplier and hence is not eligible to any threshold exemptions. He has made the following taxable supplies:

<b>Outward Taxable Supplies</b>	
Intra State	12,00,000
Inter State	4,50,000

He has also furnished the following details about his purchases:

<b>Outward Taxable Supplies</b>	
Intra State	4,50,000
Inter State	75,000

He has opening balances of ITC as under :

CGST INR 45,000

SGST INR 45,000

IGST INR 105,000

If the supplies are exclusive of taxes (18% GST), compute his tax liability.

The following represents his tax liability with respect to Outward Taxable Supplies:

Tax Liability		
CGST	SGST	IGST
1,08,000	1,08,000	81,000

The following statement explains his ITC situation:

	Tax Liability		
	CGST	SGST	IGST
For Current Purchases	40,500	40,500	13,500
Opening	45,000	45,000	1,05,000
	85,500	85,500	1,18,500

The following table represents his discharge of liabilities:

	Discharge		
	IGST	CGST	SGST
Liability	81,000	1,08,000	1,08,000
ITC (IGST)	81,000	22,500	15,000
ITC (CGST/SGST)		85,500	85,500
Paid	NIL	NIL	7,500

### Multiple Choice Questions :

Illustration 1: M gave goods for processing by Zebra. While M is registered in GST, Zebra is not registered in GST. Both are at Chennai. The processing is liable for GST @ 5%. The goods were received after processing on 11-07-2019. Entries in the books were made by Mr. M on 12-07-2019. The delivery challan was also received on 11-07-2019. Job work charges amount to ₹ 1,00,000 (without GST). When and how much is the GST liability? And who must pay?

- (a) 11-07-2019; ₹ 5,000 and Zebra must pay
- (b) 12-07-2019; ₹ 1,050; and Zebra must pay
- (c) 11-07-2019; ₹ 5,000 and M must pay
- (d) 12-07-2019; ₹ 2,500 and M must pay

**Answer:**

- (c) 11-07-2019; ₹ 5,000 and M must pay

Illustration 2: R., applied for voluntary registration under CGST Act, 2017 on 5th July, 2018 and the registration was granted on 15th July, 2019. R., was having the stock available against the invoices for a period of 3 months old. R., shall be eligible for input tax credit on such stock as held as on:

- (a) 30th June, 2019      (b) 05th July, 2019
- (c) 15th July, 2019      (d) 14th July, 2019

**Answer:**

- (c) 15th July, 2019

### Computation of GST Liability

Every registered person is required to compute his tax liability on a monthly basis by setting off the Input Tax

Credit(ITC) against the Outward Tax Liability. If there is any balance tax liability the same is required to be paid to the government.

For the **calculation of GST**, the taxpayer should know the **GST** rate applicable to various categories. Example : If a goods or services is sold at Rs. 1,000 and the **GST** rate applicable is 12%, then the net price calculated will be =  $1,000 + (1,000 \times (12/100)) = 1,000 + 120 = \text{Rs } 1,120$

There are 3 ledgers prescribed by the government that is required to be maintained by every tax payer –

### 1. Electronic Liability Ledger

The electronic liability register specified under sub-section (7) of section 49 shall be maintained in FORM GST PMT-01

This ledger records all liabilities of a taxable person including:

- The tax, interest, late fees, or any other amount payable per the return furnished by the taxpayer or per any proceedings
- The tax and interest payable arising out of any mismatch of ITC or output tax liability
- Any interest that may accrue from time to time
- The reversal of ITC or interest

Taxpayers should settle their liabilities in the following order:

- Self-assessed tax and other dues, such as interest, penalty, fees, or any other amount relating to previous tax period returns
- Self-assessed tax and other dues relating to the current tax period return
- Any other amount payable under the act/rules (liability arising out of demand notice, proceedings, etc.)

### 2. Electronic Cash Ledger

The electronic liability register specified under sub-section (7) of section 49 shall be maintained in FORM GST PMT-05

Any amount paid by the taxpayer will be reflected in the electronic cash ledger. The amount available in this ledger may be used for making any payment towards tax, interest, penalty, fees, or any other amount due under the act/rules in the time and manner prescribed. (It is reiterated that any credit in the electronic credit ledger can be utilized only for payment of output tax.)

To initiate a payment, taxpayers should generate a challan online using form GST PMT-06, which will be valid for a period of 15 days. Payment can then be remitted through any of the following modes:

- Internet banking (authorized banks only)
- Credit or debit card (authorized banks only)
- National Electronic Fund Transfer (NEFT) or real-time gross settlement (RTGS) (any bank, authorized or unauthorized)
- Over-the-counter (OTC) payment (authorized banks only) for deposits up to ten thousand rupees per challan and per tax period by cash, cheque or demand draft

The taxpayer is responsible for any commission due on the payment.

The payment date shall be recorded as the date the payment is credited to the appropriate government account.

### 3. Electronic credit ledger

The electronic liability register specified under section 49 shall be maintained in FORM GST PMT-02

Every claim of Input Tax Credit self-assessed by the taxpayer shall be credited to this ledger. The amount available in this ledger may be used for payment towards output tax only. Under no circumstance can an entry be made directly in the electronic credit ledger.

This ledger may include the following:

- ITC on inward supplies from registered taxpayers
- ITC available based on distribution from input services distributor (ISD)
- ITC on input of stock held/semi-finished goods or finished goods held in stock on the day immediately preceding the date on which the taxpayer became liable to pay tax, provided he applies for registration within 30 days of becoming liable
- Permissible ITC on inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the day of conversion from composition scheme to regular tax scheme
- ITC eligible on a payment made on a reverse charge basis.

### LESSON ROUND UP

- Taxes paid on inward supply of inputs, capital goods and services are called input taxes which include Integrated GST, Central GST, State GST or Union Territory GST.
- The credit of these taxes is called input tax credit.
- Under GST, a seamless flow of credit throughout the value chain is available removing the cascading effect of taxes.
- The office of the company which distributes the credit to the beneficiary units on the basis of their previous year turnover is called input service distributor.
- Input tax credit (ITC) is a provision of reducing the tax already paid on inputs, to avoid the cascading effect of taxes.
- It is one of the cutting edge features available under the GST Law, unavailable in previous regime of indirect taxation.
- Certain conditions need to be fulfilled in order to avail the Input Tax Credit.
- Basic condition for availing Input Tax Credit amounts to payment of GST by the supplier.
- When another person (job worker) undertakes the work of a manufacturer, to whom the goods belong (Principal), is known as job work.
- GST law lays down the conditions for ITC in the case of a job worker.
- There is no offset of ITC available between the CGST and the SGST.
- General exemption is granted by notification and is available to all persons which may be absolute or conditional and may be total or partial.
- Specific, also known as ad hoc exemption is granted to persons under circumstances of an exceptional nature by a special order communicated to the party seeking exemption.



# Lesson 15

## Procedural Compliance Under GST

### LESSON OUTLINE

- Registration
- Tax Invoices, Debit & Credit Note
- Accounts and Records
- Electronic way Bills
- Returns
- Payments
- Refunds
- Audit
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

In any tax system, registration is the most fundamental requirement for identification of tax payers ensuring tax compliance in the economy. Without registration, a person can neither collect tax from his customers nor claim any input tax credit of tax paid by him. As India is moving towards digitization, GST has provided an easy and simple way of payment of taxes with three electronic ledgers namely E-cash Ledger, E-credit Ledger & E-liability Ledger. A registered person is required to maintain proper accounts and records and keep it at his registered principal place of business. To facilitate digitisation, there is a facility to maintain accounts and other records in electronic form under GST.

At the end of this lesson, you will be able to learn:

- Registration
- Tax Invoice
- Debit & Credit Note
- Account and Record
- Electronic way Bill
- Return
- Payment of Tax
- Refund Procedures
- Audit

## REGISTRATION

Registration of any business entity under the GST Law implies obtaining a unique number from the concerned tax authorities for the purpose of collecting tax on behalf of the government and to avail Input Tax Credit for the taxes on his inward supplies. Section 22 of Central Goods & Services Tax Act, 2017 mandates that every person who has an aggregate turnover of more than Rs 40 Lacs in the relevant financial year, is liable to be registered under the Act (with effect from 1st April, 2019)

However, where such person makes taxable supplies of goods or services or both from any of the special category States, he shall be liable to be registered if his aggregate turnover in a financial year exceeds Rs 20 lacs.

Note : As per Notification No. 10/2019-Central Tax dated 7th March, 2019 any person, who is engaged in exclusive supply of goods and whose aggregate turnover is more than forty lakh rupees, is liable to be registered under the act.

Aggregate Turnover under the Act includes all taxable supplies, exempt supplies, zero-rated supplies, inter-state supplies, but doesn't include the inward taxable supplies under the Reverse Charge Mechanism. If the person has taxable and exempt supplies as a part of the turnover, example, machine oil and petrol, the turnover from both would be added to determine whether the aggregate exceeds the threshold, and if it does, then registration become mandatory for such supplier. The supplies by the agents on behalf of the principal would be included in the aggregate turnover of both, the principal and the agent. Registration is mandatory at every place of business from wherein a taxable supply has been made.

The registration under GST is Permanent Account Number (PAN) based and state-specific. GST Identification Number (GSTIN) is a 15-digit number and a certificate of registration, incorporating the GSTIN is made available to the applicant upon registration.

- The first two digits of this number will represent the state code
- The next ten digits will be the PAN number of the taxpayer
- The thirteenth digit will be assigned based on the number of registrations within a state
- The fourteenth digit will be Z by default
- The last digit will be for check code

Registration under GST is not tax specific, which means that there is single registration for all the taxes i.e. CGST, SGST/UTGST, IGST and cesses.

### Persons liable for Registration [Section 22]

(1) Every supplier shall be liable to be registered under this Act in the State or Union territory, other than special category States, from where he makes a taxable supply of goods or services or both, if his aggregate turnover in a financial year exceeds forty lakh rupees (Threshold limit for sale of goods is enhanced to Rs. 40 Lacs as per notification No. 10/2019 – Central Tax dated 7th March, 2019) :

Provided that where such person makes taxable supplies of goods or services or both from any of the special category States, he shall be liable to be registered if his aggregate turnover in a financial year exceeds twenty lakh rupees (with effect from 1.04.2019)

(2) Every person who, on the day immediately preceding the appointed day, is registered or holds a licence under an existing law, shall be liable to be registered under this Act with effect from the appointed day.

(3) Where a business carried on by a taxable person registered under this Act is transferred, whether on account of succession or otherwise, to another person as a going concern, the transferee or the successor, as the case may be, shall be liable to be registered with effect from the date of such transfer or succession.

(4) Notwithstanding anything contained in sub-sections (1) and (3), in a case of transfer pursuant to sanction of a scheme or an arrangement for amalgamation or, as the case may be, demerger of two or more companies pursuant to an order of a High Court, Tribunal or otherwise, the transferee shall be liable to be registered, with effect from the date on which the Registrar of Companies issues a certificate of incorporation giving effect to such order of the High Court or Tribunal.

*Explanation.* – For the purposes of this section, –

- (i) the expression “aggregate turnover” shall include all supplies made by the taxable person, whether on his own account or made on behalf of all his principals;
- (ii) the supply of goods, after completion of job work, by a registered job worker shall be treated as the supply of goods by the principal referred to in section 143, and the value of such goods shall not be included in the aggregate turnover of the registered job worker;
- (iii) the expression “special category States” shall mean the States as specified in sub-clause (g) of clause (4) of article 279A of the Constitution [except the State of Jammu and Kashmir] and States of Arunachal Pradesh, Assam, Himachal Pradesh, Meghalaya and Uttarakhand.

### Persons not liable for Registration [Section 23]

(1) The following persons shall not be liable to registration, namely: –

- (a) any person engaged exclusively in the business of supplying goods or services or both that are not liable to tax or wholly exempt from tax under this Act or under the Integrated Goods and Services Tax Act;
- (b) an agriculturist, to the extent of supply of produce out of cultivation of land.

(2) The Government may, on the recommendations of the Council, by notification, specify the category of persons who may be exempted from obtaining registration under this Act.

### Compulsory Registration in certain cases [Section 24]

Notwithstanding anything contained in sub-section (1) of section 22, the following categories of persons shall be required to be registered under this Act,–

- (i) persons making any inter-State taxable supply;
- (ii) casual taxable persons making taxable supply;
- (iii) persons who are required to pay tax under reverse charge;
- (iv) person who are required to pay tax under sub-section (5) of section 9;
- (v) non-resident taxable persons making taxable supply;
- (vi) persons who are required to deduct tax under section 51, whether or not separately registered under this Act;
- (vii) persons who make taxable supply of goods or services or both on behalf of other taxable persons whether as an agent or otherwise;
- (viii) Input Service Distributor, whether or not separately registered under this Act;
- (ix) persons who supply goods or services or both, other than supplies specified under sub-section (5) of section 9, through such electronic commerce operator who is required to collect tax at source under section 52;
- (x) every electronic commerce operator who is required to collect tax at source under section 52;

- (xi) every person supplying online information and database access or retrieval services from a place outside India to a person in India, other than a registered person; and
- (xii) such other person or class of persons as may be notified by the Government on the recommendations of the Council.

### Analysis

In terms of Section 22 (Persons liable for registration) of the CGST Act, 2017 the expression “special category States” shall mean the States as specified in sub-clause (g) of clause (4) of Article 279A of the Constitution except the States of

- 1) Jammu and Kashmir,
- 2) Arunachal Pradesh,
- 3) Assam,
- 4) Himachal Pradesh,
- 5) Meghalaya,
- 6) Sikkim &
- 7) Uttarakhand.

Total 11 special category states are provided under sub-clause (g) of clause (4) of Article 279A of the Constitution which are as below:

- 1) Jammu and Kashmir,
- 2) Arunachal Pradesh,
- 3) Assam,
- 4) Himachal Pradesh,
- 5) Meghalaya,
- 6) Sikkim,
- 7) Uttarakhand,
- 8) Manipur,
- 9) Mizoram,
- 10) Nagaland, and
- 11) Tripura

Therefore, for the purpose of registration under GST laws only 4 States are special category States which are as below:

- 1) Manipur,
- 2) Mizoram,
- 3) Nagaland, and
- 4) Tripura

**Threshold limit for registration for those engaged in exclusive supply of goods enhanced to Rs. 40 lacs vide Notification No. 10/2019 – Central Tax dated 7th March, 2019 except.**

- Persons engaged in making intra-State supplies in the States of
  - 1) Arunachal Pradesh,
  - 2) Manipur,
  - 3) Meghalaya,
  - 4) Mizoram,
  - 5) Nagaland,
  - 6) Puducherry,
  - 7) Sikkim,
  - 8) Telangana,
  - 9) Tripura,
  - 10) Uttarakhand
- Persons required to take compulsory registration under section 24
- Suppliers of
  - Ice cream and other edible ice, whether or not containing cocoa;
  - Pan masala;
  - Tobacco and manufactured tobacco substitutes
- Persons taking voluntary registration under section 25(3)

Threshold limit for registration for service providers would continue to be Rs 20 lakhs and in case of special category States Rs 10 lakhs.

<b>Threshold Limit for Registration for Suppliers of Goods</b>	
<b>Rs. 20 Lacs</b>	<b>Rs. 40 Lacs</b>
1. Arunachal Pradesh 2. Meghalaya 3. Puducherry 4. Sikkim 5. Telangana 6. Uttarakhand 7. Manipur 8. Mizoram 9. Nagaland 10. Tripura	Remaining 21 States and 5 Union Territories.
<b>Notes:</b> 1. For the purpose of GST, Delhi and Puducherry are considered as States. Therefore, there are total 31 States where SGST + CGST is levied and 5 Union Territories where UTGST + CGST is levied on intra-state supplies.	

2. In case of inter-state supply of goods registration is mandatory u/s 24 of the CGST Act but the exemption is granted to person making inter-state taxable supplies of handicraft goods upto an aggregate turnover of Rs. 20 lacs as long as the person has a PAN and the goods move under the cover of an e-way bill, irrespective of the value of the consignment.

#### Threshold Limit for Registration for Suppliers of Services

Rs. 10 Lacs	Rs. 20 Lacs
1. Manipur 2. Mizoram 3. Nagaland 4. Tripura	Remaining 27 States and 5 Union Territories.

#### Notes:

1. Service suppliers are not eligible for exemption limit of Rs. 40 Lacs.
2. All service providers, whether supplying intra-state, inter-state or through e-commerce operator, will be exempt from obtaining GST registration, provided their aggregate turnover doesn't exceed Rs. 20 lacs (Rs. 10 lacs in case of Manipur, Mizoram, Nagaland & Tripura).
3. Mandatory registration is required for only those e-commerce operators who are required to collect tax at source.

#### Threshold Limit for Registration for Suppliers of Ice cream and other edible ice, whether or not containing cocoa; Pan masala; Tobacco and manufactured tobacco substitutes

Rs. 10 Lacs	Rs. 20 Lacs
1. Manipur 2. Mizoram 3. Nagaland 4. Tripura	Remaining 27 States and 5 Union Territories.

#### Notes:

1. These suppliers are also not eligible for exemption limit of Rs. 40 Lacs.
2. Registration is mandatory in case of inter-state supply of these goods.

**Compulsory Registration**

- For a supplier who makes inter-state supplies;
- Casual taxable person ;
- Non-resident taxable person ;
- E-commerce operators ; and
- Persons discharging liabilities under reverse charge mechanism;
- Person who are required to pay tax under sub-section (5) of section 9;
- Persons who are required to deduct tax under section 51, whether or not separately registered under this Act;
- Persons who make taxable supply of goods or services or both on behalf of other taxable persons whether as an agent or otherwise;
- Input Service Distributor;
- Persons who supply goods or services or both, other than supplies specified under sub-section (5) of section 9, through such electronic commerce operator who is required to collect tax at source under section 52;
- Every person supplying online information and database access or retrieval services from a place outside India to a person in India, other than a registered person;
- Any other notified by the Government on the recommendations of the Council

All service providers, whether supplying intra-state, inter-state or through e-commerce operator, will be exempt from obtaining GST registration, provided their aggregate turnover doesn't exceed Rs. 20 lacs (Rs. 10 lacs in case of Manipur, Mizoram, Nagaland & Tripura).

**Persons not liable to register**

- Engaged exclusively in the supply of goods / services / both which are not liable to tax ;
- Engaged exclusively in the supply of goods / services / both which are wholly exempt from tax ;
- Agriculturalist to the extent of supply of produce from land cultivation ; and
- Specified categories as may be notified by the Government.

**Procedure for Registration [Section 25]**

Every person who is liable to register themselves under the CGST Act, 2017 must do so within thirty days from the date when he becomes first liable or five days prior to commencement of business in case of casual / non-resident taxable person.

If the proper officer doesn't take any action within three days of submission of application along with necessary details and documents, or within seven days of receiving the clarifications so solicited, the application for grant of registration is deemed to be approved.

The effective date of registration is:

- In case the application is submitted within 30 days of the person becoming liable to register, it shall be the date on which the person becomes liable
- And if the application is submitted after 30 days of the person becoming liable to register, it shall be the date on which the registration is granted

**Section 2(20)** of Central Goods & Services Tax Act, 2017 defines “casual taxable person” as a person who occasionally undertakes transactions involving supply of goods or services or both in the course or furtherance of business, whether as principal, agent or in any other capacity, in a State or a Union territory where he has no fixed place of business.

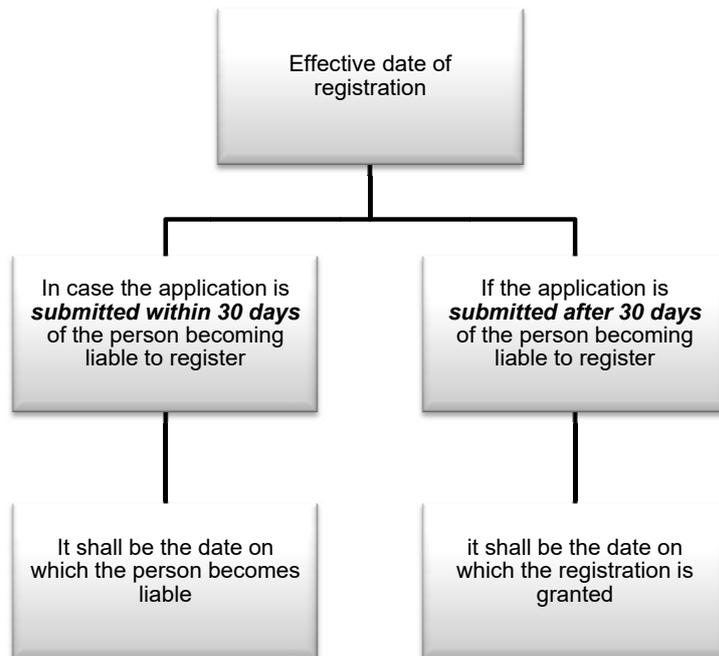
Thus, a casual taxable person is someone who has a business in a different state, but comes to a different state for a business purpose temporarily.

For example, a footwear dealer registered in Agra comes for an exhibition at Azad Maidan, Mumbai for participating in the exhibition, then such person would need to register as a casual taxable person at Mumbai and he will be granted registration for a maximum period of 90 days.

**Section 2(77)** of Central Goods & Services Tax Act, 2017 defines “non-resident taxable person” as any person who occasionally undertakes transactions involving supply of goods or services or both, whether as principal or agent or in any other capacity, but who has no fixed place of business or residence in India.

Hence, a non-resident taxable person is someone who has a business outside India, but comes to a different state for a business purpose temporarily.

For example, a person from Paris, comes to participate in an exhibition at Azad Maidan, Mumbai for participating in the exhibition, then such person would need to register as a non-resident taxable person at Mumbai and he will be granted registration for a maximum period of 90 days.



Ordinarily, a person seeking registration under this Act shall be granted a single registration in a State or Union territory. However, a person having multiple places of business in a State or Union territory may be granted a separate registration for each such place of business.

It may also be noted that a person having a unit in a Special Economic Zone or being a Special Economic Zone developer shall have to apply for a separate registration, as distinct from his place of business located outside the Special Economic Zone in the same State or Union territory.

Where, a person makes a supply from the territorial waters of India, it shall obtain registration in the coastal State or Union territory where the nearest point of the appropriate baseline is located.

**Cancellation or Suspension of Registration [Section 29]**

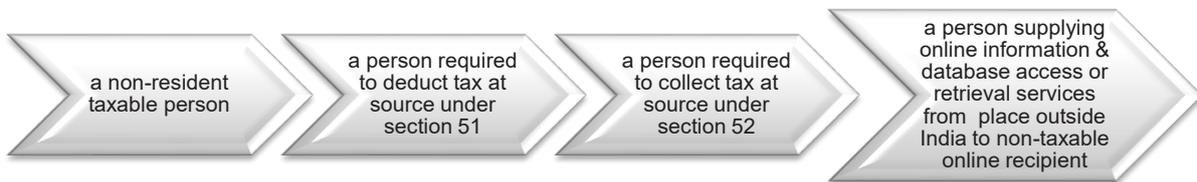
The proper officer may, either himself or on application filed by a registered person, or his legal heirs in case of a death of a registered person, cancel / revoke the registration of such person. This cancellation could be from a prospective / retrospective date as the officer may deem fit. This cancellation would in no way interfere with the liabilities of the said person. A registered person whose registration is cancelled will have to debit the electronic cash ledger or electronic credit ledger, by an amount equal to Input Tax Credit (ITC) so availed or the output tax liability, whichever is higher.

**RULES FOR REGISTRATION [CHAPTER III]**

CHAPTER III of Central Goods & Services Tax Act, 2017 deals with the registration provisions.

**Application for registration [Rule 8]**

Rule 8(1): Every person other than :



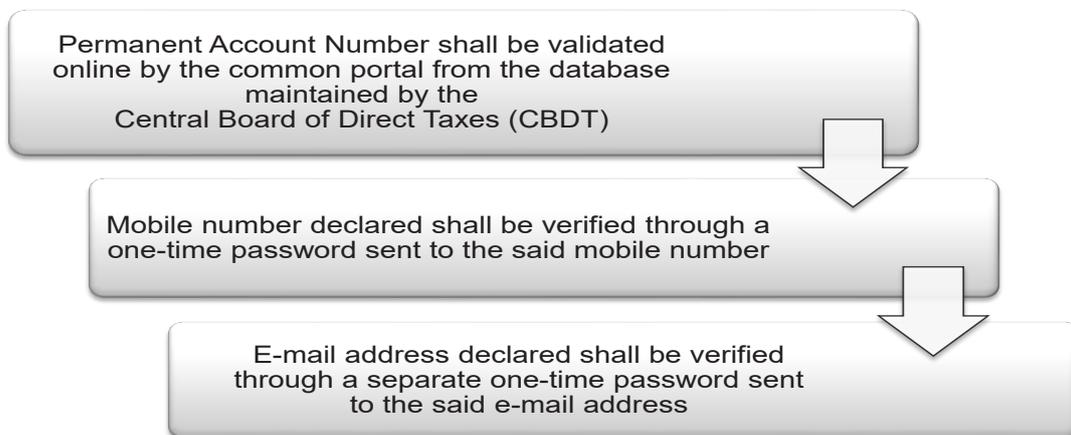
who is liable to be registered under section 25(1) and every person seeking registration under section 25(3) (hereafter in this Chapter referred to as “the applicant”) shall, before applying for registration, declare his:



in Part A of Form GST REG-01 on the common portal, either directly or through a Facilitation Centre notified by the Commissioner.

Every person being an Input Service Distributor shall make a separate application for registration as such Input Service Distributor.

Rule 8(2): It lays down the verification of details entered for registration:



Rule 8(3) lays down that on successful verification of the Permanent Account Number, mobile number and email address, a temporary reference number shall be generated and communicated to the applicant on the said mobile number and e-mail address.

## Rule 8(4)

•Using the reference number generated, the applicant shall electronically submit an application in **Part B of FORM GST REG-01**, duly signed or verified through electronic verification code, along with the documents specified in the said Form at the common portal, either directly or through a Facilitation Centre notified by the Commissioner

## Rule 8(5)

•On receipt of an application, an acknowledgement shall be issued electronically to the applicant in **FORM GST REG-02**

## Rule 8(6)

•A person applying for registration as a casual taxable person shall be given a temporary reference number by the common portal for making advance deposit of tax in accordance with the provisions of section 27 and the acknowledgement under sub-rule (5) shall be issued electronically only after the said deposit

### Verification of the application and approval [Rule 9]

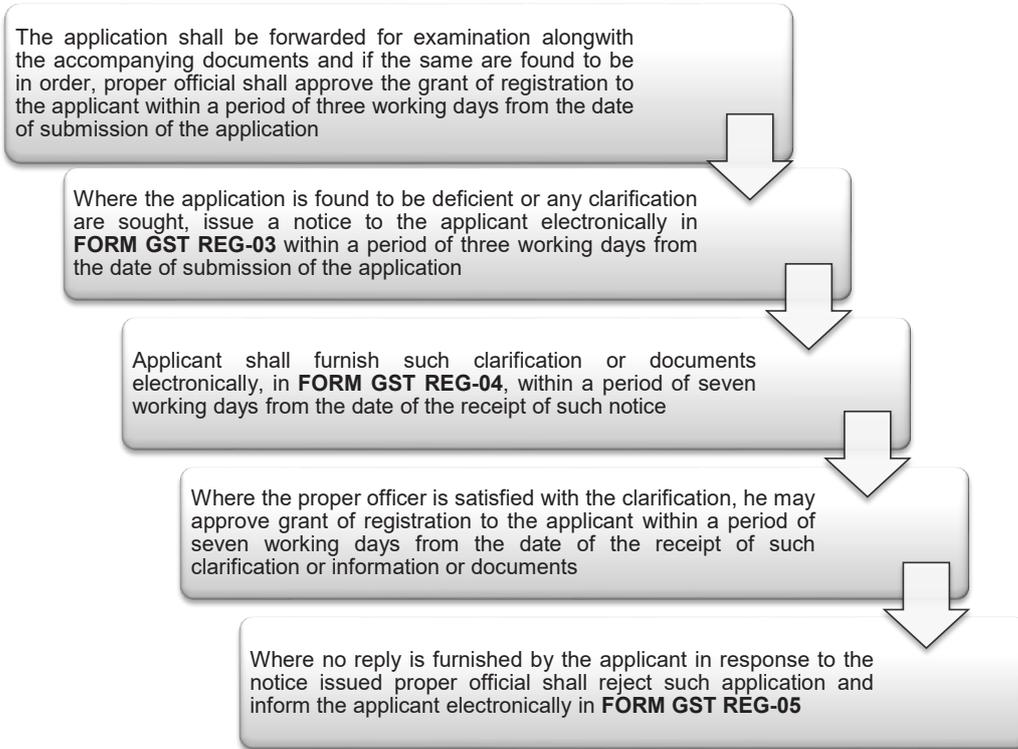
- (1) The application shall be forwarded to the proper officer who shall examine the application and the accompanying documents and if the same are found to be in order, approve the grant of registration to the applicant within three working days from the date of submission of application.
- (2) Where the application submitted under rule 8 is found to be deficient, either in terms of any information or any document required to be furnished under the said rule, or where the proper officer requires any clarification with regard to any information provided in the application or documents furnished therewith, he may issue a notice to the applicant electronically in FORM GST REG-03 within three working days from the date of submission of application and the applicant shall furnish such clarification, information or documents sought electronically, in FORM GST REG-04, within seven working days from the date of receipt of such intimation.

*Explanation.* – For the purposes of this sub-rule, the expression —“clarification” includes modification or correction of particulars declared in the application for registration, other than Permanent Account Number, State, mobile number and e-mail address declared in Part A of FORM GST REG-01.

- (3) Where the proper officer is satisfied with the clarification, information or documents furnished by the applicant, he may approve the grant of registration to the applicant within seven working days from the date of receipt of such clarification or information or documents.
- (4) Where no reply is furnished by the applicant in response to the notice issued under sub-rule (2) within the prescribed period or where the proper officer is not satisfied with the clarification, information or documents furnished, he shall, for reasons to be recorded in writing, reject such application and inform the applicant electronically in FORM GST REG-05.

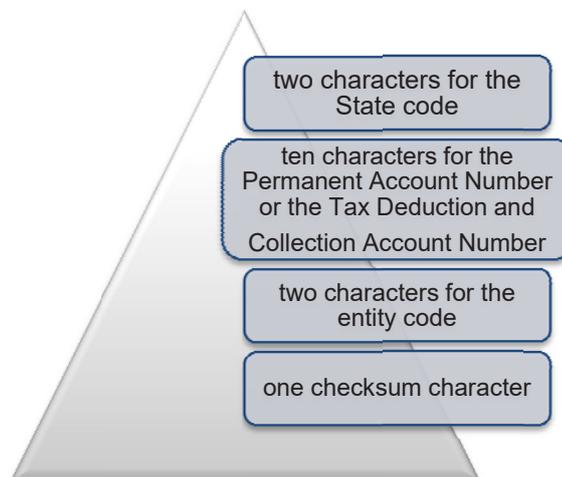
- (5) If the proper officer fails to take any action - (a) within three working days from the date of submission of application, or (b) within seven working days from the date of receipt of clarification, information or documents furnished by the applicant under sub-rule (2), the application for grant of registration shall be deemed to have been approved.

Rule 9 can thus be summarised as under:



**Issue of registration certificate [Rule 10]**

- (1) Subject to the provisions of sub-section (12) of section 25, where the application for grant of registration has been approved under rule 9, a certificate of registration in FORM GST REG-06 showing the principal place of business and additional place(s) of business shall be made available to the applicant on the Common Portal and a Goods and Services Tax Identification Number (hereinafter in these rules referred to as “GSTIN”) shall be assigned in the following format:



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- (2) The registration shall be effective from the date on which the person becomes liable to registration where the application for registration has been submitted within thirty days from such date.
- (3) Where an application for registration has been submitted by the applicant after thirty days from the date of his becoming liable to registration, the effective date of registration shall be the date of grant of registration under sub-rule (1) or sub-rule (3) or sub-rule (5) of rule 9.
- (4) Every certificate of registration shall be duly signed or verified through electronic verification code by the proper officer under the Act.
- (5) Where the registration has been granted under sub-rule (5) of rule 9, the applicant shall be communicated the registration number and the certificate of registration under sub-rule (1), duly signed or verified through electronic verification code, shall be made available to him on the common portal within three days after expiry of the period specified in sub-rule (5) of rule 9.

**Separate registration for multiple places of business within a State or a Union territory [Rule 11]**

(1) Any person having multiple places of business within a State or a Union territory, requiring a separate registration for any such place of business under sub-section (2) of section 25 shall be granted separate registration in respect of each such place of business subject to the following conditions, namely:-

- a. such person has more than one place of business as defined in clause (85) of section 2;
- b. such person shall not pay tax under section 10 for any of his places of business if he is paying tax under section 9 for any other place of business;
- c. all separately registered places of business of such person shall pay tax under the Act on supply of goods or services or both made to another registered place of business of such person and issue a tax invoice or a bill of supply, as the case may be, for such supply.

*Explanation.* - For the purposes of clause (b), it is hereby clarified that where any place of business of a registered person that has been granted a separate registration becomes ineligible to pay tax under section 10, all other registered places of business of the said person shall become ineligible to pay tax under the said section.

(2) A registered person opting to obtain separate registration for a place of business shall submit a separate application in FORM GST REG-01 in respect of such place of business.

(3) The provisions of rule 9 and rule 10 relating to the verification and the grant of registration shall, mutatis mutandis, apply to an application submitted under this rule.

## Grant of registration to persons required to deduct tax at source or to collect tax at source [Rule 12]

The procedure is as under :

Any person required to deduct tax under section 51 or a person required to collect tax at source under section 52 shall electronically submit an application, duly signed or verified, in **FORM GST REG-07** for the grant of registration through the common portal [Rule 12(1)]

A person applying for registration to collect tax in accordance with the provisions of section 52, in a State or Union territory where he does not have a physical presence, shall mention the name of the State or Union territory in PART A of the application in FORM GST REG-07 and mention the name of the State or Union territory in PART B thereof in which the principal place of business is located which may be different from the State or Union territory mentioned in PART A. [Rule 12(1A)]

The proper officer may grant registration after due verification and issue a certificate of registration in **FORM GST REG-06** within a period of three working days from the date of submission of the application. [Rule 12(2)]

Where, upon an enquiry or pursuant to any other proceeding under the Act, the proper officer is satisfied that a person to whom a certificate of registration in **FORM GST REG-06** has been issued is no longer liable to deduct tax at source under section 51 or collect tax at source under section 52, the said officer may cancel the registration issued under sub-rule (2) and such cancellation shall be communicated to the said person electronically in **FORM GST REG-08**.  
Provided that the proper officer shall follow the procedure prescribed in rule 22 for cancellation of registration. [Rule 12(3)]

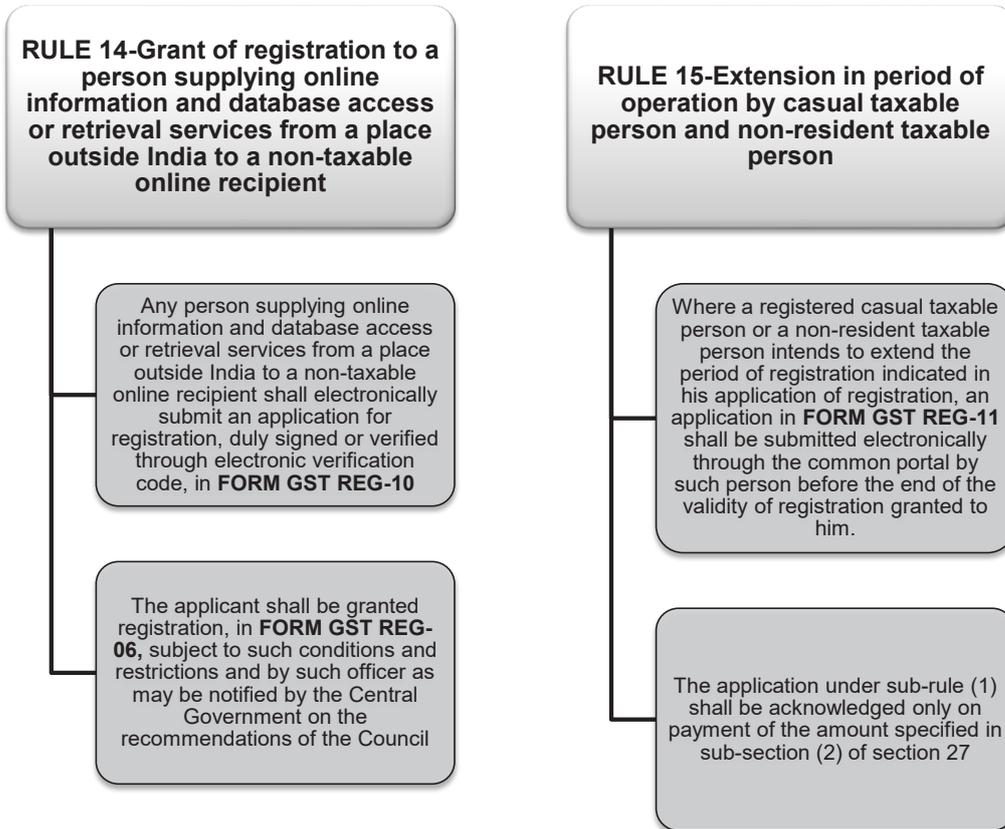
## Grant of registration to non-resident taxable person [Rule 13]

- (1) A non-resident taxable person shall electronically submit an application, along with a valid passport, for registration, duly signed, in FORM GST REG-09, at least five days prior to the commencement of business at the Common Portal either directly or through a Facilitation Centre notified by the Commissioner.

Provided that in the case of a business entity incorporated or established outside India, the application for registration shall be submitted along with its tax identification number or unique number on the basis of which the entity is identified by the Government of that country or its Permanent Account Number, if available.

- (2) A person applying for registration as a non-resident taxable person shall be given a temporary reference number by the common portal for making an advance deposit of tax in accordance with the provisions of section 27 and the acknowledgement under sub-rule (5) of rule 8 shall be issued electronically only after the said deposit in his electronic cash ledger.

- (3) The provisions of rule 9 and rule 10 relating to the verification and the grant of registration shall, mutatis mutandis, apply to an application submitted under this rule.
- (4) The application for registration made by a non-resident taxable person shall be duly signed or verified through electronic verification code by his authorised signatory who shall be a person resident in India having a valid Permanent Account Number.



**Suo moto registration [Rule 16]**

- (1) Where, pursuant to any survey, enquiry, inspection, search or any other proceedings under the Act, the proper officer finds that a person liable to registration under the Act has failed to apply for such registration, such officer may register the said person on a temporary basis and issue an order in FORM GST REG-12.
- (2) The registration granted under sub-rule (1) shall be effective from the date of order granting registration.
- (3) Every person to whom a temporary registration has been granted under sub-rule (1) shall, within ninety days from the date of the grant of such registration, submit an application for registration in the form and manner provided in rule 8 or rule 12 unless the said person has filed an appeal against the grant of temporary registration, in which case the application for registration shall be submitted within thirty days from the date of issuance of order upholding the liability to registration by the Appellate Authority.
- (4) The provisions of rule 9 and rule 10 relating to verification and issue of certificate of registration shall, mutatis mutandis, apply to an application submitted under sub-rule (3).
- (5) The GSTIN assigned pursuant to verification under sub-rule (4) shall be effective from the date of order granting registration under sub-rule (1).

**Assignment of unique identity number to certain special entities [Rule 17]**

- (1) Every person required to be granted a unique identity number under sub-section (9) of section 25 may submit an application, electronically in FORM GST REG-13, duly signed, in the manner specified in rule 1 at the Common Portal, either directly or through a Facilitation Centre, notified by the Board or Commissioner.
- (1A) The Unique Identity Number granted under sub-rule (1) to a person under clause (a) of sub-section (9) of section 25 shall be applicable to the territory of India (as inserted vide Notification No. 75/2017-Central Tax)
- (2) The proper officer may, upon submission of an application in FORM GST REG-13 or after filling up the said form or after receiving a recommendation from the Ministry of External Affairs, Government of India, assign a Unique Identity Number to the said person and issue a certificate in FORM GST REG-06 within three working days from the date of submission of application.

**Display of registration certificate and GSTIN on the name board [Rule 18]**

Every registered person to display certificate of registration in a prominent location at his **principal place of business** and at every **additional place or places of business**



Every registered person shall display his Goods and Services Tax Identification Number on the name board exhibited at the entry of his **principal place of business** and at every **additional place or places of business**.

**Amendment of Registration [Rule 19]**

- (1) Where there is any change in any of the particulars furnished in the application for registration in FORM GST REG-01 or FORM GST REG-07 or FORM GST REG-09 or FORM GST REG10 or FORM GST-REG-13, as the case may be, either at the time of obtaining registration or as amended from time to time, the registered person shall, within fifteen days of such change, submit an application, duly signed, electronically in FORM GST REG-14, along with documents relating to such change at the Common Portal either directly or through a Facilitation Centre notified by the Commissioner.

Provided that –

- (a) Where the change relates to –
  - (i) legal name of business;
  - (ii) address of the principal place of business or any additional place of business; or
  - (iii) addition, deletion or retirement of partners or directors, Karta, Managing Committee, Board of Trustees, Chief Executive Officer or equivalent, responsible for day to day affairs of the business, –

which does not warrant cancellation of registration under section 29, the proper officer shall approve the amendment within fifteen working days from the date of receipt of application in FORM GST REG-14 after due verification and issue an order in FORM GST REG-15 electronically and such amendment shall take effect from the date of occurrence of the event warranting amendment.

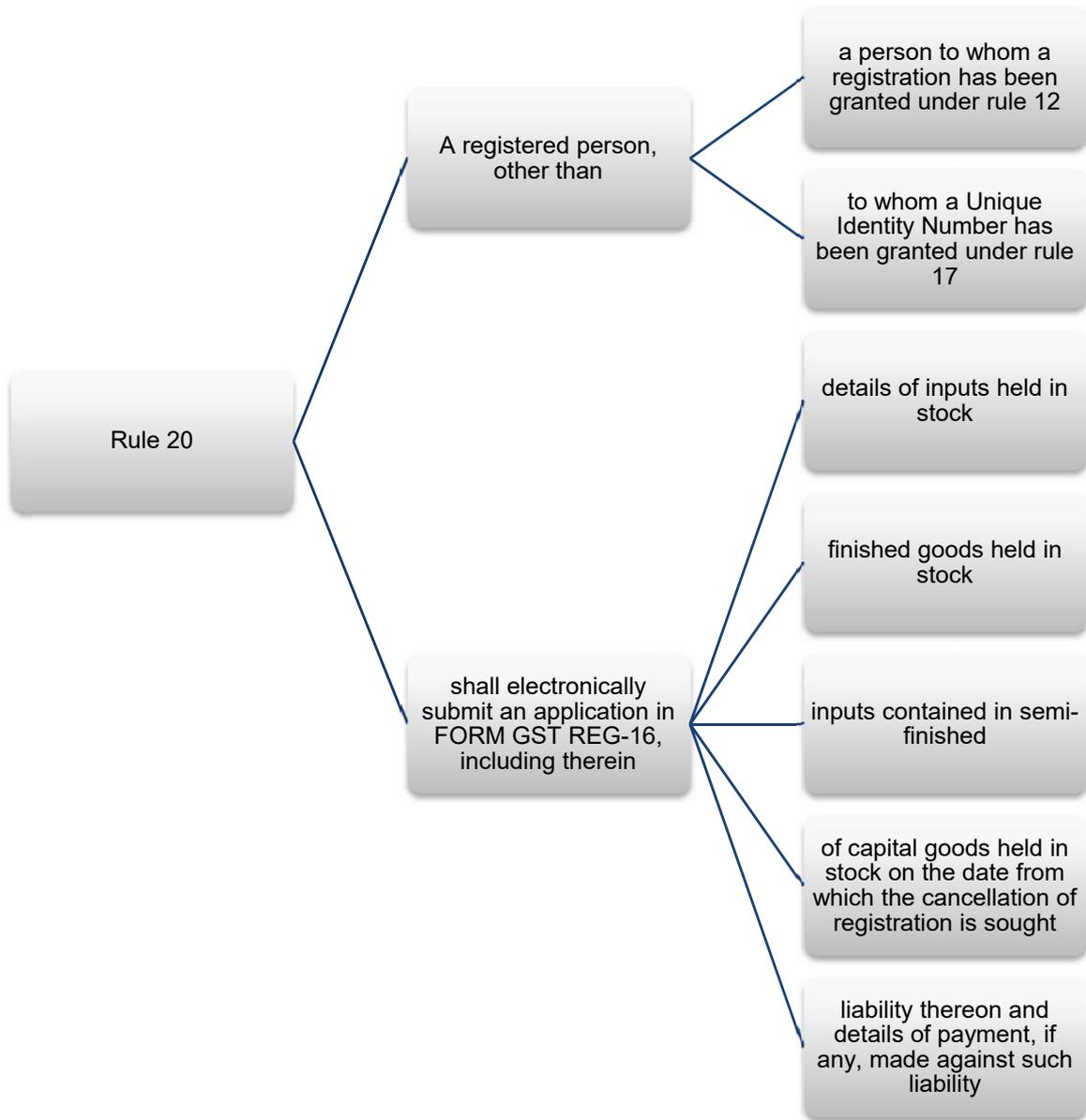
- (b) The change relating to sub-clause (i) and sub-clause (iii) of clause (a) in any State or Union territory shall be applicable for all registrations of the registered person obtained under these rules on the same PAN.
- (c) Where the change relates to any particulars other than those specified in clause (a), the certificate of registration shall stand amended upon submission of the application in FORM GST REG 14 on the Common Portal
- (d) where a change in the constitution of any business results in the change of the Permanent Account Number of a registered person, the said person shall apply for fresh registration in FORM GST REG-01

Provided that any change in the mobile number or e-mail address of the authorised signatory submitted under rule 1, as amended from time to time, shall be carried out only after online verification through the Common Portal in the manner provided under sub-rule (2) of rule 8.

- (1A) Notwithstanding anything contained in sub-rule (1), any particular of the application for registration shall not stand amended with effect from a date earlier than the date of submission of the application in FORM GST REG-14 on the common portal except with the order of the Commissioner for reasons to be recorded in writing and subject to such conditions as the Commissioner may, in the said order, specify.
- (2) Where the proper officer is of the opinion that the amendment sought under sub-rule (1) is either not warranted or the documents furnished therewith are incomplete or incorrect, he may, within fifteen working days from the date of receipt of the application in FORM GST REG-14, serve a notice in FORM GST REG-03, requiring the registered person to show cause, within seven working days of the service of the said notice, as to why the application submitted under sub-rule (1) shall not be rejected.
- (3) The taxable person shall furnish a reply to the notice to show cause, issued under sub-rule (2), in FORM GST REG-04 within seven working days from the date of the service of the said notice.
- (4) Where the reply furnished under sub-rule (3) is found to be not satisfactory or where no reply is furnished in response to the notice issued under sub-rule (2) within the period prescribed in sub-rule (3), the proper officer shall reject the application submitted under sub-rule (1) and pass an order in FORM GST REG -05.
- (5) If the proper officer fails to take any action-
  - (a) within fifteen working days from the date of submission of application, or
  - (b) within seven working days from the date of receipt of reply to the notice to show cause under sub-rule (3),

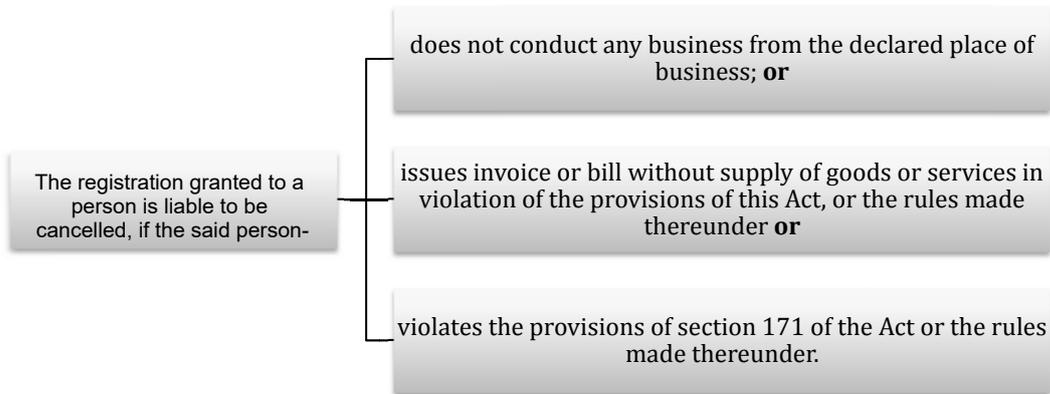
the certificate of registration shall stand amended to the extent applied for and the amended certificate shall be made available to the registered person on the Common Portal.

**Application for cancellation of registration [Rule 20]**



A registered person, other than a person to whom a registration has been granted under rule 12 or a person to whom a Unique Identity Number has been granted under rule 17, seeking cancellation of his registration under sub-section (1) of section 29 shall electronically submit an application in FORM GST REG-16, including therein the details of inputs held in stock or inputs contained in semi-finished or finished goods held in stock and of capital goods held in stock on the date from which the cancellation of registration is sought, liability thereon, the details of the payment, if any, made against such liability and may furnish, along with the application, relevant documents in support thereof, at the common portal within a period of thirty days of the occurrence of the event warranting the cancellation, either directly or through a Facilitation Centre notified by the Commissioner.

**Registration to be cancelled in certain cases [Rule 21]**



**Suspension of Registration [Section 31 & Rule 21A]**

- (1) Section 31 provides that during pendency of the proceedings relating to cancellation of registration filed by the registered person, the registration may be suspended for such period and in such manner as may be prescribed
- (2) Where a registered person has applied for cancellation of registration under rule 20, the registration shall be deemed to be suspended from the date of submission of the application or the date from which the cancellation is sought, whichever is later, pending the completion of proceedings for cancellation of registration under rule 22.
- (3) Where the proper officer has reasons to believe that the registration of a person is liable to be cancelled under section 29 or under rule 21, he may, after affording the said person a reasonable opportunity of being heard, suspend the registration of such person with effect from a date to be determined by him, pending the completion of the proceedings for cancellation of registration under rule 22.
- (4) A registered person, whose registration has been suspended under sub-rule (1) or sub-rule (2), shall not make any taxable supply during the period of suspension and shall not be required to furnish any return under section 39.

*Explanation.* – For the purposes of this sub-rule, the expression “shall not make any taxable supply” shall mean that the registered person shall not issue a tax invoice and, accordingly, not charge tax on supplies made by him during the period of suspension.

- (5) The suspension of registration under sub-rule (1) or sub-rule (2) shall be deemed to be revoked upon completion of the proceedings by the proper officer under rule 22 and such revocation shall be effective from the date on which the suspension had come into effect, and Pending returns to be filed before revocation of cancellation of registration.
- (6) Where any order having the effect of revocation of suspension of registration has been passed, the provisions of clause (a) of sub-section (3) of section 31 and section 40 in respect of the supplies made during the period of suspension and the procedure specified therein shall apply

The intent of the aforesaid provision is to ensure that a taxpayer is freed from the routine compliances, including filing returns, under GST law during the pendency of the proceedings related to cancellation of registration.

**Cancellation of registration [Rule 22]**

- (1) Where the proper officer has reasons to believe that the registration of a person is liable to be cancelled under section 29, he shall issue a notice to such person in FORM GST REG-17, requiring him to show cause within seven working days from the date of service of such notice as to why his registration should not be cancelled.
- (2) The reply to the show-cause notice issued under sub-rule (1) shall be furnished in FORM REG-18 within the period prescribed in the said sub-rule.
- (3) Where a person who has submitted an application for cancellation of his registration is no longer liable to be registered or his registration is liable to be cancelled, the proper officer shall issue an order in FORM GST REG-19, within thirty days from the date of application submitted under rule 20 or, as the case may be, the date of reply to the show cause issued under sub-rule (1), cancel the registration, with effect from a date to be determined by him and notify the taxable person, directing to pay arrears of any tax, interest or penalty including the amount liable to be paid under sub-section(5) of section 29.
- (4) Where the reply furnished under sub-rule (2) is found to be satisfactory, the proper officer shall drop the proceedings and pass an order in FORM GST REG -20.

Provided that where the person instead of replying to the notice served under sub-rule (1) for contravention of the provisions contained in clause (b) or clause (c) of sub-section (2) of section 29, furnishes all the pending returns and makes full payment of the tax dues along with applicable interest and late fee, the proper officer shall drop the proceedings and pass an order in FORM GST-REG 20.

- (5) The provisions of sub-rule (3) shall, mutatis mutandis, apply to the legal heirs of a deceased proprietor, as if the application had been submitted by the proprietor himself.

**Revocation of cancellation of registration [Rule 23]**

- (1) A registered person, whose registration is cancelled by the proper officer on his own motion, may submit an application for revocation of cancellation of registration, in FORM GST REG-21, to such proper officer, within thirty days from the date of service of the order of cancellation of registration at the Common Portal either directly or through a Facilitation Centre notified by the Commissioner :

Provided that no application for revocation shall be filed if the registration has been cancelled for the failure of the taxable person to furnish returns, unless such returns are filed and any amount due as tax, in terms of such returns has been paid along with any amount payable towards interest, penalties and late fee payable in respect of the said returns.

Provided further that all returns due for the period from the date of the order of cancellation of registration till the date of the order of revocation of cancellation of registration shall be furnished by the said person within a period of thirty days from the date of order of revocation of cancellation of registration:

Provided also that where the registration has been cancelled with retrospective effect, the registered person shall furnish all returns relating to period from the effective date of cancellation of registration till the date of order of revocation of cancellation of registration within a period of thirty days from the date of order of revocation of cancellation of registration.

- (2) (a) Where the proper officer is satisfied, for reasons to be recorded in writing, that there are sufficient grounds for revocation of cancellation of registration, he shall revoke the cancellation of registration by an order in FORM GST REG-22 within thirty days from the date of receipt of the application and communicate the same to the applicant.
- (b) The proper officer may, for reasons to be recorded in writing, under circumstances other than those

specified in clause (a), by an order in FORM GST REG-05, reject the application for revocation of cancellation of registration and communicate the same to the applicant.

- (3) The proper officer shall, before passing the order referred to in clause (b) of sub-rule (2), issue a notice in FORM GST REG-23 requiring the applicant to show cause as to why the application submitted for revocation under sub-rule (1) should not be rejected and the applicant shall furnish the reply within seven working days from the date of the service of notice in FORM GST REG-24.
- (4) Upon receipt of the information or clarification in FORM GST REG-24, the proper officer may proceed to dispose of the application in the manner specified in sub-rule (2) within thirty days from the date of receipt of such information or clarification from the applicant.

### **Physical verification of business premises in certain cases [Rule 25]**

Where the proper officer is satisfied that the physical verification of the place of business of a registered person is required after grant of registration, he may get such verification done and the verification report along with other documents, including photographs, shall be uploaded in FORM GST REG-30 on the Common Portal within fifteen working days following the date of such verification.

### **Method of Authentication [Rule 26]**

- (1) All applications, including reply, if any, to the notices, returns, appeals or any other document required to be submitted under these rules shall be so submitted electronically at the Common Portal with digital signature certificate or through e-signature as specified under the Information Technology Act, 2000 (21 of 2000) or through any other mode of signature notified by the Board in this behalf.

Provided that a registered person registered under the provisions of the Companies Act, 2013 (18 of 2013) shall furnish the documents or application verified through digital signature certificate.

- (2) Each document including the return furnished online shall be signed or verified through electronic verification code –
  - (a) in the case of an individual, by the individual himself or by some other person duly authorised by him in this behalf, and where the individual is mentally incapacitated from attending to his affairs, by his guardian or by any other person competent to act on his behalf;
  - (b) in the case of a Hindu Undivided Family, by a Karta and where the Karta is absent from India or is mentally incapacitated from attending to his affairs, by any other adult member of such family or by the authorised signatory of such Karta;
  - (c) in the case of a company, by the chief executive officer or authorised signatory thereof;
  - (d) in the case of a Government or any Governmental agency or local authority, by an officer authorised in this behalf;
  - (e) in the case of a firm, by any partner thereof, not being a minor or authorised signatory;
  - (f) in the case of any other association, by any member of the association or persons or authorised signatory;
  - (g) in the case of a trust, by the trustee or any trustee or authorised signatory; or
  - (h) in the case of any other person, by some person competent to act on his behalf, or by a person authorised in accordance with the provisions of section 48.
- (3) All notices, certificates and orders under the provisions of this Chapter shall be issued electronically by

the proper officer or any other officer authorised to issue such notices or certificates or orders, through digital signature certificate or through E-signature as specified under the provisions of the Information Technology Act, 2000 (21 of 2000) or 17 verified by any other mode of signature or verification as notified by the Board in this behalf.

## TAX INVOICES, DEBIT & CREDIT NOTES

Whenever a transaction takes place, different kinds of documents are issued under different circumstances, like invoice, credit note, debit note and bill of supply.

### Tax Invoices

Section 2(66) of Central Goods & Services Tax Act, 2017 mandates “invoice” or “tax invoice” as the tax invoice referred to in section 31.

An invoice is a commercial instrument, issued by a supplier of goods / services, to a recipient. It identifies both the parties involved, and lists and describes the items sold / services supplied, quantifies them, exhibits the dates, prices and necessary discounts.

The significance of this document has increased substantially with the advent of GST. Since the invoice matching mechanism has been introduced under GST. The details of the invoice furnished under the statement of outward taxable supplies by the Supplier and that in the inward taxable supplies furnished by the Recipient must match and that's a pre-requisite for the recipient to claim Input Tax Credit. A tax invoice must be issued by a registered person making taxable supplies. There is no format prescribed. Certain fields however are mandatory and they have been specified. The invoices could be manual or electronic.

The time limit for issuing the invoices are of extreme importance as that is a major step influencing the determination of time of supply

In case of supply of taxable goods, the invoice must be issued before or at the time of removal of goods for supply, where the supply involves movement of goods and before or at the time of delivery to the recipient where the supply doesn't involve movement of the goods.

In case of supply of taxable services, the invoice must be issued before or after the provision of service but maximum within 30 days of the provision of service, and this period is 45 days in case of BFSI companies.

In case there is a continuous supply of goods, and where successive Statement of Accounts (SOA) are issued or where successive payments are involved, the invoice must be issued before or at the time of issue of each such SOA / the receipt of each such payment.

In case there is a continuous supply of services

- Where the due date of payment is ascertainable from the contract, the invoice must be issued on or before such due date
- Where the due date of payment is not ascertainable, the invoice must be issued on / before receipt of such payment by the supplier
- Where the payment is linked to the completion of event, the invoice must be issued on / before the completion of that event

Earlier a credit/debit note, which is issued by the registered person under section 34, was required to be issued invoice-wise. Now a registered person can issue one (consolidated) note or more debit notes/ credit notes in respect of multiple invoices issued in a financial year without linking the same to individual invoices. This used to cause avoidable compliance burden for tax payers.

### Illustration 1

Meenakshi enterprises, Kolkata makes a supply of goods to Dhirani enterprises, Ghaziabad. The goods were removed from the factory at Kolkata on 3rd May. Hence, the tax invoice must be issued on or before 3rd May.

### Illustration 2

Mohan Ltd. an event management company has provided its services for an event at Photo Film Agencies at Kolkata, on 1st June. The tax invoice must therefore be issued within 30 days, that is, within 30th June.

### Illustration 3

Seema & Co. has entered into an AMC (Annual Maintenance Contract) with Vir Enterprises for one-year effective 1st September, 2017 for the stabilisers installed in the factory. As per contract, the invoice must be issued by 9th September, 2017. In this case, since there is a continuous supply of services where the due date is ascertainable from the contract, the tax invoice must be issued before or on 9th September, 2017.

### Particulars of a tax invoice [Section 31]

- Name, address and GSTIN of the supplier
- A consecutive serial number not exceeding 16 digits, unique for a FY
- Date of issue
- If the recipient is registered, name, address and GSTIN of the Recipient
- Description of goods / services along with HSN Code
- Value of Supply after effecting the necessary discounts
- Rate of Tax (incl. description i.e., CGST/SGST/IGST)
- Amount of Tax
- Value of Invoice
- Place of Supply
- Address of delivery where the same is different from place of supply
- Forward Charge or Reverse Charge
- Signature of supplier / authorised representative

### Modus

In case of supply of goods, the invoice must be issued in triplicate, i.e., original for recipient, duplicate for transporter and triplicate for supplier.

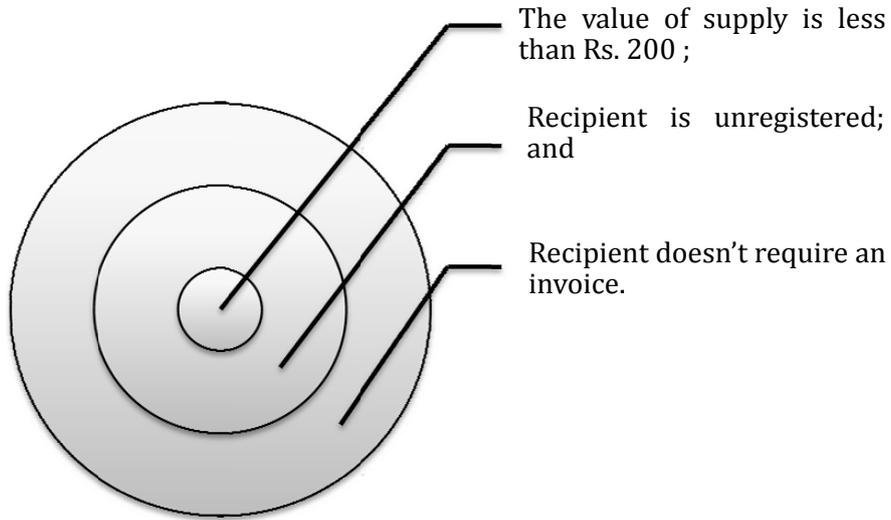
In case of supply of services, the invoice must be issued in duplicate, i.e., original for recipient and duplicate for supplier.

Where the goods being sent or taken on approval for sale or return are removed before the supply takes place, the invoice shall be issued before or at the time of supply or six months from the date of removal, whichever is earlier.

Here, "tax invoice" shall include any revised invoice issued by the supplier in respect of a supply made earlier. The Government may, on the recommendations of the Council, by notification, specify the categories of goods or services in respect of which a tax invoice shall be issued or any other document issued in relation to the supply shall be deemed to be a tax invoice.

## Exceptions

It must be noted that no tax invoice is to be issued when:



Instead such registered person shall issue the consolidated tax invoice for such supplies at the close of each day for all such supplies. In case the registered person is making exempted supplies, or he is registered under composition levy, he cannot issue a tax invoice in which case, he will issue a bill of supply.

## Reverse Charge Mechanism

A registered person, who is liable to pay tax under the Reverse Charge Mechanism, shall issue an invoice in respect of the goods / services so received by him from the supplier, who is not registered on the date of receipt of goods / services / both, and he shall issue a payment voucher at the time of making payment to such supplier.

Although all GST taxpayers are free to design their own invoice format, it is required that certain fields as mentioned in the invoice rule be incorporated in all invoices. A draft template of invoice (GST INV-1) under GST is given below:

**Government of India/State**  
**Department of.....**

**Form GST INV-1**  
**(See Rule-----)**  
**Application for Electronic Reference Number of an Invoice**

1. GSTIN  
2. Name  
3. Address  
4. Serial No. of Invoice  
5. Date of Invoice

<p><b>Details of Receiver (Billed to)</b></p> <p>Name Address State State Code GSTIN/Unique ID</p>	<p><b>Details of Consignee (Shipped to)</b></p> <p>Name Address State State Code GSTIN/Unique ID</p>
--	--

Sr. No.	Description of Goods	HS N	Qty.	Unit	Rate (per item)	Total	Discount	Taxable value	CGST		SGST		IGST	
									Rate	Amt.	Rate	Amt.	Rate	Amt.
	Freight													
	Insurance													
	Packing and Forwarding Charges													
	<b>Total</b>													
Total Invoice Value (In figure)														
Total Invoice Value (In Words)														
Amount of Tax subject to Reverse Charges														

**Receipt Voucher**

When an advance payment is received with respect to any supply of goods or services or both, a receipt voucher is required to be issued by the registered person. Further, if no supply is made and no tax invoice is issued after the issue of receipt voucher, the said registered person may issue to the person who had made the payment, a refund voucher against such payment.

**Credit / Debit Notes**

Under Section 2(37) of Central goods & Services tax Act, 2017, “credit note” means a document issued by a registered person under sub-section (1) of section 34.

Under Section 2(38) of Central goods & Services tax Act, 2017, “debit note” means a document issued by a registered person under sub-section (3) of section 34.

Where a tax invoice has been issued for supply of goods / services / both, and where the taxable value in the invoice is greater than the taxable value of supply; the tax charged per invoice is greater than the tax payable in respect of such supply; OR where the goods so supplied have been returned by the recipient OR where the goods / services have been found to be deficient; in these cases, the registered supplier may issue a credit note to the recipient.

Where a tax invoice has been issued for supply of goods / services / both, and where the taxable value in the invoice is less than the taxable value of supply; the tax charged per invoice is less than the tax payable in respect of such supply; the registered supplier may issue a debit note to the recipient.

**Declaration**

Any registered person who has issued a credit note, in relation to supply of goods / services / both, must declare the details of such credit note, in the return for the month during which such credit note was issued, but not later than:

- a) September following the end of Financial Year in which the supply was made OR
- b) Date of furnishing the relevant annual return

whichever is earlier.

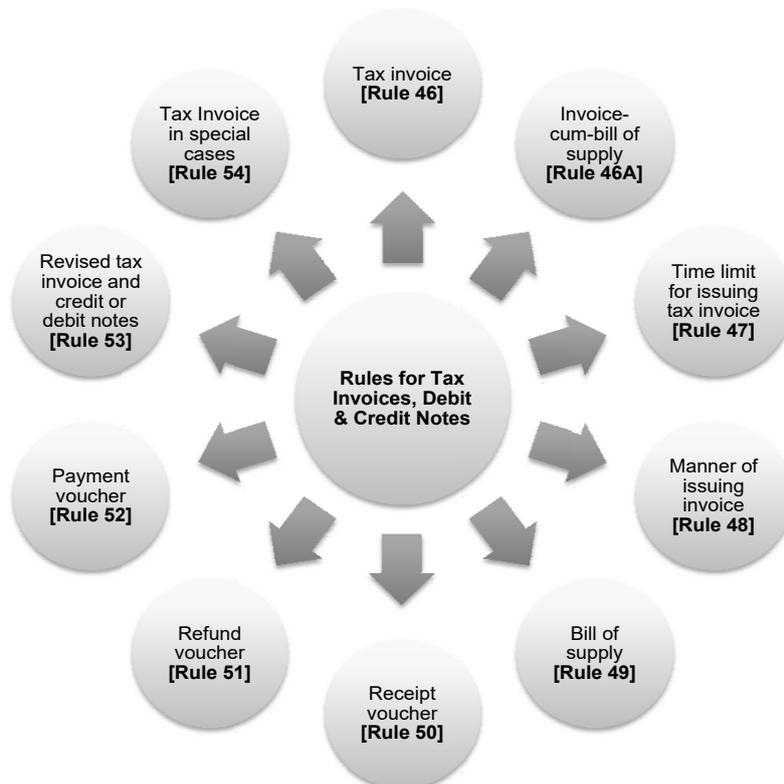
No reduction in tax liability of the supplier shall be permitted, if the incidence of tax on such supply has been passed on to any other person.

Any registered person who has issued a debit note, in relation to supply of goods / services / both, must declare the details of such debit note, in the return for the month during which such debit note was issued. The tax liability can be adjusted upwards appropriately.

**RULES FOR TAX INVOICES, DEBIT & CREDIT NOTES**

Chapter VI contains rules for tax invoices debit & credit notes.

**Tax Invoice [Rule 46]**



Subject to rule 54, a tax invoice referred to in section 31 shall be issued by the registered person containing the following particulars:-

- (a) name, address and GSTIN of the supplier;
- (b) a consecutive serial number, in one or multiple series, containing alphabets or numerals or special characters hyphen or dash and slash symbolised as “-” and “/” respectively, and any combination thereof, unique for a financial year;
- (c) date of its issue;
- (d) name, address and GSTIN or UIN, if registered, of the recipient;
- (e) name and address of the recipient and the address of delivery, along with the name of State and its code, if such recipient is un-registered and where the value of taxable supply is fifty thousand rupees or more;
- (f) name and address of the recipient and the address of delivery, along with the name of the State and its code, if such recipient is un-registered and where the value of the taxable supply is less than fifty thousand rupees and the recipient requests that such details be recorded in the tax invoice;
- (g) HSN code of goods or Accounting Code of services;
- (h) description of goods or services;
- (i) quantity in case of goods and unit or Unique Quantity Code thereof;
- (j) total value of supply of goods or services or both;
- (k) taxable value of supply of goods or services or both taking into account discount or abatement, if any;
- (l) rate of tax (central tax, State tax, integrated tax, Union territory tax or cess);
- (m) amount of tax charged in respect of taxable goods or services (central tax, State tax, integrated tax, Union territory tax or cess);
- (n) place of supply along with the name of State, in case of a supply in the course of inter-State trade or commerce;
- (o) address of delivery where the same is different from the place of supply;
- (p) whether the tax is payable on reverse charge basis; and
- (q) signature or digital signature of the supplier or his authorized representative:

Provided that the Board may, on the recommendations of the Council, by notification, specify -

- (i) the number of digits of HSN code for goods or the Accounting Code for services, that a class of registered persons shall be required to mention, for such period as may be specified in the said notification, and
- (ii) the class of registered persons that would not be required to mention the HSN code for goods or the Accounting Code for services, for such period as may be specified in the said notification

Provided further that where an invoice is required to be issued under clause (f) of sub-section (3) of section 31, a registered person may issue a consolidated invoice at the end of a month for supplies covered under subsection (4) of section 9, the aggregate value of such supplies exceeds rupees five thousand in a day from any or all the suppliers:

Provided also that in the case of the export of goods or services, the invoice shall carry an endorsement – “SUPPLY MEANT FOR EXPORT/SUPPLY TO SEZ UNIT OR SEZ DEVELOPER FOR AUTHORISED OPERATIONS ON PAYMENT OF INTEGRATED TAX” or – “SUPPLY MEANT FOR EXPORT/SUPPLY TO SEZ UNIT OR SEZ DEVELOPER FOR AUTHORISED OPERATIONS UNDER BOND OR LETTER OF UNDERTAKING WITHOUT PAYMENT OF INTEGRATED TAX”, as the case may be, and shall, in lieu of the details specified in clause (e),

contain the following details, namely, – (i) name and address of the recipient; (ii) address of delivery; and (iii) name of the country of destination:

Provided also that a registered person may not issue a tax invoice in accordance with the provisions of clause (b) of sub-section (3) of section 31 subject to the following conditions, namely:-

- (a) the recipient is not a registered person; and
- (b) the recipient does not require such invoice, and

shall issue a consolidated tax invoice for such supplies at the close of each day in respect of all such supplies.

Provided also that the signature or digital signature of the supplier or his authorised representative shall not be required in the case of issuance of an electronic invoice in accordance with the provisions of the Information Technology Act, 2000 (21 of 2000).

Provided also that the Government may, by notification, on the recommendations of the Council, and subject to such conditions and restrictions as mentioned therein, specify that the bill of supply shall have Quick Response (QR) code.

Vide Notification No. 72/2019 (C.R.) dated 13.12.2019, which shall come into effect from 1.4.2020, it has been notified that an invoice issued by a registered person, whose aggregate turnover in a financial year exceeds five hundred crore rupees, to an unregistered person (hereinafter referred to as B2C invoice), shall have Quick Response (QR) code. It has further notified that where such registered person makes a Dynamic Quick Response (QR) code available to the recipient through a digital display, such B2C invoice issued by such registered person containing cross-reference of the payment using a Dynamic Quick Response (QR) code, shall be deemed to be having Quick Response (QR) code.

#### **Invoice-cum-bill of supply [Rule 46A]**

Notwithstanding anything contained in rule 46 or rule 49 or rule 54, where a registered person is supplying taxable as well as exempted goods or services or both to an unregistered person, a single “invoice-cum-bill of supply” may be issued for all such supplies.

#### **Time limit for issuing tax invoice [Rule 47]**

The invoice referred to in rule 46, in case of taxable supply of services, shall be issued within a period of thirty days from the date of supply of service

Provided that where the supplier of services is an insurer or a banking company or a financial institution, including a non-banking financial company, the period within which the invoice or any document in lieu thereof is to be issued shall be forty five days from the date of supply of service

Provided further that where the supplier of services is an insurer or a banking company or a financial institution, including a non-banking financial company, or a telecom operator, or any other class of supplier of services as may be notified by the Government on the recommendations of the Council, making taxable supplies of services between distinct persons as specified in section 25, may issue the invoice before or at the time such supplier records the same in his books of account or before the expiry of the quarter during which the supply was made.

#### **Manner of issuing invoice [Rule 48]**

- (1) The invoice shall be prepared in triplicate, in case of supply of goods, in the following manner: –
  - (a) the original copy being marked as ORIGINAL FOR RECIPIENT; (b) the duplicate copy being marked as DUPLICATE FOR TRANSPORTER; and (c) the triplicate copy being marked as TRIPLICATE FOR SUPPLIER.

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- (2) The invoice shall be prepared in duplicate, in case of supply of services, in the following manner: -
  - (a) the original copy being marked as ORIGINAL FOR RECIPIENT; and (b) the duplicate copy being marked as DUPLICATE FOR SUPPLIER.
- (3) The serial number of invoices issued during a tax period shall be furnished electronically through the Common Portal in FORM GSTR-1.

### E Invoicing

Notification No. 13/2019 C.T. dated 13.12.2019 has been issued so as to insert sub-rule (4), (5) and (6) in Rule 48 of the CGST Rules, w.e.f 1.4.2020, to provide for issuance of e invoices by certain category of persons. Such newly introduced provisions are briefed as under.

- Rule 48(4) The invoice shall be prepared by such class of registered persons as may be notified by the Government, on the recommendations of the Council, by including such particulars contained in FORM GST INV-01 after obtaining an Invoice Reference Number by uploading information contained therein on the Common Goods and Services Tax Electronic Portal in such manner and subject to such conditions and restrictions as may be specified in the notification.
- Rule 48(5) Every invoice issued by a person to whom sub-rule (4) applies in any manner other than the manner specified in the said sub-rule shall not be treated as an invoice.
- Rule 48(6) The provisions of sub-rules (1) and (2) shall not apply to an invoice prepared in the manner specified in sub-rule (4).
- Vide Notification No. 70/2019-CT dated 13.12.2019, the Government has notified registered person, whose aggregate turnover in a financial year exceeds one hundred crore rupees, as a class of registered person who shall prepare invoice in terms of sub-rule (4) of rule 48 of the said rules in respect of supply of goods or services or both to a registered person.
- Vide Notification No. 69/2019-CT dated 13.12.2019, the Government has further issued Notifications so as to notify the portals where e-invoices in terms of sub-rule (4) of rule 48 shall be prepared. List of portals are as below;
  - (i) [www.einvoice1.gst.gov.in](http://www.einvoice1.gst.gov.in);
  - (ii) [www.einvoice2.gst.gov.in](http://www.einvoice2.gst.gov.in);
  - (iii) [www.einvoice3.gst.gov.in](http://www.einvoice3.gst.gov.in);
  - (iv) [www.einvoice4.gst.gov.in](http://www.einvoice4.gst.gov.in);
  - (v) [www.einvoice5.gst.gov.in](http://www.einvoice5.gst.gov.in);
  - (vi) [www.einvoice6.gst.gov.in](http://www.einvoice6.gst.gov.in);
  - (vii) [www.einvoice7.gst.gov.in](http://www.einvoice7.gst.gov.in);
  - (viii) [www.einvoice8.gst.gov.in](http://www.einvoice8.gst.gov.in);
  - (ix) [www.einvoice9.gst.gov.in](http://www.einvoice9.gst.gov.in);
  - (x) [www.einvoice10.gst.gov.in](http://www.einvoice10.gst.gov.in).

The above changes shall come into effect from 1.4.2020. However, the trade can initiate e-invoicing w.e.f 1.1.2020 on voluntary basis.

### Bill of supply [Rule 49]

A bill of supply referred to in clause (c) of sub-section (3) of section 31 shall be issued by the supplier containing the following details:-

- (a) name, address and GSTIN of the supplier;
- (b) a consecutive serial number not exceeding sixteen characters, in one or multiple series, containing alphabets or numerals or special characters -hyphen or dash and slash symbolised as “-” and “/” respectively, and any combination thereof, unique for a financial year;
- (c) date of its issue;
- (d) name, address and GSTIN or UIN, if registered, of the recipient;
- (e) HSN Code of goods or Accounting Code for services;
- (f) description of goods or services or both;
- (g) value of supply of goods or services or both taking into account discount or abatement, if any; and
- (h) signature or digital signature of the supplier or his authorized representative:

Provided that the provisos to rule 46 shall, mutatis mutandis, apply to the bill of supply issued under this rule.

Provided further that any tax invoice or any other similar document issued under any other Act for the time being in force in respect of any non taxable supply shall be treated as a bill of supply for the purposes of the Act.

Provided also that the signature or digital signature of the supplier or his authorised representative shall not be required in the case of issuance of an electronic bill of supply in accordance with the provisions of the Information Technology Act, 2000 (21 of 2000).

#### **Receipt voucher [Rule 50]**

A receipt voucher referred to in clause (d) of sub-section (3) of section 31 shall contain the following particulars:

- (a) name, address and GSTIN of the supplier;
- (b) a consecutive serial number containing alphabets or numerals or special characters -hyphen or dash and slash symbolised as “-” and “/” respectively, and any combination thereof, unique for a financial year
- (c) date of its issue;
- (d) name, address and GSTIN or UIN, if registered, of the recipient;
- (e) description of goods or services;
- (f) amount of advance taken;
- (g) rate of tax (central tax, State tax, integrated tax, Union territory tax or cess);
- (h) amount of tax charged in respect of taxable goods or services (central tax, State tax, integrated tax, Union territory tax or cess);
- (i) place of supply along with the name of State and its code, in case of a supply in the course of inter-State trade or commerce;
- (j) whether the tax is payable on reverse charge basis; and
- (k) signature or digital signature of the supplier or his authorized representative.

Provided that where at the time of receipt of advance,-

- (i) the rate of tax is not determinable, the tax shall be paid at the rate of eighteen per cent.;
- (ii) the nature of supply is not determinable, the same shall be treated as inter-State supply.

#### **Refund voucher [Rule 51]**

A refund voucher referred to in clause (e) of sub-section (3) of section 31 shall contain the following particulars, namely:-

**692 EP-TL**

- (a) name, address and Goods and Services Tax Identification Number of the supplier;
- (b) a consecutive serial number not exceeding sixteen characters, in one or multiple series, containing alphabets or numerals or special characters hyphen or dash and slash symbolised as “-” and “/” respectively, and any combination thereof, unique for a financial year;
- (c) date of its issue;
- (d) name, address and Goods and Services Tax Identification Number or Unique Identity Number, if registered, of the recipient;
- (e) number and date of receipt voucher issued in accordance with the provisions of rule 50;
- (f) description of goods or services in respect of which refund is made;
- (g) amount of refund made;
- (h) rate of tax (central tax, State tax, integrated tax, Union territory tax or cess);
- (i) amount of tax paid in respect of such goods or services (central tax, State tax, integrated tax, Union territory tax or cess);
- (j) whether the tax is payable on reverse charge basis; and
- (k) signature or digital signature of the supplier or his authorised representative.

**Payment voucher [Rule 52]**

A payment voucher referred to in clause (g) of sub-section (3) of section 31 shall contain the following particulars, namely:-

- (a) name, address and Goods and Services Tax Identification Number of the supplier if registered;
- (b) a consecutive serial number not exceeding sixteen characters, in one or multiple series, containing alphabets or numerals or special characters hyphen or dash and slash symbolised as “-” and “/” respectively, and any combination thereof, unique for a financial year;
- (c) date of its issue;
- (d) name, address and Goods and Services Tax Identification Number of the recipient;
- (e) description of goods or services;
- (f) amount paid;
- (g) rate of tax (central tax, State tax, integrated tax, Union territory tax or cess);
- (h) amount of tax payable in respect of taxable goods or services (central tax, State tax, integrated tax, Union territory tax or cess);
- (i) place of supply along with the name of State and its code, in case of a supply in the course of inter-State trade or commerce; and
- (j) signature or digital signature of the supplier or his authorised representative.

**Revised tax invoice and credit or debit notes [Rule 53]**

(1) A revised tax invoice referred to in section 31 shall contain the following particulars, namely:-

- (a) the word “Revised Invoice”, wherever applicable, indicated prominently;
- (b) name, address and Goods and Services Tax Identification Number of the supplier;
- (c) [omitted vide Notification No. 03/2019-CT dt. 29.01.2019 w.e.f. 01.02.2019] ;
- (d) a consecutive serial number not exceeding sixteen characters, in one or multiple series, containing alphabets or numerals or special characters hyphen or dash and slash symbolised as “-” and “/”

respectively, and any combination thereof, unique for a financial year;

- (e) date of issue of the document;
- (f) name, address and Goods and Services Tax Identification Number or Unique Identity Number, if registered, of the recipient;
- (g) name and address of the recipient and the address of delivery, along with the name of State and its code, if such recipient is un-registered;
- (h) serial number and date of the corresponding tax invoice or, as the case may be, bill of supply, and
- (i) [omitted vide Notification No. 03/2019-CT dt. 29.01.2019 w.e.f. 01.02.2019] ;
- (j) signature or digital signature of the supplier or his authorised representative.

(1A) A credit or debit note referred to in section 34 shall contain the following particulars, namely:—

- (a) name, address and Goods and Services Tax Identification Number of the supplier;
- (b) nature of the document;
- (c) a consecutive serial number not exceeding sixteen characters, in one or multiple series, containing alphabets or numerals or special characters-hyphen or dash and slash symbolised as — “-“ and — “/” respectively, and any combination thereof, unique for a financial year;
- (d) date of issue of the document;
- (e) name, address and Goods and Services Tax Identification Number or Unique Identity Number, if registered, of the recipient;
- (f) name and address of the recipient and the address of delivery, along with the name of State and its code, if such recipient is un-registered;
- (g) serial number(s) and date(s) of the corresponding tax invoice(s) or, as the case may be, bill(s) of supply;
- (h) value of taxable supply of goods or services, rate of tax and the amount of the tax credited or, as the case may be, debited to the recipient; and
- (i) signature or digital signature of the supplier or his authorised representative.

(2) Every registered person who has been granted registration with effect from a date earlier than the date of issuance of certificate of registration to him, may issue revised tax invoices in respect of taxable supplies effected during the period starting from the effective date of registration till the date of the issuance of the certificate of registration.

Provided that the registered person may issue a consolidated revised tax invoice in respect of all taxable supplies made to a recipient who is not registered under the Act during such period.

Provided further that in the case of inter-State supplies, where the value of a supply does not exceed two lakh and fifty thousand rupees, a consolidated revised invoice may be issued separately in respect of all the recipients located in a State, who are not registered under the Act.

(3) Any invoice or debit note issued in pursuance of any tax payable in accordance with the provisions of section 74 or section 129 or section 130 shall prominently contain the words “INPUT TAX CREDIT NOT ADMISSIBLE”

### **Tax Invoice in special cases [Rule 54]**

(1) An ISD invoice or, as the case may be, an ISD credit note issued by an Input Service Distributor shall contain the following details:-

- (a) name, address and GSTIN of the Input Service Distributor;

**694 EP-TL**

- (b) a consecutive serial number containing alphabets or numerals or special characters hyphen or dash and slash symbolised as , “-”, “/”, respectively, and any combination thereof, unique for a financial year;
- (c) date of its issue;
- (d) name, address and GSTIN of the recipient to whom the credit is distributed; (e) amount of the credit distributed; and
- (f) signature or digital signature of the Input Service Distributor or his authorized representative:

Provided that where the Input Service Distributor is an office of a banking company or a financial institution, including a non-banking financial company, a tax invoice shall include any document in lieu thereof, by whatever name called, whether or not serially numbered but containing the information as prescribed above.

(1A) (a) A registered person, having the same PAN and State code as an Input Service Distributor, may issue an invoice or, as the case may be, a credit or debit note to transfer the credit of common input services to the Input Service Distributor, which shall contain the following details:-

- i. name, address and Goods and Services Tax Identification Number of the registered person having the same PAN and same State code as the Input Service Distributor;
- ii. a consecutive serial number not exceeding sixteen characters, in one or multiple series, containing alphabets or numerals or special characters -hyphen or dash and slash symbolised as — “-” and “/” respectively, and any combination thereof, unique for a financial year;
- iii. date of its issue;
- iv. Goods and Services Tax Identification Number of supplier of common service and original invoice number whose credit is sought to be transferred to the Input Service Distributor;
- v. name, address and Goods and Services Tax Identification Number of the Input Service Distributor;
- vi. taxable value, rate and amount of the credit to be transferred; and
- vii. signature or digital signature of the registered person or his authorised representative.

(b) The taxable value in the invoice issued under clause (a) shall be the same as the value of the common services.

(2) Where the supplier of taxable service is an insurer or a banking company or a financial institution, including a non-banking financial company, the said supplier may issue a consolidated tax invoice or any other document in lieu thereof, by whatever name called, for the supply of services made during a month at the end of the month, whether or not serially numbered, and whether or not containing the address of the recipient of taxable service but containing other information as prescribed under rule 46.

Provided that the signature or digital signature of the supplier or his authorised representative shall not be required in the case of issuance of a consolidated tax invoice or any other document in lieu thereof in accordance with the provisions of the Information Technology Act, 2000 (21 of 2000).

(3) Where the supplier of taxable service is a goods transport agency supplying services in relation to transportation of goods by road in a goods carriage, the said supplier shall issue a tax invoice or any other document in lieu thereof, by whatever name called, containing the gross weight of the consignment, name of the consignor and the consignee, registration number of goods carriage in which the goods are transported, details of goods transported, details of place of origin and destination, GSTIN of the person liable for paying tax whether as consignor, consignee or goods transport agency, and also containing other information as prescribed under rule 46.

(4) Where the supplier of taxable service is supplying passenger transportation service, a tax invoice shall include ticket in any form, by whatever name called, whether or not serially numbered, and whether or not containing the address of the recipient of service but containing other information as prescribed under rule 46.

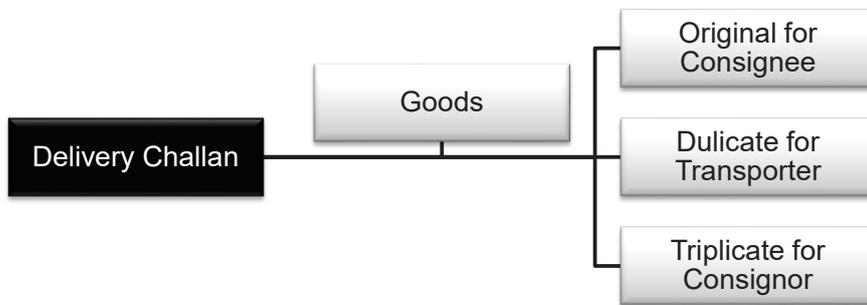
Provided that the signature or digital signature of the supplier or his authorised representative shall not be required in the case of issuance of ticket in accordance with the provisions of the Information Technology Act, 2000 (21 of 2000).

(5) The provisions of sub-rule (2) or sub-rule (4) shall apply, mutatis mutandis, to the documents issued under rule 49 or rule 50 or rule 51 or rule 52 or rule 53.

### Delivery Challan [Rule 55]

Few situations where a delivery challan, serially numbered, should be issued instead of invoice. Such situations are as follows:

- supply of liquid gas where the quantity at the time of removal from the place of business of the supplier is not known
- transportation of goods for job work
- transportation of goods for reasons other than by way of supply, or
- such other supplies as may be notified by the Board



The supplier is required to issue a tax invoice after delivery of goods where tax invoice could not be issued at the time of removal of goods for the purpose of supply.

Where the goods are being transported in a semi knocked down or completely knocked down condition or in batches or lots –

- the supplier shall issue the complete invoice before dispatch of the first consignment;
- the supplier shall issue a delivery challan for each of the subsequent consignments, giving reference of the invoice;
- each consignment shall be accompanied by copies of the corresponding delivery challan along with a duly certified copy of the invoice; and
- the original copy of the invoice shall be sent along with the last consignment.

### Rule 55A : Tax Invoice or bill of supply to accompany transport of goods.

The person-in- charge of the conveyance shall carry a copy of the tax invoice or the bill of supply issued in accordance with the provisions of rules 46, 46A or 49 in a case where such person is not required to carry an e-way bill under these rules.

## ACCOUNTS AND RECORDS

### Accounts and other Records [Section 35]

Assessment in GST is substantially focused around self-assessment. Every taxpayer thereby is expected to self-assess the liability, file the returns and pay the tax by the 20th of the following month. The authenticity and

completeness of the same is subject to audits, inspection and that casts a responsibility upon the taxpayer to maintain the necessary accounts and records.

Every registered person is expected to maintain the necessary accounts and records at the principal place of business and these records could be electronic or manual.

### Place of maintenance

Section 35 of Central Goods & Services Tax Act, 2017 states that every registered person shall maintain books of accounts at his principal place of business and where more than one place of business is specified in the certificate of registration, at every such place of business too.

### Nature of records

Section 35 of Central Goods & Services Tax Act, 2017 mandates that the following records must be maintained:

- Production Records
  - o Raw Materials
  - o WIP
  - o Finished Goods
- Inward supplies
- Outward supplies
- Taxes Paid
- ITC availed
- Output tax liabilities

Also, the CGST Rules, 2017 prescribes the following records:

- Goods / services imported
- Supplies attracting payment of taxes under reverse charge mechanism along with all ancillary and related documents
- Names and addresses of persons he has received the goods / services
- Names and addresses of persons to whom he has supplied the goods / services

### Audit requirements

Section 35(5) of Central Goods & Services Tax Act, 2017 also mandates that every registered person must get his accounts audited by a Chartered Accountant or a Cost Accountant if his aggregate turnover during a Financial Year exceeds Rs. 2 Crores.

Such person has the additional responsibility of furnishing along with the annual return:

- Audited annual accounts and
- Reconciliation statement duly certified which reconciles the value of supplies declared in the Annual Return with the Annual Audited Financial Statements

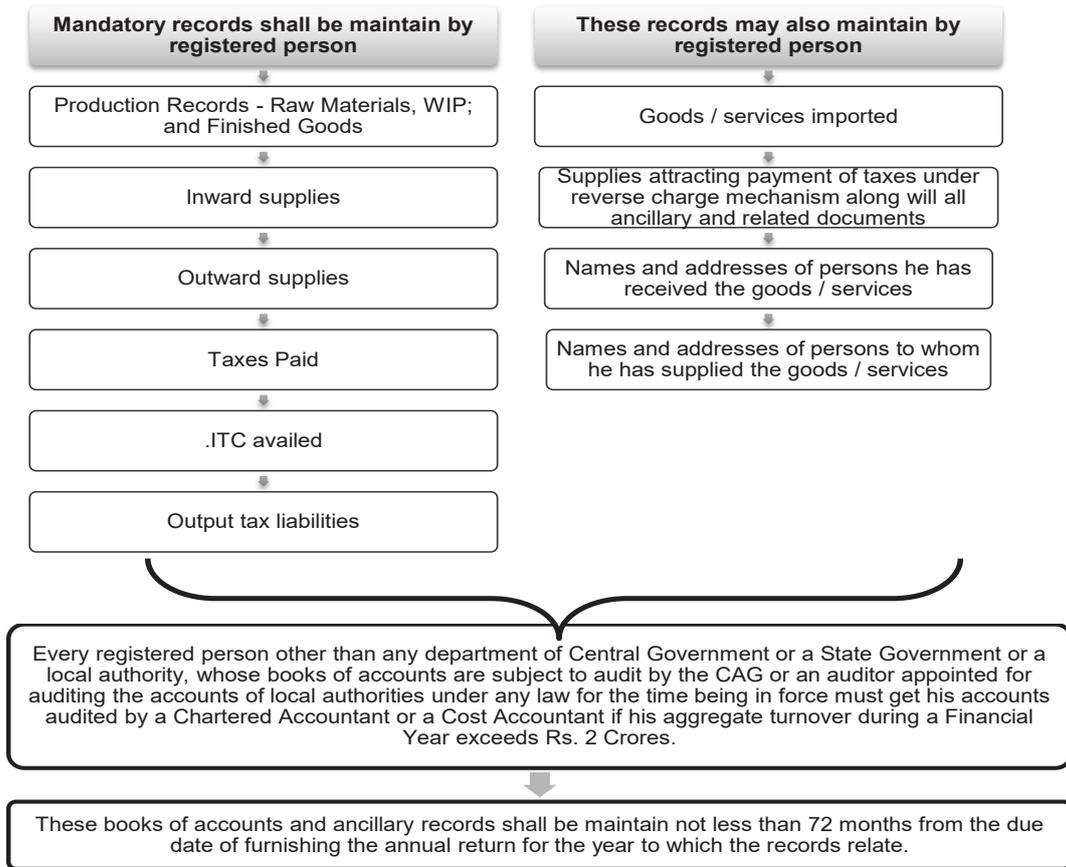
Provided that nothing contained in this sub-section shall apply to any department of the Central Government or a State Government or a local authority, whose books of account are subject to audit by the Comptroller and Auditor-General of India or an auditor appointed for auditing the accounts of local authorities under any law for

the time being in force.

**Period of retention of accounts [Section 36]**

Every taxpayer shall maintain the books of accounts and ancillary records, until the expiry of 72 months, from the due date of furnishing the annual return for the year to which the records relate.

However, a registered person who is party to an appeal / any other proceedings, before any authority / tribunal, shall have to maintain the accounts and books / records, pertaining to the matters of such appeal for a minimum period of 1 year after disposal of such appeal / revision as the case may be.



**ELECTRONIC WAY BILLS**

The Government may require the person in charge of a conveyance carrying any consignment of goods of value exceeding the prescribed amounts, to carry with himself such documents and devices as may be prescribed.

Where any such conveyance is intercepted by the proper officer, he may require the person in charge of the conveyance to produce the documents & devices for verification and that person then has the duty to cooperate and allow the inspection.

It is for the same reason that Electronic Way Bills (E-way bills) have been prescribed.

Rule 138 of the CGST Rules, 2017 stipulates as under, with regard to the E-Way Bills:

Every registered person who causes movement of goods of consignment value greater than Rs. 50,000 whether for supply or otherwise or due to the inward supply from an unregistered person, shall before commencement of such movement, furnish the necessary information in the prescribed form, electronically on the portal.

Where the E-way bill hasn't been generated and the consignment is handed over to a transporter, the transporter will generate the E-way bill on the basis of information furnished on the portal by the registered person. Upon the generation of the E-way bill, a unique E-way bill number (EBN), is generated and made available to the supplier, the recipient and the transporter. Where multiple consignments are being carried, a transporter may also generate a consolidated E-way bill.

For the purpose of calculating the consignment value of goods, the value as declared in an invoice, a bill of supply or a delivery challan shall include includes the Central tax, State or Union territory tax, integrated tax and cess charged, if any, in the document and shall exclude the value of exempt supply of goods where the invoice is issued in respect of both exempt and taxable supply of goods.

The E-way bill so generated is valid for one day if the distance involved is less than or equal to 100 kms, and one additional day for every 100 kms over and above. In case of over dimensional cargo, the validity shall be one day for first 20 KM and one additional day for every 20 KM.

## RETURNS

As per law, a taxpayer is required to file a document with the administrative authority which is commonly known as a "return". There are various types of returns under GST like the First return, Monthly return, Return for Composition Scheme, TDS return, Return for Input Service Distributor Annual return and final return. Under GST, everything is online and is updated and matched regularly. If a business is done from offices in multiple states, the number of returns will go up accordingly. The entire procedure of filling returns can be divided into 5 parts as follows:



## Furnishing details of outward supplies [Section 37]

Section 37 of Central Goods & Services tax Act, 2017 mentions that the details of outward supplies (form GSTR 1), of goods / services / both, are required to be furnished by every registered person, including casual taxable person, but excluding:

- a) Input Service Distributor (ISD)
- b) Non-resident taxable person
- c) Person paying tax under composition scheme
- d) Person effecting TDS
- e) Person effecting TCS
- f) Supplier of Online Information and Data Base Access / Retrieval Services (OIDAR)

GSTR 1 of any month has to be filed by 10th of the following month. It is prudent to note that GSTR 1 cannot be filed within 11th to 15th of the month.

Outward Taxable Supplies could be Business to Business (B2B) or Business to Consumer (B2C). In case of B2B supplies, invoice-wise details must be uploaded for all supplies. In case of B2C supplies, if the supplies are intra-state, consolidated details of all supplies need to be uploaded. If the supplies are inter-state, for the Invoices which are greater than Rs. 2,50,000, invoice-wise details need to be uploaded, for the Invoices which

are less than Rs. 2,50,000, state-wise details need to be uploaded.

The details of the Outward Taxable Supplies are made available electronically to all the recipients in Form GSTR 2A after the 10th of the following month. This gives the recipient the opportunity to accept or modify or propose necessary changes.

Post the changes, the recipients file the GSTR 2, which is the monthly return for all inward taxable supplies, by the 15th of the following month.

The changes are either accepted or rejected by the supplier and the amended details are reflected in GSTR 3/ GSTR 3B which is to be filed by the 20th of the following month.

A registered person may authorise an approved goods and services tax practitioner to furnish the details of outward supplies under section 37, the details of inward supplies under section 38 and the return under section 39 or section 44 or section 45 and to perform such other functions in such manner as may be prescribed.”

### Furnishing details of inward supplies [Section 38]

Section 38 of Central Goods & Services tax Act, 2017 mentions that the details of inward supplies (form GSTR 2), of goods / services / both, are required to be furnished by every registered person, including casual taxable person, but excluding:

- a) Input Service Distributor (ISD)
- b) Non-resident taxable person
- c) Person paying tax under composition scheme
- d) Person effecting TDS
- e) Person effecting TCS
- f) Supplier of Online Information and Data Base Access / Retrieval Services (OIDAR)

GSTR 2 of any month has to be filed within 11th to 15th of the following month.

GSTR 1 signifies the tax liability whilst GSTR 2 signifies the ITC availability.

The timelines can be summarised as under:

Return Form	Particulars	Frequency	Due Date
GSTR-1	Details of outward supplies of taxable goods and/or services affected	Monthly	11th of the next month with effect from October 2018  Previously, the due date was 10th
GSTR-2 Suspended	Details of inward supplies of taxable goods and/or services affected claiming the input tax credit.	Monthly	15th of the next month
GSTR-3 Suspended	Monthly return on the basis of finalization of details of outward supplies and inward supplies along with the payment of tax.	Monthly	20th of the next month

GSTR-3B	Simple Return in which summary of outward supplies along with Input Tax Credit is declared and payment of tax is affected by taxpayer	Monthly	20th of the next month
GSTR-4	Return for a taxpayer registered under the composition levy	Annually	30th April following the end of financial year
GSTR-5	Return for a Non-Resident foreign taxable person	Monthly	20th of the next month
GSTR-6	Return for an Input Service Distributor	Monthly	13th of the next month
GSTR-7	Return for authorities deducting tax at source.	Monthly	10th of the next month
GSTR-8	Details of supplies effected through e-commerce operator and the amount of tax collected	Monthly	10th of the next month
GSTR-9	Annual Return for a Normal Taxpayer	Annually	31st December of next financial year
GSTR-9A	Annual Return for a taxpayer registered under the composition levy anytime during the year	Annually	31st December of next financial year
GSTR-10	Final Return	Once, when GST Registration is cancelled or surrendered	Within three months of the date of cancellation or date of cancellation order, whichever is later.
GSTR-11	Details of inward supplies to be furnished by a person having UIN and claiming a refund	Monthly	28th of the month following the month for which statement is filed

## Notes:

1. Due dates are subject to changes by Notifications/ Orders.
2. Filing of GSTR-2 and GSTR-3 has been postponed till further announcement.
3. Entities with an annual aggregate turnover of less than Rs.1.5 crores have been given an option to file quarterly GSTR-1 returns.
4. Notification No. 32/2018- Central Tax has extended the due date of filing GSTR 1 for registered persons having aggregate turnover of more than Rs. 1.5 crore in the preceding financial year or the current financial year for each of the months from July, 2018 to March, 2019 till the eleventh day of the month succeeding such month. Further Notification No. 12/2019 – Central Tax has extended the due date of filing GSTR 1 for registered persons having aggregate turnover of more than 1.5 crore rupees in the preceding financial year or the current financial year, for each of the months from April, 2019 to June, 2019 till the eleventh day of the month succeeding such month.

5. The revised due dates of GSTR 9 & GSTR 9A is now 30th June 2019 for the financial year 2017-18.
6. Notification No.21 /2019 – Central Tax dated 23rd April, 2019
  - Notifies the registered persons paying tax under the provisions of section 10 of the CGST Act or by availing the benefit of notification No. 02/2019– Central Tax (Rate), dated the 7th March, 2019, as the class of registered persons who shall follow the special procedure for furnishing of return and payment of tax
  - Quarterly Statement in form GST CMP-08 by 18th of the month succeeding such quarter, for payment of self assessed tax
  - Annual Return in GSTR-4 by 30th April following the end of such financial year
7. All tax payers filing returns GSTR 1 to GSTR 3 are required to file an annual return. The following are not required to do so:
  - a) Casual taxable persons
  - b) Non-Resident taxable persons
  - c) Input Service Distributor
  - d) Persons effecting TDS / TCS

### Matching

The process of ITC matching begins after the due dates for filing the return that is 20th. This is carried out by the portal, GSTN. The details of every inward supply per return filed by recipient vide GSTR 2 is matched with the outward taxable supplies' return filed by supplier vide GSTR 1. Once the details match, the ITC claimed by the recipient is considered valid. Failure to deposit the tax immediately by the taxable person by the due date OR failure to file valid return within time therefore can deny the recipient his timely ITC. Excess ITC claimed is added back to the tax liability of the recipient in the following month.

The concept of revised returns is not provided in the GST return rules and accordingly, the businesses would have to avail and re-avail, the mismatched credit by way of credit notes, debit notes, and supplementary invoices. The return rules have prescribed different forms to be filled by a registered person.

### PAYMENTS

As India is moving towards digitisation, GST have provided an easy and simple way of payment of taxes. Under GST regime, all the taxpayers get three electronic ledgers namely E-cash Ledger, E-credit Ledger & E-liability Ledger through their GST profile.

The Electronic Cash Ledger contains a summary of all payments made by a taxpayer. This ledger is maintained on the GST Portal.

The electronic cash ledger under sub-section (1) of section 49 shall be maintained in FORM GST PMT-05 for each person, liable to pay tax, interest, penalty, late fee or any other amount, on the Common Portal for crediting the amount deposited and debiting the payment there from towards tax, interest, penalty, fee or any other amount.

Thus, payment can be made in cash by debiting the e-cash ledger maintained on the common portal. Money can be deposited in the Cash Ledger by different modes, namely, E-Payment (Internet Banking, Credit Card, Debit Card); Real Time Gross Settlement (RTGS)/ National Electronic Fund Transfer (NEFT); Over the Counter Payment in branches of Banks Authorized (for deposits upto ten thousand rupees per challan per tax period, by cash, cheque or demand draft) to accept deposit of GST.

A challan in FORM GST PMT-06 is required to be generated and the details of the amount to be deposited towards tax, interest, penalty, fees or any other amount will be entered in the challan. Challan in FORM GST PMT-06 generated at the Common Portal shall be valid for a period of fifteen days. On successful credit of the amount in the Central / State Government account, a Challan Identification Number (CIN) is generated by the collecting bank, which will be indicated on the challan. This amount will then be credited to the Electronic Cash Ledger of the taxable person and on receipt of the CIN from the collecting bank, this amount will then stand credited to the electronic cash ledger of the person on whose behalf the payment was deposited to the credit of the Government. The amount available under any head in the Electronic Cash Ledger (SGST / CGST / IGST) cannot be utilised for discharging the liability under any other head.

Manual Challans are not allowed under the GST Regime and thus, it is mandatory to create the challans online on the GST portal.

### **Payment of tax, interest, penalty and other amounts [Section 49]**

(1) Every deposit made towards tax, interest, penalty, fee or any other amount by a person by internet banking or by using credit or debit cards or National Electronic Fund Transfer or Real Time Gross Settlement or by such other mode and subject to such conditions and restrictions as may be prescribed, shall be credited to the electronic cash ledger of such person to be maintained in such manner as may be prescribed.

(2) The input tax credit as self-assessed in the return of a registered person shall be credited to his electronic credit ledger, in accordance with section 41 or section 43A, to be maintained in such manner as may be prescribed.

(3) The amount available in the electronic cash ledger may be used for making any payment towards tax, interest, penalty, fees or any other amount payable under the provisions of this Act or the rules made thereunder in such manner and subject to such conditions and within such time as may be prescribed.

(4) The amount available in the electronic credit ledger may be used for making any payment towards output tax under this Act or under the Integrated Goods and Services Tax Act in such manner and subject to such conditions and within such time as may be prescribed.

(5) The amount of input tax credit available in the electronic credit ledger of the registered person on account of –

- (a) integrated tax shall first be utilised towards payment of integrated tax and the amount remaining, if any, may be utilised towards the payment of central tax and State tax, or as the case may be, Union territory tax, in that order;
- (b) the central tax shall first be utilised towards payment of central tax and the amount remaining, if any, may be utilised towards the payment of integrated tax;
- (c) the State tax shall first be utilised towards payment of State tax and the amount remaining, if any, may be utilised towards payment of integrated tax;

Provided that the input tax credit on account of State tax shall be utilised towards payment of integrated tax only where the balance of the input tax credit on account of central tax is not available for payment of integrated tax

- (d) the Union territory tax shall first be utilised towards payment of Union territory tax and the amount remaining, if any, may be utilised towards payment of integrated tax;

Provided that the input tax credit on account of Union territory tax shall be utilised towards payment of integrated tax only where the balance of the input tax credit on account of central tax is not available for payment of integrated tax

- (e) the central tax shall not be utilised towards payment of State tax or Union territory tax; and

(f) the State tax or Union territory tax shall not be utilised towards payment of central tax.

**Utilisation of input tax credit subject to certain conditions [Section 49A]**

Notwithstanding anything contained in section 49, the input tax credit on account of central tax, State tax or Union territory tax shall be utilised towards payment of integrated tax, central tax, State tax or Union territory tax, as the case may be, only after the input tax credit available on account of integrated tax has first been utilized fully towards such payment.

**Powers Assumed by the Government to Notify Order of Utilization of Input Tax Credit [Section 49B]**

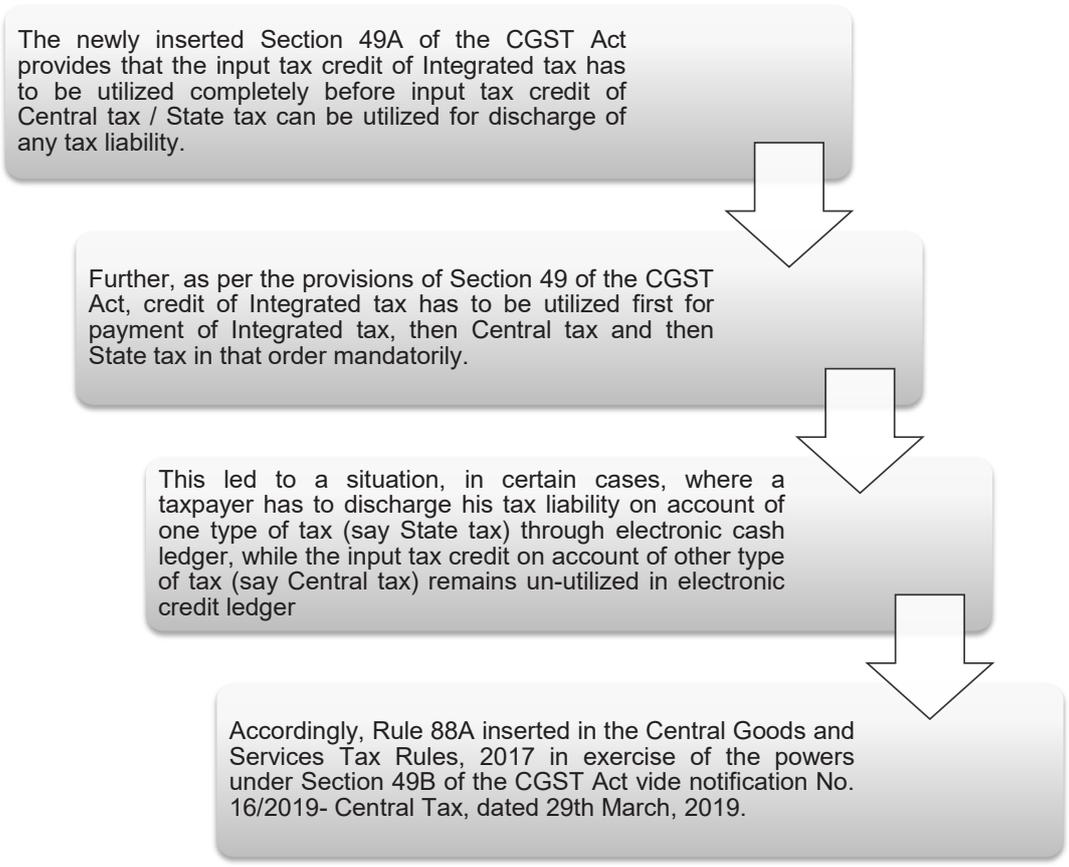
Notwithstanding anything contained in this Chapter and subject to the provisions of clause (e) and clause (f) of sub-section (5) of section 49, the Government may, on the recommendations of the Council, prescribe the order and manner of utilisation of the input tax credit on account of integrated tax, central tax, State tax or Union territory tax, as the case may be, towards payment of any such tax.

**Analysis**

The payments to be made are as under:

- a) For the intra-state supplies, CGST + SGST to be paid in equal proportions
- b) For the inter-state supplies, IGST to be paid

Input Tax Credit as self-assessed vide the monthly returns will be reflected in the Electronic Credit Ledger.



The newly inserted rule 88A in the CGST Rules allows utilization of input tax credit of Integrated tax towards the payment of Central tax and State tax, or as the case may be, Union territory tax, in any order subject to the condition that the entire input tax credit on account of Integrated tax is completely exhausted first before the input tax credit on account of Central tax or State / Union territory tax can be utilized.

To further clarify the utilization mechanism, the Government has issued Circular No. 98/17/2019-GST, dated 23-4-2019, which clarifies the revised position as under;

Input tax credit on account of	Output liability on account of Integrated tax	Output liability on account of Central tax	Output liability on account of State tax/ Union Territory tax
<b>Integrated tax</b>	(I)	(II) – In any order and in any proportion	
(III) Input tax credit on account of Integrated tax to be completed exhausted mandatorily			
<b>Central tax</b>	(V)	(IV)	Not permitted
<b>State tax/ Union Territory tax</b>	(VII)	Not permitted	(VI)

There is no offset available between the CGST and the SGST/ UTGST.

Section 49 also talks of the third type of ledger, called the Electronic Liability Ledger. This is basically a control ledger which sums up all the liabilities of the taxable person in a separate register.

The chronological order of discharge of liabilities of a taxable person would be:

- i. Self-assessed tax and other dues for the previous tax periods will be discharged first
- ii. Self-assessed tax and other dues for the current tax periods will be discharged next
- iii. Post which the amount payable under demand would be extinguished last

Interest is payable when

- i. There is a delay in payment of tax in part or in full within the prescribed period
- ii. There is undue or excess claim of ITC
- iii. There is undue or excess reduction of Output Tax Liability

The rate of interest would be as notified by the Central Government which shall not exceed 18% in case of delay in payment of tax and 24% in the remaining two scenarios. The period of interest will be from the date following the due date of payment until the date of actual payment of tax.

## **PAYMENT RULES [CHAPTER IX]**

### **Electronic Liability Register [Rule 85]**

- (1) The electronic liability register specified under sub-section (7) of section 49 shall be maintained in FORM GST PMT-01 for each person liable to pay tax, interest, penalty, late fee or any other amount on the Common Portal and all amounts payable by him shall be debited to the said register.
- (2) The electronic tax liability register of the person shall be debited by:-
  - (a) the amount payable towards tax, interest, late fee or any other amount payable as per the return

- furnished by the said person;
- (b) the amount of tax, interest, penalty or any other amount payable as determined by a proper officer in pursuance of any proceedings under the Act or as ascertained by the said person;
  - (c) the amount of tax and interest payable as a result of mismatch under section 42 or section 43 or section 50; or
  - (d) any amount of interest that may accrue from time to time.
- (3) Subject to the provisions of section 49, section 49A and section 49B payment of every liability by a registered person as per his return shall be made by debiting the electronic credit ledger maintained as per rule 86 or the electronic cash ledger maintained as per rule 87 and the electronic tax liability register shall be credited accordingly.
  - (4) The amount deducted under section 51, or the amount collected under section 52, or the amount payable under sub-section (3) or sub-section (4) of section 9, or the amount payable under section 10, or sub-section (3) or sub-section (4) of section 5 of the Integrated Goods and Services Act or sub-section (3) or sub-section (4) of section 7 of the Union Territory Goods and Services Tax Act any amount payable towards interest, penalty, fee or any other amount under the Act or the Integrated Goods and Services Act shall be paid by debiting the electronic cash ledger maintained as per rule 87 and the electronic tax liability register shall be credited accordingly.
  - (5) Any amount of demand debited in the electronic tax liability register shall stand reduced to the extent of relief given by the appellate authority or Appellate Tribunal or court and the electronic tax liability register shall be credited accordingly.
  - (6) The amount of penalty imposed or liable to be imposed shall stand reduced partly or fully, as the case may be, if the taxable person makes the payment of tax, interest and penalty specified in the show cause notice or demand order and the electronic tax liability register shall be credited accordingly.
  - (7) A registered person shall, upon noticing any discrepancy in his electronic liability ledger, communicate the same to the officer exercising jurisdiction in the matter, through the common portal in FORM GST PMT-04.

### Electronic Credit Ledger [Rule 86]

- (1) The electronic credit ledger shall be maintained in FORM GST PMT-02 for each registered person eligible for input tax credit under the Act on the Common Portal and every claim of input tax credit under the Act shall be credited to the said Ledger.
- (2) The electronic credit ledger shall be debited to the extent of discharge of any liability in accordance with section 49 or section 49A or section 49B.
- (3) Where a registered person has claimed refund of any unutilized amount from the electronic credit ledger in accordance with the provisions of section 54, the amount to the extent of the claim shall be debited in the said ledger.
- (4) If the refund so filed is rejected, either fully or partly, the amount debited under sub rule (3), to the extent of rejection, shall be re-credited to the electronic credit ledger by the proper officer by an order made in FORM GST PMT-03.
- (5) Save as provided in these rules, no entry shall be made directly in the electronic credit ledger under any circumstance.
- (6) A registered person shall, upon noticing any discrepancy in his electronic credit ledger, communicate

the same to the officer exercising jurisdiction in the matter, through the Common Portal in FORM GST PMT-04.

*Explanation.*— For the purposes of this rule, it is hereby clarified that a refund shall be deemed to be rejected, if the appeal is finally rejected or if the claimant gives an undertaking to the proper officer that he shall not file an appeal.

### **Conditions of use of amount available in electronic credit ledger [Rule 86A]**

Vide Notification No. 75/2019-C.T. dated 26.12.2019, the Government has inserted Rule 86A in the CGST Rules, 2017 which empowers GST officers to block utilization input tax credit in certain scenarios as below.

(1) The Commissioner or an officer authorised by him in this behalf, not below the rank of an Assistant Commissioner, having reasons to believe that credit of input tax available in the electronic credit ledger has been fraudulently availed or is ineligible in as much as-

- a) the credit of input tax has been availed on the strength of tax invoices or debit notes or any other document prescribed under rule 36-
  - i. issued by a registered person who has been found non-existent or not to be conducting any business from any place for which registration has been obtained; or
  - ii. without receipt of goods or services or both; or
- b) the credit of input tax has been availed on the strength of tax invoices or debit notes or any other document prescribed under rule 36 in respect of any supply, the tax charged in respect of which has not been paid to the Government; or
- c) the registered person availing the credit of input tax has been found non-existent or not to be conducting any business from any place for which registration has been obtained; or
- d) the registered person availing any credit of input tax is not in possession of a tax invoice or debit note or any other document prescribed under rule 36,
 

may, for reasons to be recorded in writing, not allow debit of an amount equivalent to such credit in electronic credit ledger for discharge of any liability under section 49 or for claim of any refund of any unutilised amount.

(2) The Commissioner, or the officer authorised by him under sub-rule (1) may, upon being satisfied that conditions for disallowing debit of electronic credit ledger as above, no longer exist, allow such debit.

(3) Such restriction shall cease to have effect after the expiry of a period of one year from the date of imposing such restriction.”.

### **Electronic Cash Ledger [Rule 87]**

- (1) The electronic cash ledger under sub-section (1) of section 49 shall be maintained in FORM GST PMT-05 for each person, liable to pay tax, interest, penalty, late fee or any other amount, on the Common Portal for crediting the amount deposited and debiting the payment therefrom towards tax, interest, penalty, fee or any other amount.
- (2) Any person, or a person on his behalf, shall generate a challan in FORM GST PMT-06 on the Common Portal and enter the details of the amount to be deposited by him towards tax, interest, penalty, fees or any other amount.

Provided that the challan in FORM GST PMT-06 generated at the common portal shall be valid for a period of fifteen days.

Provided further that a person supplying online information and database access or retrieval services from a place outside India to a non-taxable online recipient referred to in section 14 of the Integrated Goods and Services Tax Act, 2017 (13 of 2017) may also do so through the Board's payment system namely, Electronic Accounting System in Excise and Service Tax from the date to be notified by the Board.

- (3) The deposit under sub-rule (2) shall be made through any of the following modes:
- (i) Internet Banking through authorized banks;
  - (ii) Credit card or Debit card through the authorised bank;
  - (iii) National Electronic Fund Transfer (NEFT) or Real Time Gross Settlement (RTGS) from any bank;
  - (iv) Over the Counter payment (OTC) through authorized banks for deposits up to ten thousand rupees per challan per tax period, by cash, cheque or demand draft.

Provided that the restriction for deposit up to ten thousand rupees per challan in case of an Over the Counter (OTC) payment shall not apply to deposit to be made by – (a) Government Departments or any other deposit to be made by persons as may be notified by the Commissioner in this behalf; (b) Proper officer or any other officer authorised to recover outstanding dues from any person, whether registered or not, including recovery made through attachment or sale of movable or immovable properties; (c) Proper officer or any other officer authorized for the amounts collected by way of cash, cheque or demand draft during any investigation or enforcement activity or any ad hoc deposit:

Provided further that a person supplying online information and database access or retrieval services from a place outside India to a non-taxable online recipient referred to in section 14 of the Integrated Goods and Services Tax Act, 2017 (13 of 2017) may also make the deposit under sub-rule (2) through international money transfer through Society for Worldwide Interbank Financial Telecommunication payment network, from the date to be notified by the Board.

*Explanation.*– For the purposes of this sub-rule, it is hereby clarified that for making payment of any amount indicated in the challan, the commission, if any, payable in respect of such payment shall be borne by the person making such payment.

- (4) Any payment required to be made by a person who is not registered under the Act, shall be made on the basis of a temporary identification number generated through the Common Portal.
- (5) Where the payment is made by way of NEFT or RTGS mode from any bank, the mandate form shall be generated along with the challan on the Common Portal and the same shall be submitted to the bank from where the payment is to be made:

Provided that the mandate form shall be valid for a period of fifteen days from the date of generation of challan.

- (6) On successful credit of the amount to the concerned government account maintained in the authorised bank, a Challan Identification Number (CIN) will be generated by the collecting Bank and the same shall be indicated in the challan.
- (7) On receipt of CIN from the authorized Bank, the said amount shall be credited to the electronic cash ledger of the person on whose behalf the deposit has been made and the Common Portal shall make available a receipt to this effect.
- (8) Where the bank account of the person concerned, or the person making the deposit on his behalf, is debited but no Challan Identification Number (CIN) is generated or generated but not communicated to the Common Portal, the said person may represent electronically in FORM GST PMT-07 through the Common Portal to the Bank or electronic gateway through which the deposit was initiated.

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- (9) Any amount deducted under section 51 or collected under section 52 and claimed in FORM GSTR-02 by the registered taxable person from whom the said amount was deducted or, as the case may be, collected shall be credited to his electronic cash ledger in accordance with the provisions of rule 87.
- (10) Where a person has claimed refund of any amount from the electronic cash ledger, the said amount shall be debited to the electronic cash ledger.
- (11) If the refund so claimed is rejected, either fully or partly, the amount debited under sub rule (10), to the extent of rejection, shall be credited to the electronic cash ledger by the proper officer by an order made in FORM GST PMT-03.
- (12) A registered person shall, upon noticing any discrepancy in his electronic cash ledger, communicate the same to the officer exercising jurisdiction in the matter, through the common portal in FORM GST PMT-04.

*Explanation 1* - The refund shall be deemed to be rejected if the appeal is finally rejected.

*Explanation 2* – For the purposes of this rule, it is hereby clarified that a refund shall be deemed to be rejected, if the appeal is finally rejected or if the claimant gives an undertaking to the proper officer that he shall not file an appeal.

### Identification number for each transaction [Rule 88]

- (1) A unique identification number shall be generated at the Common Portal for each debit or credit to the electronic cash or credit ledger, as the case may be.
- (2) The unique identification number relating to discharge of any liability shall be indicated in the corresponding entry in the electronic tax liability register.
- (3) A unique identification number shall be generated at the Common Portal for each credit in the electronic tax liability register for reasons other than those covered under sub-rule (2).

## REFUNDS

Refund refers to an amount that is due to the tax payer from the tax administration.

### Refund of tax [Section 54]

According to section 54 of the CGST Act, 2017, any person claiming refund of any tax and interest, if any, paid on such tax or any other amount paid by him, may make an application before the expiry of two years from the relevant date. If there is any balance in the electronic cash ledger or electronic credit ledger after payment of tax, interest, penalty, fee or any other amount payable may claim such refund in the return furnished under section 39.

A specialised agency of the United Nations Organisation or any Multilateral Financial Institution and Organisation notified under the United Nations (Privileges and Immunities) Act, 1947, Consulate or Embassy of foreign countries or any other person or class of persons, as notified under Section 55, entitled to a refund of tax paid by it on inward supplies of goods or services or both, may make an application for such refund, in such form and manner as may be prescribed, before the expiry of six months from the last day of the quarter in which such supply was received.

However, vide Notification No. 20/2018-C.T., dated 28-3-2018, in exercise of the powers conferred by section 148 of the said Act, the Central Government, has allowed the persons notified under Section 55 to file refund application before the expiry of eighteen months from the last date of the quarter in which such supply was received.

### Refund of unutilised input tax credit

Section 54(3) of CGST Act, 2017 states that, subject to the provisions of section 54(10), a registered person may claim refund of any unutilised input tax credit at the end of any tax period, subject to provisions under the section in the following cases :

- (i) zero rated supplies made without payment of tax;
- (ii) where the credit has accumulated on account of rate of tax on inputs being higher than the rate of tax on output supplies (other than nil rated or fully exempt supplies)

However, refund of unutilized input tax credit shall not be allowed in the following cases :

- (i) where the goods exported out of India are subjected to export duty;
- (ii) if the supplier of goods or services or both avails of drawback in respect of central tax or claims refund of the integrated tax paid on such supplies.

Section 54(4), (5) & (7) mandate that after receipt of the application or declaration as the case may be, if the proper officer is satisfied that the whole or part of the amount claimed as refund is refundable, he may make an order within sixty days from the date of receipt of application and the amount so determined shall be credited to the Consumer Welfare Fund. However, the refundable amount shall, instead of being credited to the Fund, be paid to the applicant, if such amount is relatable to –

- a. refund of tax paid on export of goods or services or both or on inputs or input services used in making such export;
- b. refund of unutilised input tax credit under sub-section (3);
- c. refund of tax paid on a supply which is not provided, either wholly or partially, and for which invoice has not been issued, or where a refund voucher has been issued;
- d. refund of tax in pursuance of section 77;
- e. the tax and interest, if any, or any other amount paid by the applicant, if he had not passed on the incidence of such tax and interest to any other person; or
- f. the tax or interest borne by such other class of applicants as the Government may, on the recommendations of the Council, by notification, specify.

### Refund of taxes to the retail outlets established in departure area of an international Airport beyond immigration counters making tax free supply to an outgoing international tourist (Rule 95A of CGST Rules)

Retail outlet established in departure area of an international airport, beyond the immigration counters, supplying indigenous goods to an outgoing international tourist who is leaving India shall be eligible to claim refund of tax paid by it on inward supply of such goods. The refund of tax paid by the said retail outlet shall be available if-

- (a) the inward supplies of goods were received by the said retail outlet from a registered person against a tax invoice;
- (b) the said goods were supplied by the said retail outlet to an outgoing international tourist against foreign exchange without charging any tax;
- (c) name and Goods and Services Tax Identification Number of the retail outlet is mentioned in the tax invoice for the inward supply; and
- (d) such other restrictions or conditions, as may be specified, are satisfied

### Interest on delayed refunds [Section 56]

Section 56 of the CGST Act, 2017 states that if any tax ordered to be refunded under section 54 is not refunded within sixty days from the date of receipt of application interest at such rate not exceeding six per cent as may be specified in the notification issued by the Government on the recommendations of the Council shall be payable in respect of such refund from the date immediately after the expiry of sixty days from the date of receipt of application under the said sub-section till the date of refund of such tax.

Where any claim of refund arises from an order passed by an adjudicating authority or Appellate Authority or Appellate Tribunal or court which has attained finality and the same is not refunded within sixty days from the date of receipt of application filed consequent to such order, interest at such rate not exceeding nine per cent as may be notified by the Government on the recommendations of the Council shall be payable in respect of such refund from the date immediately after the expiry of sixty days from the date of receipt of application till the date of refund. Where any order of refund is made by an Appellate Authority, Appellate Tribunal or any court against an order of the proper officer under subsection (5) of section 54, the order passed by the Appellate Authority, Appellate Tribunal or by the court shall be deemed to be an order passed under the said sub-section (5). However, the refundable amount shall, instead of being credited to the Fund, be paid to the applicant, if such amount is relatable to –

- a. refund of tax paid on export of goods or services or both or on inputs or input services used in making such export;
- b. refund of unutilised input tax credit under sub-section (3);
- c. refund of tax paid on a supply which is not provided, either wholly or partially, and for which invoice has not been issued, or where a refund voucher has been issued;
- d. refund of tax in pursuance of section 77;
- e. the tax and interest, if any, or any other amount paid by the applicant, if he had not passed on the incidence of such tax and interest to any other person; or
- f. the tax or interest borne by such other class of applicants as the Government may, on the recommendations of the Council, by notification, specify.

### Refund of taxes to the retail outlets established in departure area of an international Airport beyond immigration counters making tax free supply to an outgoing international tourist (Rule 95A of CGST Rules)

Retail outlet established in departure area of an international airport, beyond the immigration counters, supplying indigenous goods to an outgoing international tourist who is leaving India shall be eligible to claim refund of tax paid by it on inward supply of such goods. The refund of tax paid by the said retail outlet shall be available if-

- (a) the inward supplies of goods were received by the said retail outlet from a registered person against a tax invoice;
- (b) the said goods were supplied by the said retail outlet to an outgoing international tourist against foreign exchange without charging any tax;
- (c) name and Goods and Services Tax Identification Number of the retail outlet is mentioned in the tax invoice for the inward supply; and
- (d) such other restrictions or conditions, as may be specified, are satisfied.

Refund may be claimed in following situations :

- Goods / Services / both are exported / supplied to a SEZ on payment of IGST and a refund of such IGST so paid is claimed;
- Refund claim for accumulated unutilised ITC, in case of supplies to a SEZ / exports of goods / services/ both;
- Refund claim for accumulated unutilised ITC, in case of supplies on account of an inverted duty structure ;
- Refund of any balance in the electronic cash ledger after payment of tax / interest / penalty; and
- On finalization of provisional assessment if tax becomes refundable to the assesseees.

No Refund shall be allowed if :

- The goods so exported are subject to export duty.
- The supplier of goods / services / both has lodged in parallel a duty drawback claims in respect of IGST on the inward imported supplies.

### Time limit

Any person claiming a refund of tax / interest / may make an application before expiry of 2 years from the “Relevant Date”. However, a person claiming a refund of unutilised ITC in case of zero rated supplies, or accumulated ITC in case of inverted duty structures may do so at the end of any tax period.

### Relevant Date

- Where goods are exported by air / sea
  - o Date on which the vessel leaves India
- When goods are exported by land
  - o Date on which the goods pass the frontiers
- When refund of unutilised ITC in case of zero rated supplies, or accumulated ITC in case of inverted duty structures is claimed
  - o End of the Financial Year in which such claim for refund arises
- In case of refund arising out of finalisation of provisional assessment
  - o Date of adjustment of tax after the final assessment
- Any other case
  - o Date of payment of tax

### Application for Refund

Section 54 states that any person claiming a refund may file an application in form GST-RFD-01 electronically through the GST portal.

In case of advance tax deposits made by a casual taxable person OR a non-resident taxable person, the same shall be refunded only when such person has, in respect of the entire period for which the certificate of registration granted was in force, filed all the returns under Section 39. Also, the advance tax so paid, after adjusting any liability shall be claimed in the last return so filed.

### Documentation and Declaration

The refund application must be accompanied with the necessary documentation. Additionally, where the amount of refund claimed doesn't exceed INR 200,000, the refund application must be accompanied with a declaration that the incidence of tax has not been passed on to any other person and that therefore there wouldn't be unjust enrichment.

However, where the amount of refund claimed is greater than INR 200,000, a certificate as a part of Form GST-RFD-01 by a Chartered Accountant or a Cost Accountant to the effect that there is no unjust enrichment and that the tax incidence has not been passed on to any other person, would be required to be submitted along with the refund application.

### Refund Amount

Rule 89 (4) states that in the case of zero-rated supply of goods or services or both without payment of tax under bond or letter of undertaking in accordance with the provisions of sub-section (3) of section 16 of the Integrated Goods and Services Tax Act, 2017, refund of input tax credit shall be granted as per the formula mentioned thereby.

Rule 89(5) states that in case of inverted duty structure supplies of goods / services / both; refund of tax would be granted proportionately, i.e., as per the formula mentioned therein.

### Refund Order

The refund order should be made by the proper officer within 60 days from date of receipt of application, which is complete in all respects.

Where the proper officer is satisfied that amount so refundable is payable to an applicant, he shall make an order in form GST-RFD-06 and the same will then be credited to the account of the applicant.

Where the proper officer is satisfied that amount so refundable is not payable to any applicant per se, he shall make an order in form GST-RFD-06 and the same will then be credited to the Consumer Welfare Fund.

### Interest

Where any tax ordered to be refunded under Section 54, is not refunded to the applicant within 60 days from the date of receipt of application, interest shall be payable to the applicant at the rate of 6% p.a. and the same shall be payable immediately on expiry of 60 days and until the date of refund.

Also, where the refund arises out of an appeal, and the same is not refunded within 60 days from date of receipt of application, interest shall be payable at the rate of 9% p.a., and the same shall be payable immediately on expiry of 60 days and until the date of refund.

## AUDIT

Audit under Goods & Services Tax can be of two types, as discussed under.

### General Audit [Section 65]

Section 65 of Central Goods & Services Tax Act, 2017 states that the Commissioner or any officer so authorised by him, by way of a general or specific order, may undertake the audit of any registered person, at the place of business of such registered person or in their office for a Financial Year or multiples thereof.

### Timelines

A notice of 15 days is required to be given prior to the conduct of the audit, by the proper officer, where it is decided to undertake the audit of a registered person. Commencement of audit would mean later of:

- o Date on which the accounts / records that have been called for inspection / verification, have been made available to them
- o The actual institution of the audit at the place of business of tax payer

The audit is required to be completed within 3 months from the date of commencement of such audit. This period is extendable for another 6 months (maximum) by the Commissioner

### **Procedure**

The proper officer so authorised to conduct the audit, shall with the assistance of the team members assigned to him, verify all the necessary accounts / books / records.

During the course of the audit, the authorised officer may require the registered person, to facilitate the verification of accounts / books / records or to provide such information / details, as the authorities may require for a complete and timely conduct of audit.

The proper officer will then inform the registered person of the discrepancies noticed, and his audit observations to which the registered person will respond to with his factual details, and post which the audit findings will be finalised after evaluation of these responses to the observations.

### **Finalisation**

The proper officer shall within 30 days, informs the registered person, whose accounts and records are being audited, about the findings.

## **Special Audit [Section 66]**

Section 66 of Central Goods & Services Tax Act, 2017 states that where any officer not below the rank of Assistant Commissioner having regard to the complexity of the case and in the interest of revenue, is of the opinion that the liability has not been correctly declared or the Input Tax Credit is availed in excess, he may, with prior approval from Commissioner, issue a direction to the registered person to get his accounts / records audited by a Chartered Accountant / Cost Accountant, as nominated by the Commissioner.

### **Timelines**

The Chartered Accountant / Cost Accountant as nominated by the Commissioner shall submit an audit report duly signed and certified by himself, within 90 days from the date of commencement of such audit, to the Assistant Commissioner. This period is extendable for another 90 days (maximum) by the Assistant Commissioner on reasonable and sufficient grounds upon application.

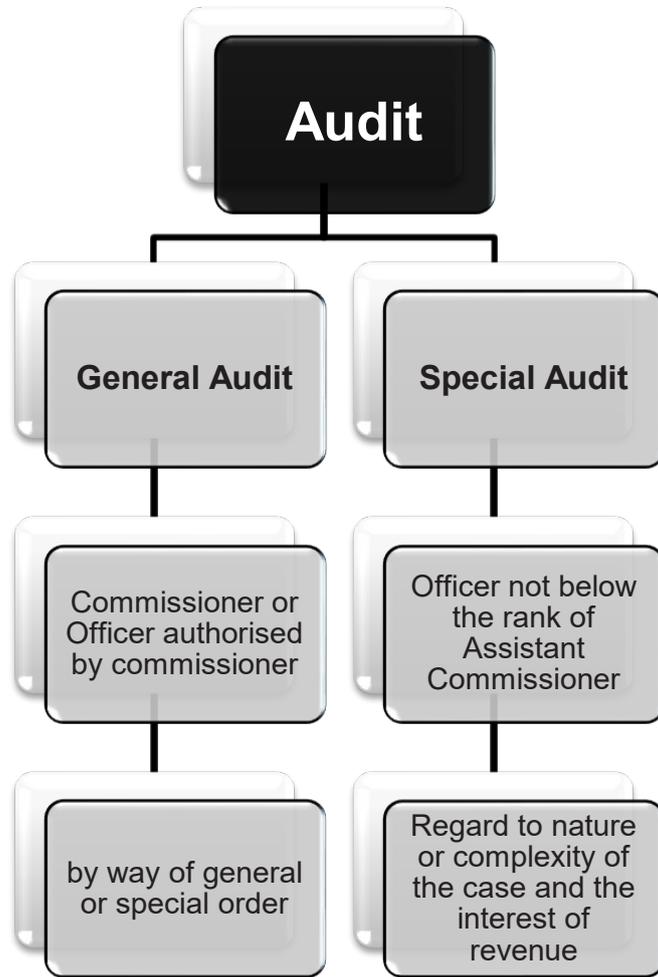
### **Procedure**

The expenses of the audit / examination and the remuneration to the Chartered Accountant / Cost Accountant shall be determined and paid by Commissioner.

### **Finalisation**

The proper officer will then inform the registered person of the discrepancies noticed, and his audit findings of special audit. Where the special audit results in detection of tax not paid / short paid / credit availed in excess, the process of demand / recovery under Section 73, 74 of Central Goods & Services Tax Act, 2017, will be initiated.

Thus, Audit under Goods & Services Tax may be summarised as under:



### LESSON ROUND UP

- Under GST, return filing is linked to the payment of tax
- Without filing pending returns, current returns cannot be filed
- E Way Bill system has been introduced under GST
- Requirements and exemptions from Registration under GST have been provided in the law
- A registered person is required to maintain prescribed Books of Accounts
- Any transaction under GST is vouched by various kinds of documents including Debit / Credit Notes, Tax Invoice, Bill of Supply and Delivery Challans
- Various monthly, quarterly and annual returns are filed under GST
- Payment options available under GST include NEFT, RTGS, net banking, debit/credit card
- Audit under GST is of two types- General and Special





# Lesson 16

## Basic Overview on IGST, UTGST and GST Compensation to States Act

### LESSON OUTLINE

- Integrated Goods and Services Tax Act, 2017
- Union Territory Goods and Services Tax Act, 2017
- Provisions relating to Advance Ruling
- GST Compensation to States
- Frequently Asked Questions
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

In India we have adopted dual GST Model in which States and Union Government impose tax simultaneously. Federal structure of the Constitution is also retained under this model. To ensure seamless flow of credit throughout the territory of India a link Act was necessary and hence IGST Act, 2017 was passed. Compensation to states for the loss due to introduction of GST is provided through an Act, GST (Compensation to States) Act, 2017.

At the end of this lesson you will be able to learn about –

- Provisions of IGST Act, 2017
- UTGST Act, 2017 and its working
- Provisions of GST (Compensation to State) Act, 2017

**INTRODUCTION TO IGST**

The Integrated Goods and Services Tax Act, 2017 [IGST] was passed by the Parliament for levy and collection of tax on inter-state supply of goods or services or both by the Central Government and for matters connected therewith or incidental thereto.

The Union Government presented the Integrated Goods and Service Tax Bill, 2017 in Lok Sabha and it was passed by the same on 29th March, 2017. The Rajya Sabha passed the bill on 6th April, 2017 and was assented to by the President on 12th April, 2017.

**INTEGRATED GOODS & SERVICES TAX ACT, 2017**

IGST is levied and collected by the Centre on inter-state supply of goods and/or services. Under Article 269A of the Constitution, IGST on supplies in the course of inter-state trade or commerce is levied and collected by the Government of India and such tax shall be apportioned between the Union and the States in the manner as may be provided by Parliament by law on the recommendations of the Goods and Services Tax Council. IGST paid is available as credit to set off against the payment of IGST, CGST and SGST on output supplies

Integrated Goods and Service Tax (IGST) means tax levied under the IGST Act on the supply of any goods and/or services in the course of inter-State trade or commerce. The IGST mechanism ensures that the tax money goes to the state where consumption takes place. IGST can be viewed as a smart-accounting mechanism serving a clearing house function in inter-state supplies to ensure that the tax money goes to the correct state.

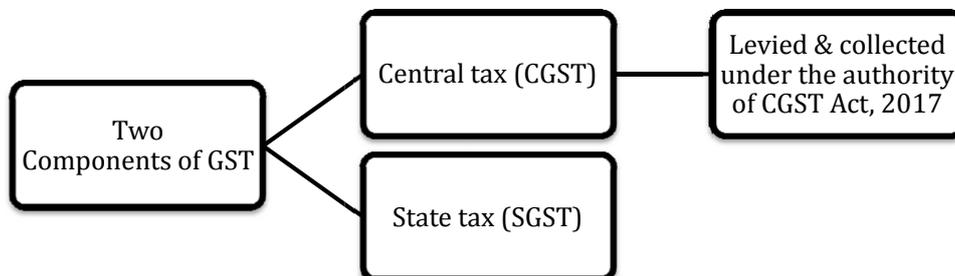
IGST (Integrated Goods & Services Tax) Act, 2017 deals with supplies interstate, import into India and supplies made outside India. The following table illustrates the same.

SUPPLY	TAX / TAXES
Intra state	CGST+ SGST
Intra UT	CGST+ UTGST
Interstate/ import/ SEZ	IGST

IGST is applicable all over India including the state of Jammu & Kashmir.

As per section 5 of IGST Act, 2017 a maximum rate of 40% may be imposed on interstate supply of goods and/or services.

A “Dual GST” model has been adopted in view of the federal structure of our country. Centre and States simultaneously levy GST on every supply of goods or services or both which, takes place within a State or Union Territory. Thus, there are two components of GST:



**Relevance of IGST**

Before discussing the IGST Model and its features, it is important to understand how inter state trade or commerce is being regulated in the present indirect tax system. It is significant to note that earlier the Central Sales Tax Act, 1956 regulated the inter-state trade or commerce (hereinafter referred to as “CST”), the authority

for which was constitutionally derived from Article 269 of the Constitution. Further, as per Article 286 of the Constitution of India, no State could levy sales tax on any sales or purchase of goods that took place outside the State or in the course of the import of the goods into, or export of the goods out of the territory of India. Only the Parliament could levy tax on such a transaction.

The Central Sales Tax Act was enacted in 1956 to formulate principles for determining when a sale or purchase of goods takes place in the course of inter-state trade or commerce. The Act also provided for the levy and collection of taxes on sales of goods in the course of inter-State trade. However, CST was collected and retained by the origin State, which was an aberration. Any indirect tax, by definition, is a consumption tax, the incidence of which, is borne by the consumer. Logically, the tax must accrue to the destination State having jurisdiction over the consumer.

Input Tax Credit (hereinafter referred to as ITC) of CST was not allowed to the buyer which, resulted in cascading of tax (tax on tax) in the supply chain.

Moreover, various accounting forms were required to be filed in CST viz., C Form, E1, E2, F, I, J Forms etc. which added to the compliance cost of the business and impeded the free flow of trade.

The IGST model was brought in to remove all such deficiencies. IGST is a mechanism to monitor the inter-State trade of goods and services and ensure that the SGST component accrues to the consumer State. It maintains the integrity of ITC chain in inter-State supplies. The IGST rate is broadly equal to CGST rate plus SGST rate. IGST would be levied by the Central Government on all inter-State transactions of taxable goods or services.

IGST rate= CGST rate + SGST rate

**Cross-utilisation of credit** requires the transfer of funds between respective accounts. The utilisation of credit of CGST & SGST for payment of IGST would require the transfer of funds to IGST accounts. Similarly, the utilisation of IGST credit for payment of CGST & SGST would necessitate the transfer of funds from IGST account.

The IGST payment can be done by utilising the ITC. The amount of ITC on account of IGST is allowed to be utilised towards the payment of IGST, CGST and SGST/UTGST.

It is very important to determine the nature of supply – whether it is inter-State or intrastate, as the kind of tax to be paid (IGST or CGST+SGST) depends on that.

**(i) Inter-State Supply**

Subject to the place of supply provisions, where the location of the supplier and the place of supply are in:

- (a) Two different States;
- (b) Two different Union Territories; or
- (c) A State and a Union Territory, such supplies shall be treated as the supply of goods or services in the course of inter-State trade or commerce. Any supply of goods or services in the taxable territory, not being an intra-State supply, shall be deemed to be a supply of goods or services in the course of inter-State trade or commerce.

Also, supplies to or by Special Economic Zones (SEZs) are defined as inter-State supply. Further, the supply of goods imported into the territory of India till they cross the customs frontiers of India or the supply of services imported into the territory of India shall be treated as supplies in the course of inter-State trade or commerce. Also, the supplies to international tourists are to be treated as inter-State supplies.

**Inter-State supply :**

Supply of goods from one State or Union Territory to another State or Union Territory

- Supply of services from one State or Union Territory to another State or Union Territory
- Import of goods till they cross customs frontier
- Import of services
- Export of goods or services
- Supply of goods/services to/by SEZ
- Supplies to international tourists
- Any other supply in the taxable territory which is not intra-State supply.

Thus, the nature of the supply depends on the location of the supplier and the place of supply.

- (ii) **Intra-State supply:** It has been defined as any supply where the location of the supplier and the place of supply are in the same State or Union Territory.

### Important Definitions

Section 2 of the IGST Act, 2017 contains the definitions of various terms used at several places in the Act. Some of the important definitions are reproduced as follows:

**Section 2(3) :** “continuous journey” means a journey for which a single or more than one ticket or invoice is issued at the same time, either by a single supplier of service or through an agent acting on behalf of more than one supplier of service, and which involves no stopover between any of the legs of the journey for which one or more separate tickets or invoices are issued.

*Explanation* – For the purposes of this clause, the term “stopover” means a place where a passenger can disembark either to transfer to another conveyance or break his journey for a certain period in order to resume it at a later point of time

**Section 2(5) :** “export of goods” with its grammatical variations and cognate expressions, means taking goods out of India to a place outside India

**Section 2(6) :** “export of services” means the supply of any service when, –

- (i) the supplier of service is located in India;
- (ii) the recipient of service is located outside India;
- (iii) the place of supply of service is outside India;
- (iv) the payment for such service has been received by the supplier of service in convertible foreign exchange or in Indian rupees wherever permitted by the Reserve Bank of India; and
- (v) the supplier of service and the recipient of service are not merely establishments of a distinct person in accordance with Explanation 1 in section 8

**Section 2(7) :** “fixed establishment” means a place (other than the registered place of business) which is characterised by a sufficient degree of permanence and suitable structure in terms of human and technical resources to supply services or to receive and use services for its own needs

**Section 2(10) :** “import of goods” with its grammatical variations and cognate expressions, means bringing goods into India from a place outside India

**Section 2(11) :** “import of services” means the supply of any service, where –

- (i) the supplier of service is located outside India;
- (ii) the recipient of service is located in India; and

(iii) the place of supply of service is in India

**Section 2(14)** : “location of the recipient of services” means,

- a) where a supply is received at a place of business for which the registration has been obtained, the location of such place of business;
- b) where a supply is received at a place other than the place of business for which registration has been obtained (a fixed establishment elsewhere), the location of such fixed establishment;
- c) where a supply is received at more than one establishment, whether the place of business or fixed establishment, the location of the establishment most directly concerned with the receipt of the supply; and
- d) in absence of such places, the location of the usual place of residence of the recipient;

**Section 2(15)**: “location of the supplier of services” means, –

- a) where a supply is made from a place of business for which the registration has been obtained, the location of such place of business;
- b) where a supply is made from a place other than the place of business for which registration has been obtained (a fixed establishment elsewhere), the location of such fixed establishment;
- c) where a supply is made from more than one establishment, whether the place of business or fixed establishment, the location of the establishment most directly concerned with the provision of the supply; and
- d) in absence of such places, the location of the usual place of residence of the supplier

**Section 2(16)** : “non-taxable online recipient” means any Government, local authority, governmental authority, an individual or any other person not registered and receiving online information and database access or retrieval services in relation to any purpose other than commerce, industry or any other business or profession, located in taxable territory.

*Explanation.* – For the purposes of this clause, the expression “governmental authority” means an authority or a board or any other body, –

- (i) set up by an Act of Parliament or a State Legislature; or
- (ii) established by any Government, with ninety per cent. or more participation by way of equity or control, to carry out any function entrusted to a Panchayat under article 243G or to a municipality under article 243W of the Constitution

**Section 2(19)** : “Special Economic Zone” shall have the same meaning as assigned to it in clause (za) of section 2 of the Special Economic Zones Act, 2005;

**Section 2(20)** : “Special Economic Zone developer” shall have the same meaning as assigned to it in clause (g) of section 2 of the Special Economic Zones Act, 2005 and includes an Authority as defined in clause (d) and a Co-Developer as defined in clause (f) of section 2 of the said Act;

**Section 2(21)** : “supply” shall have the same meaning as assigned to it in section 7 of the Central Goods and Services Tax Act;

**Section 2(22)** : “taxable territory” means the territory to which the provisions of this Act apply

## **Levy and Collection Under IGST, ACT 2017 [Section 5]**

(1) Subject to the provisions of sub-section (2), there shall be levied a tax called the integrated goods and services tax on all inter-State supplies of goods or services or both, except on the supply of alcoholic liquor for human consumption, on the value determined under section 15 of the Central Goods and Services Tax Act and

at such rates, not exceeding forty per cent., as may be notified by the Government on the recommendations of the Council and collected in such manner as may be prescribed and shall be paid by the taxable person.

Provided that the integrated tax on goods imported into India shall be levied and collected in accordance with the provisions of section 3 of the Customs Tariff Act, 1975 on the value as determined under the said Act at the point when duties of customs are levied on the said goods under section 12 of the Customs Act, 1962 (52 of 1962).

(2) The integrated tax on the supply of petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas and aviation turbine fuel shall be levied with effect from such date as may be notified by the Government on the recommendations of the Council.

(3) The Government may, on the recommendations of the Council, by notification, specify categories of supply of goods or services or both, the tax on which shall be paid on reverse charge basis by the recipient of such goods or services or both and all the provisions of this Act shall apply to such recipient as if he is the person liable for paying the tax in relation to the supply of such goods or services or both.

(4) The Government may, on the recommendations of the Council, by notification, specify a class of registered persons who shall, in respect of supply of specified categories of goods or services or both received from an unregistered supplier, pay the tax on reverse charge basis as the recipient of such supply of goods or services or both, and all the provisions of this Act shall apply to such recipient as if he is the person liable for paying the tax in relation to such supply of goods or services or both.

(5) The Government may, on the recommendations of the Council, by notification, specify categories of services, the tax on inter-State supplies of which shall be paid by the electronic commerce operator if such services are supplied through it, and all the provisions of this Act shall apply to such electronic commerce operator as if he is the supplier liable for paying the tax in relation to the supply of such services.

Provided that where an electronic commerce operator does not have a physical presence in the taxable territory, any person representing such electronic commerce operator for any purpose in the taxable territory shall be liable to pay tax.

Provided further that where an electronic commerce operator does not have a physical presence in the taxable territory and also does not have a representative in the said territory, such electronic commerce operator shall appoint a person in the taxable territory for the purpose of paying tax and such person shall be liable to pay tax.

Provisions for levy are similar for both under CGST & IGST Act. Section 15 of Central Goods & Services Act, 2017 is common to both the charges for valuation. CGST is for intrastate supply and IGST for interstate supply.

CGST rate is 20% maximum whereas under IGST it is 40%, because IGST is a combined tax of CGST +SGST. The following may be noted :

- (1) IGST is imposed on interstate supply
- (2) Value is as determined under Section 15 of CGST Act, 2017
- (3) Alcohol for human consumption is out of purview of IGST
- (4) The maximum rate of levy under IGST is 40%
- (5) Interstate supply includes imports
- (6) IGST is levied on imported goods under Section 3 of Customs Tariff Act
- (7) Such levy is simultaneous with the levy of Basic Customs Duty under section 12 of the Customs Act, 1962
- (8) Petroleum product items will be chargeable under IGST but at a later date to be recommended by the GST Council.

A supply would be treated as import or export, if certain conditions are satisfied as defined.

**Zero rated supply** : Exports and supplies to SEZs are considered as ‘zero rated supply’ on which no tax is payable. However, ITC is allowed, subject to such conditions, safeguards and procedure as may be prescribed, and refunds in respect of such supplies may be claimed by following either of these options:

- (i) Supply made without the payment of IGST under Bond/LUT and claim refund of unutilised ITC or
- (ii) Supply made on payment of IGST and claim refund of the same

**Refund of integrated tax paid on supply of goods to tourists leaving India** : Section 15 of the IGST Act, 2017 provides for refund of IGST paid to an international tourist leaving India on goods being taken outside India, subject to such conditions and safeguards as may be prescribed. An international tourist has been defined as a non-resident of India who enters India for a stay of less than 6 months. IGST would be charged on such supplies, similarly as in the course of export.

**The IGST Rules, 2017** were notified vide Notification No. 4 /2017-Integrated Tax dated 28th June 2017 and further as amended by Notification No. 12/2017-Integrated Tax, dated 15th November, 2017 and Notification No. 04/2018 – Integrated Tax, dated 31st December, 2018.

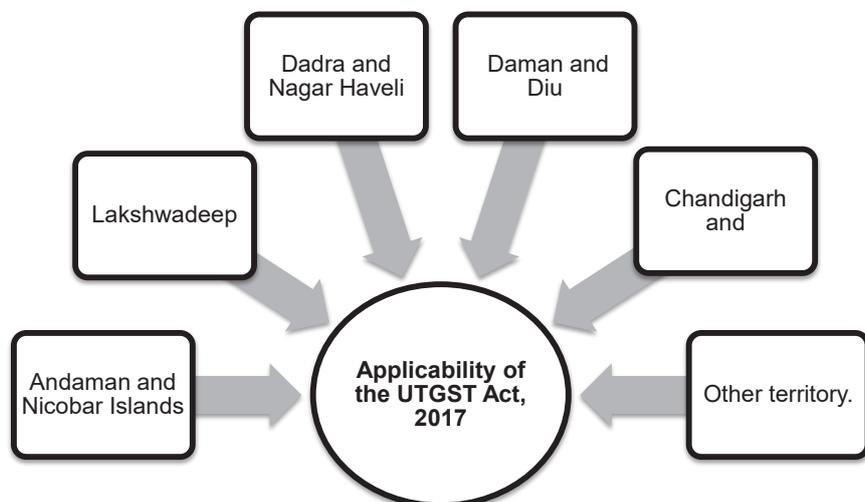
Rule 2 of IGST Rules, 2017 lay down that the Central Goods and Services Tax Rules, 2017, for carrying out the provisions specified in Section 20 of the Integrated Goods and Services Tax Act, 2017 shall, so far as may be, apply in relation to integrated tax as they apply in relation to central tax.

**INTRODUCTION TO UNION TERRITORY GOODS & SERVICES TAX ACT, 2017**

The Central GST Act, 2017 will be applicable on all the intra state transactions of supply of goods and/or services and is the revenue of the Central Government. As CGST would be levied on all the transactions of taxable goods and services, and is therefore applicable in all the states and union territories of India. The Integrated GST Act, 2017 will be applicable on all the inter-state transactions of goods and services. It is regulated by the Central Government and therefore will be applicable on all the transactions of goods and services applicable in India or import / export transactions. However, for the purpose of levy and collection of SGST levied on each intra state transactions of goods and services, all the states / union territories of India have their own state / union territory legislation. The Union Territory Goods & Services Tax Act, 2017 intends to make a provision for levy and collection of tax on intra-State supply of goods or services or both by the Union Territories and for matters connected therewith or incidental thereto.

**APPLICABILITY OF THE UTGST ACT, 2017**

This Act may be called the Union Territory Goods and Services Tax Act, 2017. It would be applicable in the following Union Territories:



Delhi and Puducherry are the other two Union Territories but this Act will not be applicable there as they have their own State Legislature and Government. State GST would be applicable in their case.

Some definitions prescribed in the Act as defined under Section 2 are as follows:

**Definitions :** In this Act, unless the context otherwise requires:

- 1) “appointed day” means the date on which the provisions of this Act shall come into force;
- 2) “Commissioner” means the Commissioner of Union territory tax appointed under section 3;
- 3) “designated authority” means such authority as may be notified by the Commissioner;
- 4) “exempt supply” means supply of any goods or services or both which attracts nil rate of tax or which may be exempt from tax under section 8, or under section 6 of the Integrated Goods and Services Tax Act, and includes non-taxable supply;
- 5) “existing law” means any law, notification, order, rule or regulation relating to levy and collection of duty or tax on goods or services or both passed or made before the commencement of this Act by Parliament or any Authority or person having the power to make such law, notification, order, rule or regulation;
- 6) “Government” means the Administrator or any Authority or officer authorised to act as Administrator by the Central Government;
- 7) “output tax” in relation to a taxable person, means the Union territory tax chargeable under this Act on taxable supply of goods or services or both made by him or by his agent but excludes tax payable by him on reverse charge basis;

### **APPLICABILITY OF GST ON UNION TERRITORY OF JAMMU & KASHMIR AND LADAKH**

As per Jammu and Kashmir Reorganisation Act, 2019, the State of Jammu & Kashmir has been divided between Union Territories, namely, Union Territory (UT) of Jammu and Kashmir and UT of Ladakh. The appointed date for the same was 1st October, 2019.

CBIC has issued Notification No. 62/2019- Central Tax dated 26th November, 2019 which seeks to notify the transition plan with respect to J&K reorganization w.e.f. 31.10.2019.

However, as per Section 2(114) of the CGST Act, “Union Territory” means (a) The Andaman and Nicobar Islands; (b) Lakshadweep; (c) Dadra and Nagar Haveli; (d) Daman and Diu; (e) Chandigarh; and (f) Other territory; Hence, Ladakh is yet to be included under the aforesaid definition. Section 3 of the said Act states that Union Territory of Ladakh shall be formed without legislature. Hence, it shall have status to that of a Union Territory.

In view thereof, Union Territory of Jammu and Kashmir shall continue to charge SGST and CGST for intra-state supplies, however for supplies made from Jammu & Kashmir to Ladakh (and vice – versa), IGST shall be charged [Section 7(1)(b) of the IGST Act]. UTGST and CGST will be charged for supplies made in Ladakh.

Now, the Ministry of Home Affairs (Department of Jammu and Kashmir Affairs) has issued a Removal of Difficulties Order dated 30-10-2019 which seeks to remove difficulties arising in giving effect to the provisions of the Jammu and Kashmir Reorganisation Act, 2019.

Now, Section 2(7) of the said order states that:

“The Jammu and Kashmir Goods and Services Tax Act, 2017 shall be applicable to the Union Territory of Jammu and Kashmir and the Union Territory Goods and Services Tax Act, 2017 shall be applicable to the Union Territory of Ladakh.”

## **ADMINISTRATION & POWERS OF OFFICERS [SECTION 4, 5 & 6]**

The Administrator may, by order, authorise any officer to appoint officers of Union Territory tax below the rank of Assistant Commissioner of Union Territory tax for the administration of this Act. The Commissioner may, subject to such conditions and limitations as may be specified in this behalf by him, delegate his powers to any other officer subordinate to him.

Without prejudice to the provisions of this Act, the officers appointed under the Central Goods and Services Tax Act, 2017 are authorised to be the proper officers for the purposes of this Act, subject to such conditions as the Government shall, on the recommendations of the Council, by notification, specify.

Subject to the conditions specified in the notification issued :

- a) where any proper officer issues an order under this Act, he shall also issue an order under the Central Goods and Services Tax Act, as authorised by the said Act under intimation to the jurisdictional officer of central tax;
- b) where a proper officer under the Central Goods and Services Tax Act has initiated any proceedings on a subject matter, no proceedings shall be initiated by the proper officer under this Act on the same subject matter.

Any proceedings for rectification, appeal and revision, wherever applicable, of any order passed by an officer appointed under this Act, shall not lie before an officer appointed under the Central Goods and Services Tax Act.

## **LEVY AND COLLECTION OF UTGST [SECTION 7]**

As per the provision of Section 7 of the UTGST Act, 2017 there shall be levied a tax called the Union territory tax on all intra-State supplies of goods or services or both, except on the supply of alcoholic liquor for human consumption, on the value determined under section 15 of the Central Goods and Services Tax Act, 2017 and at such rates, not exceeding twenty per cent, as may be notified by the Central Government on the recommendations of the Council and collected in such manner as may be prescribed and shall be paid by the taxable person.

However, the Union territory tax on the supply of petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas and aviation turbine fuel shall be levied with effect from such date as may be notified by the Central Government on the recommendations of the Council.

The GST Council has already approved the total tax rates of 0%, 5%, 12%, 18% and 28%. The highest applicable approved rate of UTGST has been prescribed at 20%. Though the highest rate of tax as charges as UTGST would not be more than 14% but an enabling limit of 20% has been prescribed in law to avoid need of changing the law, in case of need to revise the rate of tax in future.

All the provisions of this Act shall apply to a recipient of goods or services or both , notified under reverse charge as if he is the person liable for paying the tax in relation to the supply of such goods or services or both.

The Government may, on the recommendations of the Council, by notification, specify a class of registered persons who shall, in respect of supply of specified categories of goods or services or both received from an unregistered supplier, pay the tax on reverse charge basis as the recipient of such supply of goods or services or both, and all the provisions of this Act shall apply to such recipient as if he is the person liable for paying the tax in relation to such supply of goods or services or both.

The Central Government may, on the recommendations of the Council, by notification, specify categories of services, the tax on intra-State supplies of which, shall be paid by the electronic commerce operator if such services are supplied through it, and all the provisions of this Act shall apply to such electronic commerce operator as if he is the supplier liable for paying the tax in relation to the supply of such services.

Provided that where an electronic commerce operator does not have a physical presence in the taxable territory, any person representing such electronic commerce operator for any purpose in the taxable territory shall be liable to pay tax.

Further it is provided that where an electronic commerce operator does not have a physical presence in the taxable territory and also he does not have a representative in the said territory, such electronic commerce operator shall appoint a person in the taxable territory for the purpose of paying tax and such person shall be liable to pay tax.

### **EXEMPTION FROM GST [SECTION 8]**

As per the provisions of Section 8 of the Act, the Central Government on the recommendations of the GST Council, by notification exempt either absolutely or subject to such conditions as may be specified therein, goods or services or both of any specified description from the whole or any part of the tax leviable on such supply. In other cases, Central Government in public interest and on recommendation of the Council, by special order, exempt from payment of tax.

The Central Government may, if it considers necessary or expedient so to do for the purpose of clarifying the scope or applicability of any notification or order issued, insert an explanation in such notification or order, as the case may be, by notification at any time within one year of issue of the notification under Section 8(1) or order under Section 8(2), and every such explanation shall have effect as if it had always been the part of the first such notification or order, as the case may be.

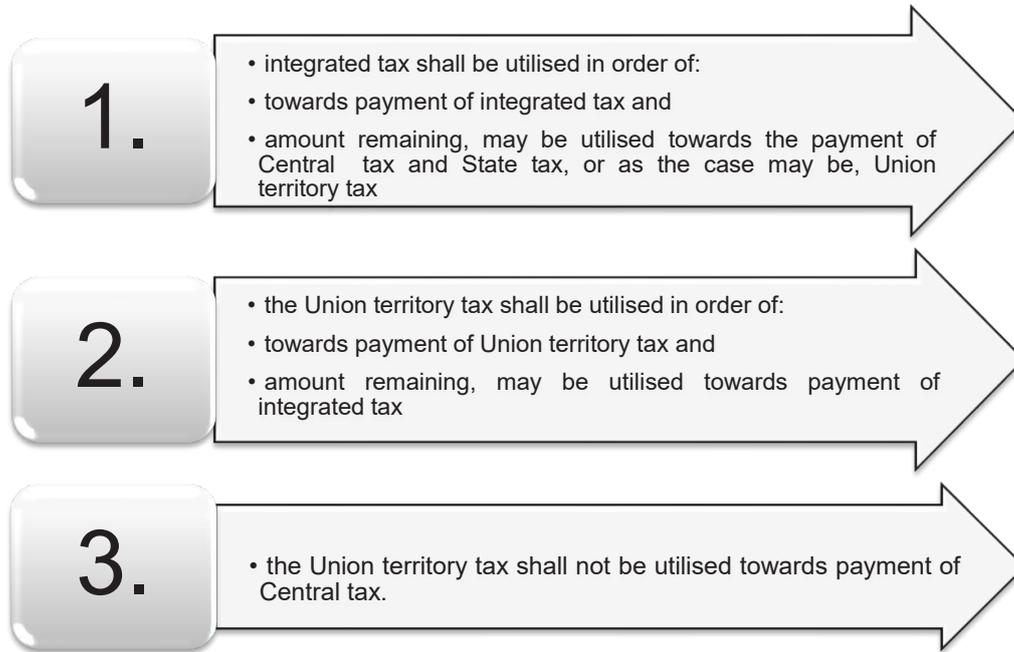
*Explanation* – For the purposes of this section, where an exemption in respect of any goods or services or both from the whole or part of the tax leviable thereon has been granted absolutely, the registered person supplying such goods or services or both shall not collect the tax, in excess of the effective rate, on such supply of goods or services or both.

### **PAYMENT OF TAX [SECTION 9]**

As per the provision of section 9 of the Act, the amount of input tax credit available in the electronic credit ledger of the registered person on account of:

- a) integrated tax shall first be utilised towards payment of integrated tax and the amount remaining, if any, may be utilised towards the payment of Central tax and State tax, or as the case may be, Union territory tax, in that order;
- b) the Union territory tax shall first be utilised towards payment of Union territory tax and the amount remaining, if any, may be utilised towards payment of integrated tax;
- c) the Union territory tax shall not be utilised towards payment of Central tax.

**The amount of input tax credit available in the electronic credit ledger of the registered person on account of:**



**Utilisation of input tax credit [Section 9A]**

Notwithstanding anything contained in section 9, the input tax credit on account of Union territory tax shall be utilised towards payment of integrated tax or Union territory tax, as the case may be, only after the input tax credit available on account of integrated tax has first been utilised towards such payment.

**Order of utilisation of input tax credit [Section 9B]**

Notwithstanding anything contained in this Chapter and subject to the provisions of clause (c) of section 9, the Government may, on the recommendations of the Council, prescribe the order and manner of utilisation of the input tax credit on account of integrated tax, Central tax, State tax or Union territory tax, as the case may be, towards payment of any such tax.

Order of utilization of input tax credit at present is as follow:

Input tax credit on account of	Output liability on account of Integrated tax	Output liability on account of Central tax	Output liability on account of State tax/ Union Territory tax
Integrated tax	(I)	(II) – In any order and in any proportion	
	(III) Input tax credit on account of Integrated tax to be completed exhausted mandatorily		
Central tax	(V)	(IV)	Not permitted
State tax/ Union Territory tax	(VII)	Not permitted	(VI)

There is no offset available between the CGST and the SGST/ UTGST.

**INPUT TAX CREDIT ON INPUT STOCKS [SECTION 18]**

The eligible input tax credits in respect of inputs held in stocks, inputs held in semi finished goods and inputs held in stock of finished goods on the day immediately preceding the appointed day will be eligible as input tax credit to be taken as UTGST in the electronic ledger.

The following registered taxable person will be eligible for the input tax credit:

- a) Who was not liable to be registered.
- b) Who was involved in dealing with exempted goods or tax free goods.
- c) Goods which have suffered tax at first point of sale and their subsequent sale was not liable to tax in the Union Territory under the previous law but which are liable to be taxed in GST.
- d) Where a person is entitled to tax at the time of sale.

However, the Input tax credit is available subject to the following conditions:

- i. such inputs or goods are used or intended to be used for making taxable supplies under GST;
- ii. the said registered person is eligible for input tax credit on such inputs under GST;
- iii. the said registered person is in possession of invoice or other prescribed documents evidencing payment of tax under the existing law in respect of such inputs; and
- iv. such invoices or other prescribed documents were issued not earlier than twelve months immediately preceding the appointed day.

However, in case such taxable person is not in possession of invoice or taxpaying document, such person can take credit at such rate as may be prescribed. However he would be required to pass the benefit of reduced taxes to his recipients.

Registered taxable person will be eligible for the input tax credit in the following cases	Conditions for availing the Input tax credit
<ul style="list-style-type: none"> <li>•Not liable to be registered</li> <li>•Involved in dealing with exempted goods or tax free goods</li> <li>•Goods which have suffered tax at first point of sale and their subsequent sale was not liable to tax in the Union Territory under the previous law but which are liable to be taxed in GST</li> <li>•Person is entitled to tax at the time of sale</li> </ul>	<ul style="list-style-type: none"> <li>•Used or intended to be used for making taxable supplies under GST</li> <li>•Registered person is eligible for input tax credit under GST law</li> <li>•Said person is in possession of invoice or other prescribed documents evidencing payment of tax</li> <li>•Such invoices or other prescribed documents were issued not earlier than twelve months immediately preceding the appointed day</li> </ul>

**INPUT TAX CREDIT: TAXABLE AS WELL AS EXEMPTED GOODS**

A registered person, who was engaged in the sale of taxable goods as well as exempted goods or tax free goods under the existing law but which are liable to tax under this Act, shall be entitled to take, in his

electronic credit ledger the amount of credit of the value added tax and entry tax, if any, carried forward in a return furnished under the previous law by him and the amount of credit of the value added tax and entry tax, if any, in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the appointed day, relating to such exempted goods or tax free goods in accordance with the provisions of the Act.

### **SWITCH OVER FROM COMPOSITION LEVY**

A registered person, who was either paying tax at a fixed rate or paying a fixed amount in lieu of the tax payable under the previous law shall be eligible for, credit of value added tax in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the appointed day subject to the following conditions:

- i. Such inputs or goods were used or intended to be used for making taxable supplies under this Act;
- ii. the said registered person is not paying tax under section 10 of the Central Goods and Services Tax Act;
- iii. the said registered person is eligible for input tax credit on such inputs under this Act;
- iv. the said registered person is in possession of invoice or other prescribed documents evidencing payment of tax under the existing law in respect of inputs; and
- v. such invoices or other prescribed documents were issued not earlier than twelve months immediately preceding the appointed day.

A registered person who has paid the Central tax and the Union territory tax on a transaction considered by him to be an intra-State supply, but which is subsequently held to be an inter-State supply, shall be refunded the amount of taxes so paid in such manner and subject to such conditions as may be prescribed.

Further, a registered person who has paid integrated tax on a transaction considered by him to be an inter-State supply, but which is subsequently held to be an intra-State supply, shall not be required to pay any interest on the amount of the central tax and the Union territory tax payable.

Where any amount of tax, interest or penalty is payable by a person to the Government under any of the provisions of this Act or the rules made thereunder and which remains unpaid, the proper officer of central tax, during the course of recovery of said tax arrears, may recover the amount from the said person as if it were an arrear of central tax and credit the amount so recovered to the account of the Government under the appropriate head of Union territory tax.

Where the amount recovered is less than the amount due to the Government under this Act and the Central Goods and Services Tax Act, the amount to be credited to the account of the Government shall be in proportion to the amount due as Union territory tax and Central tax.

### **ADVANCE RULING [SECTION 14 OF UTGST ACT, 2017]**

“Advance Ruling” means a decision provided by the Authority or the Appellate Authority to an applicant on matters or on questions specified in sub-section (2) of section 97 or sub-section (1) of section 100 of the Central Goods and Services Tax Act, in relation to the supply of goods or services or both being undertaken or proposed to be undertaken by the applicant;

“Appellate Authority” means the Appellate Authority for Advance Ruling constituted under section 16;

“Applicant” means any person registered or desirous of obtaining registration under this Act;

“Authority” means the authority for Advance Ruling constituted under Section 15.

### Questions for which Advance Ruling can be Sought ?

Advance Ruling can be sought for the following questions:

- classification of any goods or services or both;
- applicability of a notification issued under provisions of the GST Act(s);
- determination of time and value of supply of goods or services or both;
- admissibility of input tax credit of tax paid or deemed to have been paid;
- determination of the liability to pay tax on any goods or services under the Act;
- whether applicant is required to be registered under the Act;
- whether any particular thing done by the applicant with respect to any goods or services amounts to or results in a supply of goods or services, within the meaning of that term.

### CONSTITUTION OF AUTHORITY FOR ADVANCE RULING [SECTION 15]

The Central Government shall, by notification, constitute an Authority to be known as the (name of the Union territory) Authority for Advance Ruling provided that the Central Government may, on the recommendations of the Council, notify any Authority located in any State or any other Union territory to act as the Authority for the purposes of this Act.

The Authority shall consist of :

- i. one member from amongst the officers of central tax; and
- ii. one member from amongst the officers of Union territory tax, to be appointed by the Central Government.

The qualifications, the method of appointment of the members and the terms and conditions of their service shall be such as may be prescribed.

### CONSTITUTION OF APPELLATE AUTHORITY FOR ADVANCE RULING [SECTION 16]

The Central Government shall, by notification, constitute an Appellate Authority to be known as the (name of the Union territory) Appellate Authority for Advance Ruling for Goods and Services Tax for hearing appeals against the advance ruling pronounced by the Advance Ruling Authority.

The Appellate Authority shall consist of:

- i. the Chief Commissioner of central tax as designated by the Board; and
- ii. the Commissioner of Union territory tax having jurisdiction over the applicant.

### MISCELLANEOUS

Subject to the provisions of this Act and the rules made thereunder, the provisions of the Central Goods and Services Tax Act, 2017 relating to –

- (i) scope of supply;
- (ii) composition levy;
- (iii) composite supply and mixed supply;
- (iv) time and value of supply;
- (v) input tax credit;
- (vi) registration;

- (vii) tax invoice, credit and debit notes;
- (viii) accounts and records;
- (ix) returns;
- (x) payment of tax;
- (xi) tax deduction at source;
- (xii) collection of tax at source;
- (xiii) assessment;
- (xiv) refunds;
- (xv) audit;
- (xvi) inspection, search, seizure and arrest;
- (xvii) demands and recovery;
- (xviii) liability to pay in certain cases;
- (xix) advance ruling;
- (xx) appeals and revision;
- (xxi) presumption as to documents;
- (xxii) offences and penalties;
- (xxiii) job work;
- (xxiv) electronic commerce;
- (xxv) settlement of funds;
- (xxvi) transitional provisions; and
- (xxvii) miscellaneous provisions including the provisions relating to the imposition of interest and penalty, shall mutatis mutandis apply.

The above provisions are applicable to IGST Act also.

The Central Government may, on the recommendations of the Council, by notification, make rules for carrying out the provisions of this Act.

### **POWER TO MAKE RULES [SECTION 22]**

Section 22 of the UTGST Act, 2017 lays down the powers of Central Government to make rules on the recommendations of the Council. The Central Government may make rules for all or any of the matters which by this Act are required to be, or may be, prescribed or in respect of which provisions are to be or may be made by rules.

The power to make rules conferred by this section shall include the power to give retrospective effect to the rules or any of them from a date not earlier than the date on which the provisions of this Act come into force.

Any rules made under sub-section (1) may provide that a contravention thereof shall be liable to a maximum penalty of ten thousand rupees (Rs.10,000).

### **GENERAL POWER TO MAKE REGULATIONS [SECTION 23]**

The Board may, by notification, make regulations consistent with this Act and the rules made thereunder to carry out the purposes of this Act.

**LAYING OF RULES, REGULATIONS AND NOTIFICATIONS [SECTION 24]**

Every rule made by the Central Government, every regulation made by the Board and every notification issued by the Central Government under this Act, shall be laid, as soon as may be, after it is made or issued, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or regulation or in the notification, as the case may be, or both Houses agree that the rule or regulation or the notification should not be made, the rule or regulation or notification, as the case may be, shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule or regulation or notification, as the case may be.

**POWER TO ISSUE INSTRUCTIONS OR DIRECTIONS [SECTION 25]**

For the purpose of uniformity in the implementation of this Act, the Commissioner may, issue such orders, instructions or directions to the Union Territory tax officers as he may deem fit, and thereupon all such officers and all other persons employed in the implementation of this Act shall observe and follow such orders, instructions or directions.

**REMOVAL OF DIFFICULTIES [SECTION 26]**

If any difficulty arises in giving effect to any provision of this Act, the Central Government may, on the recommendations of the Council, by a general or a special order published in the Official Gazette, make such provisions not inconsistent with the provisions of this Act or the rules or regulations made thereunder, as may be necessary or expedient for the purpose of removing the said difficulty. However, no such order shall be made after the expiry of a period of three years from the date of commencement of this Act.

Every order made under this section shall be laid, as soon as may be, after it is made, before each House of Parliament.

**THE GOODS AND SERVICES TAX (COMPENSATION TO STATES) ACT, 2017****Background**

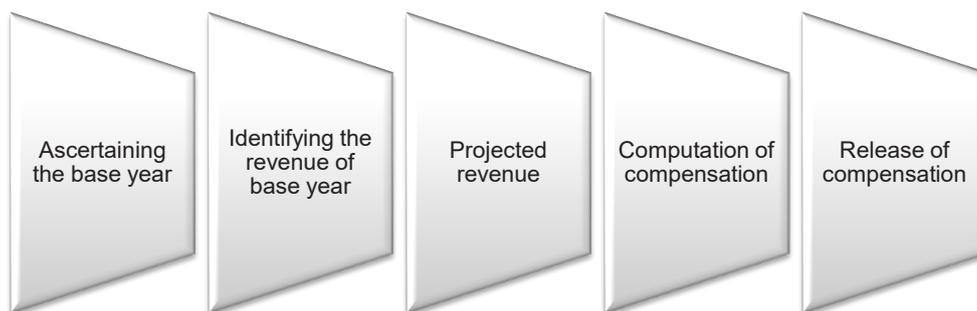
The GST Council in its 10th meeting held on 18th February, 2017 approved the GST (Compensation to States) Bill that provides for the compensation of loss arising out of introduction of Goods and Services Tax to states in India. The Act which provides for compensation to the states for the loss of revenue arising on account of implementation of Goods and Services Tax for a period of five years in pursuance of the provisions of the Constitution (One Hundred and First Amendment) Act, 2016, came in force as the Goods & Services Tax (Compensation to States) Act, 2017.

The Union Government presented the Goods and Service Tax (Compensation to States) Bill, 2017 in Lok Sabha on 27th March, 2017 and the same has been passed by Lok Sabha on 29th March, 2017. The Rajya Sabha passed the bill on 6th April, 2017 and was assented by the President on 12th April, 2017.

This Act may be called the Goods and Services Tax (Compensation to States) Act, 2017. It extends to the whole of India.

**SALIENT FEATURES OF GST (COMPENSATION TO STATES) ACT, 2017**

The GST(Compensation to States) Act,2017 provides for the manner of ascertaining the amount of compensation that shall be payable to states during the transition period of five years by the Centre on account of revenue loss attributable to levy of Goods and Services Tax in India. It involves the following steps:



The compensation shall be met out from compensation cess for which the provisions in relation to collection, payment return, refund etc. have been provided for in the GST(Compensation to States) Act,2017.

**Objectives of the Act:**

1. It provides for the compensation of loss to the states arising due to implementation of Goods and Services Tax in India
2. The financial year 2015-16 shall be taken as base year for the purpose of calculating compensation amount payable to the states.
3. The revenue to be compensated consists of revenues from all the taxes that are levied by the states which have subsumed under Goods and Services Tax, as audited by the Comptroller and Auditor General of India.
4. The projected growth rate of revenue during transition period shall be 14%.
5. The compensation shall be released at the end of every two months period on a provisional basis and final adjustment shall be made after getting audited accounts of the year from the Comptroller and Auditor General of India.
6. In case of eleven special category states referred to in Article 279A of the Constitution, the revenue forgone on account of exemption of taxes granted shall be counted towards the definition of Revenue for the base year 2015-16 for calculating compensation.
7. The revenues of the states that were not credited to the consolidated fund of states government but were directly collected by “mandi” or “municipality” would also be included in the definition of revenue if these were subsumed in the Goods and Services Tax.
8. To generate revenue to compensate states for five years for loss suffered by the states on account of implementation of Goods and Services Tax, is by levy of a cess on such goods as recommended by the GST Council over and above the GST rate on that item.
9. The proceeds of the cess shall be credited to the fund called Goods and Services Tax Compensation Fund and all the compensation payable to the states as GST compensation shall be paid from this fund. The balance if any left out in the GST compensation fund after five year shall be equally shared between the Centre and the states.

Some definitions prescribed in Section 2 of the Act are as follows:

**Section 2 :** In this Act, unless the context otherwise requires:

- a) “central tax” means the central goods and services tax levied and collected under the Central Goods and Services Tax Act;
- b) “Central Goods and Services Tax Act” means the Central Goods and Services Tax Act, 2017;
- c) “cess” means the goods and services tax compensation cess levied under section 8;

- d) “compensation” means an amount, in the form of goods and services tax compensation, as determined under section 7;
- e) “Council” means the Goods and Services Tax Council constituted under the provisions of article 279A of the Constitution;
- f) “Fund” means the Goods and Services Tax Compensation Fund referred to in section 10;
- g) “input tax” in relation to a taxable person, means,
  - i. cess charged on any supply of goods or services or both made to him;
  - ii. cess charged on import of goods and includes the cess payable on reverse charge basis;
- h) “Integrated Goods and Services Tax Act” means the Integrated Goods and Services Tax Act, 2017;
- i) “integrated tax” means the integrated goods and services tax levied and collected under the Integrated Goods and Services Tax Act;
- j) “prescribed” means prescribed by rules made, on the recommendations of the Council, under this Act;
- k) “projected growth rate” means the rate of growth projected for the transition period as per section 3;
- l) “Schedule” means the Schedule appended to this Act;
- m) “State” means,
  - i. for the purposes of sections 3, 4, 5, 6 and 7 the States as defined under the Central Goods and Services Tax Act; and
  - ii. for the purposes of sections 8, 9, 10, 11, 12, 13 and 14 the States as defined under the Central Goods and Services Tax Act and the Union territories as defined under the Union Territories Goods and Services Tax Act;
- n) “State tax” means the State goods and services tax levied and collected under the respective State Goods and Services Tax Act;
- o) “State Goods and Services Tax Act” means the law to be made by the State Legislature for levy and collection of tax by the concerned State on supply of goods or services or both;
- p) “taxable supply” means a supply of goods or services or both which is chargeable to the cess under this Act;
- q) “transition date” shall mean, in respect of any State, the date on which the State Goods and Services Tax Act of the concerned State comes into force;
- r) “transition period” means a period of five years from the transition date; and
- s) “Union Territories Goods and Services Tax Act” means the Union Territories

The words and expressions used and not defined in this Act but defined in the Central Goods and Services Tax Act and the Integrated Goods and Services Tax Act shall have the meanings respectively assigned to them in those Acts.

### **PROJECTED GROWTH RATE [SECTION 3]**

The projected nominal growth rate of revenue subsumed for a State during the transition period shall be fourteen per cent (14%) per annum.

### **BASE YEAR [SECTION 4]**

For the purpose of calculating the compensation amount payable in any financial year during the transition

period, the financial year ending 31st March, 2016, shall be taken as the base year. Thus, the base year shall be Financial Year 2015-16.

### **BASE YEAR REVENUE [SECTION 5]**

Section 5(1) mandates that subject to the provisions of sub-sections (2), (3), (4), (5) and (6), the base year revenue for a State shall be the sum of the revenue collected by the State and the local bodies during the base year, on account of the taxes levied by the respective State or Union and net of refunds, with respect to the following taxes, imposed by the respective State or Union, which are subsumed into GST:

- a) the Value Added Tax 'VAT', sales tax, purchase tax, tax collected on works contract, or any other tax levied by the concerned State under the erstwhile entry 54 of List-II (State List) of the Seventh Schedule to the Constitution;
- b) the central sales tax 'CST' levied under the Central Sales Tax Act, 1956 (74 of 1956);
- c) the entry tax, octroi, local body tax or any other tax levied by the concerned State under the erstwhile entry 52 of List-II (State List) of the Seventh Schedule to the Constitution;
- d) Luxuries tax, entertainments tax, amusements, betting and gambling or any other tax levied by the concerned State under the erstwhile entry 62 of List-II (State List) of the Seventh Schedule to the constitution;
- e) Advertisement tax or any other tax levied by the concerned State under the erstwhile entry 55 of List-II (State List) of the Seventh Schedule to the Constitution;
- f) the duties of excise on medicinal and toilet preparations levied by the Union but collected and retained by the concerned State Government under the erstwhile article 268 of the Constitution;
- g) any cess or surcharge or fee leviable under entry 66 read with entries 52, 54, 55 and 62 of List-II of the Seventh Schedule to the Constitution by the State Government under any Act notified under sub-section (4),  
prior to the commencement of the provisions of the Constitution (One Hundred and First Amendment) Act, 2016.

The following amounts shall not be included in the revenue collected during the base year in a State, net of refunds, in the calculation of the base year revenue for that State:

- a) any taxes levied under any Act enacted under the erstwhile entry 54 of List-I (State List) of the Seventh Schedule to the Constitution, prior to the coming into force of the provisions of the Constitution (One Hundred and First Amendment) Act, 2016, on the sale or purchase of petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas, aviation turbine fuel and alcoholic liquor for human consumption;
- b) tax levied under the Central Sales Tax Act, 1956, on the sale or purchase of petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas, aviation turbine fuel and alcoholic liquor for human consumption;
- c) any cess imposed by the State Government on the sale or purchase of petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas, aviation turbine fuel and alcoholic liquor for human consumption; and
- d) the entertainment tax levied by the State but collected by local bodies, under any Act enacted under the erstwhile entry 62 of List-II (State List) of the Seventh Schedule to the Constitution, prior to coming into force of the provisions of the Constitution (One Hundred and First Amendment) Act, 2016.

The base year revenue shall include the amount of tax collected on sale of services by the said State Government during the base year in respect of the State of Jammu and Kashmir.

Also, in respect of the States mentioned in sub-clause (g) of clause (4) of article 279A of the Constitution, the amount of revenue foregone on account of exemptions or remission given by the said State Governments to promote industrial investment in the State, with respect to such specific taxes referred to in sub-section (1), shall be included in the total base year revenue of the State, subject to such conditions as may be prescribed.

The base year revenue shall be calculated as mentioned above and on the basis of the figures of revenue collected and net of refunds given in that year, as audited by the Comptroller and Auditor-General of India.

In respect of any State, if any part of revenues mentioned above are not credited in the Consolidated Fund of the respective State, the same shall be included in the total base year revenue of the State, subject to such conditions as may be prescribed.

### **PROJECTED REVENUE FOR ANY YEAR [SECTION 6]**

The projected revenue for any year in a State shall be calculated by applying the projected growth rate over the base year revenue of that State.

*Illustration* – If the base year revenue for 2015-16 for a concerned State, calculated as per section 5 is one hundred rupees, then the projected revenue for financial year 2018-19 shall be as follows –

Projected Revenue for 2018-19 =  $100 (1 + 14/100)^3$

### **GST COMPENSATION [SECTION 7]**

The compensation payable to a State shall be provisionally calculated and released at the end of every two months period, and shall be finally calculated for every financial year after the receipt of final revenue figures, as audited by the Comptroller and Auditor General of India. However, in case any excess amount has been released as compensation to a State in any financial year during the transition period, as per the audited figures of revenue collected, the excess amount so released shall be adjusted against the compensation amount payable to such State in the subsequent financial year. [Section 7(2)]

The total compensation payable for any financial year during the transition period to any State shall be calculated in the following manner:

- a) the projected revenue for any financial year during the transition period, which could have accrued to a State in the absence of the goods and services tax, shall be calculated by applying the projected growth rate over the base year revenue of that state.
- b) the actual revenue collected by a State in any financial year during the transition period shall be :
  - i. the actual revenue from State tax collected by the State, net of refunds given by the said State under Chapters XI and XX of the State Goods and Services Tax Act;
  - ii. the integrated goods and services tax apportioned to that State; and
  - iii. any collection of taxes on account of the taxes levied by the respective State under the Acts specified in sub-section (4) of section 5, net of refund of such taxes, as certified by the Comptroller and Auditor-General of India;
- c) the total compensation payable in any financial year shall be the difference between the projected revenue for any financial year and the actual revenue collected by a State referred to in clause (b).

[Section 7(3)]

The loss of revenue at the end of every two months period in any year for a State during the transition period shall be calculated, at the end of the said period, in the following manner:

- a) The projected revenue that could have been earned by the State in absence of the goods and services

tax till the end of the relevant two months period of the respective financial year shall be calculated on a pro-rata basis as a percentage of the total projected revenue for any financial year during the transition period, calculated in accordance with section 6.

*Illustration:* If the projected revenue for any year calculated in accordance with section 6 is one hundred rupees, for calculating the projected revenue that could be earned till the end of the period of ten months for the purpose of this sub-section shall be  $100 \times (10/12) = \text{Rs.}83.33$ ;

- b) The actual revenue collected by a State till the end of relevant two months period in any financial year during the transition period shall be:
- i. the actual revenue from State tax collected by the State, net of refunds given by the State under Chapters XI and XX of the State Goods and Services Tax Act;
  - ii. the integrated goods and services tax apportioned to that State, as certified by the Principal Chief Controller of Accounts of the Central Board of Indirect Taxes and Customs; and
  - iii. any collection of taxes levied by the said State, under the Acts specified in sub-section (4) of section 5, net of refund of such taxes;
- c) the provisional compensation payable to any State at the end of the relevant two months period in any financial year shall be the difference between the projected revenue till the end of the relevant period in accordance with clause (a) and the actual revenue collected by a State in the said period as referred to in clause (b), reduced by the provisional compensation paid to a State till the end of the previous two months period in the said financial year during the transition period.

[Section 7(4)]

In case of any difference between the final compensation amount payable to a State calculated in accordance with the provisions of sub-section (3) upon receipt of the audited revenue figures from the Comptroller and Auditor-General of India, and the total provisional compensation amount released to a State in the said financial year in accordance with the provisions of sub-section (4), the same shall be adjusted against release of compensation to the State in the subsequent financial year. [Section 7(5)]

Where no compensation is due to be released in any financial year, and in case any excess amount has been released to a State in the previous year, this amount shall be refunded by the State to the Central Government and such amount shall be credited to the Fund in such manner as may be prescribed. [Section 7(6)]

## **COMPENSATION CESS [SECTION 8]**

There shall be levied a cess on such intra-State supplies of goods or services or both, as provided for in section 9 of the Central Goods and Services Tax Act, 2017 and such inter-State supplies of goods or services or both as provided for in section 5 of the Integrated Goods and Services Tax Act, 2017 and collected on the recommendations of the Council, for the purposes of providing compensation to the States for loss of revenue arising on account of implementation of the goods and services tax with effect from the date from which the provisions of the Central Goods and Services Tax Act, 2017 is brought into force, for a period of five years or for such period as may be prescribed on the recommendations of the Council.

However, no such cess shall be leviable on supplies made by a taxable person who has decided to opt for composition levy under section 10 of the Central Goods and Services Tax Act, 2017.

The cess shall be levied on such supplies of goods and services as are specified in column (2) of the Schedule, on the basis of value, quantity or on such basis at such rate not exceeding the rate set forth in the corresponding entry in column (4) of the Schedule, as the Central Government may, on the recommendations of the Council, by notification in the Official Gazette, specify;

Where the cess is chargeable on any supply of goods or services or both with reference to their value, the value

of such supply shall be determined under section 15 of the Central Goods and Services Tax Act for all intra-State and inter-State supplies of goods or services or both.

The cess on goods imported into India shall be levied and collected in accordance with the provisions of Section 3 of the Customs Tariff Act, 1975, at the point when duties of Customs are levied on the said goods under Section 12 of the Customs Act, 1962, on a value determined under the Customs Tariff Act, 1975.

### **PAYMENTS RETURN AND REFUND [SECTION 9]**

Every taxable person, making a taxable supply of goods or services or both, shall:

- a) pay the amount of cess as payable under this Act in such manner;
- b) furnish such returns in such forms, along with the returns to be filed under the Central Goods and Services Tax Act; and
- c) apply for refunds of such cess paid in such form,

as may be prescribed.

For all purposes of furnishing of returns and claiming refunds, except for the form to be filed, the provisions of the Central Goods and Services Tax Act, 2017 and the rules made thereunder, shall, as far as may be, apply in relation to the levy and collection of the cess leviable under section 8 on all taxable supplies of goods or services or both, as they apply in relation to the levy and collection of central tax on such supplies under the said Act or the rules made thereunder.

### **CREDITING PROCEEDS OF CESS TO FUND [SECTION 10]**

(1) The proceeds of the cess leviable under section 8 and such other amounts as may be recommended by the Council, shall be credited to a non-lapsable Fund known as the Goods and Services Tax Compensation Fund, which shall form part of the public account of India and shall be utilised for purposes specified in the said section.

(2) All amounts payable to the States under section 7 shall be paid out of the Fund.

(3) Fifty per cent. of the amount remaining unutilised in the Fund at the end of the transition period shall be transferred to the Consolidated Fund of India as the share of Centre, and the balance fifty per cent. shall be distributed amongst the States in the ratio of their total revenues from the State tax or the Union territory goods and services tax, as the case may be, in the last year of the transition period.

(3A) Notwithstanding anything contained in sub-section (3), fifty per cent. of such amount, as may be recommended by the Council, which remains unutilised in the Fund, at any point of time in any financial year during the transition period shall be transferred to the Consolidated Fund of India as the share of Centre, and the balance fifty per cent. shall be distributed amongst the States in the ratio of their base year revenue determined in accordance with the provisions of section 5:

Provided that in case of shortfall in the amount collected in the Fund against the requirement of compensation to be released under section 7 for any two months' period, fifty per cent. of the same, but not exceeding the total amount transferred to the Centre and the States as recommended by the Council, shall be recovered from the Centre and the balance fifty per cent. from the States in the ratio of their base year revenue determined in accordance with the provisions of section 5.

(4) The accounts relating to Fund shall be audited by the Comptroller and Auditor General of India or any person appointed by him at such intervals as may be specified by him and any expenditure in connection with such audit shall be payable by the Central Government to the Comptroller and Auditor-General of India.

(5) The accounts of the Fund, as certified by the Comptroller and Auditor-General of India or any other person

appointed by him in this behalf together with the audit report thereon shall be laid before each House of Parliament.

### OTHER PROVISIONS RELATING TO CESS [SECTION 11]

The provisions of the Central Goods and Services Tax Act, 2017 and Integrated Goods and Services Tax Act, 2017, and the rules made thereunder, including those relating to assessment, input tax credit, non-levy, short-levy, interest, appeals, offences and penalties, shall, as far as may be, mutatis mutandis, apply, in relation to the levy and collection of the cess leviable under section 8 on the intra-State supply of goods and services, as they apply in relation to the levy and collection of central tax and integrated tax on such intra-State supplies under the said Act or the rules made thereunder.

The input tax credit in respect of cess on supply of goods and services leviable under section 8, shall be utilised only towards payment of said cess on supply of goods and services leviable under the said section.

### POWER TO MAKE RULES [SECTION 12]

The Central Government shall, on the recommendations of the Council, by notification in the Official Gazette, make rules for carrying out the provisions of this Act. In particular, and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters:

- a) the conditions which were included in the total base year revenue of the States
- b) the conditions subject to which any part of revenues not credited in the Consolidated Fund of the respective State shall be included in the total base year revenue of the State
- c) the manner of refund of compensation by the States to the Central Government
- d) the manner of levy and collection of cess and the period of its imposition
- e) the manner and forms for payment of cess, furnishing of returns and refund of cess
- f) any other matter which is to be, or may be, prescribed, or in respect of which provision is to be made, by rules.

### Overview of the IGST Act [Source : [www.cbic.gov.in](http://www.cbic.gov.in)]

#### Q 1. What is IGST?

**Ans.** “Integrated Goods and Services Tax” (IGST) means tax levied under the IGST Act on the supply of any goods and/ or services in the course of inter-State trade or commerce.

#### Q 2. What are inter-state supplies?

**Ans.** A supply of goods and/or services in the course of inter-State trade or commerce means any supply where the location of the supplier and the place of supply are in different States, two different union territory or in a state and union territory Further import of goods and services, supplies to SEZ units or developer, or any supply that is not an intra state supply. (Section 7 of the IGST Act).

#### Q 3. How will the Inter-State supplies of Goods and Services be taxed under GST?

**Ans.** IGST shall be levied and collected by Centre on interstate supplies. IGST would be broadly CGST plus SGST and shall be levied on all inter-State taxable supplies of goods and services.

The inter-State seller will pay IGST on value addition after adjusting available credit of IGST, CGST, and SGST on his purchases. The Exporting State will transfer to the Centre the credit of SGST used in payment of IGST. The Importing dealer will claim credit of IGST while discharging his output tax liability in his own State.

The Centre will transfer to the importing State the credit of IGST used in payment of SGST. The relevant

information is also submitted to the Central Agency which will act as a clearing house mechanism, verify the claims and inform the respective governments to transfer the funds.

**Q 4. What are the advantages of IGST Model?**

**Ans.** The major advantages of IGST Model are: a. Maintenance of uninterrupted ITC chain on inter-State transactions; b. No upfront payment of tax or substantial blockage of funds for the inter-State seller or buyer; c. No refund claim in exporting State, as ITC is used up while paying the tax; d. Self-monitoring model; e. Ensures tax neutrality while keeping the tax regime simple; f. Simple accounting with no additional compliance burden on the taxpayer; g. Would facilitate in ensuring high level of compliance and thus higher collection efficiency. Model can handle 'Business to Business' as well as 'Business to Consumer' transactions.

**Q 6. How will imports/exports be taxed under GST?**

**Ans.** All imports/exports will be deemed as inter-state supplies for the purposes of levy of GST (IGST). The incidence of tax will follow the destination principle and the tax revenue in case of SGST will accrue to the State where the imported goods and services are consumed. Full and complete set-off will be available as ITC of the IGST paid on import on goods and services. Exports of goods and services will be zero rated. The exporter has the option either to export under bond without payment of duty and claim refund of ITC or pay IGST at the time of export and claim refund of IGST. The IGST on imports is leviable under the provisions of the Customs Tariff Act and shall be levied at the time of imports along with the levy of the Customs Act (Section 5 of the IGST Act)

**Q 7. How will the IGST be paid?**

**Ans.** The IGST payment can be done utilizing ITC or by cash. However, the use of ITC for payment of IGST will be done using the following hierarchy, - First available ITC of IGST shall be used for • payment of IGST; Once ITC of IGST is exhausted, the ITC of CGST • shall be used for payment of IGST; If both ITC of IGST and ITC of CGST are • exhausted, then only the dealer would be permitted to use ITC of SGST for payment of IGST.

Remaining IGST liability, if any, shall be discharged using payment in cash. GST System will ensure maintenance of this hierarchy for payment of IGST using the credit.

**Q 8. How will the settlement between Centre, exporting state and importing state be done?**

**Ans.** There would be settlement of account between the Centre and the states on two counts, which are as follows :

- *Centre and the exporting state* : The exporting state shall pay the amount equal to the ITC of SGST used by the supplier in the exporting state to the Centre.
- *Centre and the importing state* : The Centre shall pay the amount equal to the ITC of IGST used by a dealer for payment of SGST on intra- state supplies. The settlement would be on cumulative basis for a state taking into account the details furnished by all the dealer in the settlement period. Similar settlement of amount would also be undertaken between CGST and IGST account.

**Q 9. What treatment is given to supplies made to SEZ units or developer?**

**Ans.** Supplies to SEZ units or developer shall be zero rated in the same manner as done for the physical exports. Supplier shall have option to make supplies to SEZ without payment of taxes and claim refunds of input taxes on such supplies (section 16 of the IGST Act).

**Q 10. Are business processes and compliance requirement same in the IGST and CGST Acts?**

**Ans.** The procedure and compliance requirement are same for processes likes registration, return filing and payment of tax. Further, the IGST act borrows the provisions from the CGST Act as relating to assessment, audit, valuation, time of supply, invoice, accounts, records, adjudication, appeal etc. (Section 20 of the IGST Act).

## LESSON ROUND UP

- President on 12th April, 2017, gave assent to the following four Acts:
  - Central Goods & Services Tax Act, 2017
  - Integrated Goods & Services Tax Act, 2017
  - Union Territory Goods & Services Tax Act, 2017
  - Goods & Services Tax (Compensation to States) Act, 2017
- Federal structure of the Constitution is continued under the GST regime of indirect taxes
- IGST is levied and collected by the Centre on inter-state supply of goods and services including imports into India and supplies made outside India along with supplies to/from SEZs
- Owing to shortcomings in previous regime like cascading effect under Central Sales Tax regime, IGST came into being
- Union Territory Goods and Services Tax Act, 2017 would be applicable in the Union Territories except Delhi and Puducherry
- Various provisions of the Central Goods and Services Tax Act, 2017 as contained in Act shall apply to Union Territories.
- The GST (Compensation to States) Act, 2017 provides for ascertaining the amount of compensation that shall be payable to states during the transition period of five years by the Centre on account of revenue loss attributable to levy of Goods and Services Tax
- The Act provides for calculation and ascertainment of base year, projected growth rate, compensation to be paid and the like.
- There shall be levied a cess and collected on the recommendations of the Council, for the purposes of providing compensation to the States for loss of revenue

## SELF TEST QUESTIONS

### ELABORATIVE QUESTIONS

1. Explain the relevance of IGST Act, 2017
2. What are the provisions under IGST Act, regarding refund to a foreign tourist?
3. Who are the authorities under UTGST Act, 2017?
4. What is the working mechanism to compensate states under GST (Compensation to States) Act, 2017?
5. Enumerate the salient features of GST (Compensation to States) Act, 2017.
6. Discuss the provisions relating to Advance Ruling under Goods & Services Tax Act.

## SUGGESTED READINGS

1. Goods & Services Tax, Laws, Concepts and Impact Analysis-Bloomsbury – Dr. Sanjiv Agarwal & Sanjeev Malhotra
2. GST Ready Reckoner- Taxmann – V.S. Datey
3. A complete guide to Goods & Services Tax Ready Reckoner in Q & A Format- Bloomsbury – Dr. Sanjiv Agarwal & Sanjeev Malhotra



# Lesson 17

## Overview of Customs Law

### LESSON OUTLINE

- Overview of Customs Law
- Levy and collection of Customs Duties
- Types of Custom Duties
- Classification and Valuation of import and export goods
- Exemptions
- Officers of customs
- Administration of Customs Law
- Import and Export Procedures under Customs Law
- Transportation and Warehousing
- Duty Drawback
- Demand and Recovery
- Confiscation of Goods and Conveyances
- Refund
- LESSON ROUND UP
- SELF TEST QUESTIONS

### LEARNING OBJECTIVES

The Customs Act of 1962 provides for the implementation and collection of duty on goods imported or exported from the country. This Act also deals with the Import and Export procedures, Prohibitions on importation and exportation of goods, penalties, offences and much more. With the implementation of Goods & Services Tax w.e.f. July 1, 2017, various indirect taxes have been subsumed into it. However, the Basic Customs Duty has not been subsumed under GST, which will continue to be levied along with Goods & Services Tax.

At the end of this lesson you will be able to learn about:

- An Overview of the Customs Act, 1962
- Types of Customs Duty
- Valuation Rules
- Import and Export Procedures
- Duty Drawback

## OVERVIEW OF CUSTOMS LAW

Customs Duty is an indirect tax, imposed under the Customs Act formulated in 1962. The Customs Act, 1962 is the basic statute which governs entry or exit of different categories of vessels, aircrafts, goods, passengers etc., into or outside the country. The Act extends to whole of India and, save as otherwise provided in this Act, it applies also to any offence or contravention thereunder committed outside India by any person.[Inserted by the Finance Act, 2018, w.e.f. 29-3-2018]

The Customs Act, 1962, not only regulates the levy and collection of duties, but also, serves equally important purposes, like :

- i) Regulation of Imports & Exports
- ii) Protection of Domestic Industry
- iii) Prevention of smuggling
- iv) Conservation and augmentation of foreign exchange

It may be pertinent to note that it is Section 12 of the Customs Act, 1962 that provides duties of customs to be levied at such rates as may be specified under the Customs Tariff Act, 1975 or other applicable Acts on goods imported into or exported from India. Customs Act, 1962 and Customs Tariff Act, 1975 are the two limbs of Customs Law in India which must be read with rules and regulations.

### Rules & Regulations

The rule making power is delegated to the Central Government while the regulation making power delegated to the Central Board of Indirect Taxes and Customs (CBIC).

#### *Differences between Rules and Regulations*

Parameter	Rules	Regulations
Power to make	Section 156	Section 157
Authority	Central Government is authorized to make the rules	CBIC is authorized to make the regulations
Purpose	To supports the Act	To support the Act and the Rules
Content	Transaction Value; Chargeability of accessories & Repairs & Maintenance Spare Parts; Detention & Confiscation of Goods; Goods mentioned in the shipping bill / Bill of Export but either not exported OR exported and subsequently re-landed;	The form of Bill of Entry; shipping bill; bill of export; import & export manifest; form & manner of making application for refund of duty; conditions for transshipment & removal of good without payment of duty; manner of conducting audit of duty assessment of imported / exported goods

### Definitions [Section 2]

Section 2 of the Customs Act, 1962 contains the definitions of various terms used at various places in the Act.

**Assessment : Section 2(2) :-** Determination of the dutiability of any goods and the amount of duty, tax, cess or any other sum so payable, if any, under this Act or under the Customs Tariff Act, 1975 (hereinafter referred to as the Customs Tariff Act) or under any other law for the time being in force and includes provisional assessment, self-assessment, re-assessment and any assessment in which the duty assessed is nil.

**Baggage : Section 2(3) :-** Includes unaccompanied baggage but does not include motor vehicles;

**Conveyance : Section 2(9) :-** Includes vessels (by sea), an aircraft (by air), and a vehicle (by land).

**Customs Area : Section 2(11) :-** Area of a customs station or a warehouse and includes any area in which imported goods or export goods are ordinarily kept before clearance by Customs Authorities.

**Customs Port : Section 2(12) :-** Any port appointed under clause (a) of section 7 to be a customs port [, and includes a place appointed under clause (aa) of that section to be an inland container depot];

**Customs Station : Section 2(13) :-** Any customs port, customs airport, international courier terminal, foreign post office or land customs station.

**Dutiable Goods : Section 2(14) :-** Any goods which are chargeable to duty and on which duty has not been paid.

**Duty : Section 2(15) :-** Duty means a duty of customs leviable under this Act.

**Export : Section 2(18) :-** Taking out of India to a place outside India.

**Export Goods : Section 2(19) :-** Any goods which are to be taken out of India to a place outside India.

**Exporter : Section 2(20) :-** Exporter, in relation to any goods at any time between their entry for export and the time when they are exported, includes any owner, beneficial owner or any person holding himself out to be the exporter.

**Foreign going Vessel / Aircraft : Section 2(21) :-** Vessel or aircraft for carriage of goods / passengers between any port / airport in India and any port / airport outside India whether touching any intermediary location or not, and includes :

- a) Any naval vessel of any foreign government taking part in any naval exercises;
- b) Any vessel engaged in fishing or any other operations outside the territorial waters of India;
- c) Any vessel or aircraft proceeding to a place outside India for any purpose whatsoever.

**Goods : Section 2(22) :-** Includes –

- a. vessels, aircrafts and vehicles;
- b. stores;
- c. baggage;
- d. currency and negotiable instruments; and
- e. any other kind of movable property;

**Import : Section 2(23) :-** Bringing in to India from a place outside India.

**Import Report : Section 2(24) :-** Report or the manifest required to be delivered under section 30.

**Imported Goods : Section 2(25) :-** Any goods brought into India from a place outside India but doesn't include Goods which have been cleared for home consumption.

**Importer : Section 2(26) :-** Importer, in relation to any goods, at any time between their importation, and the time when they are cleared for home consumption, includes any owner, beneficial owner or any person holding himself out to be the importer.

**India : Section 2(27) :-** Includes the territorial waters of India.

**Note:** Territorial waters extend upto 12 nautical miles from the baseline on the coast of India.

**Indian Customs Waters : Section 2(28) :-** The waters extending into the sea upto the limit of Exclusive Economic Zone under section 7 of the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976, (80 of 1976) and includes any bay, gulf, harbor, creek or tidal river.

**Note:** Indian Customs Waters extend upto 24 nautical miles from the baseline on the coast of India. It means an area extended upto 12 nautical miles beyond territorial waters.

**Person-in-charge : Section 2(31) :-** Means

- (a) in relation to a vessel, the master of the vessel;
- (b) in relation to an aircraft, the commander or pilot-in-charge of the aircraft;
- (c) in relation to a railway train, the conductor, guard or other person having the chief direction of the train;
- (d) in relation to any other conveyance, the driver or other person-in-charge of the conveyance;

**Prohibited Goods : Section 2(33) :-** Any goods, the import or export of which is prohibited by the Customs Act or any law for the time being in force, but doesn't include any goods, in respect of which the conditions subject to which the goods are permitted to be imported or exported have been complied with.

**Smuggling : Section 2(39) :-** Any act or omission which will render such goods liable to confiscation under section 111 or 113.

**Warehouse : Section 2(43) :-** A public warehouse licensed under section 57 or a private warehouse licensed under section 58 or a special warehouse licensed under section 58A.

**Warehoused Goods : Section 2(44) :-** Goods deposited in a warehouse.

## LEVY & COLLECTION OF CUSTOMS DUTIES

### Levy of and Exemption from Customs Duty

Goods become liable for import OR export duty when Goods are Imported into India OR Exported out of India. Levy is the stage where the declaration of such liability is made and the persons / properties in respect of which the duty is to be levied is identified. If the Central Government is satisfied that it is necessary in the public interest to do so, it may, by notification in the Official Gazette, exempt generally either absolutely or subject to such conditions (pre-clearance) as may be specified in such notification, goods of the specified description, from the whole or any part of the customs duty leviable thereon. An exemption notification cannot be withdrawn and duty cannot be demanded with retrospective method.

Section 12 of the Customs Act, 1962 is the charging section, which is the basis for levy of tax. As per section 12, customs duty is imposed on goods imported into or exported out of India as per the rates provided in Customs Tariff Act, 1975 or any other law for the time being in force. This can be analyzed as below:

- Customs duty is levied on goods where such goods are imported into or exported out of India.
- Levy is subject to other provisions of this Act or any other law.
- The rates of Basic Custom Duty are specified under the Tariff Act, 1975 or any other Law.
- Even goods belonging to Government are subject to levy, though they may be exempted by notification(s).

Customs Tariff Act, 1975 has two schedules:

**Schedule I :** Tariff rates for imported goods known as Import Tariff

**Schedule II :** Tariff rates for exported goods known as Export Tariff

## TYPES OF CUSTOMS DUTIES

### Import Duty

#### a) Basic Customs Duty

- i) Levied as a percentage of value as determined under section 14(1)
- ii) Could be levied at "Standard" OR "Preferential Rates" (where imported from a preferential area as

may be specified by the Government)

- iii) Onus is on the person (owner) to substantiate with the supporting evidence that the goods are chargeable with a preferential rate of duty

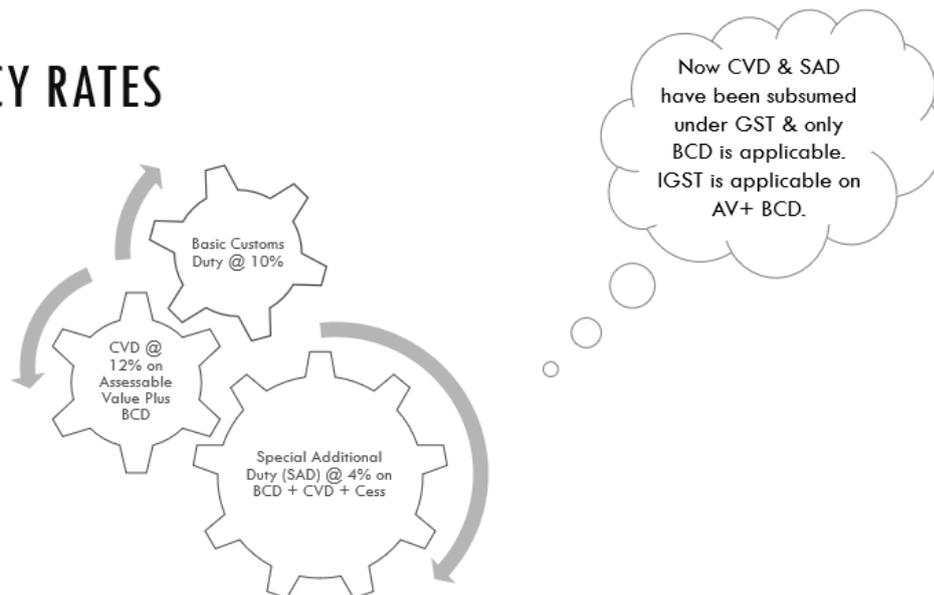
**b) Additional Customs Duty / Countervailing Duty (CVD)**

- i) It is equivalent to the amount of excise duty on like goods manufactured / produced in India
- ii) Under the GST regime, this duty is subsumed under GST and additional duty / IGST is payable on assessable value plus basic customs duty
- iii) In case of alcoholic liquor for human consumption is imported into India, the same is still under state excise which has not been subsumed under GST. Therefore, IGST is not leviable under Import
- iv) In case inward taxable supplies are in the nature of Imported Goods, which have been taxed and have been consumed in the manufacture of outward taxable supplies, Input Tax Credit is available to the extent of IGST paid

**c) Additional Duty / Special Additional Duty (SAD)**

- i. It used to be levied to offset the Sales Tax / VAT
- ii. However, this has now been subsumed under GST and as such is leviable only on imported goods for which GST is not applicable (example : Petroleum Products)

## LEGACY RATES



Provisions under GST regime:

The goods imported in to India, are now subject to IGST and not CVD or SAD. However, petroleum is outside the scope of GST, and hence CVD and SAD are applicable to them. IGST is now payable on Assessable Value + Basic Customs Duty.

+ plus Basic Customs Duty.

As per section 3(7) of the Customs Tariff Act, 1975 Any article which is imported into India shall, in addition, be liable to integrated tax at such rate, as is leviable under section 5 of the Integrated Goods and Services Tax Act, 2017 on a like article on its supply in India, on the value of the imported article as determined under section 3(8) of The Customs Tariff Act, 1975.

**d) GST Compensation Cess:**

Any article which is imported into India shall, in addition, be liable to the goods and services tax compensation cess at such rate, as is leviable under section 8 of the Goods and Services Tax (Compensation to States) Cess Act, 2017 on a like article on its supply in India, on the value of the imported article as determined under section 3(10) of The Customs Tariff Act, 1975 [Section 3(9) of the Customs Tariff Act, 1975].

**e) Protective Duty:** In order to protect any industry established in India, a duty may be imposed on imported goods on the recommendation of Tariff Commission [Section 6 of the Customs Tariff Act, 1975].

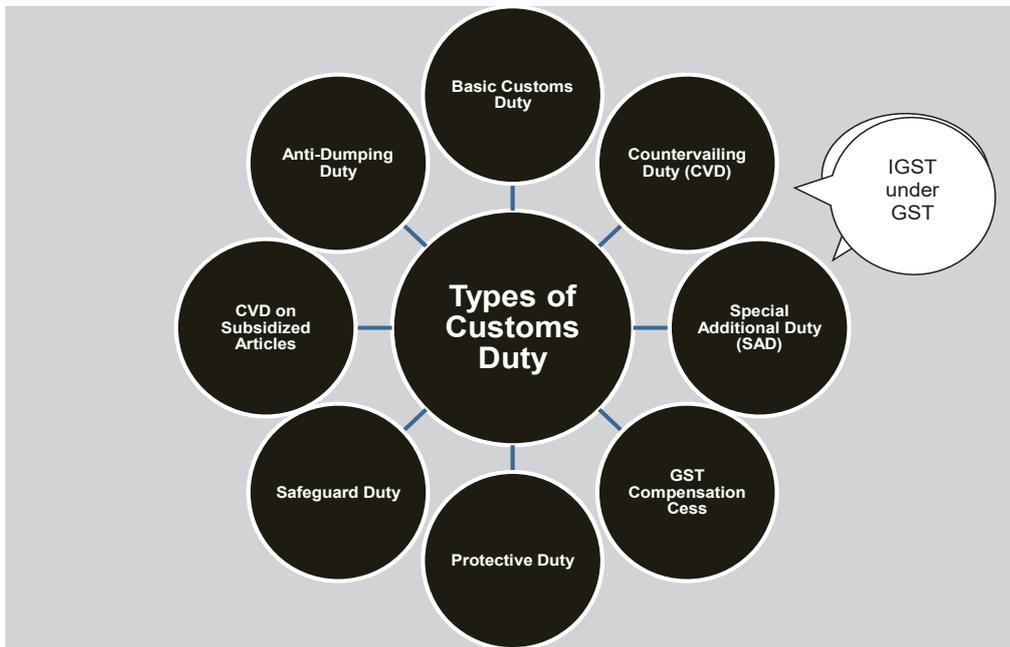
**f) Safeguard Duty:** The Central Government may impose safeguard duty on specified imported goods, if it is of the opinion that the goods are being imported in large scale and they are causing injury to the industry in India [Section 8B(1) of the Customs Tariff Act, 1975].

This is levied on goods imported into India, when such goods are already manufactured in India, but the costs are higher as compared to import prices. It is levied to ensure that the Indian manufacturers don't suffer owing to import of cheaper goods from outside and therefore aims to create a level playing field for the Indian manufacturers and importers, thereby with the intent of safeguarding the National interest.

Provisional Safeguard Duty may also be imposed by the Central Government subject to section 8B(1) of the Customs Tariff Act, 1975 on the basis of a preliminary determination that increased imports have caused or threatened to cause serious injury to a domestic industry [Section 8B(2) of the Customs Tariff Act, 1975].

**g) Countervailing Duty on Subsidized Articles:** Where any country or territory pays, bestows, directly or indirectly, any subsidy upon the manufacture or production therein or the exportation therefrom of any article including any subsidy on transportation of such article, then, the Central Government may, by notification in the Official Gazette, impose a countervailing duty [Section 9(1) of the Customs Tariff Act, 1975].

**h) Anti-Dumping Duty on dumped articles:** Where any article is exported by an exporter or producer from any country or territory to India at less than its normal value, then, upon the importation of such article into India, the Central Government may, by notification in the Official Gazette, impose an anti-dumping duty [Section 9A(1) of the Customs Tariff Act, 1975].

**Diagrammatic view of types of customs duties.****Social Welfare Surcharge (SWS) on imported goods [Section 110 of Finance Act, 2018 w.e.f 02-02-2018]**

It is a duty of customs levied for the purpose of the Union on the goods specified in the First Schedule to the Customs tariff Act, 1975, being goods imported into India. It is levied @10% on the aggregate of duties, taxes and cesses which are levied and collected by the Central Government under section 12 of the Customs Act, 1962. It is not applicable on safeguard duty, countervailing duty, antidumping duty, IGST and GST Compensation cess.

**Road and Infrastructure Cess on imported goods [Section 111 of Finance Act, 2018 w.e.f 02-02-2018]**

It is levied as duty of custom @ rupee 8 per litre on motor spirit (petrol) and high speed diesel (HSD) imported into India for the purpose of financing infrastructure projects.

**CLASSIFICATION & VALUATION OF IMPORT AND EXPORT GOODS****Classification**

Classification enables categorising the goods into groups / sub-groups, in order to apply a single rate of duty on each group / sub-group. This classification is based on the concept of Harmonised System of Nomenclature (HSN).

HSN is an internationally accepted coding system and the same was formulated and thereby enunciated under the General Agreement on Tariffs & Trade (GATT). At international level, the HSN classification of goods is a six digit coding system but India follows 8 digit coding system, wherein first two digit represent chapter number, next two digits represents heading number, next two digits represents sub heading number and last two digits product code.

**Interpretation Rules under the Customs Tariff Act, 1975****General Rule for Classification [Rule 1]**

The essence of this rule is that the reference to the rules may be made in case of ambiguity, that is, the reference to the six rules of interpretation is not required when classification of the goods is possible on the basis of description in the heading, sub-heading etc.

### Unfinished Articles & Mixtures [Rule 2]

- a) Any reference in a heading to an article, shall be deemed to include a reference to that article in an unfinished stage too, as long as in the present stage, the incomplete article exhibits the essential character of that article in complete / finished form

*Example* : Car without tyres or without seats would be still construed as Cars, but not Cars without engines

- b) Any reference in a heading to a material or substance, shall be deemed to include a reference to the mixtures and combinations of that material / substance with other materials / substances

*Example* : natural rubber would include its mixture with synthetic or other forms of rubber

### Classification of Goods classifiable under more than one head [Rule 3]

- a) "Specific Identification", i.e., the goods shall be classified under the heading which is closest to the specific description

*Example* : Mint Tea is not separately classified, but the classification should be tea as the product is closest to the one under the heading "tea", mint is only a flavour

- b) "Essential Character Principle", i.e., if composite goods cannot be classified as per Rule 3(a), then, shall be classified on the basis of material / substance that defines the essential character

*Example* : If one imports "Liquor Gift Sets" that have both, liquor and glasses, it should be classified under the heading, "Liquor", as the essential character of the composite item is the liquor itself and the glasses are pure ancillaries

- c) "Latter the Better Principle", i.e., when goods can't be classified under rules 3(a) or 3(b), the goods would be classified under the heading that appears last in the numerical order amongst those which equally merit consideration

*Example* : A gift set, which has socks and ties, can be classified under any of the above rules, and therefore should be classified as ties (heading 6117) over socks (heading 6115)

### Akin Principle [Rule 4]

This rule states that the goods which cannot be classified in accordance with Rules 1, 2 or 3, shall be classified under the heading which includes goods that are the most "akin or similar". An example would be anti-glare films used for car windows, venetian blinds, all of these are not separately classified, they would be classified under the heading for "builders' ware of plastic", as that's the closest these fit into.

### Cases / Containers for packaging of goods [Rule 5]

Goods which are in the nature of containers / packages such as necklace boxes, camera cases, musical instrument cases, will be classified with the specific article which are generally sold within these packages. However, this is applicable to containers, which are fitted for the article they will contain, are suitable for long term use, protect the article when not in use, and are of a kind normally sold with such articles.

### Sub-headings [Rule 6]

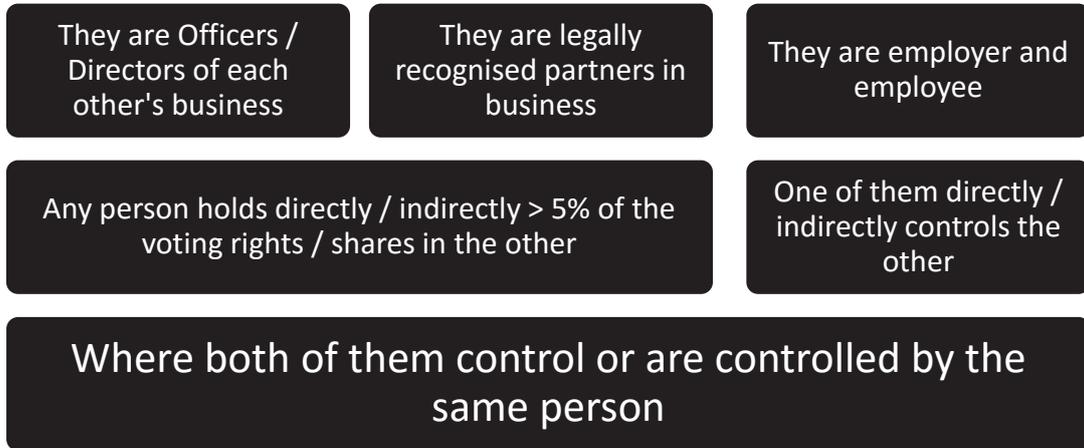
Only sub-headings at the same level are comparable.

## Valuation for Customs Duty

Valuation for Customs Duty begins with determination of "Transaction Value". Transaction Value includes the price paid / payable as consideration. In case of transaction between related parties, sale transaction would be examined to ascertain the influence of relationship on the declared value, and whether the same could then be

accepted as transaction value (it needs to be at arm's length)

Parties are said to be related when –



### Valuation Rules

The Customs Value fixed as per Section 14 is the value that would be used for calculating the Customs Duty Payable. This is also called Assessable Value.

Criteria for deciding Value –



### **Rule 3(1)**

Value of Imported Goods shall be the Transaction Value adjusted in accordance with provisions of rule 10; as under :

#### ***For Imports***

Price paid / payable for delivery at the time and place of Importation, which essentially implies that the price up to a port in India when goods are imported has to be considered (i.e. C.I.F. Value)

#### ***For Exports***

Price paid / payable for delivery at the time and place of Exportation, which essentially implies that the price up to a port in India when goods are exported has to be considered (i.e. F.O.B. Value)

- C.I.F. = F.O.B. + Cost of Transport (Freight) and Insurance
- Freight to be taken at actuals capped to a maximum of 20% of F.O.B.
- Insurance to be taken at actuals capped to a maximum of 1.125% of F.O.B.
- Exchange rate as applicable on date of presentation of a shipping bill or bill of export, as determined by Central Board of Indirect Taxes (CBIC) or ascertained in manner determined by CBIC should be considered

If the valuation as above cannot be determined, then sequentially, the following rules will be applied.

### **Identical Goods / Comparison Method [Rule 4]**

Transaction Value (TV) of identical goods will be used in determining the value of imported goods, only when such identical goods are sold at the same commercial level, and these goods are substantially the same quantity as the goods being valued. TV of goods exported would be based on the transaction value of the goods of like kind and quality exported at or about the same time to the same destination country, or in absence, another destination country.

In applying this rule, if more than one transaction value of identical goods is found, the lowest such value shall be used to determine the value of imported goods.

### **Similar Goods for Imports and Computed Value Method for Exports [Rule 5]**

The TV for Imported Goods would be based on that of the similar goods (i.e., like characteristics & country of production). The TV of goods exported, would be taken at computed value, i.e., Cost of Production + Charges for design/brand + Reasonable profit.

### **Residual Method [Rule 6]**

For exports, the TV would then be arrived at by reasonable and consistent means by Customs Officer. For Imports, Rule 7 and 8, as below would be invoked.

### **Deductive Value [Rule 7]**

Unit price at which the imported goods (or) identical (or) similar imported goods are sold in the greatest aggregate quantity

Less : - Commission, Selling Expenses, and Profit made, Transport & Insurance & Taxes within India.

The goods at or about same time can be considered, if not at the earliest date of importation but before the expiry of 90 days after such importation

**Computed Value [Rule 8]**

This would be the cost of materials used in producing the imported goods, including fabrication costs, and usual profits commensurate with sale of goods of same class in India, including specific additions as per Rule 10 (i.e., Insurance, Freight and Landing Charges)

**Valuation Terminologies**

*FOB* : This is also known as “Free on Board” OR “Freight on Board”. It signifies the cost of delivering the goods to the nearest port and thereafter the Buyer is responsible to ship from there to the buyer’s address.

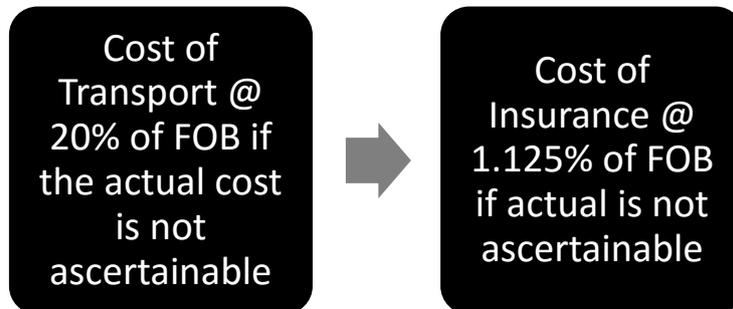
*CIF* : This is known as “Cost, Insurance & Freight” Value. This would add on the Insurance and Freight to the FOB Values, as explained below.

Addition of cost of freight in case of imports:

Mode of Transportation ->	By Air	Any other mode
Actual Freight Ascertainable	Actual Freight; or 20% of FOB value of the goods, Whichever is less	Actual Freight
Actual Freight Not Ascertainable	20% of FOB value of the goods	

Addition of cost of insurance in case of imports:

If Actual cost of insurance available	Actual cost of insurance
If Actual cost of insurance not available	1.125% of the FOB value of the goods



**Relevant date for rate of duty on -**

**Imported Goods (Section 15):**

Section	Types of Goods	Relevant Date
15(1)(a)	Goods cleared for home consumption under section 46	Rate prevailing on the : a. date of presentation of bill of entry; or b. date of entry inwards of the vessel/aircraft/vehicle whichever is later

15(1)(b)	Goods cleared from a warehouse under section 68	Rate prevailing on the date of presentation of Ex-Bond bill of Entry for home consumption
15(1)(c)	In case of any other goods	Rate prevailing on the date of payment of duty

Exported Goods (Section 16):

Section	Types of Goods	Relevant Date
16(1)(a)	Goods entered for export under section 50	Rate prevailing on the date on which proper officer makes an order permitting clearance and loading of the goods for exportation under section 51

Note: Provisions of both section 15 and 16 are not applicable to baggage and goods imported/exported by post.

### Specific Additions

These would include expenses incurred by the buyer and not included in the price. Any payments made to the seller as a condition of sale

### Template for Calculation of Import Duties

	INR	
Assessable Value (AV)	1000	
Basic Custom Duty (BCD)	100	Taken at 10% of AV
Safeguard Duty	300	Taken at 300% of AV
Social Welfare Surcharge (SWS)	10	Taken at 10% of BCD
Anti Dumping Duty	200	
Total	1610	
IGST	289.8	Taken 18% of Total
GST Compensation Cess(GCC)	241.50	Taken 15% of Total
Total Taxes and Duties	1141.30	

### Illustration 1

Use the information appended below to find out the assessable value.

Item No.	Description	USD
1	Cost of Machine at the factory of the US Exporter	17500
2	Transport Charges from the said factory until the sea port for onward shipment	2500
3	Handling Charges at the Port of Shipment	200
4	Buying Commission paid by Importer	50
5	Freight Charges until the Indian Port	2500
	Please use an exchange rate of \$1=63.84 INR	

Description	USD	INR
Cost of Machine at the factory of the US Exporter	17,500	

Transport Charges from the said factory until the sea port for onward shipment	2,500	
Handling Charges at the Port of Shipment	200	
F.O.B. Value	20,200	
Insurance Charges @ 1.125%	227	
Freight Charges	2,500	
Buying Commission paid by Importer	-	
C.I.F. Value	22,927	
Assessable Value	22,927	14,63,660

**Notes :**

- 1) All costs up to the Port of Shipment will be included in the F.O.B. Value
- 2) Insurance Charges shall be added on @ 1.125% of F.O.B. Value as the value of Insurance Charges as it is not ascertainable
- 3) The actual freight charges of USD 2500 are included as it is within the maximum that can be added on is USD 4040 (which is 20% of F.O.B. Value)
- 4) Buying Commission is not to be included in the computation

**Illustration 2**

Ms. Nisha imported 2500 Tonnes of goods and materials valued at USD 50 per tonne (C.I.F.). Exchange Rate per notification (CBIC) was \$1= INR 63.84. The Basic Customs Duty was chargeable @ 10% and over and above, there was an anti-dumping duty levied on the goods, which was the differential between the amount so calculated as the Landed Value Incl. Basic Customs Duty and Cess is INR 100,00,000/-. Calculate the Anti-Dumping Duty.

Description	Tonnes	Rate	USD	INR
C.I.F Value	2,500	50	1,25,000	79,80,000
Assessable Value				79,80,000
Basic Custom Duty(BCD) @ 10%				7,98,000
Social Welfare Cess @ 10% of BCD				79,800
Landed Value				88,57,800
Landed value as per Notification				1,00,00,000
Anti Dumping duty				11,42,200

*Note :* Anti-Dumping duty is levied to promote the local industry and to curb imports, and to ensure that India is not used as a dumping ground, which could otherwise have serious repercussions on the economic growth of the Nation. This Anti-dumping duty is continued even under the GST regime.

**Illustration 3**

XYZ imports Pan Masala into India and the C.I.F value is INR 500/-. The rates of tax for Pan Masala (HSN Code

21069020) are Basic Customs Duty 37.5%; IGST 28% and Compensation Cess 60%.

Compute Total Import Duty.

Description	INR	
CIF Value	500	
Assessable Value(AV)	500	
Basic Custom duty @ 37.5%	188	A
Social Welfare Cess @ 10% of A	18.8	B
AV + BCD + Cess = 500 + 188 + 18.8 =706.8		
IGST @ 28%	197.90	C
Compensation Cess @ 60%	424.08	D
Total Import duty payable(A+B+C+D)	828.78	
Total Value incl Import Duty	1328.78	

*Note : The CBIC notified rate of exchange in force as on the date on which the bill of entry is filed, is what will be applied for computation of assessable value. Note also, that the above cess, Compensation Cess is leviable under GST and hence applicable on the same base; i.e. AV + BCD, like IGST.*

#### Illustration 4

M/s XYZ Chemicals Ltd. imported a machine from ABC Inc. at USA (Boston). The price of the machine was contracted at USD 12500 and the machine was shipped on 1st February, 2018. Meanwhile XYZ Chemicals, renegotiated a price reduction owing to the past relationship, and this price reduction was agreed vide an e-mail and a fax on 15th February, 2018. The machine arrived in India (Mumbai Port) on 1st March, 2018.

The assessing authorities claimed that the duty would be payable basis the Original Contracted price, pre-shipment.

Please advise your stand as a Tax Consultant to XYZ Chemicals Ltd.

The stand taken by the Customs Authorities is factually incorrect and can be challenged under the Law. The basic reason is that the Transaction Value is considered at the time and place of importation. Hence, it was contended that the Import is complete only when the Goods become a part of the Country. Here, in the present case, the price was mutually revised while the Goods were still in transit. Hence, the revised price could be considered for arriving at the Assessable Value and the same was also enunciated under the case law : *Gujarat Heavy Chemicals v. Commissioner of Customs, Ahmedabad 2004.*

#### Illustration 5

Calculate the total import duty payable if :

- F.O.B. Value is GBP 18000
- Freight Charges incurred (actual) are GBP 7500
- Design & Development Charges incurred at UK are GBP 2500
- Selling Commission at India paid to a local agent @ 2% of F.O.B. Value
- Date of Bill of Entry : 24th Oct 2017 (Rate of Basic Customs Duty is 20% and Exchange Rate as notified by CBIC is INR 68 to 1 GBP)
- Date of Entry Inward : 20th Oct 2017 (Rate of Basic Customs Duty is 18% and Exchange Rate as

notified by CBIC is INR 70 to 1 GBP)

- g) IGST @ 18%
- h) Insurance Charges could not be ascertained

ITEM	GBP	INR	
F.O.B	18,000		
Design & Development	2,500		
Insurance	202.5		
Freight	3,600		
C.I.F	24,302.5	16,52,570	
Local commission		24,480	
C.I.F Value(Adj)		16,77,050	
Assessable Value		16,77,050	
Basic Custom Duty		3,35,410	A
Social Welfare cess @ 10%		33,541	B
Total for IGST(AV + All Custom Duties)		2,04,6001	
IGST	3,68,280	3,71,963	C
Total Import Duty	7,37,231	7,44,603	A+B+C

Notes :

- a) Insurance is taken @ 1.125% of F.O.B. value, as the charges aren't ascertainable
- b) Freight can be taken at actuals but capped to 20% of F.O.B.
- c) Selling Commission is paid in Indian Rupees to local agents appointed by exporters to usher their sales in India and hence included in C.I.F. Value
- d) The Exchange Rate in force per CBIC notification, on the date when the Bill of Entry is presented is to be considered
- e) IGST is levied on Assessable Value + All Customs Duties
- f) Social welfare Cess is levied on BCD @ 10%

### Illustration 6

Determine the Customs Duty payable including the safeguard duty of 20%, for Goods with Assessable Value of INR 50,00,000 considering BCD @ 10%, IGST @ 18%

Item	INR	
Assessable Value	50,00,000	
Basic Custom Duty`	5,00,000	A
Social Welfare Surcharge	50,000	B

Safeguard Duty	10,00,000	C
Total for IGST(AV + All Custom Duties)	65,50,000	
IGST	11,79,000	D
Total Duty & Taxes payable(A+B+C+D)	27,29,000	

**EXEMPTIONS**

**Exemptions under the Customs Act**

If the Central Government is satisfied that it is necessary in the public interest to do so, it may, by notification in the Official Gazette, exempt generally or subject to such conditions as may be specified in the notification, which would need to be fulfilled before / after clearance, goods of the specified description from the whole or any part of the duty of customs.

It may, by special order, exempt from duty, any goods, on which duty is leviable only under exceptional circumstances. Further, no duty is to be collected, if the amount of duty leviable is less than or equal to INR 100.

Both the general and specific exemptions mentioned above, may be granted by providing for the levy of duty at a rate expressed in a form which is different from the statutory rate.

An exemption notification cannot be withdrawn and the duty cannot be demanded with retrospective effect.

**OFFICERS OF CUSTOMS LAW**

**Power of Customs Officers**

The Customs Officers are authorised to :

- a) Declare warehousing stations
- b) Allow setting up warehouses (Public / Private)
- c) Power to search any vessel / conveyance / person
- d) Power of Seizure of Goods
- e) Power to Arrest

**ADMINISTRATION OF CUSTOMS LAW**

Person in Charge : Master (in case of a Vessel), Commander or Pilot (in case of an aircraft), Conductor, guard or any other person having the chief direction of the train (in case of a train), Driver or other person in charge of the conveyance (any other conveyance).

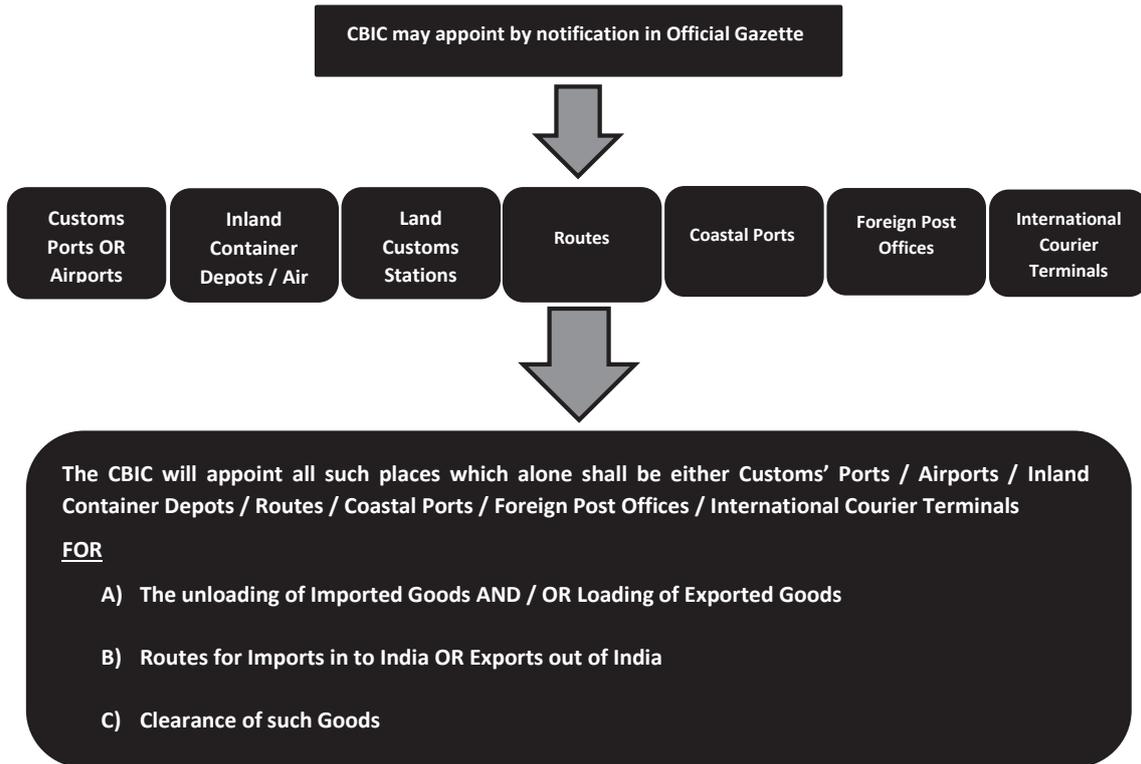
**Responsibilities of a Person In Charge (PIC)**

- Submitting the Import / Export Manifest
- Ensuring that the conveyance comes through the proper route
- Ensuring that the conveyance lands at the appropriate place
- Ensure that the Goods are loaded / unloaded only after proper permissions / orders

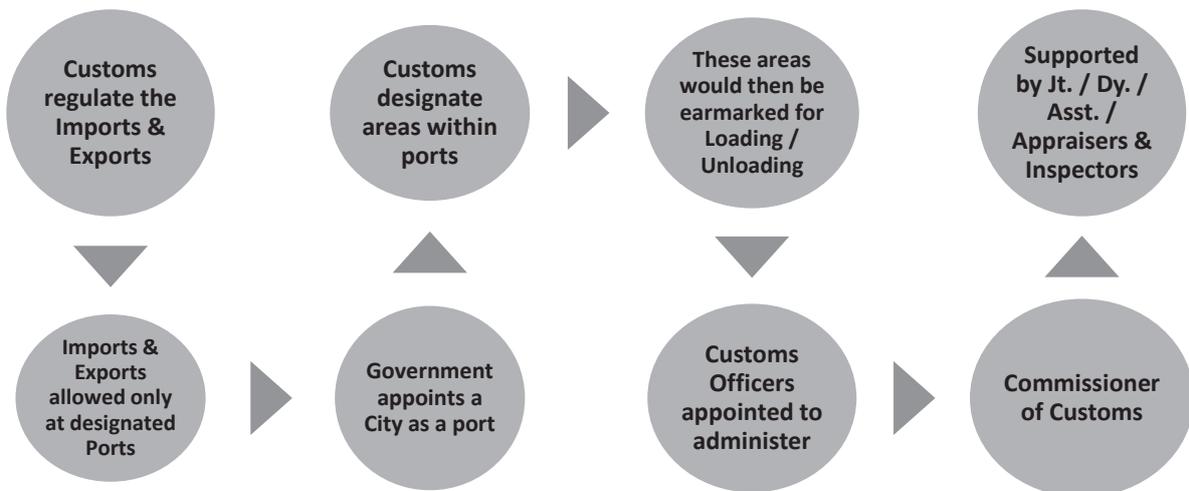
The *Import Manifest* means the report which is required to be delivered under section 30, which states that the PIC, in the case of a vessel / an aircraft, shall deliver to the proper officer an import manifest PRIOR to the arrival of vessel / aircraft and in case of a vehicle, within 12 hours post the arrival at the customs station, in the prescribed format.

Also, it's imperative to note that the import is completed only when the goods so imported are cleared for home consumption.

### Establishment under Customs



### Administration



### Types of Ports

- a) Sea Ports
- b) Airports
- c) Land Customs Stations (LCS)
- d) Inland Container Depots (ICD)
- e) Container Freight Stations (CFS) attached to ports

### Mode of Clearance

- a) Regular Cargo
- b) Courier
- c) Foreign Post Office
- d) Baggage

## IMPORT & EXPORT PROCEDURES UNDER CUSTOMS LAW

### Procedure for Import through Sea Route (Cargo Clearance)

#### For the Carrier

**Section 30** : Filing the Import General Manifest (IGM) prior to the arrival of the vessel

IGM is generally filed on the basis of Bill of Lading / Airway Bill and is issued by the Carrier. It contains details around the shipper, consignee, no. of packages, description of goods, date, vessel details etc.

**Section 31** : Entry Inward granted by the Customs

It acts as permission for unloading the Goods. The date herein would be construed as the relevant date for arrival of goods in India

#### For the Custodian

**Section 45** : Custodian is appointed by the Customs

The custodian would be responsible for keeping proper record of unloaded goods. The custodian is also responsible to ensure that the goods don't leave the customs area (that is clearance) without proper authorisation from the Customs Officer

#### For the Importer

**Section 46** : The importer needs to submit the bill of entry. This Bill of Entry needs to be signed by the Importer. The Bill of Entry contains the details of goods along with :

- Bill of Lading
- Invoice
- Packing List
- Product Literature
- Licence
- Import Permit

- GATT declaration form duly signed by the Importer

### For the Customs

The Customs Authorities note the Bill of Entry by assigning a number and date stamp. This date is then construed as the date of presentation of Bill of Entry.

Post the above procedures, the assessment as described above is undertaken, and once the assessed duty is paid vide TR6 Challan, this Challan is submitted as evidence of payment to the Customs authorities, and the Out of Charge Order is issued, and on the basis of this Order, the Custodian allows the Clearance of Goods from the Customs Area.

Demurrage is the charges levied by the port authorities, if not cleared within 3 days of unloading.

## Procedure for Export through Sea Route (Cargo Clearance)

### For the Carrier

**Section 41** : Filing the EGM prior to the departure of the vessel

Export General Manifest (EGM) is generally filed on the basis of Bill of Lading / Airway Bill and is issued by the Carrier. It contains details around the shipper, consignee, number of packages, description of goods, date, vessel details etc.

**Section 39** : Entry Outward granted by the Customs

It acts as permission for loading the Goods. The date herein would be construed as the relevant date for exportation of goods out of India

### For the Exporter

**Section 50** : The Exporter needs to submit the Shipping Bill. This Shipping Bill needs to be signed by the Exporter. The Shipping Bill contains the details of goods along with :

- Invoice
- Packing List
- Product Literature
- Licence
- Export Permit
- Softex / other compliances

### For the Customs

The Customs Authorities note the Shipping Bill by assigning a number and date stamp. This date is then construed as the *date of presentation of Shipping Bill*.

Post the above procedures, the assessment as described above is undertaken, and once the assessed Duty is paid vide TR6 Challan, this Challan is submitted as evidence of payment to the Customs authorities, and the Let Export Order is issued, and post that the loading can commence.

## TRANSPORTATION & WAREHOUSING

### Transit and Transhipment

A conveyance/vessel may reach a port but may not unload the goods at that port. It may halt at the port for any other purpose such as repairs, replenishment of supplies, refuelling etc. Once the purpose is over, it may start sailing to the destination port. In this case two ports are involved :-

**762 EP-TL**

- 1) the halting port(known as transit port) and
- 2) the destination port (called as port of clearance).

Such a phenomenon of temporary stay at a port other than a destination port is called transit.

In transit; the goods remain in the same vessel and consequently reach the port of clearance.

In transshipment, however, the vessel after reaching an intermediate port, transfers the goods to another vessel and the second vessel into which the goods are transferred (loaded) from the first vessel, carries the goods to the destination port.

**Transit of Goods without payment of duty [Section 53]**

**Section 53** : Accordingly, any goods imported in a conveyance and mentioned in the import manifest or the import report, as the case may be, for transit in the conveyance to any place outside India or any Customs station may be allowed to be so transited without payment of duty, subject to such conditions, as may be prescribed.

**Transshipment of Goods without payment of duty [Section 54]**

In case any goods imported into a Customs station are intended for transshipment, a bill of transshipment shall be presented to the proper officer in the prescribed form.

However, where the goods are being transhipped under an international treaty or bilateral agreement between the Government of India and Government of a foreign country, a declaration for transshipment instead of a bill of transshipment shall be presented to the proper officer in the prescribed form.

Where any goods imported into a Customs station are mentioned in the Import Manifest or import report as the case may be, as for transshipment to any place outside India, such goods may be allowed to be so transhipped without payment of duty.

**Differences between Transit & Transshipment**

<b>Transit</b>	<b>Transshipment</b>
Goods remain in the same vessel at the intermediate port	Goods are transferred to a different vessel at the intermediate port
Only import manifest has to be submitted for entry	Bill of Transshipment / declaration is also required to be submitted
No supervision is required at the Intermediate Port	Transshipment process is conducted under the supervision of the Customs Officer
The same vessel reaches the destination port	A different vessel reaches the destination port

**Warehousing**

Imported goods need not be cleared for home consumption immediately on arrival. If importer wish or he may not require the goods immediately or sometime to avoid demurrage charges or intends to re-export of such imported goods or for any other reasons, he may store such goods in Warehouse without payment of goods. Warehouses allow goods to be stored and thus deferment of duty. The Goods are to be released from the Warehouse, subject to "clearance"; i.e.; post assessment and payment of Duty. Warehouse may public warehouse licensed u/s 57 or private warehouse licensed u/s 58 or special warehouse licensed u/s 58A.

**Public Bonded Warehouse**

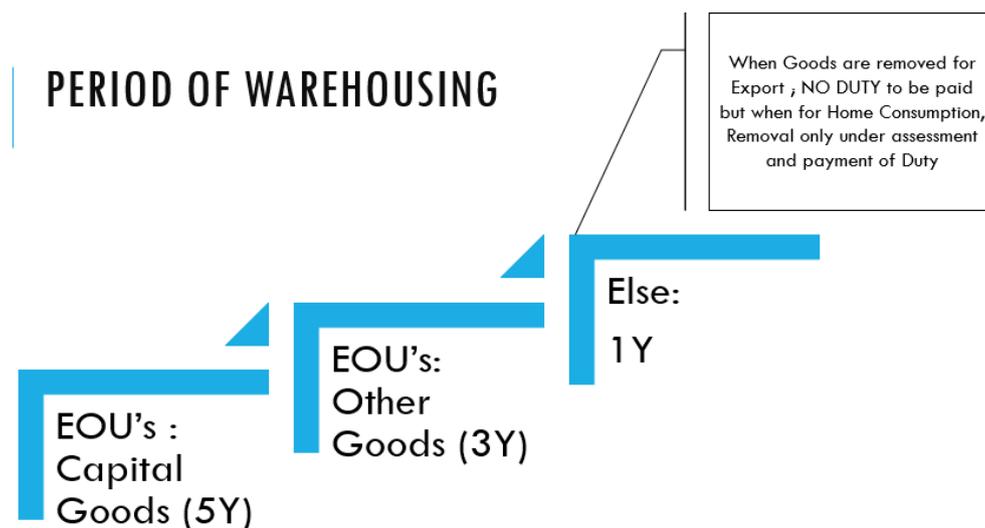
- 1) These are owned and managed by Government / Governmental Bodies / Agencies

- 2) Only dutiable goods can be warehoused therein
- 3) Availability of space certificate from the warehouse keeper would be required
- 4) A double duty bond would also be required to be furnished for deposit of goods
- 5) Also, the person seeking warehousing would need to pay rental / warehousing charges to the warehouse keeper

### **Private Bonded Warehouse**

- 1) These are owned and managed by private entities
- 2) These aren't generally allowed where the public bonded warehouses are available
- 3) Only dutiable goods can be warehoused therein
- 4) Availability of space certificate from the warehouse keeper would not be required in this case
- 5) Double bond duty would still be required but, customs officers would need to be posted at the expense of the warehouse keeper

The Goods so warehoused, can vary, depending on whether these are for 100% Export Oriented Units (EOU's) or otherwise, as explained by the diagram below (up to a period of 5 years / 3 years / 1 year) :



## **BAGGAGE RULES**

Goods imported by a passenger or a member of crew in his baggage are classified under one tariff heading and levied to a single rate of duty. Section 77 provides that the owner of any baggage shall for the purpose of clearing it make a declaration of its contents to the proper officer. Baggage includes unaccompanied baggage but excludes motor car, alcoholic drink (beyond certain limit) and goods imported through courier. Baggage Rules, 2016 provide for duty free clearance, up to a certain limit, of articles such as used personal effects, travel souvenirs and other articles when carried on the person or in the accompanying baggage of the passenger arriving in India. Personal effect means things required for satisfying daily necessities but does not include jewellery. Generally, duty free allowance is allowed to the Indian resident or foreigner residing in India.

**Duty Free Baggage Allowances of Dutiable and Non-Prohibited Articles  
(Baggage Rules, 2016)**

Rule	Passenger	Passenger arriving from countries	Amount of Duty Free Baggage Allowance
Rule 3	An Indian resident or a foreigner residing in India or tourist of Indian origin	Other than Nepal, Bhutan or Myanmar	Rs. 50,000
Proviso to Rule 3	Tourist of foreign origin	Other than Nepal, Bhutan or Myanmar	Rs. 15,000
Rule 4	An Indian resident or a foreigner residing in India or tourist	Nepal, Bhutan or Myanmar	Rs. 15,000
Rule 5	Any passenger residing abroad for more than one year	Any country	Gold Jewellery: a. Gentlemen – 20 grams with a value cap of Rs. 50,000 b. Lady – 40 grams with a value cap of Rs. 1 lac

## DUTY DRAWBACK

### Duty Drawback

Duty drawback provisions enables the exporter to obtain a refund of the Import Duties (Customs Duty) paid on :

- imported goods which are meant for re-exportation; or
- inputs, which are processed for / used in manufacture of final products to be exported.

The Central Government is empowered to grant duty drawback (Section 74 & Section 75).

This benefit is available not only on the re-export of the duty paid goods (Section 74), but also, on imported materials used in the manufacture of Goods which are exported (Section 75).

These goods should be entered for export within 18 months.

The procedure is as under :

- ✓ At the time of export, the Exporter shall endorse the shipping bill to the Proper Customs Officer
- ✓ Necessary forms like ARE1 are submitted
- ✓ Customs Officer makes an order permitting clearance for exportation (Section 51)
- ✓ If an amount of drawback, and interest paid to the exporter turns out to be higher than what he is eligible to, this amount would have to be repaid back to the Customs authorities
- ✓ If there is a drawback which is made to an exporter, who eventually cannot realise the Invoice (export proceeds) within the period(s) specified by FEMA, such drawback could be recovered from the exporter

An exporter could opt for drawback as per the All Industry Rate (AIR) or the Brand Rate. The AIR's are fixed annually by the Directorate of Drawback, but the brand rates are for special products.

Where the goods are not put into use after import, 98% of Duty Drawback is admissible under Section 74 of the Customs Act, 1962. In cases where the goods have been put into use after import, Duty Drawback is granted on

a sliding scale basis depending upon the extent of use of the goods. No Duty Drawback is available if the goods are exported 18 months after import. Application for Duty Drawback is required to be made within 3 months from the date of export of goods, which can be extended up to 12 months subject to conditions and payment of requisite fee as provided in the Drawback Rules, 1995.

If the goods were in possession of the importer, they might be treated as used by the importer. As per the rules framed by Central Government, percentage of drawback is enumerated in given below table :

SI No	Period of Use	Percentage of Drawback
1	Upto 3 months	95%
2	More than 3 months to 6 months	85%
3	More than 6 months to 9 months	75%
4	More than 9 months to 12 months	70%
5	More than 12 months to 15 months	65%
6	More than 15 months to 18 months	60%
7	More than 18 months	Nil

Drawback is allowed if the use is over 24 months only with permission of Commissioner of Customs if sufficient cause is shown.

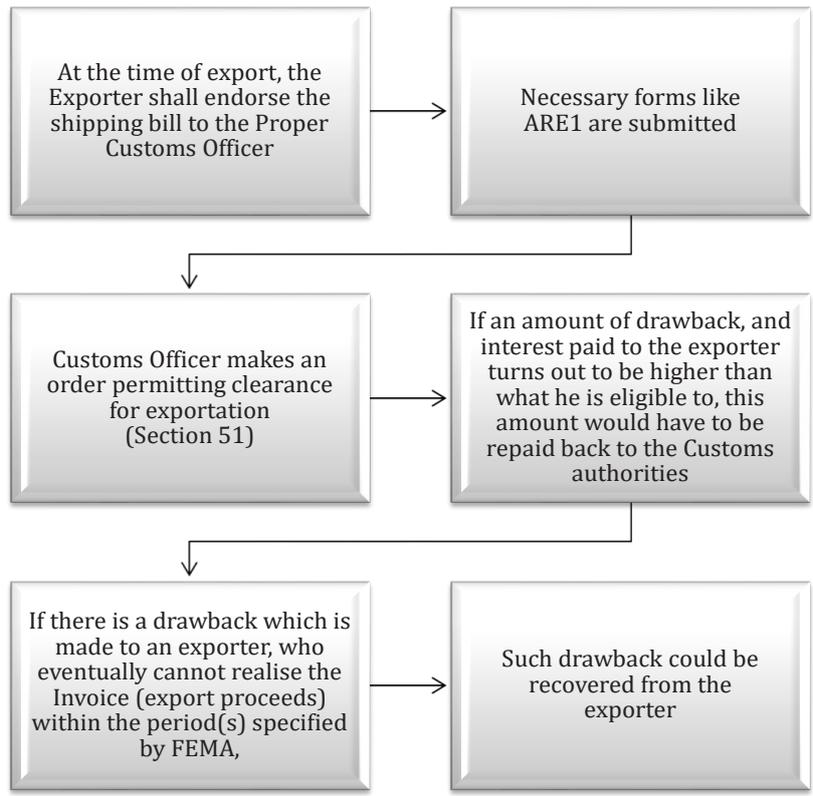
The Customs Act, 1962 lays down certain limitations and conditions for grant of Duty Drawback. No Duty Drawback shall be admissible where :

- I. The Duty Drawback amount is less than Rs.50/-.
- II. The Duty Drawback amount exceeds one third of the market price of the export product.
- III. The Duty Drawback amount is less than 1% of FOB value of export (except where the amount of Duty Drawback per shipment exceeds Rs.500/-).
- IV. Where value of export goods is less than the value of imported material used in their manufacture. If necessary, certain minimum value addition over the value of imported materials can also be prescribed by the Government.

The duty drawback needs to be paid, within 1 month, and if not paid, interest is payable to the claimant, at a specified rate.

Also, where drawback has been paid to the claimant in excess of what he is eligible to, the claimant has a time period of 2 months, to repay the excess, else, interest would be charged on the exporter from the date of payment of drawback until the date of recovery.

Duty Drawback is a scheme that encourages exports and thereby accelerates aggregate demand. It is intended to propel the economic growth of the nation and thereby accelerates the GDP.



**DEMAND & RECOVERY**

**Demand of Duty**

The notice of demand, must be served in writing, clearly mentioning the reasons, and providing the party an opportunity of being heard.

Generally, the Show Cause Notice, should be served within 1 year from the relevant date; that is; 1 year from the date of assessment / payment of duty.

However, in specific cases, where the duty or interest is not paid, or short paid, by reason of collusion, wilful suppression of facts, or misstatement, then the notice could be served within a period of 5 years.

The demand of duty provisions also calls for attachment of property for upto 6 months, for protection of interest of revenue and that could be extended for another period of 6 months, but the attachment period cannot exceed 2 years.

Post which the duty must be collected, in the name of customs duty and paid to the credit of the Government.

**CONFISCATION OF GOODS & CONVEYANCES**

**Confiscation of Goods**

Confiscation would generally tend to connote the forceful seizure / repossession of goods by the Government, without any compensation to the owner, as the possession of the goods was contrary to the law.

- ✓ **Section 111** states that the following improperly imported goods, shall be liable to confiscation
  - those which are imported by sea / air and offloaded / attempted to be offloaded in a port other than the appointed customs' port

- those which are imported by land / inland water, through a route other than a specified route
  - any dutiable / prohibited goods brought in to any bay / creek / gulf etc. for the purpose of being landed at a place other than customs' port
  - any dutiable / prohibited goods, found concealed in a conveyance
  - any dutiable / prohibited goods which should have been disclosed in the Import General Manifest but were not
  - any dutiable / prohibited goods removed / attempted to be removed from a warehouse / customs station, without permission
  - goods which do not match the description in the documents, vis-à-vis value / any other particulars
  - any goods, which were exempted from duty subject to a condition, which was eventually not met
- ✓ **Section 113** states that the following improperly exported goods, shall be liable to confiscation
- those which are exported by sea / air and loaded / attempted to be loaded in a port other than the appointed customs' port
  - those which are exported by land / inland water, through a route other than a specified route
  - any dutiable / prohibited goods brought near any bay / creek / gulf etc. for the purpose of being exported from a place other than customs' port
  - any dutiable / prohibited goods, found concealed in a conveyance
  - any goods loaded in a wrongful manner without necessary permissions
  - goods which do not match the description in the documents, vis-à-vis value / any other particulars
  - any goods, on which import duty wasn't paid and entered for export under a claim for drawback
- ✓ **Section 115** deals with Conveyances which are liable to confiscation
- Any vessel which has been within the Indian customs waters, any aircraft in India, or any vehicle, which has been adapted or fitted or structured in a manner that it purports or enables the concealment of goods
  - Any conveyance from which the goods are destroyed to prevent seizure
  - Any conveyance which had to stop / land but didn't do so except for sufficient cause
  - Any vessel from which goods which have been cleared for exportation, under a claim for drawback, were unloaded without necessary permissions
  - Any conveyance which carried goods into India, but which were later missing without any account for the loss
  - Any conveyance / animal used for smuggling
- ✓ **Section 118** deals with confiscation of packages
- Where the goods imported / exported are liable to confiscation, the packages within which they are cased and carried, are also liable for confiscation
- ✓ **Section 119** states that any goods used to conceal the smuggled goods are also liable to confiscation
- ✓ **Section 120 & 121** state that where the smuggled goods undergo a change in their physical form, post smuggling, even then they would be liable for confiscation (example : gold bars, later converted to ornaments). Also, where the smuggled goods are mixed in a manner with other goods such that they

are inseparable, entire goods would be liable to confiscation, and if the smuggled goods are sold off, the sale proceeds thereof are liable to confiscation

- ✓ **Section 122** states that the adjudicating authorities shall be give an opportunity of being heard to the party concerned
- ✓ **Section 123** clearly states that if goods are seized, the onus is on the owner to prove that they were not smuggled
- ✓ **Section 124** clearly states that before confiscation, it is necessary that a show cause notice (SCN) is issued to the owner, citing grounds and he should be given an opportunity to make a representation / of being heard. The SCN can be issued by a person not below the rank of Assistant Commissioner of Customs
- ✓ **Section 125** states that the authorised officer may allow the owner an option to pay fine in lieu of confiscation
- ✓ **Section 126** mentions that confiscated goods vest with the Central Government
- ✓ **Section 127** clarifies that any award of confiscation / penalty shall not interfere with or prevent the owner from being punished under any other provisions of this or any other law for the time being in force.

## REFUND

### Refund of Export Duty

Where on the export of goods; any duty has been paid, such duty shall be refunded to the person by whom or on whose behalf it was paid, if -

- (a) the goods are returned to such person otherwise than by way of re-sale;
- (b) the goods are re-imported within one year from the date of exportation; and

An application for refund of such duty is made within 6 months from the date on which the proper officer makes an order for the clearance of the goods when they are imported back.

### Refund of Import Duty

Where on the import of any goods, duty has been paid upon clearance for home consumption, such duty can be refunded to the person by whom or on whose behalf it was paid, if -

- a) The goods are found to be defective or not in conformity with the specifications
- b) The importer does not claim any duty draw back with respect to these goods
- c) If the goods are exported back / importer relinquishes his title to the goods / they are destroyed in the presence of the proper officer

An application for refund of duty is to be made within 6 months from the relevant date, i.e.,

- a) The date when the proper officer makes an order for clearance of goods when they are exported back
- b) Date of relinquishment if the importer relinquishes his title to the goods
- c) Date of destruction, where the goods are destroyed

Moreover, for all general refunds of duty, apart from the ones covered above, have a limitation period of 1 year, that is, the refund application must be filed within 1 year from the date of payment of such duty.

## MISCELLANEOUS

### Assessment of Duty [Section 17]

Section 17 of the Customs Act, prescribes the method for self-assessment of duty. The importer and exporter must self-assess the duty if any leviable on such goods. These self-assessed goods may be verified, examined or tested by the proper officer.

For verification, the proper officer may require the importer, exporter or any other person to produce any document or information, on the basis of which the duty leviable on the imported goods or export goods, as the case may be, can be ascertained and thereupon, the importer, exporter or such other person shall be bound to produce such document or furnish such information.

Where it is found on verification, examination or testing of the goods or otherwise that the self-assessment is not done correctly, the proper officer may, re-assess the duty leviable on such goods.

Where any re-assessment so done is contrary to the self-assessment done by the importer or exporter with respect to valuation of goods, classification, or concessions of duty availed and where the importer or exporter, as the case may be, confirms his acceptance of the said re-assessment in writing, the proper officer shall pass a speaking order on the re-assessment, within fifteen days from the date of re-assessment.

Where the importer or exporter is unable to make self-assessment and makes a request in writing to the proper officer for assessment; or where the proper officer deems it necessary for any reason whatsoever, the officer may direct that the duty leviable on such goods be subject to provisional assessment if the importer or the exporter, as the case may be, furnishes such security as the proper officer deems fit for the payment of the deficiency, if any, between the duty as may be finally assessed and the duty provisionally assessed.

When the duty leviable on such goods is assessed finally or reassessed by the proper officer in accordance with the provisions of this Act, then (a) in the case of goods cleared for home consumption or exportation, the amount paid shall be adjusted against the duty finally assessed and if the amount so paid falls short of, or is in excess of the duty finally assessed, the importer or the exporter of the goods shall pay the deficiency or be entitled to a refund, as the case may be; and (b) in the case of warehoused goods, the proper officer may, where the duty finally assessed or re-assessed, as the case may be, is in excess of the duty provisionally assessed, require the importer to execute a bond, binding himself in a sum equal to twice the amount of the excess duty.

The importer or exporter shall be liable to pay interest, on any amount payable to the Central Government, consequent to the final assessment order or re-assessment order, at the rate fixed by the Central Government from the first day of the month in which the duty is provisionally assessed till the date of payment thereof.

If any refundable amount is not refunded within 3 months from the date of assessment of duty finally or reassessment of duty, as the case may be, there shall be paid an interest on such un-refunded amount at such rate fixed by the Central Government until the date of refund of such amount.

### Prohibitions

Central Government may prohibit, either absolutely or subject to such conditions specified in the notification, the import / export of goods of the specified description, for :

- a) Maintenance of national security
- b) Maintenance of public order / decency
- c) Prevention of smuggling

## 770 EP-TL

- d) Conservation of exchange
- e) Safeguarding the balance of payments
- f) Protection of human lives / animals
- g) Protection of national treasures
- h) Protection of Patents & Trade Marks
- i) Prevention of contravention of any laws or in the interest of the public

### Offences

The following would constitute offences under the Act.

- a) Any mis-declaration in respect of the goods vis-à-vis its value or description or weight or origin
- b) Violation of allied acts, example, Violation of wild life, Drug & Cosmetics Act, Food laws etc.
- c) Landing of Goods at unauthorised ports

Such offences could result in civil or criminal liabilities or both and both could run simultaneously. Criminal prosecution could result in imprisonment + fines, and civil prosecution could result in alienation of wealth and penalties.

### Criminal Liabilities

- ✓ Punishment up to 7 years
- ✓ Offences involving duty evasion of more than INR 50 Lakhs, or prohibited goods, are non-bailable
- ✓ Fraudulent duty drawback claims, exceeding INR 50 Lakhs is also non bailable

### Civil Liabilities

- ✓ Recovery of duties short paid
- ✓ Interest charge
- ✓ Penalties
- ✓ Confiscation of import / export goods
- ✓ Confiscation of conveyances used for smuggling
- ✓ Up to 200% duty for unaccounted goods
- ✓ Up to 5 times the value of goods for forged documents

The normal limit for the above prosecution is one year, whereas for intended fraud, the time limit is 5 years.

### Advance Ruling

This refers to the determination, by the authority, of a question of law / fact specified in the application, regarding the liability to pay duty in relation to an activity proposed to be undertaken by an applicant.

In the context of Customs Act, the activity above in the definition would imply import / export.

The application is made in quadruplicate with the fees specified, and can be withdrawn within 30 days of the application. It is imperative to note that, for matters already pending before the Tribunal / Court, would not be admissible under Advance Ruling separately.

The ruling must be made within 90 days of the application.

### Settlement Commission

Settlement Commission has been constituted under the Customs Act to provide speedy resolution of disputes pending before an adjudicating authority. The cases can be referred by applicants with the Commission. However, no application for determining the

Once the case is submitted before it, it enjoys exclusive jurisdiction over it and then can consequently perform the functions of a customs officer, and thereafter the customs officer cannot investigate, adjudicate or issue notice / corrigendum.

The application will be disposed effectively and suitable orders would be issued by the Commission.

The orders of the Commission are non – appealable, however, amenable to writ jurisdiction of High Court.

The appellants can also take the route of Tribunal / High Court and Supreme Court under the litigation mode.

## LESSON ROUND UP

1. The CBIC is the authority to appoint and designate establishments under the Act
2. The types of Customs Duties are Basic Customs Duty (BCD). ), Countervailing duty (CVD) and Special Additional Duty (CVD) are now subsumed under GST, GST Compensation Cess, Protective Duty, Safeguard Duty, CVD on subsidized articles, Anti-Dumping Duty.
3. Goods become liable for duty when they are imported in to / exported out of India
4. The rates of customs duty are specified under the Customs Tariff Act
5. BCD is calculated on Assessable Value (AV). IGST is calculated on the entire amount (AV plus all Customs Duties). GST Compensation Cess, like IGST is calculated on (AV plus all Duties)
6. Warehouses allow goods to be stored and deferment of duty. The goods are to be released from the warehouse, subject to “clearance”; i.e.; post assessment and payment of Duty
7. The Duty Drawback is a facility that enables the Exporter to obtain a refund of the Import Duties (Customs Duty) paid on inputs, which are processed for manufacture of goods to be exported
8. In transit, the goods remain in the same vessel and consequently reach the port of clearance. In transshipment, however, the vessel after reaching an intermediate port, transfers the goods to another vessel and the second vessel into which the goods are transferred (loaded) from the first vessel, carries the goods to the destination port
9. The Act and the Rules provide well defined procedures for import / export and the roles and responsibilities of the parties involved, including the Importer, the Exporter, the Custodian, the Customs and the Carrier
10. Varied types of assessments could take place pre-post clearances and there could be circumstances that could allow the refund of the import / the export duty, subject to timelines and conditions being fulfilled
11. The Act provides and enunciates circumstances wherein the goods can be confiscated or fines and penalties can be levied in lieu of the confiscation
12. Offences under the Act could attract civil or criminal liabilities or both



**EXECUTIVE PROGRAMME  
TAX LAWS**

**EP-TL**

**TEST PAPER**

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*Explanation* – Misconduct for the purpose of this regulation shall mean and include behaviour in a disorderly manner in relation to the Institute or in or near an Examination premises/centre, breach of any regulation, condition, guideline or direction laid down by the Institute, malpractices with regard to postal or oral tuition or resorting to or attempting to resort to unfair means in connection with the writing of any examination conducted by the Institute".

**EXECUTIVE PROGRAMME**  
**TAX LAWS – TEST PAPER**

(This test paper is for practice and self study only and not to be sent to the Institute)

*Time allowed: 3 hours*

*Maximum Mark: 100*

*Note :* All the references to sections mentioned in Part I of the Question Paper relate to the Income Tax Act, 1961 and relevant Assessment Year 2020-21, unless stated otherwise.

**DIRECT TAXES (PART I) – 50 MARKS**

- 1) The rate of surcharge applicable in case of Foreign Company having an income below Rs. 10 crores during the previous year 2019-20 ?
  - a) 5%
  - b) 10 %
  - c) 12 %
  - d) 2 %
- 2) Dividend of Rs. 2,00,000 received in London from UK based company will be taxable in case of:
  - a) Resident and ordinary resident (ROR) only
  - b) Not ordinary resident (NOR) only
  - c) Non resident (NR) only
  - d) ROR, NOR and NR all
- 3) The rate of tax leviable on STCG under section 111A:
  - a) 10%
  - b) 15%
  - c) 20%
  - d) 30%
- 4) Profits of Rs. 10,00,000 is earned from a business in UK which is controlled in India, half of the profits being received in India. How much amount is taxable in India for a Non-resident individual:
  - a) Rs. 10,00,000
  - b) Nil
  - c) Rs. 5,00,000
  - d) Rs. 2,50,000
- 5) The maximum limit of rebate allowed under section 87A of the Income tax Act, 1961 in case of a non-resident individual whose total income does not exceeds Rs. 5,00,000 during the previous year 2019-20 is:
  - a) Rs. 12,500
  - b) Rs. 5,000
  - c) Rs. 10,000

- d) Nil
- 6) In permanent establishment includes:
- a) A person or a place
  - b) Construction site
  - c) Business preserve
  - d) All of the above
- 7) Mr. Sujit (aged 47 years), a doctor by profession based at Mumbai, earned an income from profession Rs. 34,00,000 and interest on bank deposit Rs. 2,00,000 (includes interest on saving bank interest Rs. 30,000). He deposits Rs. 1,20,000 in public provident fund. Compute his taxable income for the assessment year 2019-20?
- a) Rs. 34,10,000
  - b) Rs. 34,50,000
  - c) Rs. 34,60,000
  - d) Rs. 34,70,000
- 8) The basic exemption limit applicable to the Super Senior Citizen (Resident in India) Individual during the previous year 2019-20 is:
- a) Rs. 2,50,000
  - b) Rs. 3,00,000
  - c) Rs. 5,00,000
  - d) Nil
- 9) In case of Advance Ruling 'AAR', an applicant may withdraw an application within \_\_\_\_\_ from the date of the application:
- a) 30 days
  - b) 45 days
  - c) 60 days
  - d) 90 days
- 10) Mr. Narendra (Aged 81) a resident of India during the previous year 2019-20 rendered services in India and earned a salary Income of Rs. 4,80,000. Compute the tax liability of Mr. Narendra for the FY 2019-20 in India?
- a) Rs. 22,660
  - b) Rs. 24,720
  - c) Rs. 11,845
  - d) NIL
- 11) The Total Income of the assessee has been computed as Rs.1,25,794.90. The total income after rounding off will be taken as:
- a) Rs.1,25,700
  - b) Rs.1,25,790

- c) Rs.1,25,795
  - d) Rs.1,25,700
- 12) The maximum amount of leave salary not chargeable to tax as specified by the Government in case of government employee is:
- a) Rs. 3 Lakhs
  - b) Rs. 5 Lakhs
  - c) Rs. 10 Lakhs
  - d) Fully Exempt
- 13) Mr. Ganesh is an employed in XYZ Private Ltd. In the previous year, he received a salary of Rs. 36,000 per month and entertainment allowance of Rs. 2,000 per month. He spent Rs. 10,000 on entertainment allowance. Calculate the amount of deduction under section 16(ii):
- a) Rs. 24,000
  - b) Rs. 10,000
  - c) Rs. 5,000
  - d) Nil
- 14) Sohan has stayed in India during the Previous Year 2019-20 for 181 days, and he is a non-resident in 9 out of 10 years immediately preceding the current Previous Year. He has stayed in India for 365 days in all in the 4 years immediately preceding the relevant Previous Year; and 480 days in all the 7 years immediately preceding the current Previous Year. His residential status for AY 2020-21 would be?
- a. Resident & Ordinarily Resident
  - b. Resident but not Ordinarily Resident
  - c. Non-resident
  - d. Not ascertainable
- 15) Which of the following is not exempt under section 10?
- a. Share income of a member from an HUF
  - b. Share income of a partner from a firm
  - c. Salary received by a partner from the firm
  - d. Both (b) & (c)
- 16) For the purposes of determining the perquisite value of the loan at a concessional rate given to the employee, the lending rate of ..... as on the ..... day of the relevant PY is required, for loans exceeding INR .....
- a. SBI, 1st, 20000
  - b. ICICI, last, 50000
  - c. SBI, last, 50000
  - d. ICICI, 1st, 20000
- 17) Deduction u/s 24(a) is?
- a. 1/3rd of NAV

- b. Repairs actually incurred by the owner  
 c. 30% of NAV  
 d. Interest on borrowed Capital
- 18) Mr. Ravi solved a crossword puzzle and received Rs. 1,68,000 after deduction of tax at source. His income from crossword puzzle chargeable to tax would be :
- a. Rs. 1,68,000  
 b. Nil  
 c. Rs. 1,44,000  
 d. Rs. 2,40,000
- 19) Which of the following is not a revenue receipt?
- i. Compensation received for the loss of a capital asset  
 ii. Compensation received for damage to or loss of a trading asset.  
 iii. Profits on purchase and sale of shares by a share broker on his own account.  
 iv. Income from letting out buildings owned by a company to its employees etc
- a) i only  
 b) i and ii both  
 c) i , ii, and iii  
 d) All of the above
- 20) U/s 54EC, capital gains are exempted, if invested in the bonds issued by NHAI & RECL, or other notified bonds, within?
- a. 6 months from date of transfer of asset  
 b. 6 months from end of relevant PY  
 c. 6 months from end of PY or date of filing of return whichever is earlier  
 d. Anytime during the PY
- 21) Mr. X a UK citizen, came to India for the first time during the FY 2014-15. His stay in India for FY 2014-15, 2015-16, 2016-17 2017-18, 2018-19 and 2019-20 are as follows:

Financial Year	No. of days in stay in India
2014 – 15	55
2015 – 16	60
2016 – 17	85
2017 - 18	90
2018 - 19	100
2019 - 20	70

Determine the residential status of Mr. X in India during the FY 2019-20?

- a) Resident and Ordinarily Resident 'ROR'
  - b) Resident but not Ordinarily Resident 'RNOR'
  - c) Non-Resident
  - d) Cannot be determined
- 22) Ram succeeded to the business of his father Ramanuj consequent upon demise of Mr. Ramanuj on 1-2-2019. Ram recovered Rs. 60,000 due from a customer which was written off by late Ramanuj as bad debt and allowed in the assessment year 2013-14. The amount recovered is :
- a) Exempt from tax
  - b) Fully taxable as business income
  - c) Rs. 30,000 being 50% taxable as business income
  - d) To be set off against current year bad debts
- 23) Appeal to High Court against the order of ITAT is filed within:
- a) 30 Days
  - b) 60 Days
  - c) 90 Days
  - d) 120 Days
- 24) The term 'Company' defined under section 2(17) of the Income Tax Act, 1961 includes:
- i. any Indian company
  - ii. any body corporate incorporated by or under the laws of a country outside India i.e. a foreign company,
  - iii. any institution, association or body which is or was assessable or was assessed as a company for any assessment year under the Indian Income Tax Act, 1922 or which is or was assessable or was assessed under this Act as a company for any assessment year commencing on or before the 1st day of April, 1970
- a) Only i
  - b) i and ii both
  - c) i , ii and iii
  - d) none of the above
- 25) Deduction u/s 80C, in respect of Life Insurance Premium, Contribution to Provident Fund etc., is allowed to?
- a. Any assessee
  - b. An individual
  - c. An individual / HUF
  - d. An individual / HUF resident in India
- 26) Income from a minor child from a Fixed Deposit with a bank, made out of income earned from scholarship, is to be?
- a. Assessed in the hands of the minor child

- b. Clubbed with the income of the parent whose total income before such clubbing is higher
  - c. Exempted from tax
  - d. Clubbed with father's income
- 27) Mr. Shyam received cash gift of Rs. 61,000 from his friends on the occasion of his 55th birthday. None of the friends are relative. The amount taxable in the hands of Mr. Shyam would be :
- a) Nil
  - b) Rs. 11,000
  - c) Rs. 61,000
  - d) None of the above
- 28) Mr. Akash derived income from sale of tea manufactured and grown in the village of Kamataka. His income for the previous year 2019-20 from the said activity is Rs. 40 lakhs. The amount exempt from tax by way of agricultural income is :
- a) Rs. 16 lakhs (40%)
  - b) Rs. 10 lakhs (25%)
  - c) Rs. 24 lakhs (60%)
  - d) Rs. 14 lakhs (35%)
- 29) Joy Charitable Trust (registered under section 12AA) has total income of Rs. 40 lakhs. It applied Rs. 20 lakhs towards its objects. How much is chargeable to tax in case the trust does not opt for accumulation of income under section 11(2) of the Act?
- a) Rs. 20 lakhs
  - b) Rs. 14 lakhs
  - c) Rs. 10 lakhs
  - d) Rs. 6 lakhs
- 30) Cost of Acquisition in case of bonus shares allotted for computing the capital gains would be.
- a) FMV of the shares on the date of allotment
  - b) Nil
  - c) Cost of original shares
  - d) None of the above
- 31) Which of the following is capital receipt?
- a) Reimbursement of capital outlay if the total amount received exceeds the cost of the outlay
  - b) Compensation received for the loss of a capital asset
  - c) Both i and ii
  - d) None of the above
- 32) To get the benefits of DTAA, it is necessary that income of the Assessee is:
- a) Taxable in the Foreign Country only
  - b) Doubly taxable with the country with whom India has DTAA Agreement.

780 EP-TL

- c) Is Taxable in India only
  - d) None of the all
- 33) Mr. B, a British citizen, came to India for the first time on 16.01.2020 for the purpose of employment in India. Determine residential status of Mr. B in India during the FY 2019-20?
- a) Resident and Ordinarily Resident 'ROR'
  - b) Resident but not Ordinarily Resident 'RNOR'
  - c) Non-Resident
  - d) Cannot be determined
- 34) Bad debts is deductible in the year:
- a) When provision for bad debts are made
  - b) When debts is first time written as bad
  - c) When debts was incurred
  - d) When it became time-barred debt
- 35) The taxable perquisites value of ESOP under section 17(2)(vi) of the Income tax Act,1961 is:
- a) FMV of the shares on the grant date less any exercise price recovered from an employee.
  - b) FMV of the shares on the vesting date less any exercise price recovered from an employee.
  - c) FMV of the shares on the exercise date less any exercise price recovered from an employee.
  - d) None of the above
- 36) An income which accrue or arise in India from a business controlled or profession set-up in India is taxable in case of:
- a) Resident only
  - b) Not ordinarily resident only
  - c) Non-resident
  - d) All assessee
- 37) Mr. Sumit (aged 67 years), a non-resident in India, has a total income of Rs. 25,00,000 during the previous year 2019-20. This income includes foreign source income of Rs. 6,00,000 from a country with which India has DTAA to avoid double taxation. Tax levied by the foreign country on that foreign income was Rs. 1,50,000, Compute the tax liability of Mr. Sumit in India for the FY 2019-20 ?
- a) Rs. 4,06,850
  - b) Rs. 3,63,075
  - c) Rs. 4,01,700
  - d) Rs. 3,95,200
- 38) The TDS Certificate issued by an employer to his employees in case of salary income is
- a) Form 16
  - b) Form 26
  - c) Form 26Q

- d) Form 27A
- 39) Which of the following income is / are exempt from tax?
- a) Payments received from family income by a member of a HUF
  - b) Share of profit received by a partner of a partnership firm.
  - c) Any income of an educational institution and hospitals
  - d) All of the above
- 40) Mr. Rony, qualifying as ROR in India during the Financial Year 2019-20, having a taxable income of Rs. 1,50,000. He owns a house property in UK. Whether Mr. Rony is required to file its return of Income in India for the Financial Year 2019-20?
- a) Yes, as he is ROR in India during the previous year.
  - b) Yes, as he is ROR in India during the previous year and owns a house property outside India.
  - c) No, as the taxable income does not exceeds the maximum amount not chargeable to tax.
  - d) None of the above.
- 41) Mr. Raghu, aged 85 (ROR), having taxable income is Rs.5,00,000 during the previous year 2019-20. The tax amount will be
- a) Rs. 25,750
  - b) Rs. 12,875
  - c) Rs. 10,400
  - d) Nil
- 42) An authority of advance shall have the following powers:
- i. Discovery and inspection
  - ii. Enforcing the attendance of person and examining him an oath
  - iii. Compelling the production of books and account and other documents
- a) (i) only
  - b) (i) and (ii) only
  - c) (i) and (iii) only
  - d) (i) (ii) and (iii)
- 43) In which of the following cases, income of previous year is assessable in the previous year itself:
- i. Assessment of persons leaving India
  - ii. A person who is into illegal business
  - iii. A person who is running a charitable institution
- a) (i) only
  - b) (i) and (ii) only
  - c) (i) and (iii) only
  - d) (i) (ii) and (iii)

- 44) Mr. Surjit, a non-resident in India during the previous year paying consultancy fees of Rs. 50 lakhs to X Ltd (a non-resident foreign company). The consultancy fees has been paid in connection with a project / liaison office in India. Under which section Mr. Surjit is obligation to deduct tax at source on the above payment?
- a) Section 194J of the Income tax Act, 1961
  - b) Section 195 of the Income tax Act, 1961
  - c) No TDS is required to be deducted
  - d) None of the above
- 45) An assessee, engaged in the business of growing and manufacturing tea in India, the agricultural income in that case shall be:
- a) 40% of the income from such business
  - b) 60% of the income from such business
  - c) Market value of the agricultural produce minus expenses on cultivation of such produce
  - d) 75 % of the Income from such business
- 46) Mr. Chanchal received a gift of Rs. 80,000 from his friend on the occasion of his own marriage. The amount shall be:
- a) Taxable
  - b) Taxable subject to standard deduction of 30%
  - c) Not taxable
  - d) None of the above
- 47) Section 80QQB of the Income tax act deals with:
- a) Royalty Income of authors
  - b) Royalties from Patent
  - c) Interest on Debentures of Govt. Company
  - d) Profits from export of software
- 48) Transfer of income without transfer of asset would be taxable in the hands of:
- a) Transferor only
  - b) Transferee only
  - c) Either transferor or transferee
  - d) Both transferor and transferee
- 49) National Traders a partnership firm paid Rs. 1,60,000 as contract charges to Vikalp & Co. (firm). No tax was deducted at source for the above said payment. The amount liable for disallowance under section 40a(ia) for the assessment year 2020-21 is :
- a) Nil
  - b) Rs. 1,60,000
  - c) Rs. 80,000

- d) Rs. 48,000
- 50) The following condition must be satisfied for claiming expenditure under section 37 while computing profits and gains from business and profession :
- a) The expenditure must not be in capital nature
  - b) The expenditure must not be in personal nature
  - c) The expenditure must be incurred wholly and exclusively for the purpose of business or profession.
  - d) All of the above

**INDIRECT TAXES (PART II) – 50 MARKS**

51. \_\_\_\_\_ contains the power to make laws with respect to GST.
- a) Article 246A
  - b) Article 246
  - c) Article 254
  - d) Article 264
52. GST came into force by the \_\_\_\_\_ Constitutional Amendment Act.
- a) 111
  - b) 101
  - c) 102
  - d) 110
53. Section 10 of the CGST Act, 2017 contains provisions related to \_\_\_\_\_.
- a) Forward Charge Mechanism
  - b) Reverse Charge Mechanism
  - c) Composition Levy
  - d) Time of supply of goods
54. What is the threshold limit of turnover in the preceding financial year for opting to pay tax under composition scheme for States other than special category States?
- a) Rs. 1.5 Crore
  - b) Rs. 1 Crore
  - c) Rs. 75 Lacs
  - d) Rs. 50 Lacs
55. The credit of CGST can be utilized for payment of \_\_\_\_\_.
- a) SGST
  - b) UTGST
  - c) IGST
  - d) All of the above

784 EP-TL

56. Which of the following goods is not exempt from GST:
- a) Pappad
  - b) Plastic Bangles
  - c) Ice cream
  - d) Fish seed
57. Input Service Distributor (ISD) may distribute the CGST credit within the State as:
- a) SGST
  - b) UTGST
  - c) CGST
  - d) Any of the above
58. The tax under GST legislation in India is being levied \_\_\_\_\_.
- a) Exclusively by Union and State Laws
  - b) Simultaneously by Union and State Laws
  - c) Only by Union Laws
  - d) Only by State Laws
59. What is the maximum rate prescribed under UTGST Act?
- a) 14%
  - b) 20%
  - c) 28%
  - d) 30%
60. Which of the following is considered as Inter State Supply?
- a) Supplies received from SEZ unit in Noida to Domestic Tariff Area
  - b) Supplies made to SEZ developer in Kandla from Kerala
  - c) Goods imported from Japan
  - d) All of the Above
61. Which of the following called the Union Territory as being covered under Union Territory Goods and Service Tax Act (UTGST), 2017?
- a) Delhi
  - b) Ponducherry
  - c) Daman and Diu
  - d) All of the above
62. How long is the prescribed transition period under the GST Compensation Act?
- a) 10 years
  - b) 7 years
  - c) 5 years
  - d) 3 years

63. In arriving at C.I.F. Value under Customs, the insurance can be taken at actual, capped to?
- a) 20% of F.O.B.
  - b) 20% of C.I.F.
  - c) 1.125% of F.O.B.
  - d) 1.125% of C.I.F.
64. When an e-way bill is not required to be generated?
- a) Where the goods being transported are specified in Annexure to Rule 138 of the CGST Rules
  - b) Where the goods are being transported from the customs port, airport, air cargo complex and land customs station to an inland container depot or a container freight station for clearance by Customs
  - c) Where the goods are being transported by a non-motorized conveyance
  - d) All of the above cases
65. ABC Consultants, registered at Delhi provides GST training to employees of XYZ & Co. at Panipat, Haryana. XYZ & Co. is unregistered under GST Act. In this case, which is the place of supply?
- a) Delhi
  - b) Haryana
  - c) Both of the above
  - d) None of the above
66. Which section of IGST Act 2017 deals with place of Supply of services, where location of supplier and recipient is in India?
- a) Section 9
  - b) Section 10
  - c) Section 11
  - d) Section 12
67. \_\_\_\_\_ of CGST Act, 2017 lists down the activities which shall be treated neither as supply of goods nor supply of services.
- a) Schedule I
  - b) Schedule II
  - c) Schedule III
  - d) Schedule IV
68. IGST Act, 2017 was passed by Parliament on the basis of \_\_\_\_\_.
- a) Article 246A
  - b) Article 268A
  - c) Article 269A
  - d) Article 279A

786 EP-TL

69. \_\_\_\_\_ of CGST Act, 2017 lists down the transactions which even without consideration are construed as supply.
- a) Schedule I
  - b) Schedule II
  - c) Schedule III
  - d) Schedule IV
70. Gifts made by employer to any employee upto \_\_\_\_\_ in any Financial Year shall not be treated as supply under GST laws.
- a) INR 25,000
  - b) INR 50,000
  - c) INR 2,00,000
  - d) INR 5,00,000
71. The features of a composite supply under GST are:
- a) Two or more taxable supplies of goods / services / both which are supplied in conjunction with each other
  - b) They are naturally bundled
  - c) One of the supplies within the package is identifiable as a principal supply
  - d) All of the above
72. The features of a mixed supply under GST are:
- a) Two or more taxable supplies of goods / services / both which are supplied in conjunction with each other
  - b) They are deliberately bundled
  - c) None of the supplies within the package is identifiable as a principal supply
  - d) All of the above
73. In which of the following situations under GST laws delivery challan will be required to be issued instead of invoice?
- a) Transportation of goods for job work
  - b) Transportation of goods for reasons other than by way of supply
  - c) Supply of liquid gas where the quantity at the time of removal from the place of business of the supplier is not known
  - d) All of the above
74. \_\_\_\_\_ of the Customs Act, 1962 provides for confiscation of improperly imported goods.
- a) Section 110
  - b) Section 111
  - c) Section 112
  - d) Section 113

75. "Improperly exported goods" under Customs Act, 1962 mean \_\_\_\_\_.
- a) Attempted to export prohibited goods
  - b) Attempted to be exported through any route other than notified route
  - c) Attempted to export goods found concealed in a package
  - d) All of the above
76. \_\_\_\_\_ of the Customs Act, 1962 deals with Conveyances which are liable to confiscation.
- a) Section 112
  - b) Section 113
  - c) Section 114
  - d) Section 115
77. What is the time limit beyond which if goods are not returned, the inputs sent for job work shall be treated as supply?
- a) Six months
  - b) One Year
  - c) Five Years
  - d) Seven Years
78. In case of goods received in instalments or lot, when can a registered person entitled to take ITC?
- a) At the time of first instalment or lot received
  - b) At the time of last instalment or lot received
  - c) At the time of 50% of instalment or lot received
  - d) None of the above
79. Who are the person compulsorily liable for registration?
- a) Casual taxable person
  - b) Input Service Distributor
  - c) persons who are required to deduct TDS
  - d) All of the above
80. Ms. Rita a Practicing Company Secretary registered at Haryana travels to Delhi for business purpose and stays at hotel Leela in Delhi. In this case, which is the place of supply?
- a) Haryana
  - b) Delhi
  - c) Chandigarh
  - d) None of the above
81. Which place will be considered as Place of Supply if goods are supplied on board of aircraft?
- a) Location at which such goods are taken on board
  - b) Location at which such goods are consumed

- c) Location at which aircraft arrived at final destination
  - d) None of the above
82. Which section of CGST Act, 2017 deals with Time of supply of goods?
- a) Section 12
  - b) Section 13
  - c) Section 14
  - d) Section 15
83. If a dealer is liable to be registered on 18th January 2019 and he has applied for registration on 1st February, 2019, what is the effective date of registration?
- a) 1st February, 2019
  - b) 18th January, 2019
  - c) 17th February, 2019
  - d) 16th February, 2019
84. The term 'taxable person' under the GST law means\_\_\_\_\_.
- a) A person who is registered
  - b) A person who is liable to be registered
  - c) Both (a) and (b)
  - d) None of the above
85. The supplier registered under Composition Levy Scheme cannot\_\_\_\_\_.
- a) Claim ITC
  - b) Collect tax on supply
  - c) Raise Tax Invoice
  - d) All of the above
86. Mr. A registered person in Delhi, is supplier of mobile Phone. Mr. B unregistered person resides in Bihar, came to Delhi for IAS coaching, bought one mobile Phone from Mr. A. Which is the place of supply in this situation?
- a) Delhi
  - b) Bihar
  - c) Any of A or B
  - d) None of the above
87. Which of the following value is taken as value of a supply of goods or services or both, as per the provisions of Section 15 of CGST Act 2017?
- a) MRP
  - b) Transaction Value
  - c) Notional Value
  - d) None of the above

88. What shall be excluded for determining value of Supply under section 15 of CGST Act 2017
- Packing Charges
  - Freight charges
  - Discounts offered to customers and recorded in the invoice
  - All of the above
89. The Union territory Goods & Services Act, 2017 is applicable on:
- Inter-state supply of goods or services or both by union territories
  - Intra-state supply of goods or services or both by union territories
  - Both (a) and (b)
  - None of the above
90. To calculate projected revenue of state for compensation, what is the projected nominal growth rate of revenue?
- 12%
  - 14%
  - 16%
  - 18%
91. Where the registered person has claimed Depreciation on the ----- of the Capital Goods, ITC shall not be allowed.
- Cost
  - Tax Component of Cost
  - Both
  - None of the above
92. Sec.111 to Sec. 127 of Customs Act, 1962 deals with \_\_\_\_\_.
- Warehousing of goods
  - Confiscation of goods
  - Types of Duties
  - None of the above
93. Which of the following is not considered as Intra state Supply?
- Supplies to and by SEZ
  - Imported goods till they cross the customs frontiers of India
  - Supplies made to a foreign tourist taking the goods out of India
  - All of the above
94. Mr. A registered person having head office in Uttar Pradesh and it's one of the Branch office is in West Bengal. From the branch office, Mr. A supply tools to Mr. B registered in Rajasthan. Which is the place of supply in this situation?
- Uttar Pradesh
  - West Bengal

790 EP-TL

- c) Rajasthan
  - d) None of the above
95. What is the time of supply of vouchers when the supply with respect to the voucher is identifiable?
- a) Date of issue of voucher
  - b) Date of redemption of voucher
  - c) Expiry date of Voucher
  - d) Earlier of A or B or C
96. What is the time of supply of vouchers when the supply with respect to the voucher is not identifiable?
- a) Date of issue of voucher
  - b) Date of redemption of voucher
  - c) Expiry date of Voucher
  - d) Earlier of A or B or C
97. Company Secretary Firm XYZ is engaged to handle the legal work pertaining to the incorporation of Company BCD, Other than its Professional fees of Rs 25000/-, XYZ Firm also recovered from BCD Rs 4000 for registration fee paid to the Registrar of Companies. XYZ firm is merely acting as a pure agent in the payment of ROC fees. In this situation, what will be the value of supply of services?
- a) Rs 25,000/-
  - b) Rs. 29,000/-
  - c) Rs 4000/-
  - d) Open market value
98. Mr. Abhay, a trader in Daman and Diu has opted for composition scheme of taxation under GST. Determine the rate of total GST payable by him under composition scheme.
- a) 0.5% CGST & 0.5% SGST
  - b) 0.5% CGST & 0.5% UTGST
  - c) 1% CGST & 1% SGST
  - d) 1% CGST & 1% UTGST
99. Which of the following are features of GST?
- a) Value added tax
  - b) Destination based tax
  - c) Tax on Supply
  - d) All of the above
100. India has adopted a ----- GST Model.
- a) Single
  - b) Dual
  - c) Triple
  - d) None of the above

## Answer Key

1	d
2	a
3	b
4	a
5	a
6	d
7	d
8	c
9	a
10	d
11	b
12	a
13	d
14	b
15	a
16	a
17	c
18	d
19	a
20	a
21	b
22	b
23	d
24	c
25	c
26	b
27	c
28	c
29	b
30	b
31	c
32	b
33	c
34	c

35	c
36	d
37	d
38	a
39	d
40	b
41	d
42	d
43	a
44	b
45	b
46	c
47	a
48	a
49	b
50	d
51	a
52	b
53	c
54	a
55	c
56	c
57	c
58	b
59	c
60	d
61	c
62	c
63	c
64	d
65	b
66	d
67	c
68	c

69	a
70	b
71	d
72	d
73	d
74	b
75	d
76	d
77	b
78	b
79	d
80	b
81	a
82	a
83	b
84	c
85	d
86	a
87	b
88	c
89	b
90	b
91	b
92	b
93	d
94	c
95	a
96	b
97	a
98	b
99	d
100	b

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