



Centre for Distance and Online
Education, Punjabi University
Patiala

Class: B.Com-Part-II

Semester: III

Paper : BC-305 (Income Tax Laws)

Unit : I

Medium : English

Updated on 20th June 2023

Lesson No.

- 1.1 : Basic Concepts
 - 1.2 : Basis of Charge and Incidence of Tax
 - 1.3 : Exempted Incomes
 - 1.4 : Income under head Salary
 - 1.5 : Income under head House Property
 - 1.6 : Agriculture Income
-

Department website: www.pbidde.org

BC305: INCOME TAX LAW -I

Time allowed : 3 hours

Pass Marks : 35%

Periods per week : 6

Max Marks: 100

Internal Assessment: 30

External Assessment:70

Note : Simple Calculator(not scientific) is allowed

INSTRUCTIONS FOR THE PAPER SETTER/ EXAMINERS

The question paper covering the entire course shall be divided into three sections as follows.

SECTION-A

It will consist of essay type and numerical questions. Four questions, (two theory and two numerical), shall be set by the examiner from Unit-I of the syllabus and the candidate shall be required to attempt two. Each question shall carry 10 marks; total weight of the section shall be 20 marks.

SECTION-B

It will consist of essay type and numerical questions. Four questions, (two theory and two numerical), shall be set by the examiner from Unit-II of the syllabus and the candidate shall be required to attempt two. Each question shall carry 10 marks; total weight of the section shall be 20 marks.

SECTION-C

It will consist of 12 very short answer questions (six theory and six numerical) from entire syllabus. Students are required to attempt 10 questions up to five lines in length. Each question shall carry 3 marks; total weight of the section shall be 30 marks

Course Objective: To objective of this paper is to impart basic knowledge of the provisions of Income Tax Act.

UNIT - I

Definitions, Distinction between Capital and Revenue; Basis of charge; Incidence of tax, Exempted incomes; Agriculture Income & its tax treatment, Computation of Income from salaries and house property .

UNIT - II

Profit and gains from business and profession including Depreciation, Capital gains, Income from other sources. Carry forward and set off of losses, Income of other persons to be included in assessee's total income.

Pedagogy:

The instructor is expected to use leading pedagogical approaches in the class room situation, lectures, case study analysis, group discussions, assignment writing and tests, research based methodology, innovative instructional methods, use of technology in the class room and comprehensive assessment practices to strengthen the teaching efforts .

Suggested Readings:

1. Mehrotra : Income Tax
2. Singhanian: Income Tax
3. Grish Ahuja and Ravi Gupta : Income Tax
4. Shailinder Sekhon: The Income Tax Law...A Simple guide to theory.

BASIC CONCEPTS

Structure of the Lesson :

1.1.0 Objectives

1.1.0 Introduction

1.1.2 Definitions

1.1.2.1 Total Income

1.1.2.2 Assessee

1.1.2.3 Person

1.1.2.4 Income

1.1.2.5 Assessment Year

1.1.2.6 Previous Year

1.1.3 Features of Income

1.1.4 Income earned in previous year and taxed in assessment year

1.1.5 Self- Check Exercise

1.1.6 Capital and Revenue Receipts

1.1.6.1 Immaterial considerations

1.1.6.2 Distinguishing test for capital receipts Vs. Revenue receipts

1.1.6.3 Examples and Illustrations

1.1.6.4 Some legal Opinions

1.1.7 Capital expenses Vs. Revenue Expenses

1.1.8 Capital losses Vs. Revenue losses

1.1.9 Summary

1.1.10 Glossary

1.1.11 Answers to Self-Check Questions

1.1.12 Exercise

1.1.13 Suggested Readings

1.1.0 OBJECTIVE

The main objective of this lesson is to introduce the students with the :

- (1) Basic terms of Income Tax Law.
- (2) Concept of Capital receipts and Revenue receipts.
- (3) Terms of capital losses and revenue losses.

1.1.1 INTRODUCTION

Income tax is a direct tax, levied by the central Government in our three tier system of administration. It occupies an important place in our fiscal system. Income tax in

India is levied on Income as determined by the provisions contained in the Income Tax Act 1961. The Income Tax Act 1961, extends to the whole of India and came into force with effect from 1st April, 1962. It has more than 400 sections, various, sub-sections and 12 schedules. The annual Finance Bills presented to Parliament alongwith budget make for reaching amendments in this act every year.

Income tax is levied on income of the assessee and not on every receipt. The method of charging different receipts is different. The Income Tax Act provides separate heads, "capital gains" and "profit and gains of business and profession" for levy tax on capital and revenue receipts respectively.

1.1.2 DEFINITIONS

1.1.2.1 Total Income

Under Sec 2 (45), Total taxable income includes income from all sources calculated according to provisions of the Act. It is the net income arrived at after giving due allowances, exemptions, deductions, rebates and reliefs as provided in the Income Tax Act. All sources of income have been grouped under five heads of income namely: -

1. Income under the head 'Salaries'.
2. Income under the head 'House property'.
3. Income under the head 'Profits and gains of business or profession'.
4. Income under the head 'Capital Gains'.
5. Income under the head 'Income from other Sources'.

1.1.2.2 Assessee [Sec. 2 (7)]

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

- (a) Every person in respect of whom any proceedings under this Act have been taken for assessment of his income or for the assessment of the income of any other person in respect of which he liable; or
- (b) In respect of whom any proceedings under this Act has been taken for the assessment for loss sustained by him or by such other person; or
- (c) In respect of whom any proceedings under this act has been taken for the amount of refund due to him or to such other person; or
- (d) Every person who is deemed to be an assessee under any provisions of this act. For example, the captain of a ship of non-resident shipping co.
- (e) Every person who is deemed to be an assessee in default under any provision of this act. For example an employer is liable while making payment to this employee, to deduct income tax thereon at source u/s 192. If he does not deduct tax or after deducting not deposit it in the Government Treasury, he will be assessee in default and is liable to pay tax.

A person deemed to be assessee includes legal representative of a deceased, agent of a non-resident, guardian of minor or manager of a lunatic or infant, trustees etc.

1.1.2.3 Person [Sec 2 (31)]

Under Sec 2 (31) the term person includes the following :-

1. An individual (i.e. a human being) : It includes a male, female and minor.
2. A Hindu Undivided Family : (Governed by Hindu law).
A Hindu Undivided Family means a Hindu family which consists of all persons lineally descended from common ancestor including their wives and unmarried daughters. The manager of HUF is called 'Karta' and its members are called 'Coparceners.'
3. Company : A Company may be defined as an artificial person created by law with a perpetual succession, common seal and shares carrying limited liability, it may be registered under Companies Act, 1956 or any other Act. For the purpose of income tax the term Company is defined in Section 2 (17) of the Income Tax Act.
4. Firm : A firm means a partnership firm, which is defined under the partnership Act. For income tax purposes a firm is assessed as firm only if it complies with the conditions mentioned in Section 184 of the Act. The condition for a partnership entity to be assessed as firm is that it must submit its instrument of partnership duly authenticated by all partners.
5. Association of Persons or Body of Individuals : An association of persons means two or more persons joining for a common purpose of earning income. The Association of persons may consist of two or more individuals or any other persons whereas a Body of Individuals consists only of Individuals. Co-operative societies, Markfed, NAFED are the examples of such associations.
6. Local Authority: Municipality, Panchayat, District Board Cantonment Board etc.
7. Artificial Person : Every artificial juridical person not covered by any of the above proceedings e.g. Statutory Corporations like L.I.C., a University etc. An deity is also assessable as an artificial juridical person but through the persons managing them.

1.1.2.4 Income [Sec 2 (24)]

The term 'Income' is easy to explain but difficult to define. The word 'Income denotes a periodical monetary return coming in with some sort of regularity from defined sources. Thus, Income is compared to the fruit of a tree or the crop of the

field. According to Income Tax Act 1961, Income under Sec 2 (24) includes following items of receipts :-

1. Profit and Gains.
2. Dividends.
3. Voluntary contribution received by a trust created wholly or partly for charitable or religious purposes or by an association of person covered by Section 23, 23(c), Sec. 10 (21).
4. Value of any perquisite or profit in lieu of salary taxable under Sec. 17.
5. Any special allowance or benefit specially granted to the assessee to meet the expenses, wholly, necessarily and exclusively for the performance of his duties.
6. Any allowance granted to the assessee to meet his personal expenses at the place of duty or at the place of his residence.
7. Value of any benefit or perquisite obtained from a company - (a) by director (b) by a person who has a substantial interest in the company, and (c) by a relative of a director or of such person.
8. Any sum chargeable to Income Tax under Sec. 41 or Sec. 59.
9. Any sum chargeable to Income Tax under clause (ii), (iii), (iii-a), (iii-b), (iii-c), of Sec. 28.
10. Any Capital Gain chargeable under Sec. 45.
11. Profit and Gains of any Insurance business carried on by mutual insurance Company or by a co-operative society, computed in accordance with Sec. 44.
12. Any winning from lotteries, cross-word puzzles, races including horse-races, card games, gambling and betting of any form.
13. Any sum received by the assessee from his employees as contribution to any provident fund or super annuation-fund or any fund set-up under the Employees State Insurance Act, 1948.
14. Any sum received under a keyman insurance policy including the sum allocated by way of bonus on such policy.

1.1.2.5 Assessment Year [Sec 2 (9)]

Assessment year means a period of 12 months commencing on the 1st day of April every year. It is also known as financial year, fiscal year and tax year etc. The total income of an assessee and his tax liability is assessed in the assessment year in respect of the income of the previous year. Every person who is liable to pay tax under this Act, files return of income by prescribed dates. These returns are processed by the income tax department officials and officers. This processing is called assessment.

For example, for the assessment year 2021-2022 (i.e. 1-4-2021 to 31-3-2022), the previous year will be year ending 31-3-2022).

1.1.2.6 Previous Year (Sec 3)

The term previous year is very important because whole income tax law is dependent upon the previous year. Income earned in the previous year is to be assessed 'Previous' means 'coming before'. Previous year is the financial year proceeding the assessment year. For example, for the assessment year 2021-2022 the previous year should be the financial year ending on 31st March, 2021. In other words the previous year is the year which comes before the assessment year.

1.1.3 FEATURES OF INCOME

The definition of the Income as given in Section 2 (24) is not exhaustive. It is inclusive and not conclusive. It includes certain receipts which are taxable. Following are some of the characteristics of the income :-

1. Income must be attributable to a definite source of Income :- In fact, Income means a monetary income which is derived from definite source with some sort of regularity or expected regularity. Income tax act classify income under five heads i.e. (1) Salaries, (2) Income from House Property, (3) Profit and Gains from Business and Profession, (4) Capital Gains, (5) Income from other sources. If the income is not related to any of these sources it cannot be termed as income.
2. Income need not necessarily be regular : A lump sum received can also be an income provided if satisfies other factors and consideration of income.
3. Income may be legal or illegal : Illegal income is taxable in the same manner as legal income provided it is derived from definite sources. Any expenditure incurred to earn such illegal income is allowed to be deducted out of such income only.
4. Temporary or Permanent : Whether the income is temporary or permanent, it is immaterial from the tax point of view.
5. Income must be received from outside : A person cannot earn income from himself. There can be no income from transactions between head office and branch office. Also in an institution, if the income from subscription from its members exceeds its expenditure on its members the excess is not the taxable income.
6. Voluntary receipts : The receipts which do not arise from the exercise of a profession or business or do not amount to remuneration and are made for reason, purely of personal nature are not included in the scope of total income.

7. Personal Nature Gifts : Such as birth-day gifts, marriage gifts or gift by colleagues on retirement etc. are not income in the hands of the recipient.
8. Sports Award : Awards received by a non-professional sportsman in the nature of personal gifts and hence not taxable. However, any award to a professional sportsman are benefits received in the courses of exercise of his professional skill and hence taxable.
9. Dispute regarding title : In case a person is receiving some income but his title to such receipts is disputed it will not free him from tax liability. The recipient of such incomes has to pay tax.
It is not essential that the income must be received in the form of money. Receipts in kind or service having money equivalent can also be income.
10. Diversion of Income vs. Application of Income :- Where an income is diverted to some other person under some legal obligation then such income is not taxable. But where after receiving the income is given voluntarily to someone or is diverted to someone voluntarily then it is called application of income and such is taxable.

1.1.4 INCOME EARNED IN PREVIOUS YEAR AND TAXED IN ASSESSMENT YEAR

- (a) Previous year in case of regular business or continuing business : It is financial year proceeding the assessment year. As such for the Assessment year 2022-2023 the previous year for a continuing business is 2021-2022 i.e. 1-4-2021 to 31-3-2022.
- (b) In case of newly-set up business : The previous year in case of a newly started business is from the date of setting up or starting the business or profession, e.g. In case of newly started business commencing its work on 1st Dec. 2021, the previous year in relation of assessment year 2022-23, shall be the period between 1st Dec. 2021 to 31st March 2022.

Exceptions : As a general rule, the income earned in the previous year is taxed in the assessment year but in the following cases, the income earned is taxable in the same year in which it is earned or received. Such exceptions to the general of previous year rule are given in Sec. 172, 174, 175 and 176.

- (1) Income of Non-Residents from Shipping Business (Sec. 172) : Where a ship is owned or chartered by a non-resident and is used for carrying passengers, livestock, mail or goods shipped at a port in India, his income from such business shall be taxed in the year in which it is earned. For this purpose 7½% of the freight paid or payable to the non-

resident, or any person, on his behalf, shall be deemed to be the income in India according to this act.

- (2) Income of persons leaving India (Sec. 174) : When it appears to the assessing officer that an individual may leave India during the current assessment year or shortly after its expiry and that he has no present intention to return to India, then he shall assess the total income of such an individual for the period from the expiry of previous year relevant to the Assessment year to probable date of his departure from India, in the same assessment year.
- (3) Income of persons likely to transfer assets to avoid tax (Sec. 175) : When it appears to the assessing officer that any person is likely to sell, transfer, dispose-off any of his asset with the intention to avoid payment of any tax liability, he may commence proceeding to assess the income for the period between the expiry of last previous year and date of commencement of such proceedings.
- (4) Discontinued business (Sec. 176) : In case any business or profession is discontinued during an assessment year, the income of the period from the expiry of the last previous year till the date of discontinuation will be assessed to tax in the Current Assessment year.
- (5) Maximum Marginal Rate (MMR) : It means the rate of tax for an individual, which is applicable on highest slab of income.

1.1.5 SELF CHECK EXERCISE

Q.1 Explain the following terms :

- (i) Previous year (ii) Assessee (iii) Income

Q.2 Income earned in a previous year is normally charged to tax in the financial year next following it. What are the exceptions to this rule?

Q.3 What will be the previous year in relation to assessment year 2023-24 in the following cases :

- (i) A business keeping its accounts on financial year basis i.e. 2022-2023.
- (ii) A newly started business commencing its operations on 1-1-2023.
- (iii) A person giving Rs. 1,00,000 as a loan @12% p.a. interest (on monthly basis) on 1-9-2022.

1.1.6 CAPITAL AND REVENUE RECEIPTS

Income tax is levied on income of assessee and not on every receipt which he receives. While calculating taxable income of assessee only revenue expenses are allowed to be deducted out of revenue receipts. Further for calculating the Profits and Gains of Business or Profession it is only the revenue receipts and revenue expenses which

are considered. Therefore the distinction between the capital and revenue items is very important.

For this distinction capital and revenue items can be divided into three sub-parts :

1.1.6.1 Immaterial Consideration

In deciding whether a particular receipt is of a capital or revenue type, the following considerations are considered to be immaterial and not going to decide or change the character or nature of such receipt.

1. Receipts in lump sum or in instalments :

Whether any income is received in lump sum or in instalments, it will not make any difference as regards its nature, e.g. An employee is to get a salary of Rs. 1,000 p.m. Instead of this he enters into an agreement to get a sum of Rs. 36,000 in lump sum to serve for a period of three years. The receipt where it is monthly remuneration or lump sum for 3 years is a revenue receipt. It has been decided in so many court cases that a lump sum receipt may be an item of revenue nature and an annual receipt recurring over few years may be a capital receipt. Thus, whether a receipt is a periodic receipt or single receipt is immaterial for the purpose of determining its nature.

2. Nature of receipt in the hands of recipient :

Whether a receipt is a capital or revenue will be determined in the hand of the person receiving such income. No attention will be paid towards the source from which the amount is coming. Salary even paid out of capital by a new business will be revenue receipt in the hands of employee.

3. Magnitude of receipt :

The magnitude of the receipt, whether big or small, cannot decide the nature of the receipt although the size of a receipt in a transaction is not a entirely irrelevant consideration. A receipt of Rs. 10,000 may be of revenue nature whereas a receipt of only Rs. 1,000 may be a capital receipt. Supreme Court has ruled in a Case *Divencha Vs.C.I.T.*(47 I.T.R. 222) that the magnitude of a receipt is immaterial for the purpose of determining its nature.

4. Name given by parties and treatment in books of accounts :

What name the receiver or payer of the receipt has given in the books of accounts or with what name he has called a particular transaction, all such considerations are immaterial to decide the nature of the receipt. A capital payment by a dealer, may be a revenue receipt in the hands of recipient. The character of the receipt shall be decided by consideration other than by what name the parties call it. The nature of the receipt will be determined in the hands of the person receiving such income.

5. Payment made out of Capital :

No attention will be paid towards the sources from which the amount is coming. Salary

even paid out of capital by a new business will be a revenue receipt in the hands of the employee. It was also decided in a case that if a receipt is made out of capital, the receipt may also be a capital receipt. If a recipient is beneficially entitled not only to the income but also to the capital, payments given to him by his trustees out of the corpus would be capital receipts.

6. Time of receipt :

The nature of the receipt has to be determined at the time when it is received and not afterwards when it has been appropriated by the recipient.

7. Quality of receipt :

Whether the income is received voluntarily or under a legal obligation, it will not make any difference as regards its nature.

1.1.6.2 Distinguishing Test for Capital Receipts Vs. Revenue Receipts

It is very difficult to draw a line of demarcation between capital receipts and revenue receipts. Even the courts have found it difficult to lay down some points of distinction on the basis of which a capital receipts may be distinguished from a revenue receipt. Some test, however, can be applied in particular cases. These tests are :

1. On the basis of nature of assets :

If a receipt is referable to fixed assets, it is capital receipt and if it is referable to circulating asset it is revenue receipt.

Fixed asset is that with the help of which owner earns profits by keeping it in his possession, e.g. Plant, machinery, building or factory etc.

Circulating asset is that with the help of which owner earns profit by parting with it and letting others to become its owner, e.g. Stock-in-trade.

Circulating asset is asset which is turned over and while being turned over yields profit or loss whereas fixed asset is one on which the owner earns profit by keeping it in his own possession.

2. Termination of source of Income :

Any sum received in compensation for the termination of source of income is capital receipt e.g. compensation received by an employee from its employer or termination of his services is a capital receipt.

3. Amount received in substitution of Income :

Any amount received in substitution of income is revenue receipt e.g. 'A' company purchases the right to produce a film from its earlier producer with the condition that no other producer will be given these rights. Afterwards it is found that the rights of producing this film had already been sold. 'A' company claimed damages and was awarded Rs. 40,000. It was held that damages received are the compensation for the profits which were to be earned. Hence this is a revenue receipt.

4. Compensation received on termination of lease :

Where a sum is received as compensation for termination of lease, it is capital receipt because it is termination of source of income.

5. Compensation on surrender of a right :

Any amount received as compensation on surrendering of a right is capital receipt whereas any amount received for loss of future income is a revenue receipt. An author given up his right to publish a book and receives Rs. 1,00,000 as compensation. It is capital receipt but if he receives it as advance royalty for 5 years it is revenue receipt.

6. Test as to purpose of keeping an article :

If a person purchases a sculpture to keep it as a decoration piece in his house, if sold later on, will bring capital receipt, but if the same sculpture is sold by art dealer it will be his revenue receipt.

1.1.6.3 Examples and Illustrations :**Capital receipts :**

The following are some important examples of capital receipts decided by courts :

1. Salami or Nazrana received for grant of permanent lease.
2. Compensation received for loss or right to future remuneration.
3. Compensation received from the employer for loss of employment due to premature termination of services.
4. Price received on sale of know-how.
5. Damages received by an employee who is wrongly dismissed or a payment received by an employee in lieu of notice.
6. Amount received by the assessee for digging and removing earth from his land for brick-making.
7. Contribution received by electric supply company from consumers for installation of service lines. (Excess of amount over cost of installation).

Revenue Receipts :

1. Lump sum royalty received in advance.
2. A "Pugree" received by the owner of the house-property from tenant.
3. Damages awarded by a court to a company for breach of contract by another company.
4. A passenger is injured in railway accident and is temporarily disabled thus losing income for a short period. Any receipt as compensation shall be a revenue receipt. But if the passenger is permanently disabled, the compensation received, would have been a capital receipt.

1.1.6.4 Some Legal Opinions

1. Compensation relating to stock-in-trade:

A Company of building contractors was refused permissions by the local authority to build houses on a certain piece of land and was paid compensation. Compensation was held to be a revenue receipt as building of houses for sale was presumed to be a trading asset or stock-in-trade.

2. Excess of amount recovered over actual cost:

An electricity generating company collected contributions from the consumers for laying service lines from its distributing main lines. Supreme Court held that the amount so collected from the consumers is essentially the reimbursement of capital expenditure incurred by the company in laying service lines and hence the receipt including the excess recovered over the actual cost was a capital receipt.

3. Compensation for the restraint on trading or on exercise of profession:

Such a compensation received is considered to be a capital receipt as it is in substitution of the source of income and not of only income.

A company sold its business including goodwill to another company for a certain sum. The company also entered into a covenant restraining itself from starting a similar business for 10 years for separate consideration of Rs. 10,000 p.a. It was held in case City Mills Store that the capital receipts had been spread over 10 years period and so the annual receipt of Rs. 10,000 was a capital receipt.

4. Compensation for breach or cancellation of contract :

Compensation received for breach or cancellation of a contract, damages received for non-completion or non-execution of a contract within the stipulated time were held to be in the nature of a trading receipt.

The receipt in the nature of damages shall be a capital receipt if it is to compensate the loss caused due to injury on the capital assets of the trade.

Supreme Court has held in C.I.T. V. Jai Ram Valji 25 I.T.R. 148 and C.I.T.V. South Indian Picture Ltd. 29 I.T.R. 910 that the compensation received for the termination of a contract entered into ordinary course of business would be a revenue receipt and on the other hand, if the agreement relates to the whole structure of the assessee's profit making apparatus and effects the whole conduct of the business, any sum received for the cancellation or variation of such an agreement would be a capital receipt.

5. Compensation for loss of employment, agency or other office or for cessation of business :

Following receipts have been held to be a capital receipt. Such a compensation may be voluntary and recipient may not have any legal right to demand such a compensation :

- (i) Compensation for cancellation of a service agreement.
- (ii) Compensation for loss of office or employment or cessation of business.
- (iii) Compensation for abandonment of the contractual rights of the recipient.

Compensation for loss of the office on cessation of business or compensation for loss of employment are although capital receipts are taxable if falling under Section 15 or 28 (ii).

6. Compensation for requisition, acquisition, interference with business by Government:

Following receipts were held to be revenue or capital receipts in a number of court case:

Revenue Receipts:

- (i) Sum paid by the government for use of requisitioned premises.
- (ii) Compensation for loss of profits to the assessee due to controlling and interfering with assessee's right of carrying on of a business [C.I.T.V. Shamsheer Printing Press, 39 I.T.R. 90].
- (iii) Compensation received in respect of stock-in-trade damaged or destroyed by enemy action.

Capital Receipts :

- (i) Compensation received for acquisition of Zamindari Lands.
- (ii) Compensation for divesting the assessee of his right to manage his business [Lakshmi Insurance Co. Ltd. Vs.C.I.T. 80 I.T.R. 575],
- (iii) Compensation for cancellation by the government of licence resulting in cessation of business [C.I.T.Vs. Kashmiri Mal Vasdev 39 I.T.R. 150]
- (iv) Compensation for requisition of business premises resulting into stoppage of assessee's business or injury to the profit-making apparatus. [Senariam Doongarmall Vs.C.I.T. 42 I.T.R. 392]

On Government orders two ships ready to proceed to sea with cargo were detained in port for two days. Later on, on a suit, the government had to pay compensation to the company for loss of use of ships and wages. Compensation received was held to be revenue receipts as it was the compensation for the loss of income caused due to government interruption.

7. Nature of Subsidies or Grants received from Public Bodies :

Where government gives grants or subsidies to assist a trader in his business, these are generally regarded as revenue receipts [Meenakshi Aslii V.C.I.T. (1966) 60 I.T.R. 253 (S.C.)].

Where the grant of subsidy is given for a specified purpose e.g. to enable the undertaking to take steps to remove unemployment, it is not taxable as income.

8. Royalties of Writers:

Royalties received by the authors of books etc. are taxable under the head Income from

other sources as revenue receipts.

But if there is complete assignment of copyrights, the amount of royalties or compensation received by the author shall constitute his capital receipt.

9. Recovery of an Embezzled sum:

Where an assessee has been allowed deduction regarding the amount embezzled by an employee as trading loss and subsequently it is recovered from that employee, it will consider as his revenue receipt.

10. Damages for Permanent and Temporary Disability:

If, in an accident, an assessee suffers a permanent disability, then any amount of damages received by the assessee shall be a capital receipt, whereas if the injury is of temporary nature, the amount of damages shall be a revenue receipt.

11. Refund of a Revenue Payment :

Any revenue payment made to discharge a liability, if refundable, shall be revenue receipt when it is so refunded. For example, an assessee was allowed a deduction in respect of payment of a licence fee, it was held to be a revenue receipt when refunded in a subsequent year [Rahmat Ali V CIT 39 ITR 505].

12. Lump sum Receipt or Recurrent and Periodic Income:

Lump sum amount received in lieu of future royalty, single amount received in advance as giving charges of cotton for ten years, a lump sum amount taken in communication of a right to future, commission, remuneration etc. all have been held to be revenue receipts and taxable as income.

1.1.7 CAPITAL EXPENSES VS REVENUE EXPENSES

For computing profits of a business taxable under this Act, only revenue expenses are allowed to be deducted. Hence it becomes essential to distinguish revenue expenditure from a capital expenditure. The following tests can be applied for this purpose:

(i) Nature of Assets : Any expenditure incurred to acquire a fixed asset or in connection with installation of fixed asset is capital expenditure.

Whereas, any expenditure incurred as price of goods purchased for resale along with other necessary expenses incurred in connection with such purchase are revenue expenses.

(ii) Nature of Liability : A payment made by a person to discharge a capital liability is a capital expenditure.

Whereas, an expenditure incurred to discharge a revenue liability is revenue expenditure, e.g. amount paid to a contractor for cancellation of contract, to contract a factory building is capital expenditure whereas amount paid by a person with whom he has entered into contract for supply of goods for a period of 5 years but fails to supply goods after 3 years, the compensation will be a revenue expenditure as it is to discharge

the revenue liability.

- (iii) Nature of transaction: If an expenditure is incurred to acquire a source of income, it is capital expenditure, e.g. purchase of patents to produce picture tubes of T.V.Sets. Whereas an expenditure incurred to earn an income is revenue expenditure e.g. Salary of staff, advertisement expenses etc.
- (iv) Purpose of Transactions : An amount spent on increasing the earning capacity of an asset is a capital expenditure whereas an amount spent on keeping an asset in running condition is revenue expenditure e.g. amount spent on repairs of plant is a revenue expenditure whereas the expenditure incurred on expansion of plant is a capital expenditure.
- (v) Nature of payment in the hands of payer : Whether an expenditure is of capital or revenue nature will be determined in the hands of payer only. No matter what is its nature in the hands of recipient.

Capital Expenditure :

- (a) Cost of acquisition and installation of a fixed asset is a capital expenditure.
- (b) Expenses incurred for securing a business or getting a service is capital expenditure.
- (c) Expenditure in obtaining capital by issuing shares is a capital expenditure
- (d) Expenditure incurred on the maintenance of business reputation.

Revenue Expenditure

- (a) Payments made for the use of patents, quota rights etc.
- (b) Compensation or other payment made to get rid of a servant in the interest of the business.
- (c) Payments made for technical assistance and access to the fruits of continuing research.
- (d) Any such expenditure incurred wholly, totally, necessarily for the business.

1.1.8 CAPITAL LOSSES VS REVENUE LOSSES

Capital losses are dealt under the head Capital Gains and are allowed to be set off against the income from capital gains only, whereas the revenue losses are business losses, thus treated under head "Profits and Gains of Business or Profession" and can be set off against any other income of the assessee. Hence it becomes essential to distinguish the two.

Although there is no clear cut distinction between the two but on the basis of various court cases the following points can be considered for distinguishing them:

- (a) Nature of Asset : Loss on sale of a capital asset is a capital loss whereas a loss incurred on sale of stock-in-trade or on account of another

circulating asset is a revenue loss.

- (b) Loss due to Embezzlement: When loss is suffered by the business man on account of embezzlement by an employee then it is a revenue loss.
- (c) Loss due to withdrawing money from bank : Where a sum is firstly withdrawn by an employee from bank and then misappropriated, then it is capital loss.
- (d) Loss due to liquidation of Company: Where an amount deposited by a person with Manufacturing Company to get its agency is lost due to company being liquidated, is a capital loss.
- (e) Loss due to theft by an employee: Loss occurring due to theft or embezzlement or misappropriation committed by an employee is revenue loss.

1.1.9 SUMMARY

Income tax is levied on income of assessee and not on every receipt which he receives. The method of tax on different types of receipts is different. Income-tax Act, 1961 provides a separate head "Capital gains" for levying tax on capital receipts, and similarly "Profits and gains from business and profession" head only for revenue receipts and revenue expenses is considered.

1.1.10 GLOSSARY

- 1. ITA : Income Tax Act
- 2. A.Y. : Assessment Year
- 3. P.Y. : Previous Year
- 4. S.C. : Supreme Court
- 5. GTI : Gross Total Income

1.1.11 ANSWERS TO SELF-CHECK QUESTIONS

Ans.1 (1) Previous Year : Previous year is the financial year preceding the assessment year in which income is earned.

- (2) Assessee : A person who is liable to pay tax as per Income Tax Act, 1961.
- (3) Income : The definition given u/s 2(24) is inclusive and not exhaustive. The term income simply means something which occurs in. As per this act, term income includes not only what is received by using the property but also amount saved by using it himself.

Ans.2. Exceptions : (1) Cases of person leaving India (Sec. 174).

- (2) Persons who are likely to transfer their assets to avoid tax (Sec. 175).
- (3) Case of discontinued business (Sec. 176).
- (4) Shipping income of non-resident ship owners (Sec. 172).
- (5) AOPs, BOIs or Artificial person's assessment who are established only

for a limited period.

Ans.3 Previous year in following cases in relation to A.Y. 2023-2024 :

1. 01.04.2022 to 31.03.2023
2. 01.01.2023 to 31.03.2024
3. 01.09.2022 to 31.03.2023

1.1.12 EXERCISE

(A) Short Questions :

- Q.1 Explain the term capital losses.
Q.2 What do you mean by revenue losses?
Q.3 Distinguish between capital receipts and revenue receipts.

(B) Long Questions :

- Q.1 Distinguish between Capital expenses and Revenue expenses and also give various examples.
Q.2 Determine the nature of the following items :
(1) Remuneration received by a retired Judge for acting as arbitrator under an agreement.
(2) Premium on issue of shares.
(3) 'Salami' for premature termination of lease.
(4) Amount paid to a Director now resigning from Directorship.
(5) Profit made from devaluation of Indian rupee.
Q.3 What tests would you apply to distinguish capital receipts from Revenue receipts?

1.1.13 SUGGESTED READINGS

1. Income Tax Law and Practice : V.P.Gaur, D.B. Narang
2. The Income Tax Law : Shailinder Sekhon
4. Direct Tax Laws : Singhanian
(A.Y=2023-24)

BASIS OF CHARGE AND INCIDENCE OF TAX LIABILITY

Structure of the Lesson :

- 1.2.0 Objectives
- 1.2.1 Introduction
- 1.2.2 Residential Status of an Individual
 - 1.2.2.1 Resident and ordinary resident
 - 1.2.2.2 Resident but not ordinary resident
 - 1.2.2.3 Non-resident
- 1.2.3 Residential status of HUF, Firm and AOPs
 - 1.2.3.1 Resident
 - 1.2.3.2 HUF, Not Ordinary Resident
 - 1.2.3.3 Non-resident, HUF, FIRM, AOPs
- 1.2.4 Residential Status of a Company
 - 1.2.4.1 Resident
 - 1.2.4.2 Non-Resident
- 1.2.5 Residential status of all other persons
- 1.2.6 Relation between residential status and incidence of tax
 - 1.2.6.1 Incidence of Tax
 - 1.2.6.2 Income received in India
 - 1.2.6.3 Income deemed to be received in India
 - 1.2.6.4 Income which accrues or arises in India
 - 1.2.6.5 Income deemed to accrue or arise in India
- 1.2.7 Self-Check Exercise
- 1.2.8 Summarized Chart
- 1.2.9 Glossary
- 1.2.10 Answers to Self-Check Questions
- 1.2.11 Exercise
- 1.2.12 Suggested Readings
- 1.2.0 **OBJECTIVES**

The objectives of this lesson are :

- (1) To study the basic and additional conditions for residential status.
- (2) To study the residential status of different persons.
- (3) To study the basis of charge of Income Tax.

1.2.1 INTRODUCTION

Tax is levied on total income of an assessee. Under the provisions of Income tax Act, 1961 the total income of each person is based upon his residential status, in India in previous year. Section 6 of the act divides the assessable person into three categories :

- (i) Ordinarily resident (OR)
- (ii) Resident but not ordinarily resident (NOR)
- (iii) Non-resident (NR)

The concept of residential status has nothing to do with nationality or domicile of a person. Residential status of a person depends upon the territorial connections of the person with his country that is for how many days he has physically stayed in India. The residential status of different types of persons is determined differently. Similarly, the residential status of the assessee is to be determined each year with the reference to the "previous year". The residential status of an assessee may change from year to year.

1.2.2 RESIDENTIAL STATUS OF AN INDIVIDUAL

An individual may be (a) resident (ordinary resident), (b) resident but not ordinarily resident (c) non-resident.

1.2.2.1 Resident and Ordinary Resident

Under section 6 (1) an individual is said to be resident in India in any previous year if he satisfies any one of the basic conditions as mentioned in Sec. 6 (1).

Basic Conditions (Sec 6. (1))

- (a) He is in India in the previous year for a period of 182 days or more (120 days) from A.Y.2020-21 ; or
 - (b) He is in India for a period of 60 days or more during the previous year and 365 days or more during the four years, preceding the previous year.
1. Exceptions to the above rules of 60 days stay in India.
- (i) An individual who is a citizen of India and leaves India in any previous year for the purpose of employment or as a member of the crew of an Indian ship must have stayed in India for atleast 182 days during the previous year instead of 60 days.
 - (ii) If any citizen of India or a foreign national of Indian origin, who is living outside India, comes on a visit of India in the previous year, he must have stayed in India for atleast 182 days or 120 days during the previous year instead of 60 days.

The practical effect of this provision is that those persons who are Indian citizens or persons of Indian origin living outside India and when they come to visit India only test (a) of 6 (1) is to be applied. This section again amended in 2020 Budget as explained in Note-1

NOTE-I : The finance Act, 2020 has amended the explanation 1(b) to sub-section 1 of section 6 to include the person who is a citizen of India/person to Indian origin, being outside India, comes on a visit to India shall be considered as RNOR who fulfils all the following conditions-

1. Total income should be more than 15 lacs (except foreign income);
2. Should stay in India for a period of 120 days or more but less than 182 days in the previous year; and
3. Should stay in India for a period of 365 days or more in 4 years preceding the previous year.

Prior to the amendment in finance act, 2020. Such person was qualified as Non-Resident (NR) not as Resident but not ordinary resident (RNOR)

1.2.2.2 Resident But not ordinary Resident

Additional Condition Sec. 6 (6) : States that an individual shall be ordinary resident if he satisfies both the following conditions.

- (a) He has been resident in India for at least 2 out of 10 previous years immediately preceding the relevant previous year.
- and
- (b) He has been in India for 730 days or more during seven previous years immediately preceding the relevant previous year.

1.2.2.3 Non-Resident

An individual is non-resident in India, if he satisfies none of the basic conditions. In the case on non-resident the additional conditions are not relevant.

1.2.3 RESIDENTIAL STATUS OF HUF, FIRM AND ASSOCIATION OF PERSONS SEC 6 (2)

1.2.3.1 Resident : A Hindu undivided family firm or association of persons are Resident in India in any previous year if the Control and Management of its affairs is situated wholly or partially in India on the relevant previous year. Further a HUF will be called ordinary Resident only when its Karta satisfies both the additional conditions of ordinary Resident as an Individual as mentioned in Sec 6 (6).

1.2.3.2 HUF (Not Ordinary Resident) : A Hindu undivided family is said to be ordinarily resident in India if the Karta of the HUF satisfy both of the following two conditions :

1. Karta must be resident in at least 2 out of 10 previous years immediately preceding the relevant previous year.
- and
2. Karta must be in India for at least 730 days during 7 previous years immediately preceding the relevant previous year.

Note II : Firms and Associations of Persons cannot have the residential status of Not

Ordinarily Resident.

1.2.3.3 Non Resident, HUF, FIRM, AOPs : All the three types of assessee's (HUF, Firm A.O.P.) are said to be Non-Resident if the control and management of affairs is situated wholly outside India.

Note III : Control and Management means de-facto control and management and not merely the right to control and manage. The place of control and management is where the head seats and directing powers are situated.

1.2.4 RESIDENTIAL STATUS OF A COMPANY [SEC 6(3)] :

Section 6 (3) provides the following tests in this connection.

A Company is resident in India if in the relevant previous year:

- (i) It is an Indian company, or
- (ii) During the year, control and management of its affairs is situated wholly in India.

1.2.4.1 Resident:

A company cannot have this status. It can either be ordinary resident or non-resident.

1.2.4.2 Non-Resident :

A company shall be non-resident if it does not satisfy any of the condition of sec. 6 (3) during the relevant accounting year. It means that a foreign company whose control and management is situated wholly or partially out of India will be a non-resident company. Normally Control and Management of Company is situated at a place where the meetings of its Board of Directors are held.

1.2.5 RESIDENTIAL STATUS OF ALL OTHER PERSONS SEC. 6 (4)

Every other person (i.e. body of individuals, a local authority and a artificial juridicial person) either 'Resident' or 'Non-Resident' but they can never be not ordinarily Resident. They are called Resident unless the control and management of its affairs is wholly situated outside India.

Important Rules

1. Whether an assessee is Resident or non-Resident, it is a question of fact. The onus to prove all the facts before the requisite authorities lies on the assessee.
2. An assessee cannot have different residential status for different sources of income.
3. The residential status of a company would change with the change in place of control and management of its affairs. A company can be resident in one year and non-resident in another.

1.2.6 RELATION BETWEEN RESIDENTIAL STATUS AND INCIDENCE OF TAX (SEC. 5)

Under this act, incidence of tax on a tax payer depends on his residential and also on the place and time of accrual or receipt of income.

1.2.6.1 Incidence of Tax :

The tax is levied on total income of a person. The total income is based upon the

residential status of an assessee. Section 5 provides a scope of total income which varies on the basis of status.

Section 5 :

(1) Subject to the provision of this act, the total income for any previous year of a person who is resident includes all incomes from whatever source derived which,

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

(2) Subject to provision of this act, the total income of any previous year of a person who is a resident but not ordinarily resident includes all incomes from whatever source derived, which,

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

(3) Subject to provision of this act, the total income of any previous year of person who is a non-resident includes all incomes from whatever source derived, which,

- (a) is received, or is deemed to be received in India in such year by or on behalf, of such person ; or
- (b) accrues or arises or is deemed to accrue to arise to him in India. The above provisions of Section 5 can be explained in followingmanner :

(i) **Scope of total income of 'Resident' Section 5 (1)**

- (a) Income received or deemed to be received in India during the relevant accounting year. The place and date of accrual is immaterial.
- (b) Income which accrues or arises or is deemed to accrue or arise in India during the relevant accounting year irrespective of the date and place to its receipt.
- (c) Income accruing during the relevant accounting year outside India from any source whether it is brought or not in India during the year.

(ii) **Scope of total income of Not ordinarily Resident (Section 5 (1))**

- (a) Income received or deemed to be received in India during the relevant accounting year. The date and place of accrual is immaterial.
- (b) Income which accrues or arises or is deemed to accrue or arise in India during the relevant accounting year irrespective of the date and place of its receipt.
- (c) Income accruing or deemed to be received outside India during the

relevant accounting year from a business or profession set up in, and controlled from India.

(iii) **Scope of total Income of Non-Resident (Section 5 (2))**

- (a) Income received or deemed to be received in India during the relevant accounting year. The date and place of accrual is immaterial.
- (b) Income which accrues or arises or is deemed to accrue or arise in India during the relevant accounting year irrespective of the date and place of its receipt.

These provisions are explained below :-

1.2.6.2 Income Received in India:

The term received means the receipt of income on the first occasion. The place of its receipt shall be the place where it is received for the first time and not the place of its receipt on subsequent remittance.

1.2.6.3 Income Deemed to be Received in India:

The incomes which are not actually received by a person but law consider then such receipt of incomes are called incomes deemed to be received in India. The term 'statutory receipt' can be easily used to cover this term. Following are instances of incomes deemed to be received :

- (i) Tax deducted at source is income deemed to be received by a person even though he never receives such incomes (U/S 198).
- (ii) Section 7 considers the following incomes as deemed to be received by an assessee.
 - (a) Annual accretion to a recognised provident fund account of an employee during the relevant previous year.
 - (b) Transferred balance of unrecognised provident fund to recognised provident fund.
- (iii) Transfer of income without transfer of assets deemed to be the income of employee u/s 60 and 61.
- (iv) Under Section 8, the dividend is deemed to be received in the year in which it is declared.

1.2.6.4 Income which accrues or arises in India

Income can be held to accrue or arise to an assessee only when the assessee obtains a right to receive that income. No amount can be said to accrue unless it is actually due. Accrue means "to fall as natural growth or increment, to come as an accretion or advantage" and arise means "to spring up, to come into existence", according to Oxford dictionary.

Income accrues or arises at a place where the origin or source of growth of income is

satisfied. As regards salaries, income accrues or arises in India if it is earned in India :

- (i) Income accrues or arises to a person, who is entitled to demand and receive the income.
- (ii) Income accrues or arises at the time or date when it ripens into a debt, at the moment when assessee acquires a right to receive it.
- (iii) In the case of salaried employees. If the person renders services in India, income earned in India obviously arises in India.
- (iv) In case of dealer of goods, if the purchases and sales of goods take place in India, the profits out of such sales arise in India.

1.2.6.5 Income deemed to Accrue or Arise in India

Under section 9 (1) of the Indian income tax act, the following incomes are deemed to accrue or arise in India :

- (i) **Income arising from business connection in India :**
Business connection involves a relation between a business carried on by a Non Resident which yields profits, and gains and some activity in India which contributes directly or indirectly to the earning of those profits and gains.
- (ii) **Income from any property held in India and assets or sources of income located in India :**
In case company carries on business in India and pays dividend out of profit made in India and taxed in India, the dividend arises directly from a source of income in India and as such dividend income of a non-resident may be deemed to accrue or arise in India.
- (iii) **Income from transfer of capital assets situated in India :**
Any gain arising from a capital asset whether movable or immovable shall be deemed to accrue in India in case of capital asset is situated in India at the time of transfer. It is immaterial that agreement is entered outside India or consideration is paid outside India.
- (iv) **Apportionment of Profits [section a(1)(i)] :**
In the case of a business of which all the operations are not carried in India, only that part of income shall be deemed to accrue or arise in India which is reasonably attributable to the operations carried on in India.
- (v) **Purchase of goods in India for export (Section 9) :**
In case of non-residents, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in India for the purpose of export. No income is

deemed to accrue in India to non-resident through or from operations confined to the purchase of goods in India for export even if the purchases are made through a regular agency established in India for that purpose.

(vi) Salaries earned in India :

This explanation provides an artificial place of accrual for income taxable under the head 'salaries'. According to it the incomes chargeable to tax as salaries shall be deemed to accrue or arise in India, if they are earned in India, i.e. if the services are rendered in India. The place of receipt and accrual of the salary is immaterial.

(vii) Salaries for Government service outside India (Section 9) (i) (iii) :

In the case of citizen of India who is employed by the government income chargeable under the head 'salaries' which is payable outside India for the services rendered outside India is deemed to accrue or arise in India and hence is taxable but allowances and perquisites paid or allowed by government outside India are exempted under Section 10 (7).

(viii) Dividend paid abroad by the Indian Company (Section 9) (i) (iv) :

Any dividend paid by an Indian company outside India is deemed to accrue or arise in India. A dividend declared abroad and payable abroad would not accrue in India even though the company may be Indian Company, but such a dividend declared by an Indian Company but payable outside India would be deemed to accrue or arise in India.

(ix) Income by way of interest (Section 9) (i) (v) :

Any interest payable by an Indian Government is deemed to accrue or arise in India, if it is payable by the Indian Government.

Royalty when payable by a person whether Resident or Non-Resident then it will be deemed to accrue or arise in India, it is payable on any right, property or information used for business or profession in India and do not deem to arise or accrue in India if the right, property or information is used for business or profession carried outside India.

(x) Income by way of royalty (Section 9) (I) (vi)

Any income from royalty shall be deemed to accrue or arise in India, if it is payable by the Indian Government.

Royalty when payable by a person whether Resident or Non-Resident then it will be deemed to accrue or arise in India if it is payable on any right, property or information used for business or profession in

India and do not deem to arise or accrue in India if the right, property or information is used for business or profession carried outside India.

- (xi) Income by way of fees for technical Services 9 (1) (vii) shall be deemed to accrue or arise in India, if it is payable by Indian Government: If such fee is payable by any person Resident or Non-Resident in respect of services used for business or profession carried on in India then it will be deemed to accrue or arise in India. But if the services are used for business or profession carried outside India then it is not deemed to accrue or arise in India.

Exceptions : The following incomes are not deemed to accrue or arise in India: -

- (1) In case of non-resident any income from the business operations in India which are confined to purchase of goods in India for export purpose.
- (2) In case of non-resident running a news agency or publishing newspapers, magazines or journals any income derived from activities confined to collection of news in India for transmission outside India.
- (3) In case of non-resident :
 - (a) individual, who is not citizen of India;
 - (b) firm, whose no any partner is a citizen of India or resident in India any income ; and
 - (c) company, whose no shareholder is a citizen or resident of India any income derived from the operations which are confined to the shooting of any cinematograph film in India.
- (4) Pension to the judges of Federal Court of High Court who were appointed before 15.08.1947 and who continued to serve on or after the commencement of the constitution as a judge in India, shall not be deemed to accrue or arise in India, if :
 - (i) it is paid or payable outside India; and
 - (ii) such person resides permanently outside India.

1.2.7 SELF-CHECK EXERCISE

- (A) Assessment year is a period of
- (i) 6 months
 - (ii) 12 months
 - (iii) 3 months
 - (iv) 15 days

- (B) Indian Income is taxable in India
- (i) Never
 - (ii) Always
 - (iii) For 6 months
 - (iv) For 9 months
- (C) Foreign Income of the Non-Resident person in India is :
- (i) Taxable in India
 - (ii) Not Taxable in India
 - (iii) Not Taxable in Foreign Country
 - (iv) Always Taxable in India
- (D) Residential status of the company may be :
- (i) Resident and ordinary resident
 - (ii) Resident but not ordinary resident
 - (iii) Resident or non-resident
 - (iv) Non-resident only
- (E) The Gross total income of the person means income earned under the
- (i) 4 Heads
 - (ii) 5 Heads
 - (iii) 3 Heads
 - (iv) 1 Head

Q (2) : The following are the details of income of S. Pritam Singh :

1. Share of income from a joint venture in India Rs. 10,000.
2. Dividend Rs. 1,000.
3. Income from Agriculture in Pakistan Rs. 20,000.
4. Salary received in India Rs. 9800 (Computed) but the services for the same was rendered in Iran.
5. Income from business (controlled from India) in Pakistan Rs. 10,000 and the income remitted to India.
6. Income earned and received in Pakistan from bank deposits Rs. 5000.
7. Income accrued in India but received in Iran Rs. 10,000.

Compute Pritam Singh's taxable income if he is :

- (i) a resident
- (ii) a not ordinarily resident
- (iii) a non-resident

1.2.8 SUMMARISED CHART

Different kinds of Incomes	Different Types of Residential Status		
	Resident and Ordinary	Not ordinary Resident	Non-Resident
1. Income received or deemed to be received in India. It is immaterial whether it is earned in India or in a foreign country.	Taxable	Taxable	Taxable
2. Income earned in India whether received in India or outside India.	Taxable	Taxable	Taxable
3. Income earned and received outside India from a business or profession setup in India. Income may or may not be remitted to India.	Taxable	Taxable	Not Taxable
4. Income earned or received outside India from a business or profession set-up outside India	Taxable	Not Taxable	Not Taxable
5. Income earned and received outside India from any other source (Except income under point 3).	Taxable	Not Taxable	Not Taxable
6. Income earned and received outside India in the year preceding the previous year in question and if the same is remitted to India during the current previous year.	Not Taxable	Not Taxable	Not Taxable

1.2.9 GLOSSARY

1. AOPs : A group of persons associated together for a common objective.
2. HUF : Hindu Undivided Family which carries a common family business.
3. ROR : Resident and ordinary resident in India
4. NRI : Non-resident in India
5. GTI : Gross Total Income

6. Person : Person means an individual, HUF, Firm, AOPs, BOIs, and a company.
7. BOIs : Body of Individuals

1.2.10 ANSWERS TO SELF-CHECK QUESTIONS

- Ans-1 Ques. (A) = II
 Ques. (B) = II
 Ques. (C) = II
 Ques. (D) = III
 Ques. (E) = II

Ans-2: Computation of total income of Pritam Singh.

Resident		Not ordinary Non-		
		Rs.	Resident Rs.	Resident Rs.
(a)	Income received in India [5 (1) (a)]			
(i)	Share of income from joint venture in India	10,000	10,000	10,000
(ii)	Dividend - Exempted u/s 10 (34)	NIL	NIL	NIL
(iii)	Salary for services rendered outside India	9,800	9,800	9,800
(b)	Income accrued in India [5 (1) (b)]	10,000	10,000	10,000
(i)	Income accrued in India but received in Iran			
(c)	Income accrued and received outside India	20,000	NIL	NIL
(i)	Income from agricultural in Pakistan	NIL	NIL	NIL
(ii)	Income from a business in Pakistan (controlled from India)	10,000	10,000	NIL
(iii)	Bank deposits income in Pakistan	5,000	NIL	NIL
Total Income		64,800	39,800	29,800

1.2.11 EXERCISE

- (A) Short Questions :
1. Give in brief basic conditions and additional conditions.
 2. What is Foreign Income?
 3. What do you mean by Incidence of Tax?

(B) Long Questions :

- Q.1 Write a detailed note on the different residential status of the person.
- Q.2 What are the basic and additional conditions for determining the residential status of a person?
- Q.3. Following are the income of Mr. Garry for the previous year 2022-23.
- (i) Profit from the business in Bangalore - 10,000
 - (ii) Income accrued in India but received in Japan - 4000
 - (iii) Profit from business in Canada but received in India - 5000
 - (iv) Income from house property in Karachi received in Bombay - 4000
 - (v) Profit from business established in England and deposited there, the business being controlled from India - 20,000
 - (vi) Income from house property in American and deposit there - 2000
 - (vii) Post untaxed income brought into India during the previous year - 10,000
- Compute the total income of Mr. Garry for the A.Y. 2022-23 if he is (a) Resident (b) Not Ordinary resident and (c) Non-Resident

Ans. Resident Rs. 45,000; NOR Rs. 43,000 and Non-Resident Rs. 23,000.

1.2.12 SUGGESTED READINGS

1. Direct Taxes by Dr. Vinod K. Singhania
2. Income Tax by V.P. Gaur and D.B. Narang
3. The Income Tax law by Shailinder Sekhon
4. Income Tax Law and Accounts by Dr. H.C. Mehrotra.
(A.Y. 2023-24)

EXEMPTED INCOMES

- 1.3.0 Objective
- 1.3.1 Introduction
- 1.3.2 List of Exempted Incomes [(Sec. 10(1) to Sec. 10(33)]
- 1.3.3 Exempted Incomes (u/s 10-A)
- 1.3.4 Exempted Incomes (u/s 10-B)
- 1.3.5 Self-Check Exercise
- 1.3.6 Summary
- 1.3.7 Glossary
- 1.3.8 Answers to Self-Check Questions
- 1.3.9 Exercise
- 1.3.10 Suggested Readings

1.3.0 OBJECTIVE

The main objective of this lesson is to enlighten the students with the various exempted incomes [u/s 10(i) to 10(33), 10(A), 10(B) and 10 (C)] on which income tax is not chargeable.

1.3.1 INTRODUCTION

Incomes can be classified into three categories as per provisions of this Act. These categories are :

- (1) Incomes forming part of total income and subject to tax (u/s 14-80)
- (2) Incomes forming part of total income but entitled to rebate or relief (u/s 86)
- (3) Incomes exempted from tax, do not form part of total income either fully or partially (u/s 10).

Thus, Exempted income is that income on which income tax is not chargeable. Some incomes are not even included in total income. Incomes which are neither included in total income nor income tax is payable on them.

1.3.2 LIST OF EXEMPTED INCOMES [(Sec. 10(1) to Sec. 10(33)]

1. Agricultural Income (Sec 10 (i) :

The Agriculture income is fully exempted from tax. However, in some cases agriculture income is taken into consideration to determine tax on non-agriculture income.

Definition of Agricultural Income (Sec 2 (IA)):

Section 2 (IA) defines agricultural income. This definition is very wide and covers the income of not only the cultivation but also the land holders who might have rented out the lands. Agricultural income may be received in cash or in kind.

Three ways :

Agriculture income may arise in any one of the following three ways :

- (1) It may be rent/revenue derived from land situated in India and used for agricultural purposes.
- (2) It may be income derived from such land through agriculture or the performance of a process ordinarily employed by a cultivator or receiver of rent in kind to render the produce fit to be taken to the market or through the sale of such agricultural produce in the market.
- (3) Lastly agricultural income may be derived from any farm building required for agricultural operations.

2. Receipts by a member of Hindu Undivided Family from family income (Sec. 10 (2)):

This exemption is based upon the principle of avoidance of double taxation. Income of a Hindu individual family is taxable, in its own hand. Section 10 (2), therefore exempts income received by a member from his Hindu undivided family. Only those members of a Hindu undivided family can claim exemption under this clause who are entitled to demand share on partition.

Exception : Sum should not be received from converted property falling u/s 64 (2) share on partition.

3. Share of Income from Firm (Sec. 10 (2A)) :

In case a partner of a firm, (which is separately assessed) received his share in the total income of the firm then such share shall be fully exempted. The share of partner in the total income of the firm shall be in same proportion as is given in partnership deed.

4. Interest paid to Non-resident (Section 10 (4) (1)):

The amount of Interest payable to non-resident on such securities or bonds as the central government may, by notification in the official Gazette, specify in this behalf, including income by way of premium on the redemption of such bonds, shall be exempted from tax. The exemption under this section shall not be allowed on interest on bonds or securities issued on or after 1.6.2002.

5. Interest to Non-resident on Non-Resident External Account (Section 10) 4 (ii):

Any income by way of interest on moneys standing to his credit in a Non-Resident Account in any bank in India shall be exempted from tax in case of an individual who is a person resident outside India or is a person who has been permitted by the RBI to maintain the aforesaid account. The person residing outside India shall have the same meaning as defined under Foreign Exchange Management Act, 1999.

This exemption shall not be available on any income by way of interest paid or credited on or after 01.04.2005.

6. Interest paid to a person of Indian origin and who is non-resident (Section 10) (4B) :

In a case of individual being a citizen of India or a person of Indian origin, who is non-resident, any income from interest on such savings certificate issued by the Central Government may specify in his behalf by notification in the official Gazettee, shall be fully exempted. But exemption is available to original subscribers of saving certificates. This exemption shall not allowed on bonds or securities issued on or after 1-6-2002.

7. Leave Travel Concession to an Indian Citizen Employee [Section 10 (5)] :
The following rules have been incorporated for journeys performed on or after 1-10-97. This clause exempts the leave travel concession received by employees from their employers for proceeding to any place in India,

- (i) either on leave ; or
- (ii) after retirement from service ; or
- (iii) after termination of his service.

In case journey is performed by Air: L.T. C. shall be exempted upto an amount not exceeding the air economy fare of the National Carrier by the shortest route to the place of journey.

In case journey is performed by any mode other than Air : If place of origin of journey and place of destination are connected by rail but journey is performed by any mode other than air, the benefit shall be exempted upto an amount not exceeding air conditioned first class rail fare by the shortest route to the place of destination.

With effect from 1-10-1998, the exemption for L.T.C shall be restricted for two children only. But this restriction shall not be applicable on children born before 1-10-1998 and also in case of multiple births after one child on or after 1-10-1998.

8. Certain income received by an individual who is not a citizen of India (Section 10(6)) :

The following incomes are exempted when received by an individual who is not a citizen of India :

- (i) **Passage Money 10 (6) :-** If any foreign national who is working in India is proceeding on home leave out of India or is proceeding to home country on retirement or termination of his services then any passage money/value of any free or concessional passage received by such employee from his Indian employer is fully exempted from tax.
- (ii) **Remuneration**
 - (a) The remuneration received by an ambassador or other officials of the embassy, high commission or legation of a foreign state in India.
 - (b) The remuneration by a consular officer of foreign a state in India.

- (c) The remuneration received by a trade commissioner or other official the representative in India of a foreign state, provided corresponding official of the government of India in that country are given a similar concession.
 - (d) The remuneration received by a foreign diplomat and other foreign nationals.
 - (e) Remuneration paid to employee of philanthropic institution.
 - (f) Remuneration of a foreign technician in India.
 - (g) Salary received by a foreign ships's crew. Those are foreign nationals and non-residents.
9. Perquisites and Allowances paid by Government to its employees serving outside India [Section 10 (7)] :

All the perquisites and allowances paid by the government to its employees for service rendered outside India are exempted from tax. This exemption is allowed only to such employees of the government who are citizen of India.

10. Employees of Foreign Countries working in India under Co-operative Technical Assistant Programme [Section 10(8)] :

The persons who are working in India under co-operative technical assistance programme in accordance with an agreement entered into by the Central government and a government of a foreign state, the following incomes of such individuals shall be exempted provided :

- (i) The remuneration received by him is directly or indirectly from the Government of the foreign State for such duties rendered in India ; and
 - (ii) Any other income for such individual which accrues or arises outside India and is not deemed to accrue or arise in India, in respect of which individual is required to pay any income or social security tax to government of that foreign State.
11. Income of a consultant [Section 10(8A)] :

Any remuneration or fees received by a consultant from an International Organisation who derives its fund under technical assistance grant agreement between such organisation and the foreign government and any other income accruing or arising to him outside India and which is subject to income tax or social security tax in foreign country, shall be fully exempted. The agreement of the service of consultant must be approved by the competent authority.

The consultant means:

- (i) An individual who is
 - (a) not a citizen of India; or
 - (b) if citizen but is non-resident in India; or is render technical services in India in connection with any technical assistance programme or project.

12. Income of Employees of Consultant [Section 10 (8B)] :

In case of an individual who is working as an employee of a consultant as referred in 8 (A) above, shall be fully exempted provided :

- (i) Such individual is not a citizen of India; or if citizen is not ordinarily resident; and
 - (ii) The contract of service is approved by the competent authority.
13. Income of family members of an employee serving under a co-operative technical assistance programme (Sec. 10(9)) :

Any income of the family member of an employee as referred under section 10 (8) or (8A) or 8(B) who is accompanying him to India, which accrues or arise outside India and is not deemed to accrue or arise in India, and in respect of which such member is required to pay any income tax or social security tax to the Government of that foreign state or the country of origin of such member, is exempted from tax.

14. Gratuity [Section 10 (10)] :

- (i) Death-cum-retirement gratuity:
Any such amount received by the employees working on Civil or Defence Services of Government of India, or on any part of State Government or local authority covered under revised Pension Rules of the Central government shall be fully exempted.
- (ii) Gratuity received under Payment of Gratuity Act 1972.

Employees covered under Payment of Gratuity Act 1972 :

Least of the following amount is exempted.

- (i) 15 days salary for every complete year of service (7 days for seasonal establishment).
 - (ii) Rs. 10,00,000 (Rs. 20,00,000 w.e.f. FY-2019-20)
 - (iii) Gratuity actually received.
- Note : (1) Calculation of 15 days salary will be last salary drawn $\frac{15}{26}$.
- (2) For calculating number of completed years period of service of more than 6 months will be taken as one year or six months.
 - (3) Salary means Basic pay + D.A.
- (iii) For other Employees not covered by Payment of Gratuity Act 1972 :
Exempted upto least of the following :-
- (i) Actual gratuity received
 - (ii) Statutory limit Rs. 10,00,000 (Rs. 20,00,000 from F.Y. 2019-20)
 - (iii) 1/2 months average salary for every completed year of service. Here calculation of 1/2 months' salary will be based on average salary of last 10 months preceding the retirement or death as the case may be.

Salary :

The word 'Salary' here has the same meaning as assigned to it for provident fund purpose, i.e. the Basic Pay plus dearness pay plus any portion of D.A. which enters into pay for service benefits, Plus commission received as a fixed percentage of turnover.

15. Commuted Value of Pension Received [Section 10(10A)] :

- (i) The full amount of commuted value of pension is exempted if it is received from the government, a local authority or a statutory corporation.
- (ii) Any payment in commutation of pension received under any scheme from any other employer to the extent it does not exceed :
 - (a) in a case where the employee receives any gratuity, the commuted value of 3/4rd of pension which he is normally entitled to receive; and
 - (b) in case where the employee doesn't receive gratuity, the commuted value of 1/2 of such pension.
- (iii) Any payment received by an individual in commutation of pension from a fund set up by life insurance corporation (LIC) of India since 1st August, 1996 under a scheme to which contribution is made by the individual receiving pension would be exempted from tax.

16. Amount received as Leave Encashment on Retirement [Section 10(10AA)]**(a) Central and State Government Employees :**

Any payment received as the cash equivalent of the leave salary in respect of the earned leave at his credit at the time of his retirement shall be fully exempted.

(b) Other employees :

Any payment received as the cash equivalent of the leave salary at his time of superannuation shall exempt up to least of the following four amounts:

- (a) Actual amount received;
- (b) Amount calculated at average salary for ten months. Average salary means (Average of salary drawn by the employee during 10 months immediately preceding the date of his retirement);
- (c) Amount specified by the government (present limit is Rs. 3,00,000) ; and
- (d) Cash equivalent of leave salary due at the time of retirement. It is by taking one month leave for every leave completed year of service less leave already availed of.

Excess of amount received over the least of the above shall be taxable.

17. Retrenchment compensation paid to workmen [Section 10 (IOB)] :

The Finance Act, 1975 has inserted a new clause 10B in Section 10 of Income Tax Act which provides that retrenchment compensation received by a workman shall be exempted from Income Tax to the extent of the least of the following amounts:

- (i) Amount calculated in accordance with the provisions of Section 15 F (b) of the Industrial Disputes Act, 1947, or
- (ii) Rs. 5 lacs.

This exemption will be available only to workmen as defined in Industrial Dispute Act, 1947.

18. Payment received under Bhopal Gas Leak Act 1985 [Section 10 (10BB)]: Payment received under the provision of such Act or any scheme formed thereunder shall be fully exempted but in case payment is received against a loss or damage, for which deduction has been claimed earlier, it shall be taxable.

19. Compensation received in case of any disaster [Section 10(10BC)]:

In case an individual or his legal heir receives any compensation on account of any disaster from Central or State government or from local authority, the same shall be exempted.

20. Retirement Compensation from a Public Sector Company or any other Company [(Section 10(10C)]:

Any payment received by an employee of a Public Sector Company or of any other company or a statutory authority or a local authority or a cooperative society or a University or an Indian Institute of Technology, or any notified Institute of Management at the time of his voluntary retirement in accordance with any such scheme is exempted to the extent of Rs. 5 lacs w.e.f. Assessment Year 2001-2002, the exemption shall also be available to an employee on termination of his services and in case of an employee of public sector company on the termination of his services under a voluntary separation scheme.

21. Income by way of tax on perks (sec 10(10cc)) :

In case employer pays, at its option, tax on value of perks given by it to an employee (not by way of monetary payment) shall be fully exempted in the hands of employees.

22. Any sum received under a Life Insurance Policy [Section 10 (10D)] :

Any sum received under a Life Insurance Policy, including the sum allocated by way of bonus on such policy is fully exempted.

23. Payment from Statutory Provident Fund [Section u/s 10 (11) :

Any amount received by employee from his statutory provident fund or public provident fund is fully exempted from tax.

24. Payment from Recognised Provident Fund [Section]10 (12) :

Any amount/accumulated balance due and becoming payable to an employee in R.P.F. is exempted to the extent provided in rule 8 of Para-A of the Fourth Schedule.

25. Payment from Superannuation Fund [Section 10 (13)] :

It means superannuation fund which has been and continues to be approved by the commissioner in accordance with rules contained in Part B of the Fourth Schedule.

The tax treatment of contribution to any payment from the fund is as under:

1. Employer's contribution is exempted from tax.
 2. Employee's contribution qualifies for tax deduction under section 80(c).
 3. Interest on accumulated balance is exempted from tax.
 4. Section 10(13) grants exemption in respect of payment from the fund
 - (a) to the legal heirs on the death of beneficiary ; or
 - (b) to an employee in lieu of or in commutation of an annuity on his retirement at or after the specified age or on his becoming incapacitated prior to such retirement or
 - (c) by way of refund of contribution on the death of the beneficiary, or
 - (d) by way of refund of contribution to an employee on his leaving the service in connection with which the fund is established otherwise than by retirement age or after a specified age of or on his becoming incapacitated prior to such retirement, to the extent to which such payment does exceed the contributions made prior to the commencement of this Act and any interest thereon.
26. House Rent Allowance [Section 10(13A)] :
- (i) Person living in rented houses : Any amount of House Rent Allowance received by the employee from his employer is exempted up to the least of the following limits :
 - (i) Excess of actual rent paid over 10% of salary;
 - (ii) An amount equal to 50% of salary where accommodation is situated in any one of the following places, namely Bombay, Calcutta, Delhi and Madras actual HRA received and 40% in any other town; or
- Note : Person living in his own house or not paying any rent but getting HRA : -
Full HRA received is taxable. No exemption under this provision.
27. Any Allowance given for Meeting Business Expenditure [Section 10 (14)] :
- (i) Any such special allowance or benefit, not being in the nature of a perquisite within the meaning of clause (2) of Section 17 specially granted to meet expenses wholly, necessarily and exclusively incurred in the performance of the duties of an office or employment of profit, as the Central government may, by notification in the official Gazette, specify to the extent to which such expenses are actually incurred for that purpose.
 - (ii) Any such allowance granted to the assessee either to meet his personal expense at the place where he ordinarily resides, or to compensate him for the increased cost of living, as the Central government may specify

in the official Gazette.

28. Interest Incomes Section 10(15) :

The following interest incomes are exempted from tax:

- (i) Interest and premium on redemption of notified securities bonds or certificates.
- (ii) In case of an individual or HUF interest on such bonds as the central government may be notification in the official Gazette, specify in this behalf.
- (iia) 7% Capital Investment Bonds held by individual and HUF. assessee only. The central government shall not specify any such bonds on or after 1-6- 2002.
- (iib) In the case of an Individual Hindu Undivided family, interest on 9% Relief Bonds shall also be exempted.
- (iic) Interest on the notified bonds arising to
 - (a) a non-resident Indian being an individual owning the bonds; or
 - (b) any individual owning the bonds by virtue of being a nominee or survivor of such non-resident Indian; or
 - (c) by an individual to whom the bonds have been gifted by the non - resident Indian.

The exemption shall be allowed if the following conditions are satisfied.

- (a) The bonds should have been purchased by a non-resident Indian in foreign exchange.
 - (b) The interest and principal received in respect of such bonds whether on their maturity or otherwise; is not allowable to be taken out of India.
 - (c) Where the individual who is non-resident Indian in any subsequent year in which the bonds are acquired, becomes a resident in India in any subsequent year the interest received from such bonds will continue to be exempted in the subsequent year as well.
 - (d) Where the bonds are encashed in a previous year prior to their maturity by an individual who is so entitled the exemption in relation to the interest income shall not be available to such individual in the assessment year relevant to such previous year in which the bonds have been encashed.
- (iii) Securities held by the issue Department of Central Bank of Sri Lanka.
 - (iv) Interest payable to any foreign bank performing central banking

function payable in respect of the deposit made by such banks with any scheduled bank in India with the approval of the Reserve Bank of India.

- (v) **Interest payable :**
- (a) by government or a local authority on money's borrowed by it from, sources outside India ;
 - (b) by an industrial undertaking in India or moneys borrowed by it under a loan agreement entered into by any such financial institutions in a foreign country as may be approved in this behalf by the central government.
 - (c) by an industrial undertaking of India on money borrowed or debt incurred by it in a foreign country in respect of the purchase outside India of raw materials or capital or plant and Machinery ;
 - (d) by the Industrial Finance Corporation in India or the Industrial Development Bank of India or the Industrial Credit and Investment Corporation of India or Export or Import bank of India or the National Housing Bank or the Small Industries Development Bank of loans raised by them in foreign countries to the extent to which such interest doesnot exceed the rate approved by the central government;
 - (e) by any other financial institution established in India or an Indian Bank on loans raised by them in foreign countries under loan agreement approved by the Government in connection with making advances to industrial undertaking in India for the purchase of raw materials and plant and machinery. The interest will be exempted to the extent of the rate approved by the Government;
 - (f) by any industrial undertaking in India on money borrowed in foreign currency from foreign sources under a loan agreement approved by the Government for the purpose of Industrial development in India; and
 - (g) by a Scheduled or Bank to a non-resident or a person who is not ordinarily resident in India on deposits in foreign currency.
29. **Payment made by an Indian Company engaged in the business of operation of aircraft [Section 10(15A)] :**
Such payment made to acquire an aircraft or an aircraft engineer on lease to Foreign government or a Foreign Enterprise under an agreement entered before 1-4-97 and between 1-4-99 to 31-3-2006 and approved by the central government shall be fully exempted.
30. **Scholarships [Section 10(16)] :**
Scholarships granted to meet the cost of education is fully exempted.

31. Daily Allowance of Legislators or Members of Parliament [Section 10 (17)] :
- (a) The daily allowance received by a member of Parliament or of any State legislature of any committee thereof is exempted.
 - (b) any allowance received by a member of Parliament is fully exempted.
 - (c) All other allowances not exceeding Rs. 2,000 per month in the aggregate received by a member of State legislation or any committee thereof shall be exempted.
32. Awards [Section 10 (17A)] :
- Any payment made, whether in cash or in kind,
- (i) In pursuance of any award instituted in the public interest by the Central Government or State Government or by any other body and approved by Central government.
 - (ii) As reward by the Central Government of any State Government for such purposes as may be approved by the Central Government in the public interest is fully exempted.
33. Pension received by winners of Gallantry Award [Sec. 10(18)] :
- Fully exempted from tax.
34. Family pension of war widow [section 10 (19)] :
- With effect from 1-4-2005, family pension received by the widow or children or nominated heirs, as the case may be, of a member of armed forces (including Paramilitary Forces) of the union, where the death has occurred in the course of operational duties, in such circumstances and subject to such conditions, shall be fully exempted.
35. Income from one palace of a former ruler [Section 10(9A)] :
- Annual Value of any one palace or a portion of a palace in the occupation of a former ruler shall be exempted but in case such palace or a portion of a palace is let-out, its income shall not be exempted.
36. Income of a Local Authority [Sec. 10(20)] :
- The income of a local Authority which is chargeable under the head Income from houses property; Capital gains or Income from other sources or from a trade or business carried on by it, which accrues or arises from, by supply of a Commodity or Service within its own jurisdiction area or for the supply of water and electricity within or outside its own Jurisdictional is exempt.
37. Income of approved Scientific Research Association [Section 10(2 1)] :
- Any income of an approved scientific research association and if the same income is applied solely for the purposes of that association, i.e. for carrying scientific research is exempt.
38. Income of a News Agency [Section 10(22B)]:
- Any income of a news agency setup solely in India for collection and distribution of news and which is so notified in this behalf shall be fully exempted if such income or

accumulated income is used for collection and distribution of news only.

39. Income of association encouraging certain Professions [Sec. 10(23A)] :

Any income of an association or institution established in India with the object to control, supervise, regulate or encourage the profession of law, medicine, accountancy, engineering or architecture or such other profession as the central government may specify in this behalf by notification in official Gazette, is exempted.

40. Income of fund set-up for the welfare of employee or their dependents [Sec. 10(23AAA)] :

Any income which is approved by commissioner of Income-Tax shall be fully exempted.

41. Income of a pension fund set-up by LIC or other Insurer [Sec. 10(23AAB)] : Any income of a fund set up by LIC of India on or after 1-8-1996 under pension scheme or by an insurer shall be fully exempted.

42. Income of Institutions established for development of Khadi and Village Industries [Section 10(23B)] :

From the Assessment year 1975-76, the public charitable trusts and societies registered under the societies registration Act, 1860 will be entitled to claim exemption.

43. Income from Khadi or Village Industries [Sec. 10(23BB)] :

Any income from an authority established in a State by or under a State of Provincial Act for the development of Khadi or Village industries in the state, shall be exempted from tax.

44. Income of Statutory bodies for the administration of Public Charitable Trust [Sec. 23 BBA] :

Any income of statutory bodies established or constituted under law of administration of public religious or charitable trust including temples, Maths, Gurudwaras, Wakfs etc. is exempted from tax.

45. Any Income of Insurance Regulatory and Development Authority [Section 10 (23BBE)] :

Any income of Insurance Regulatory and Development Authority established under IRDA Act, 1999 shall be fully exempted.

46. Income of Certain National Funds [Sec. 10 (23 C)] :

Any income of following funds is totally exempted

- (i) The Prime Minister's National Relief Fund.
- (ii) The Prime Minister's Fund (Promotion of Folk Art)
- (iii) The Prime Minister's Aid to Student Fund.
- (iv) The National Foundation of Communal Harmony.

- (v) Any trust or institution set-up, wholly for religious purpose or purpose for which may be notified by the Central Government.

The condition for exemption for a fund or institution specified in (v) and (v) are the same as discussed u/s 23 except that the maximum period of accumulation will not apply to these clauses.

47. Income of a Mutual Fund (Sec. 10 (23D)) :

Any income of a notified mutual fund set up by a public sector bank or public financial institution and subject to such conditions as the Central Government specify in this behalf under the scheme SBI Mutual Fund, LIC of India Mutual Fund, Canara Bank Mutual Fund, BCI Mutual Fund, GIC Mutual Fund, India Bank Mutual etc. have been specified. The following are the public financial institutions :

- (i) Industrial Credit and Investment Corporation of India Limited.
- (ii) Industrial Finance Corporation of India.
- (iii) Industrial Development Bank of India.
- (iv) Life Insurance Corporation of India.
- (v) Unit Trust of India.

48. Income of Investor Protection Fund [Section (10)23EA] : Income of Investor Protection Fund set-up recognised stocks exchanges in India is exempted.

49. Income of Registered Trade Unions [Sec. 10 (24)] :

The following incomes of registered trade unions are exempted from tax:

- (i) Income from house property.
- (ii) Income from other sources.

The trade union must be registered one and formed primarily for the purpose of regulating the relations between workmen and employer or between workmen and workmen.

50. Income of Provident and Superannuation Funds (Sec. 10 (25)):

The following incomes are exempted:

- (i) Interest on securities which are held or are the property of any provident fund to which Provident Funds Act, 1925 applies and any capital gains of the fund arising from the sale, exchange or transfer of such securities;
- (ii) any income received by the trustee on behalf of a recognised provident fund; and
- (iii) any income received by the trustees on behalf of an approved superannuation fund.

51. Income of Member of Scheduled Tribe [Sec. 10 (26A)] :

Certain income of a member of scheduled tribe, residing in a tribal area or in the State of Nagaland or in the Union Territories of Manipur and Tripura are exempted provided the income is derived :

- (i) from any source in tribal area, State or Union Territories mentioned above;
or
- (ii) by way of dividend or interest on securities.
52. Income of Cooperative Societies looking after the interest of Scheduled Castes or Scheduled Tribes or Both [Sec. 10 (27)] :
- Such income shall be fully exempted provided the membership of such society consists of only other cooperative societies formed for similar purposes and the finances of the society are provided by Government and such other securities.
53. Amount received as subsidy from or through the Tea Board (Sec. 10 (30)) : This exemption is available to assessee carrying on the business of growing and manufacturing tea in India. The subsidy by such assessee from or through the Tea Board under any such scheme of replantation or replacement of tea bushes or for rejuvenation or reconsolidation of areas used for tea cultivation as the Central Government may notify in the official gazette is exempted. For getting this exemption, the assessee is required to furnish to Assessing Officer, alongwith his return of income a certificate from the Tea Board showing the amount of subsidy received by him during the previous year. The Assessing Officer may allow the assessee such time as he thinks desirable and the assessee is required to submit the said certificate in the allowed time.
54. Amount received as subsidy from or through the concerned Board [Section 10(31)] :
- Any amount received as subsidy, from or through the concerned Board for replantation of Rubber, Coffee, Cardamon Plants or plants for growing of such other commodities or for any other scheme so notified shall be fully exempted.
55. Income of Minor Child from his manual work or Profession [Sec. 10 (32)]: Such income shall be exempted upto Rs. 1500 / - in case of each minor child whose income is to be clubbed with the income of his parents.
56. Income from Transfer of Capital assets of UTI [Sec. 10(33)] :
- Any income arising from the transfer of a capital asset, being a unit of the unit scheme, 1964, referred to in schedule I of the UTI Act, 2002 and transfer takes place on or after 1-4-2002 shall be fully exempted.
57. Dividend from an Indian Company [Section 10 (34)]:
- Any dividend distributed paid or declared by Indian company has been made fully exempted from 1-4-2003 (referred to in section 115-0). But now dividend Income is exempted only upto Rs. 10 lacs.
58. Long term Capital Gain on transfer of shares and securities covered under Security Transaction Tax (STT) [Section 10(38)] :
- Any income arising from the transfer of a long-term capital asset, being securities (i.e.

shares of a company or units of an equity oriented fund) and transaction of such sale is entered into a recognised stock exchange in India on or after 01.10.2004 shall be fully exempted.

59. Reverse Mortgage [Section 10(43)] :

Any amount received by an individual as a loan, either in lumpsum or in installment in a transaction of reverse mortgage referred in clause (xvi) of Section-47 shall be exempted.

60. Exemption of Income of New Pension Scheme Trust [Section 10(44)] :

Any income received by any person for or on behalf of New Pension Scheme Trust under the provisions of Income Tax Act of 1962, shall be exempt from income tax.

1.3.3 EXEMPTION REGARDING PROFITS OF NEWLY ESTABLISHED INDUSTRIAL UNDERTAKINGS IN FREE TRADE ZONE (Section 10-A)

If an undertaking derives profits and gains from the export of articles or things or computer software it shall be entitled to a deduction of such profit from its income.

I. Period of Deductions will be the ten consecutive assessment years beginning with the Assessment Year relevant to the Previous Year in which the undertaking begins to manufacture or produce articles or things or computer software. However, no deduction will be allowed to any undertaking for the assessment year 2012-13 and thereafter. In other words, deduction shall be allowed maximum upto assessment year 2011-12.

II. Conditions for Deductions :

- (i) It has begun or begins to manufacture or produce articles or things or computer software.
 - (a) after 31.03.80 in any Free Trade Zone ; or
 - (b) after 31.03.93 in any electronic hardware technology park of Software technology park (STP); or
 - (c) after 31.03.2000 in any special economic zone.
- (ii) It is not formed by splitting up or the reconstruction of business already in existence.
- (iii) It is not formed by the transfer to a new business of machinery or plant previously used for any purpose.
- (iv) The sale proceeds in respect of the aforesaid business are received in or brought into India by the assessee in convertible foreign exchange within a period of six months from the end of the previous year or within such further period as may be allowed by the competent authority.
- (v) The assessee furnishes in the prescribed form alongwith the return of income the report of an accountant certifying that the deduction has been correctly claimed.

- (vi) The profits derived from export of articles or things or computer software shall be the amount which bears to the profits of the business, the same proportion as the export turnover in respect of such articles or things or computer software bears to the total turnover of the business carried on by the assessee.

III. Impact of availing exemption under Section 10-A :- The assessee who avails the benefit of tax concession u/s 10-A and he files a declaration to this effect along with the return of income then he can claim all such other tax concessions as available to such units.

IV. Option available to new Undertakings not to claim tax holiday under Section 10-A: The benefits under the Section 10-A are optional. In case the assessee do not wish to claim such exemptions u/s 10-A and he files a declaration to this effect along with the return of income then he can claim all such other tax concessions as available to such units.

1.3.4 Newly Established Units in Special Economic Zones (Section 10-AA) : A Person can claim exemption if he derives profits out of special Economic Zones subjects to following conditions:-

1. The person is an entrepreneur as defined in section 2(j) of SEZ Act, 2005.
2. The person has income from export of articles or services from such unit.
3. Books of accounts need to be audited
4. Amount of deduction shall be calculated as per following formula-

Profits of the Business	XS	<u>Export turnover</u>
Undertaking		Total turnover of such business
5. Period of deduction is as mentioned below:-

-> First five years	->	100% of profit and gains from export of articles or services
-> Next five years	->	50% of profit or gains from export of articles or services
-> Next five years	->	Further deduction would be available upto 50% of profit subject to condition that an <u>equivalent amount is debited to P & L A/c and created to the special economic zone</u> Re-investment Allowance Reserve account

1.3.5 Income not taxable of Political Parties (Section- 13A)

As per this section income of Political parties falls under the head 'Income from house property', 'Income from capital gains' or 'Income from other sources' is exempted if received by parties by way of voluntary contributions.

1.3.6 Voluntary contribution received by Electoral trust is exempt from tax (Section 13-B):

From Assessment year 2010-11, if any voluntary contributions received by an electoral trust is exempted from tax as per following conditions-

1. The electoral functions in accordance with rules made by the central government.
2. A minimum 90% of the aggregate donations received by such electoral trust should distribute to any political party.

1.3.7 SELF-CHECK EXERCISE

- Q.1. Define the term exempted incomes. Also give five examples.
- Q.2. Explain the provisions of law relating to tax holiday in respect of Newly Established 100% EOU.

1.3.8 SUMMARY

As mentioned in this lesson, Section 10 of Income Tax Act has given a long list of incomes which are totally exempt from tax and so these incomes are not included in the gross total income of the assessee. In other sense, we can say that these incomes are totally tax-free.

In computing the total income of any previous year of any person, any income falling within any of the clauses (which mentioned in this lesson) shall be exempted.

1.3.9 GLOSSARY

- | | | | |
|----|-----------------|---|--------------------------------|
| 1. | Exempted Income | : | Income not chargeable to tax |
| 2. | HUF | : | Hindu Undivided Family |
| 3. | EOU | : | Export Oriented Undertakings |
| 4. | Tax Holiday | : | Period when tax is not charged |
| 5. | Casual Income | : | Irregular Income |

1.3.10 ANSWERS TO SELF-CHECK QUESTIONS

Ans.1 Exempted incomes are those incomes which are totally tax-free, and are not included in the gross total income of the assessee.

Examples :

1. Agriculture Income
2. Share from HUF
3. Share from the firm.
4. Interest paid to Non-Resident.
5. Perquisites and Allowances paid by Government to its employees serving outside India.

Ans.2 Discuss under mentioned provisions in detail in respect of Free-Trade Zones :

1. Conditions for deductions
2. Period of deduction
3. Withdrawal of benefits

1.3.11 EXERCISE**(A) Short Questions :**

- Q.1. Give ten examples of incomes which are totally exempt from income-tax.
- Q.2. Give tax provisions which are applicable on Interest paid to NRI.
- Q.3. Write short notes on the following :
- (i) Casual Income
 - (ii) Interest earned u/s 10 (15)
 - (iii) Tax Exemption for 100% export-oriented units.

(B) Long Questions :

- Q.1. Explain the provisions of law relating to tax holiday in respect of Free Trade Zones u/s 10-A.
- Q.2. In the following cases, state whether the receipts are taxable or not. Give reasons for your answers:
- (a) Salary income received by X, as general manager of M/S A & Co. who derives its full income from agricultural crop produced on its own land.
 - (b) Z, a film actress, is awarded a cash prize of Rs. 1,00,000 under the scheme of State awards for actresses. Z, claims this to be exempt from tax.
- Q.3. Write one paragraph of about 100 words on :
- 1. H.R.A.
 - 2. Commuted pension
 - 3. LTC (Leave Travel concession)

1.3.12 SUGGESTED READINGS

- (i) Direct Taxes: By Sanghania
- (ii) The Income Tax Law : By Shailinder Sekhon
- (iii) Income Tax: By Gaur & Narang.
(A.Y. 2023-2024)

INCOME UNDER THE HEAD SALARY

Structure of the Lesson :

- 1.4.0 Objectives
- 1.4.1 Introduction
- 1.4.2 Computation of Income under the head 'Salaries'
- 1.4.3 Meaning of 'Salary'
- 1.4.4 Annuity
- 1.4.5 Death-cum-Retirement Gratuity [Sec. 10 (10)]
- 1.4.6 Pension [Sec. 10 (10 A)]
- 1.4.7 Leave Salary [Sec. 10 (10 AA)]
- 1.4.8 Retrenchment Compensation [Sec. 10 (10 B)]
- 1.4.9 Compensation received on Voluntary Retirement [Sec. 10 (10 C)]
- 1.4.10 Provident Fund
 - 1.4.10.1 Statutory Provident Fund
 - 1.4.10.2 Recognised Provident Fund
 - 1.4.10.3 Unrecognised Provident Fund
 - 1.4.10.4 Public Provident Fund
- 1.4.11 Allowances
- 1.4.12 Perquisites [Sec. 17(2)]
- 1.4.13 Deductions out of Gross Salary [(Sec. 16)]
 - Self check exercise
- 1.4.14 Summary
- 1.4.15 Exercise
- 1.4.16 Answers to self-check questions
- 1.4.17 Suggested Readings

1.4.0 OBJECTIVE

The main objective of this lesson is to introduce the students with the latest provisions of the income chargeable to tax under the head salary.

1.4.1 INTRODUCTION

According to Sec. 4 of the Income Tax Act 1961 tax is to charge on total income of an assessee which is divided under five head of income. Each head of income has its own method of Computation.

These five heads are :

1. Income from 'Salaries'
2. Income from 'House Property'
3. Income from 'Profit and Gains of Business and Profession.'
4. Income from 'Capital Gains'
5. Income from 'Other Sources'

1.4.2 COMPUTATION OF INCOME UNDER THE HEAD 'SALARIES'

The first head of income is income from "Salaries". Sections 15, 16 and 17 of the Income-Tax Act deal with computation of income under the head "Salaries."

To understand the computation of income under the head "Salaries", the following important concepts must first be understood :

1. Employer and Employee Relationship

An income can be taxed under the head "Salaries" only if there is a relationship of an employee between the payee and the payer. If this relationship does not exist, then the income would not be deemed to be income from salary. The relation of employer and employee should be of master and servant. A master is one who not only directs what and when a thing is to be done but how it is to be done, and the servant is one who is bound to carry out the instructions given to him by such masters.

2. Surrender of Salary

Any salary surrendered by the employee to Central Government, under the Voluntary Surrender of Salaries (Exemption from Taxation) Act, 1961 will not be included while computing his taxable income, whether he is a private sector/public sector or Government employee.

3. Place of Accrual [Section 9 (1)]

The golden rule is that salary will be deemed to accrue or arise at a place where services are rendered. If the services are rendered in India and salary on an account of such services are received outside India, it will be treated as an income which is deemed to accrue or arise in India. Similarly, if a person, who after rendering services in India, retires and settles abroad, receives any pension on account of the same, such pension shall be an income which is deemed to accrue to arise in India as the services on account of which pension accrues, were rendered in India.

4. Tax Free Salary

When the employee receives tax-free salary from his employer, it normally means that the employer himself pays the tax which is due on the salary of such employee. The amount of tax, so paid by the employer, is also to be considered as the income of the employee and will be added to his salary.

5. Foregoing of Salary

Once salary has been earned by an employee, it becomes taxable in his hands though

he may subsequently waive the right to receive the same from employer. The waiver of salary by the employee would be treated as application of the income and salary though waived would be taxable in his hands.

6. Salary paid by Foreign Government/Enterprises

Salary paid by Foreign Government/Enterprises to its employees serving in India is taxable under the head Salaries, unless it is specifically exempt u/s 10.

7. Basis of Charge (Section 15)

As per Section 15, the following income shall be chargeable to income-tax under the head "Salaries".

- (a) any salary due from an employer or a former employer to an assessee in the previous year, whether paid in that previous year or not;
- (b) any salary paid or allowed to him in the previous year by or on behalf of an employer or a former employer though not due in that previous year or before it became due to him;
- (c) any arrears of salary paid or allowed to him in the previous year by or on behalf of an employer or a former employer, if not charged to income tax in any earlier previous year. (Arrear is taxable in the year in which received.)

1.4.3 MEANING OF 'SALARY'

Section 17 (1) gives an inclusive definition of 'Salary'

Salary includes-

- (i) wages;
- (ii) any annuity of pension;
- (iii) any gratuity;
- (iv) any fees, commissions, perquisites of profits in lieu of or in addition to any salary or wages;
- (v) any advance of salary;
- (vi) any payment received by an employee in respect of any period of leave not availed by him;
- (vii) the annual accretion to the balance at the credit of an employee participating in a recognized provident fund, to the extent to which it is chargeable to tax;
- (viii) the aggregate of all sums that are comprised in the transferred balance of an employee participating in a recognized provident fund to the extent to which it is chargeable to tax.

The aggregate of above income, after getting the exemptions, if any, is known as 'Gross Salary'. From the gross salary, the following two deductions are allowed under Section 16:

- (i) Deduction for entertainment allowance {Section 16 (ii)}; and

- (ii) Deduction on account of any sum paid towards tax on employment
(Section 16 (iii))

The amount arrived at, after allowing the above deductions, is the income under the head 'Salaries'.

1.4.4 ANNUITY

Annuity is an annual grant and when made by an employer falls under the head 'Salaries', it may be paid by the employer voluntarily or on account of a contractual agreement. When annuity is payable by a present employer, it is taxable as salary. If it is received from a former employer then it is taxed as profits in lieu of salary.

1.4.5 DEATH-CUM-RETIREMENT GRATUITY SEC. 10 (10)

Gratuity is a payment made by employer to an employee in appreciation of the past services rendered by the employee. Gratuity can either be received by :

- (a) the employee himself at the time of his retirement ; or
- (b) the legal heir on the event of the death of the employee.

Gratuity received by an employee on his retirement is taxable under the head 'Salary' whereas gratuity received by the legal heir of the deceased employee shall be taxable under the head " Income from other Sources". However, in both the above cases, according to Section 10 (10) gratuity is exempt upto a certain limit.

For the purpose of exemption of gratuity under Section 10 (10), the employees are divided into 3 categories :

- (a) Government employees and employees of local authorities
- (b) Employees covered under the Payment of Gratuity Act, 1972
- (c) Other employees

1.4.5.1 (a) Exemption in the case of Government Employees and Employee of Local Authorities {Section 19 (10) (i) :

In the case of such employees, the entire amount of death-cum-retirement gratuity received under the following rules/ schemes is exempt from tax under section 10 (10) (i). Nothing will, therefore, be taxable under the head 'salaries' or income from other sources, as the case may be on account of gratuity.

1.4.5.2 (b) Exemption in the case of non-government employees who have received gratuity under the Payment of Gratuity Act, 1972 {Section 10 (10) (ii)} :

In the case of employees, who are covered under the Payment of Gratuity Act, any gratuity received shall be exempt to the Section 4(2) and (3) of the Payment of Gratuity Act, 1972.

Therefore, the minimum of the following amount is exempt from tax :

- (a) The amount of gratuity actually received.
- (b) 15 days' salary for every completed year of service or part thereof in

excess of six months. However in the case of an employee who is employed in a seasonal establishment and is not so employed throughout the year, the exemption shall be for

seven days wages for each season.

- (c) Rs. 20,00,000 w.e.f. financial year 2019-20 (notified limit).

For purpose of calculating completed year of service, more than 6 months shall be taken as a completed year. A period of 6 months or less than 6 months shall be ignored.

In case of a seasonal workman, when gratuity at the rate of 7 days wages for each season requires to be worked out, then one has to see the number of seasons in each completed year of service of the workman.

Salary = Basic Pay + Dearness Allowance (Whether enter or not)

$$\left(\frac{2600}{26} \times 15 \right)$$

In the case of monthly rated employees for calculating 15 days salary, the number of days in a month will be taken as 26 working days. Therefore, the monthly salary shall be divided by 26 and multiplied by 15. For example if the monthly salary of an employee at the time of retirement is Rs. 2600, 15 days salary would be Rs. 1,500

Illustration: I

R retires on 4.1.2023 after serving XY Company Ltd. For a period of 16 years and 11 months. At the time of retirement his basic salary was Rs. 4,400 per month and he was also entitled to Dearness Allowance of Rs. 800 per month. On his retirement, he received Rs. 60,000 as gratuity. Compute the amount of gratuity exempt from tax and the amount to be included in gross salary. He is covered under the Payment of Gratuity Act.

Solution

The exemption shall be to the extent of the minimum of the following three amounts :

- (a) Amount of Gratuity received Rs. 60,000
- (b) 15 days' salary for every year of service i.e. $\frac{5200}{26} \times 15 \times 17 = \text{Rs. } 51,000$
- (c) Rs. 20,00,000 (notified limit).

Therefore Rs. 51,000 shall be exempt from tax and the balance Rs. 9,000 shall, be included in the gross salary.

1.4.5.3 Treatment in the case of other non-government employees :

{Section 10(10)(iii)}

In the case of any other employee, gratuity received by him, on his retirement or on his becoming incapacitated prior to such retirement or on termination of his employment or by legal heirs on his death, shall be exempt to the extent of the minimum of the

following amounts:

- (a) Actual amount of gratuity received
- (b) Half month's average salary for every completed year of service
- (c) Rs. 20,00,000 (notified limit) with effect from financial year 2019-20

Meaning of Salary/Average Salary, etc.

Salary=Basic Pay+ D.A. (if enter)+Commission on (turnover. +D.P.)

Average Salary

Average Salary is to be calculated on the basis of the average of the salary (as mentioned above) for 10 months immediately preceding the month in which retirement or death occurs. For example, if an employee retires on 2.1.2023 the average salary shall be taken as the aggregate of salary for the period from 1.3.2022 to 31.12.2022 divided by 10.

Completed years of service

In calculating the number of years of service only completed years are to be taken into account and part of the year whether more or less than 6 months, will be ignored. For example, if a person retires after serving for 24 years and 11 months, the period of service will be taken as 24 years only.

Illustration : II

R, who employed with P Company Ltd. retired on 21.10.2022, received Rs. 1,20,000 as gratuity. He served the company for 26 years and 8 months. At the time of preceding the month of retirement is Rs. 4800 per month. He is not covered under the Payment of Gratuity Act, 1972, (A) Compute the taxable gratuity.

- (B) What amount of gratuity shall be taxable, if R, earlier to his appointment with P Company Ltd. had worked for 4 years with X Ltd. and was not entitled to gratuity from X Ltd?

Solution

- (A). The minimum of the following three amounts will be exempt :

- (a) Actual amount received i.e. Rs. 1,20,000
- (b) Half month's salary for every completed year of service i.e.

$$\frac{4800 \times 26}{2} = 62,400$$

- (c) Rs. 20,00,000 (notified limit)

Hence, Rs. 62,400 shall be exempt and the balance Rs. 57,600 would be included in his gross salary.

- (B). The minimum of the following three amounts will be exempt :

- (a) Rs. 1,20,000 (actual amount received)

$$\frac{4800 \times 30}{2}$$

- (b) = 72,000 (half month salary for every completed year of service)

- (c) Rs. 20,00,000 (notified limit),

Hence Rs. 72,000 shall be exempt and the balance (1,20,000 - 72,000) Rs. 48,000 shall be taxable.

Note: Completed year of service will include the period of 4 years of earlier appointment.

1.4.6 TREATMENT OF PENSION [SECTION 10 (10A)]

Pension is a payment made by employer after the retirement/death of the employee as a reward of past service.

Pension is normally paid as periodical payment on monthly basis but certain employers also allow the pension to be fully or partly commuted i.e. in lieu of the pension, a lump sum payment is made to the employee. The treatment of these two kinds of pensions is as under :

1.4.6.1 Uncommuted Pension i.e. the periodical Pension

It is fully taxable in the hands of all employees, whether government or non-government.

1.4.6.2 Commuted Pension

Exemption in the case of Government employees or employees of local authorities or statutory corporation [Section 10 (10 A) (i)]

Committed pension received by these employees under the Civil Pensions (Commutation) rules of the Central Government or under any similar scheme applicable e.g. as per Central Civil Services (Pension) rules 1972, is wholly exempt under Section 10(10A) (i).

Exemption in the case of other employees {Section 10(10A) (ii)}

Committed value of pension received by any employee under any scheme of any other employer is exempt under Section 10(10 A) (ii) to the following extent :

(a) *Where the employee receives gratuity also :* The committed value of 1/3rd of the full pension, which he is normally entitled to receive, is exempt from tax. Any amount received over and above the exempted pension is taxable and hence included in gross salary.

(b) *Where the employee does not receive any gratuity :* The committed value of ½ of the full pension, which he is normally entitled to receive, is exempt from tax. Any amount received in excess of the amount would be taxable.

Illustration : III

A retired on 15.4.2022 from B Company Ltd. He was entitled to a pension of Rs. 4,000 p.m. At the time of retirement he got 75% of the pension commuted and received Rs. 1,20,000 as committed pension. Compute the taxable portion of the committed pension if

(i) He is also entitled to gratuity.

(ii) He is not entitled to gratuity.

Solution

- I. 75% of commuted pension is equal Rs. 1,20,000. Hence commuted value of 1/3 of the full pension would amount to $1,20,000 \times \frac{100}{75} \times \frac{1}{3} = \text{Rs. } 53,333$ Thus, Rs. 53,333 would therefore, be exempt and balance Rs. 66,667 would be taxable.
- II. 75% of commuted pension is equal to Rs. 1,20,000. Hence commuted value of 50 % of full pension would amount to $1,20,000 \times \frac{100}{75} \times \frac{1}{2} = \text{Rs. } 80,000$. Therefore, Rs. 80,000 would be exempt and Rs. 40,000 would be taxable.

1.4.6.3 NEW PENSION SCHEME

After 1st January, 2004 contribution made by central govt, other employer and employee towards the notified pension scheme (NPS) is taxable, except 10 % of the salary. (exempt upto 14% of salary in case of central govt. employees.

1.4.7 TREATMENT OF LEAVE SALARY {SECTION 10 (10AA)}

Employees are entitled to various types of leave while they are in service. The leave may either be availed by them or in case these are not availed of, these may either lapse or these are allowed to be encashed every year or these are accumulated and encashed after retirement or death e.g. an employee is entitled to 60 days leave in year, but he avails of only 20 days leave during the years. Depending upon the rules of the company, he may be entitled to get the leave of 40 days encashed.

Encashment of leave during tenure of service

Leave encashment to an employee, while he continues to be in service with the same employer, is fully taxable. In this case, however, the assessee can claim relief under Section 89 (1).

Encashment of accumulated leave at the time of retirement [Section 10(10AA)]

For the purpose of exemption of accumulated leave encashment, employees are divided into two categories :

- (i) ***Government Employees which means Central and State Government Employees only [Section 10 (10AA)(i)]***

Leave encashment of accumulated leave at the time of retirement, whether on superannuation or otherwise, received by Government employee, is fully exempt from tax. Since full leave encashment is exempt, nothing is to be included in gross salary.

- (ii) ***Other Employees [Section 10(10AA) (ii)]***

Leave encashment of accumulated leave at the time of retirement whether on superannuation or otherwise received by other employees (including employees

of local authority and public sector undertakings) is exempted to the extent of the minimum of the following amounts :

- (a) Leave encashment actually received;
- (b) 10 months' average salary;
- (c) Cash equivalent of unavailed leave calculated on the basis of maximum 30 days leave for every year of actual service rendered to the employer from whose service he has retired. The cash equivalent is to be calculated on the basis of the *average salary*;
- (d) Amount specified by the Government after 1.4.1998 is 3,00,000.

Meaning of Salary

Salary = Basic Pay+ D.A. (if enter)+ commission on turnover + D.P.

Average Salary

Average salary is to be calculated on the basis of the Average Salary (as calculated above) drawn by the employee during the period of 10 months immediately preceding his date of retirement. For example, if any employee retires on 31.01.2023 the average salary shall be taken as the aggregate of salary drawn by him for the period 1.4.2022 to 30.1.2023 divided by 10.

1.4.8 RETRENCHMENT COMPENSATION {SECTION 10 (10B)}

Any compensation received by a workman at the time of his retrenchment, under the Industrial Disputes Act, 1947 shall be exempt to the extent of minimum of the following limits :

- (i) Actual amount received
- (ii) Amount calculated in accordance with provisions of Section 25F(b) of the Industrial Disputes Act 1947, which is equal to 15 days average pay for every completed year of service or part therefore in excess of 6 months;
- (iii) Amount specified by the Central Government, i.e. Rs. 5,00,000.

Meaning of Average Pay

Average pay means the average of the wages payable to a workman :

- (a) in the case of monthly paid workman, in the three complete calendar months,
- (b) in the case of weekly paid workman, in the four complete months,
- (c) in the case of daily paid workman, in the twelve full working days.

1.4.9 COMPENSATION RECEIVED ON VOLUNTARY RETIREMENT [SECTION 10 (10C)/RULE 2BA]

The compensation received by the employee of the following, on voluntary retirement, under the golden hand shake scheme, is exempt under Section 10(10C):

- (i) a public sector company; or
- (ii) any other company; or
- (iii) an authority established under a Central, State or Provincial Act; or

- (iv) a local authority; or
- (v) a co-operative society; or
- (vi) a University established or incorporated by or under a Central, State or Provincial act and an institution declared to a University under Section 3 of the University Grants Commission Act 1956 ;or
- (vii) State Government
- (viii) Central Government

Quantum of Exemption

The exemption of amount received under VRS has been extended to employees of the Central Govt. w.e.f. A.Y. 2002-2003 and State Govt. w.e.f. A.Y. 2001-2002. It shall be exempted upto least of following :

- (a) Statutory limit Rs. 5,00,000.
- (b) Three months' salary for every completed year of service.
- (c) Salary for number of months remaining service (i.e. number of months to be counted from the month of voluntary retirement to the month of actual retirement).
- (d) Actual salary received.

Salary for this purpose shall have the same meaning as for provident fund for the month of retirement.

Guidelines [Rule 2BA]

The guidelines of the government for best owing the exemption from tax on the Golden Handshake Scheme are given here in below:

- (i) it applies to an employee, who has completed 10 years of service of completed 40 years of age ;
- (ii) it should apply to all employees (by whatever name called) including workers and executives of a company or of an authority or of a cooperative society ;
- (iii) the scheme of voluntary retirement or voluntary separation should have been drawn to result in overall reduction in the existing strength of the employee;
- (iv) the vacancy caused by the voluntary retirement or voluntary separation is not to be filled up ;
- (v) the retiring job is not be filled up;
- (vi) the amount receivable on account of voluntary retirement or voluntary separation of the employee does not exceed:
 - (a) the amount equivalent to three months' salary for each completed year of service ; or
 - (b) salary at the time of retirement multiplied by the balance months

of service left before the date of his retirement on superannuation.

1.4.10 PROVIDENT FUND

To encourage savings for the social security of employees, the government has set up various types of Provident Funds. The employee contributes a fixed percentage of his salary towards these funds. Provident Funds are of four types :

- (1) Statutory Provident Fund
- (2) Recognized Provident Fund
- (3) Unrecognized Provident Fund
- (4) Public Provident Fund

1.4.10.1 Statutory Provident Fund

This is the oldest type of fund started in 1925 this fund is maintained by Government and Semi Government departments like RBI, Colleges, Railways, Universities, Insurance Companies etc. In this fund employer contribution and interest earned on the credit balance of the account, are not to be included in the income of employee and so it is ignored.

When the employee retires or leave the service, any amount received from this fund will not be included in employee's total income.

Employee's own contribution in this fund will qualify for deduction U/S 80C.

1.4.10.2 Recognized Provident Fund

This fund is recognized by the Commissioner of Income Tax. Generally, this fund is maintained by industrial undertakings, business houses, banks etc. This fund is maintained under P.F. Act 1952. In this fund employer's contribution above 12% of employee's salary*, will not be treated as income.

* (Salary = Basic Pay + dearness Allowance (if enter) + commission on turnover basis) + D.P.

Interest on credit balance for this fund is exempted upto 9.5% and more than 9.5% is included in Gross salary of the employee.

Employee's own contribution in this fund will qualify for deduction U/S 80C.

1.4.10.3 Unrecognized Provident Fund

This is the fund which is not recognized by the Commissioner of Income Tax. Employee's contribution is added in his salary and he will not allowed any deduction of u/s 80C.

Employer's contribution and interest on the credit balance of this fund are ignored for the time being.

1.4.10.4 Public Provident Fund

So far all these funds were for the salaried people. This fund was started on 1st

July, 1968 for the self-employed people like Doctors, lawyers, Actors, Accountants, so that they can get deduction u/s 80C. The interested persons can open their account in State Bank of India and its subsidiaries. The subscription can be between Rs. 500 (minimum) and 1,50,000 (maximum) in one year. At one time one can deposit in multiples of fifty and in one month only one deposit is possible.

Full withdrawal is possible after 15 year but in case of death, full repayment will be given to the legal heir of the nominee. Partial withdrawal and loans are also possible. Interest credited in PPF a/c is fully exempted.

I Transferred Balance

The balance of unrecognized Provident Fund when transferred to recognized Provident Fund (RPF) is called "Transferred Balance". Such Balance is taxable in the hands of employee and hence included in his gross salary.

II Refund from Provident Fund

- (i) In case of Statutory Provident Fund, amount received is fully exempted.
- (ii) In case of RPF, amount received is fully exempted if service is more than 5 years and it is taxable if service is less than 5 years.
- (iii) In case of URPF taxable portion is equal to employer's contribution and interest thereon. Interest on employees contribution is taxable as income from other sources.

III. With effect from Finance Act, 2020, contribution made to three funds (Provident fund, NPS and superannuation fund) in excess of Rs. 7.50 by employer is taxable as perquisite in the hands of employee.

1.4.11 ALLOWANCES

Allowance is a fixed monetary amount paid by the employer for meeting some particular expenses, whether personal or for the performance of his duties. These allowances are generally taxable and are to be included in the gross salary.

1.4.11.1 House Rent Allowance [Section 10(13A) and Rule 2A]

House Rent Allowance is given by the employer to the employee to meet the expenses in connection with rent of the accommodation which the employee might have to take. HRA is exempt under Section 10(13A) to the extent of the minimum of the following three amounts :

- (a) Actual House Rent Allowance received by the employee in respect of the period during which the rented accommodation is occupied by the employee during previous year.
- (b) Excess of Rent paid- 10% of Salary
- (c) 50% of the salary where the residential house is situated at Mumbai, Calcutta, Delhi or Chennai and 40% of the salary where the house is situated at any other place, for the relevant period.

The minimum of the above three amounts shall be exempted

from tax and the balance, shall be taxable and thus included in gross salary of the employee.

Salary for H.R.A. = Basic Pay + D.A. (if enter) + Commission + on turn over basis. +D.P.

Illustration- IV: (Where there is no change in any factor during the previous year)

A is entitled to a basic salary of Rs. 5,000 p.m. and dearness allowance of Rs. 1,000 per month, 40% of which forms part of retirement benefits. He is also entitled to HRA of Rs. 2,000 p.m. He actually pays Rs. 2,000 p.m. as rent for a house to Delhi. Compute the taxable HRA.

Solution

The minimum of the following three amounts shall be exempted u/s 10(13A):

	Rs.
(i) Actual HRA received (2,000 X 12)	24,000
(ii) Rent paid in excess of 10% of salary (24,000-6,480)	17,520
(iii) 50% of salary	32,400

Therefore, Rs. 17,520 shall be exempt and the balance Rs. 6,480 shall be included in gross salary.

Working Note : Salary for the above purpose is calculated as under :

(i) Salary	5000x12	60,000
(ii) Dearness Allowance 40% of 12,000		<u>4,800</u>
		<u>64,800</u>

1.4.11.2. Allowance which are exempt to the extent of actual amount received or the amount spent for the specified purpose for which these were received, whichever is less.

These allowances are covered u/s 10(14)

(a) *Travelling Allowance*

Any allowance granted to meet the cost of travel on tour or on transfer of duty.

Explanation

"Allowance granted to meet the cost of travel on transfer includes any sum paid in connection with transfer, packing and transportation of personal effects on such transfer.

(b) *Daily Allowance*

Any allowance, whether granted on tour or for the period of journey in connection with transfer, to meet the ordinary daily charges incurred by an employee on account of absence from his normal place of duty ;

(c) *Conveyance Allowance*

Any allowance granted to meet the expenditure incurred on conveyance in performance of duties of an office or employment of profit, provided that free

- conveyance is not provided by the employer;
- (d) *Helper Allowance*
Any allowance, by whatever name called, granted to meet the expenditure incurred on a helper where such helper is engaged for the performance of the duties of an office or employment of profit;
- (e) *Academic Allowance*
Any allowance, by whatever name called, granted for encouraging academic, research and training pursuits in education and research institutions.
- (f) *Uniform Allowance*
Any allowance, by whatever name called, granted to meet the expenditure incurred on the purchase or maintenance of uniform for wearing during the duties of an office or employment of profit.

1.4.11.3 Allowances which are exempt to the extent of amount received or the limit specified, whichever is less

- (a) *Children education allowance*
Exempt upto actual received per child or Rs. 100 p.m. per child upto a maximum of 2 children, whichever is less, provided children are studying in India.
- (b) *Hostel expenditure allowance*
Exempt upto actual received per child or Rs. 300 p.m. per child upto a maximum of two children, whichever is less, provided children are staying in hostel in India.
- (c) *Tribal area allowance*
Exempt upto actual amount received or Rs.200 per month, whichever is less.
- (d) *Composite hill compensatory allowance or high altitude allowance etc.*
Exemption varies from Rs.300 to Rs. 7000 per month.
- (e) *Border area, Remote area allowance, Disturbed area allowance, etc.*
Exemption varies from Rs. 200 p.m. to Rs. 1300 p.m.
- (f) *Compensatory field area allowance*
Exempt to extent of Rs. 2,600 p.m.
- (g) *Compensatory, modified field area allowance*
Exempt to extent of Rs. 1000 p.m.
- (h) *Counter insurgency allowance*
Exempt to the extent of Rs. 3900 p.m.
- (i) *Transport allowance*
Any transport allowance granted to an employee to meet his expenditure for the purpose of commuting between the place of his residence and the place of his duty, to the extent of Rs. 800 per month. In case physically handicapped Exemption is of Rs. 1600 p.m.

1.4.11.4 Allowances where exemption is allowed upto certain percentage of amount

- received
- (a) Allowance allowed to transport employees (Flight allowance/Running Allowance)
- If any fixed allowance is given by the employer to the employee who is working in any transport system, to meet his personal expenditure during his duty performed in the course of running of such transport from one place to another, the amount of exemption shall be 70% of such allowance or Rs. 10,000 p.m. whichever is less.

Exemption will be allowed to the transport employees only when they are not in receipt of daily allowance.

- (b) Treatment of Entertainment Allowance

This deduction is allowed only to a Government employee. Non-Government employees shall not be eligible for any deduction on account of any entertainment allowance received by them.

The Government employee is, then, entitled to deduction from gross salary under Section 16(ii) on account of such entertainment allowance to the extent of minimum of the following three limits :

- (i) Actual entertainment allowance received during the previous year.
- (ii) 1/5 or 20% of his Basic salary only.
- (iii) Rs. 5000 (notified limit)

Note: Salary includes Basic Pay only.

1.4.11.5 Allowances which are exempt in case of certain persons

- (1) Allowance to a citizen of India, who is a Government employee, rendering services outside India {Section 10(7)}
- (2) Allowance to High Court Judges under Section 22A(2) of the High Court Judges (Condition of Service) Act, 1954.
- (3) Sumptuary allowance given to High Court and the Supreme Court Judges.
- (4) Allowance received by an employee of UNO from his employer.

1.4.11.6. Allowances which are fully taxable

The following allowances are fully taxable.

- (1) Dearness Allowance (DA), Additional Dearness Allowance (ADA)
- (2) City Compensatory Allowance (CCA)
- (3) Medical Allowance : Fully taxable, irrespective of whether any amount has been spent on Medical treatment or not.
- (4) Lunch Allowance/Tiffin Allowance
- (5) Overtime Allowance
- (6) Servant Allowance

- (7) Warden Allowance
- (8) Non-practicing Allowance (NDA)
- (9) Family Allowance
- (10) Deputation allowance

1.4.12 PERQUISITES SEC. 17(2)

Under section 17(1) 'Salary' includes the value of any perquisite allowed or amenity provided by employer to employee. The word 'perquisite' has not been defined under the Income-Tax Act 1961. Perquisite simply means any casual emolument to an office. Oxford English Dictionary also defines perquisite as "any casual emolument, fee or profit attached to an office or position, in addition to salary or wages." Perquisites may be given in a variety of forms. If the perquisite does not accrue to the employee it will not be taxable.

I. Taxable Perquisites in case of all Employees (u/s 17(2)) :

For income tax purposes the perquisites have been divided into three categories I Taxable Perquisites in case of all Employees u/s 17(2).

- II. Tax Free Perquisites
- III. Perquisites Taxable in case of specified Employees only u/s 17(2) (iii)
- IV. Obligation of Employees met by Employer u/s 17(2) (iv).
 - (1) The value of the rent-free accommodation provided to the assessee by his employer ;
 - (2) The value of any concession in the matter of rent respecting any accommodation provided to the assessee by his employer.
 - (3) The value of any benefit or amenity granted or provided free of cost or at concessional rate in any of the following cases :
 - (a) by a company to an employee who is a director thereof;
 - (b) by a company to an employee being a person who has a substantial interest in the company ;
 - (c) by an employer (including a company to an employee to whom the provisions of Section (17(2) (iii) (a) and (b) do not apply and whose income under the head "Salaries", exclusive of all benefits or amenities not provided for by way of monetary payment, exceedsRs. 50,000 p.a.
 - (4) Any sum paid by the employer in respect of any obligation which, would have been payable by the employee (e.g. Employee's electricity bill paid by the employer);
 - (5) Any sum payable by the employer, whether directly through a fund, other than a recognizes provident fund or an approval superannuation fund to

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

II. Tax Free Perquisites :

Value of the following benefits is not added in salary income :

1. Free medical facilities or reimbursement of medical expenditure
 - (i) If treatment was taken from a hospital maintained by employer Fully exempted
 - (ii) If treatment is taken from a hospital maintained by Central, State Government, Local authority or a hospital is approved by Chief Commissioner of Income Tax Fully exempted
 - (iii) In case treatment is taken from a private or unrecognized hospital, the benefits are exempted up to Rs. 15,000 p.a. -----
 - (iv) In case employer under a scheme approved by the Central Government pay medical insurance Premium of employees Fully exempted
 - (v) In case any health insurance premium is paid by employer to General Insurance Corporation under notified scheme (Mediclaime u/s 80 D) to insure the health of its employees and members of their families. Fully exempted
 - (vi) In case treatment is taken outside India the expenses on stay and treatment of patient and stay of one attendant shall be exempted upto foreign exchange allowed by RBI ; and the expenses on travel of patient and attendant shall be fully exempted provided gross total income of employee does not exceed Rs. 2,00,000 p.a. Fully exempted
2. Free refreshment supplied by employer to its employees during office hours in office premises free meals. Fully exempted
3. Free meals given during working hours or non-Transferable vouchers given to employees shall be exempted up to Rs. 50 per meal. Excess, if any shall be taxable. Free meals given at remote area of offshore installation shall be fully exempted. -----
4. Free recreational facilities provided by employer to its employees Fully exempted
5. Provision of telephones including mobile phones given by the employer to the employee to facilitate the business of the employer. Fully exempted

- | | | |
|-----|---|----------------|
| 6. | Free education which is provided by employer from its own resources who is engaged in such business provided value of such benefit does not exceed Rs. 1000 p.m. per child. | ----- |
| 7. | Cost of refresher course attended by employee Employer meets expenditure of higher education or training whether in India or abroad. | Fully exempted |
| 8. | Any rent-free residential accommodation to Judges of High Court or Supreme Court. | Fully exempted |
| 9. | Goods sold by an employer to his employees at concessional rate. | Fully exempted |
| 10. | Free ration received by members of armed forces. | Fully exempted |
| 11. | Value of any gift up to Rs. 5000 in a year (Gifts in cash are fully taxable) | Fully exempted |
| 12. | Perquisites allowed by Government to its employees posted abroad. | Fully exempted |
| 13. | Rent free house given to an officer of Parliament, a Union Minister and leader of opposition in Parliament. | Fully exempted |
| 14. | Conveyance facilities to Judges of Supreme Court and High Court. | Fully exempted |
| 15. | Free Conveyance provided by employer to employees for going to or coming from place of employment | Fully exempted |
- II. Perks Taxable for all employees
- I. Rent Free House
- A. Value of Unfurnished House
Before calculating the value of rent free house, following information is collected :
- Nature of employment* : Government, Semi Government or any other .
- B. Place where rent free house is provided
- (1) In cities having population in more than 25 lakhs as per census of 2001 ; or
- (2) In cities having population more than 10 lakh but upto 25 lakhs.
- (3) Any other town
- C. Meaning of accommodation
It shall include a house, farm-house, flat, hotel accommodation, guest house, a caravan, mobile home, ship etc.

D. Nature of accommodation

Owned by Employer/Hired or leased by employer.

E. Meaning of Salary for rent free house.

It shall include Pay + D.A. (which Enters) + Fee + Commission of all types + Profit Bonus + All Fully Taxable Allowances Except D.A. which does not enter + Taxable Portion of other allowances + Taxable Entertainment Allowance. + special pay + Interim relief + Leave Encashment of current year.

Rules regarding calculation of value of rent free house

1. For unfurnished accommodation

A. Owned by employer

(a) Government Employees

The value of house will be rent fixed (Licence fee) by the Government for such house. It can be, rent charged by government from another employee of same status for similar type of house.

(b) Other employees

Value of house is calculated in following manner :

- (i) In cities whose population : 15% of Salary is taxable. is more than 25 lakhs
- (ii) In cities whose population is : 10% of Salary is taxable. up to 25 lakhs but exceeding 10 lakhs
- (iii) Any other : 7.5% of salary is taxable
- (iii) Hotel accommodation (for more : 24% of Salary or actual than 15 days on transfer bill whichever is less is from one place to another) taxable.

This benefit shall be taxable for full period of stay if stay exceeds 15 days.

- (B) Hired by employer 15% of Salary or Actual rent paid whichever is less is taxable in all cities.

2. For Furnished Accommodation

In case of all types of employees calculate value of unfurnished house.

If furniture is owned by employer add 10% of cost of furniture.

If furniture is hired actual hire charges paid by employer are added.

Illustration-V

Mr. A.B. Sen has furnished following particulars :

- (i) Salary @ Rs. 10,000 p.m.
- (ii) Dearness Allowance @ Rs. 500 p.m. (It enters into pay for retirement

benefits).

(iii) Entertainment Allowance @ Rs. 600 p.m.

(iv) Bonus Rs. 8,400

(v) Cost of furnishing Rs. 20,000

Calculate the value of rent-free house if :

Case-I Mr. A.B. Sen is Government employee and rent of house fixed by Govt. is Rs. 300 p.m.

Case-II Mr. A.B. Sen is working in a semi-Government, undertaking at Chennai and Fair Rental Value of the house is Rs. 1000 p.m.

Case-III Mr. A.B. Sen is working in private sector at Chandigarh (population below 25,00,000) and Fair Rental Value of the house hired by employer is Rs. 3000 p.m. He is also provided with hired refrigerator whose hire charges or Rs. 600 p.m. are paid by employer.

Case-IV Calculate concessional Rent of the house

Solution

Calculation of Value of rent free house.

Rs.

Case-I Government Employee

The value of perquisite of rent free house is the rent fixed by Government for such house which 20,000 in the present case is (12x300=3600) 3,600

Add : 10% of cost of furnishing $20000 \times \frac{10}{100} = 2000$ 2,000

Value of Rent-Free Furnished House 5,600

Case-II Semi-Government Employee

The value of rent free house at Chennai is 10% of Salary (1,20,000 + 6,000 + 8,400 + 7,200 = 1,41,600) 14,160

Add : 10% of cost of furnishing (10% of Rs. 20,000) 2,000

Value of Rent-Free Furnished House 16,160

Case-III Any other employee (City having population below 4,00,000)

Value of rent free house hired by employer :

Salary of employer = 1,20,000 + 6,000 + 8,400 + 7,200 = 1,41,600

10% of employee's salary = 14,160

Rent paid by employer = 36,000

Whichever is less shall be the value of rent free house i.e. Rs. 14,160

Add : 10% of cost of furnishing 2,000

Add : Actual Hire charges of refrigerator 7,200

Value of Rent-Free Furnished House

23,360

Case-IV Concessional Rent House

Calculate value of rent free house as per above calculation and deduct rent paid by employee.

III Perquisites Taxable in Case of Specified Employees only u/s 17(2) (iii)

Who is specified employee :

- (a) Who is director of the company; or
- (b) Who has substantial interest in the affairs of the company i.e. he holds at least 20% of the voting power (equity shares) in the company; or
- (c) His monetary salary is more than Rs. 50,000 p.a.

Salary for this purpose means all what he gets in cash from one employer or more than one employer if he works for more than one employer simultaneously whether full time or part time, and is taxable under the head salary. The total of these items is to be treated as gross salary out of which deduction u/s 16 (ii) and (iii) are to be allowed and balance salary should be more than Rs. 50,000. p.a.

1. Value of perquisite of use of employer's moveable asset :

If employee is using any moveable asset owned by the employer except computers, cars and laptops, the value of this perk is taxable in the hands of employee shall be treated as 10% of the cost of the asset to the employer by reducing any amount paid by employee. It is taxable in both specified and non-specified type of employee.

The value of benefit shall be reduced as per the number of days, if asset is given to the employee for less than one year.

2. Value of perquisite of sale of moveable assets to the employee at nominal price: In case the employer sells certain moveable assets to an employee, the value of perk is calculated by computing W.D.V. of the asset first by deducting depreciation for each year of 12 months for which asset was used by the employer. Out of the W.D.V. deduct the amount, if any, paid by the employee and resultant figure shall be treated as the value of perks to be taxed.

3. Free Education

Payment of fees of school, college paid by employer directly or paid by the employee is reimbursed by the employer is a taxable perquisite in all type of employees.

Free Educational facilities in employer's school, college or institutions

If such facilities are given to the children of employee or any other member of his household, the valuation of this perk is to be calculated as under :

1. Free educational facilities to employee's own children : (a) where the cost of education in that school or college or in a similar type of institution or near the locality does not exceed Rs. 1,000 p.m., the taxable value of perk shall be taken nil.

(b) If cost exceeds Rs. 1,000 p.m., the taxable value of perk shall be the cost of the employer minus Rs. 1,000 minus any amount received from the employee.

2. If employer provides free education to the member of the household of employee, cost to the employer minus any amount paid by employee or recovered from employee is the taxable value of the perk.

4. Free Gas, Light, Water

In case connection is on the name of employer and bill is also paid by employer, actual cost of such benefit is taxable. It shall be reduced by any amount paid by the employee.

5. Free servants

(a) In case an employee employs a servant or servants but their salary is paid by employer, fully salary is taxable for all employees u/s 17(2) (iv)

(b) In case employer provides services of sweeper, and watchman, full salary of these employees is taxable and it shall be reduced by any amount paid by employee. It is taxable for full month even if given for part of a month.

(c) In case gardener is provided along with rent free house owned by employer, the salary of gardener is added in FRV and is not taxable separately. But if house is owned by employee or is hired by employee full salary of gardener is taxable. It is taxable for full month even if given for part of the month.

(d) In case employer provides any other servant, his full salary is taxable. It is taxable for full month even if given for part of month.

6. Perquisite of car, transport facility, food and beverages, gifts club or credit card facility etc.

The perquisite of car, conveyance facility, club facility etc. is not taxable in employee's hands and the employer will pay Fringe Benefit tax on these facilities.

In case employer is not liable to pay tax under Fringe Benefit Tax, then, the employee would be chargeable to tax under the Income Tax Act for all these perquisites.

Obligation of employee met by employer U/s 17 (2) (iv)

In case any of the following payments are made by employer these are fully taxable. These are :

(a) Club bills issued on the name of employee but paid by employer actual expenses met by employer are taxable.

(b) Gas and electricity bills issued on the name of employee but paid by employer. Actual expenses met by employer are taxable.

- (c) Education of children bills issued on the name of the employee but paid by employer. Actual expenses met by employer are taxable. Reimbursement of tuition fee of children is also fully taxable.
- (d) Income- Tax, Professional tax of the employee paid by employer. Actual expenses met by employer are taxable.
- (e) Salary of domestic servants employed by employee but paid by employer. Actual amount paid by employer is taxable.

1.4.13 DEDUCTIONS FROM GROSS SALARY (SECTION 16)

To calculate the taxable income under the head 'Salaries' following two deduction are allowed u/s 16 :

1.4.13.1 Standard deduction (Section-16 (i)):

The Standard deduction of Rs. 40,000 is allowed to salary employees and Pensioner w.e.f financial year 2018-19 (Rs. 50,000 w.e.f. 2019-20)

1.4.13.2 Entertainment Allowance (Section 16(ii))

A deduction is allowed to those persons who receive this allowance. Till assessment year 2001-02. This deduction was admissible both to Government as well as private sector employees. But with effect from assessment year 2002-03. This deduction is admissible to Government employees (Central or State) for an amount equal to lease of following :

- (a) Statutory Limit Rs. 5,000;
- (b) 1/5 of basic salary only ; or
- (c) Actual Entertainment Allowance

1.4.13.3 Tax on Employment Section 16 (iii) }

In case any sum is paid by the assessee on account of tax on employment with the meaning of clause (2) article 276 of the constitution livable by or under any law, such amount shall be fully allowed as deduction. The example of this tax is professional tax levied by any State Government.

Development Tax: From Financial year 2018-19, every employer or person doing business or profession in punjab is liable to pay development tax if after deduction his income is above maximum exemption limit i.e. Rs. 2,50,000. In case of employee, if employer deduct the development tax and paid to the government them employee can claim deduction of 'tax on employment' (or professional tax) u/s 16 (iii) for the amount so paid by employer. On the other hand businessman or professionals are liable to register themselves and pay development tax to the government.

The Senior citizen and person exclusively engaged in agricultural activities are exempted from this tax.

The amount of tax is Rs. 200/- per month i.e. $200 \times 12 = 2400$ /- for a year.

SELF CHECK EXERCISE

Ques.1. What are main types of Allowance?

Ques.2. What are main types of Perquisites?

Ques.3. What are main types of Provident Funds?

1.4.14 SUMMARY

So far in this chapter we have discussed the following items in detail under the head salaries :

1. Salary (Definition)
2. Gratuity
3. Pension
4. Leave Encashment
5. Allowances
6. Perquisites
7. Provident Funds
8. Deductions from Salary

1.4.15 EXERCISE

(A) Short Questions :

Q.1 What is Salary?

Q.2 Explain the various features of salary tax.

Q.3 Write short notes on the following :

1. Gratuity
2. Leave Encashment
3. Pension
4. Leave Travel Concession

(B) Long Questions :

Q.1 Explain various types of provident funds in detail.

Q.2 Define the term 'allowance? Explain in detail the following types of Allowances

- (i) Exempted Allowance
- (ii) Partially Taxable Allowance
- (iii) Fully Taxable Allowance

Q.3 What is 'Perquisites? Explain the perquisites taxable in specified case only.

1.4.16 ANSWERS TO SELF CHECK QUESTIONS

ANS.1 Main types of allowance are:

- a) Exempted Allowance
- b) Fully Taxable Allowance
- c) Partially Taxable Allowance

ANS.2 Main types of Perquisites are:

- a) Exempted Perquisites

- b) Taxable in all Cases
- c) Taxable in specified cases

ANS.3 Main types of Provident Funds are:

- a) Statutory Provident Funds
- b) Recognized Provident Funds
- c) Unrecognized Provident Funds
- d) Public Provident Funds

1.4.17 SUGGESTED READINGS

- | | |
|---|---------------------------|
| 1. Income Tax Laws and Practice | V.P. Gaur and D.B. Narang |
| 2. Income Tax Laws | H.C. Mehrotra |
| 3. Direct Tax Laws | V.K. Singhania |
| 4. The Income Tax law
(A.Y. 2023-2024) | Shailinder Sekhon |

INCOME FROM HOUSE PROPERTY

Structure of the Lesson :

- 1.5.0** Objective
- 1.5.1** Introduction
- 1.5.2** Basis of Charge
 - 1.5.2.1 Building or Land Appurtenant
 - 1.5.2.2 Annual Value
 - 1.5.2.3 Assessee should be the owner of the Property
 - 1.5.2.4 Property should not be used for the assessee's business or profession
 - 1.5.2.5 Rental Income of a Dealer in House Property
 - 1.5.2.6 Income from House Property Incidental to Business
 - 1.5.2.7 Composite Rent
- 1.5.3** Determination of Annual Value
 - 1.5.3.1 Annual Rental Value of Let-out House Property
 - 1.5.3.2 Annual Rental Value of Self-Occupied House Property
- 1.5.4** Exempted House Property Incomes
- 1.5.5** Treatment of Unrealised Rent Recovered
- 1.5.6** Loss from House Property
- 1.5.7** Self-Check Exercise
- 1.5.8** Summary
- 1.5.9** Glossary
- 1.5.10** Answers to Self-Check Questions
- 1.5.11** Exercise
- 1.5.12** Suggested Readings

1.5.0 OBJECTIVE

The main objective of this lesson is to introduce the students with the latest provisions of the income tax law under the head of 'Income from House Property'.

1.5.1 INTRODUCTION

The income from houses, buildings, bungalows, godowns etc. is to be computed and assessed to tax under the head Income from house property.

According to Section 22 of the Income Tax Act, the annual value of property consisting of any building or land appurtenant thereto of which the assessee is the owner, shall be chargeable to tax under the head 'Income from house property'. But any portion of

such property which is occupied for the purpose of any business or profession carried on by him, the profit of which is chargeable to income tax, shall not be chargeable to income tax under the head Income from house property.

1.5.2 BASIS OF CHARGE

On the basis of the provisions of section 22, the following important points emerge for careful consideration while taking income under this head :

1.5.2.1. Building or Land Appurtenant Thereto :

The scope of this head of income is limited to the income from building or lands appurtenant (attached or situated in vicinity of building), to building only. Building includes residential house, bungalow, docks, warehouses, any block of bricks or stone work covered by roof etc. land which is not appurtenant to any building does not come under the scope of this section.

However, the term 'building' does not include vacant plots. Accordingly, any rent received from a vacant plot of land is assessable under the head "Income from other sources."

1.5.2.2. Annual Value [Section. 23 (1)] :

For the purpose of Section 22, 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 and local authority in respect of the property shall be deducted in determining the annual value of the property of the previous year in which such taxes are actually paid by him.

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, subject to such rules as may be made in this behalf, the amount of rent which the owner cannot realise. Section 23 (1) of Income-tax Act has defined the word 'annual value' as, "the sum for which the property might reasonably be expected to let from year to year." The annual value is the value which any house can fetch from the market under the prevailing circumstances such as local conditions, the demand for house, municipal valuation, type and standard of construction, rent for similar type of house in the similar type of

locality, etc. A property can be let out at a rent which is lower than its reasonable rent but its annual value will be its reasonable rent.

The Finance Act 2001 has changed the definition of the Annual value as under:

- (a) The amount of rent at which the property might reasonably be expected to let from year to year ; or
- (b) If the property or any part of the property is let and the actual rent received or receivable by the owner in respect of such property is more than the reasonable rent as per (a) above the annual value shall be amount so received or receivable ; or
- (c) If 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 reasonable rent as per (a) above, the annual value shall be the amount so received or receivable.

From the above definition it becomes clear that the annual value is based on different types of rental values. These are explained below:

Different Types of Rental Values

1. **Actual Rent:** It is the rent actually received by the owner of the house property from the tenant. In case tenant pays composite rent i.e. rent of building, plant and machinery, furniture etc. and rent is separable, actual rent is reduced by the amount of rent of plant and machinery, furniture etc. Balance is actual rent of house property. Any amount of local taxes paid by tenant, cost of repairs borne by tenant or any interest on advance deposit are not to be added.

As per explanation attached to Section 23 (1) for the purposes of calculating Annual Value the actual rent received or receivable shall not include any amount of unrealised rent if it satisfies certain conditions.

2. **Real Rental Value (RRV) :** In case cost of common facilities such as lift and pump maintenance, salary of common gardener and watchman, lighting of common stairs and corridors and water and electricity bills (if included in rent) are borne by the owner and rent includes the cost of these items. Such cost is reduced out of actual rent received and balance is called Real Rental Value. In case the cost of facilities is charged separately by owner i.e. over and above the rent, it is treated as a separate source of income. The expenses incurred on such facilities are deducted out of amount so collected and balance is taxable under the head, " Income from other sources".

3. **Municipal Rental Value (MRV) :** For the purposes of levying local taxes the local authority i.e. Municipal Corporation/Committee etc. conducts a periodical survey of the house properties in their local limits. On the basis of such survey the rental values are fixed which serves as the basis for levying tax. The rental value so fixed is called Municipal Rental Value (M.R.V.)

4. Fair Rental Value (FRV) : It is rental value a house property can fetch, is based on the rent prevailing for similar type of accommodation is same as similar type of locality. It is based on the principle that rent prevailing in same locality for similar sized property is almost the same. Such rental value is called Fair Rental Value [F.R.V.).

5. Standard Rent : The rent fixed under Rent Control Act, where so ever applicable is called Standard Rent.

6. Expected Rental Value (ERV) : MRV or FRV whichever is higher is selected and then such higher figure is compared with Standard Rent and whichever is less is selected as ERV.

The basic principle to be kept in view is that (i) Expected Rental Value (ERV) cannot exceed the Standard Rent. As such MRV and FRV are compared and if the higher of these two figures is less than Standard Rent, such higher figure in ERV and in case higher figure is more than Standard Rent then such Standard Rent shall be selected as ERV.

(ii) Deduct the cost of facilities or amenities provided by the owner to tenant out of rent received and balance is taken as actual rent.

1.5.2.3 Assessee should be the owner of the Property:

It is the owner of house property who is liable to tax on income under this head. It is immaterial whether the owner is in possession of the house property or living himself in the same. The property may be let out to a third party either for residential purposes or for business purposes. The basic condition to be satisfied is that the person to be taxed under this head is a legal owner of the property.

Income from sub-letting will be chargeable to tax under the head 'Income from other sources' and not under the head 'Income from House Property.'

According to this section, the following persons are considered as deemed owners of house property for tax liability under this head.

(i) Transfer to Spouse :-

If a husband transfers a house property to his wife either for no consideration or for inadequate consideration the husband is deemed as the owner, although his wife is the legal owner. In such case the same rules will apply where the wife transfer a house property to her husband.

(ii) Holder to Impartible Estate :-

The holder of an impartible estate is deemed to the owner of all the properties comprised in the estate.

(iii) A member of co-operative society, company or 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 the owner of the building or part thereof; and

- (iv) A person who is allowed to take, to retain possession of any building in part performance of a contract of the nature referred in Section 53-A of the Transfer of Property Act, 1882, shall be deemed to be the owner of that building or part thereof.

1.5.2.4 Property should not be used for the purpose of assessee's business or profession :

Where the assessee is carrying on business or profession in his own house, building or in a portion of it and the income of such business or profession is taxable under the head profit and gains of business or profession the annual value in respect of property or portion of it is not taxable under the head house property.

1.5.2.5 Rental Income of a dealer in House Property :

If a person is engaged in the business of purchasing house properties with a view of letting them on high rents and disposing off these properties will be taxed under the head 'Income from business or profession'. Thus, any rent from house property whether received by a dealer or by a landlord is taxable under the head 'Income from house property'.

1.5.2.6 Income from House Property Incidental to Business :

It should be noted here that if an employer builds quarters for residential use by his employees and the letting out of these quarters is considered as incidental to his business. The income from such property is not taxable under this head because the property in this case is considered to be used by the owner for his own business. It shall, therefore, be taxed under the head 'Income from Business or profession'.

1.5.2.7 Composite Rent:

Rent received from letting out of building alongwith the furniture and other amenities etc. is called composite rent. It shall be split out in two parts i.e. (i) rent from building (ii) rent from furniture, other amenities. Rent received from second part is liable under the head 'Income from other source'. Where such rent cannot be split up, the whole rent received shall be taxable under the head Income from Other Sources and not under house property head.

1.5.3 DETERMINATION OF ANNUAL VALUE

The annual value of house property can be determined for different types of situations. These situations are :

Annual Value of Let-out House Property

- 1 . House property is let-out for full year and there is no vacancy or unrealised rent ;
2. House property is let-out and there is vacancy
 - (a) *If rent actually received or receivable is more than ERV.*

(b) *If rent actually received or receivable is less than ERV.*

3. House property is let out and there is unrealised rent :
 - (a) If rent actually received (after deducting unrealised rent as per conditions given) is less than ERV.
 - (b) If rent actually received or receivable (after deducting unrealised rent as per conditions given) is less than ERV.

Annual Value of Self-Occupied House Property

1. Only one house under own occupation.
2. More than one house under own occupation.
3. House property is partly let-out and party under own occupation.
4. House property is used for own business or profession.

1.5.3.1 Annual Rental Value for let out House Property :

1. House property is let-out for full year and there is no vacancy or unrealised rent :

Step 1. Compare MRV with FRV, whichever is higher is compared with Standard Rent and whichever is less is ERV.

Step II. If actual rent received or receivable is more than ERV, such rent received or receivable is Annual Rental Value.

Step III. If actual rent received or receivable is less than ERV (Expected Rental Value) such ERV is Annual Rental Value and clause (b) is not applicable.

2. House property is let-out and there is vacancy :

A. If house property was vacant for full year the ARV is taken as NIL.

B. If house property was vacant for part of the year then:

(i) *If rent actually received or receivable is more than ERV.*

Step I. Compare MRV with FRV, whichever is higher is compared with Standard Rent and whichever is less is ERV.

Step II. If rent actually received or receivable is more than ERV inspite of vacancy then such rent received or receivable is Annual Rental Value (ARV)

(ii) If rent actually received or receivable is less than ERV due to such vacancy, then such rent is ARV [clause (c) of section 23 (1)].

3. House property is let out and there is unrealised rent

(i) If rent actually received or receivable (after deducting unrealised rent as per conditions given below), is more than ERV.

Step I. Compare MRV with FRV and whichever is higher is compared with Standard Rent and whichever is less is ERV.

Step II. If rent actually received or receivable (after deducted unrealised rent as per conditions given below) is more than ERV (Expected Rental Value) such rent received or receivable is Annual Rental Value (ARV).

4. House property is let out, there are both vacancy and unrealised rent:
 Step I. Compare MRV with FRV, whichever is higher is compared with Standard Rent and whichever is less is ERV,
 Step II. If rent actually received or receivable for full year (after deducting unrealised rent as per conditions given) is more than ERV, such rent received or receivable is ARV.
 Step III. Such ARV is reduced by an amount of actual rent in proportion of vacancy.
 Step IV. If rent actually received or receivable (after deducting unrealised rent and vacancy) is less than ERV, such ERV is ARV.
5. House property is completed or acquired during the previous year:
 The rental value is selected for full year and then it is reduced as per the number of months for which this property remained completed and owned by the assessee during the previous year.

Important point : (i) If following conditions are fulfilled, the amount of unrealised rent shall be deducted out of actual rent received.

- (a) that the tenancy is bonafide.
- (b) that the tenant has vacated the house or steps have been taken to get the house vacated.
- (c) the tenant is not occupying any other house owned by the assessee ; and
- (d) that all efforts to recover the rent have failed or the assessing officer is satisfied that there is no way to recover the rent.
- (e) Unrealised rent of earlier years is not deductible.
- (ii) If rent actually received or receivable (after deducting unrealised rent as per conditions given) is less than ERV

Step I. Compare MRV with ERV, whichever is higher is compared with Standard Rent and whichever is less is ERV.

Step II. If rent actually received or receivable (after deducting unrealised rent as per conditions given) is less than ERV, then ERV is Annual Rental Value.

Deduction in respect of Municipal Taxes

Let-Out House Property

- (i) Determine annual rental value as per above.
- (ii) Deduct amount of Municipal/local taxes actually paid by the owner during the previous year. Local taxes shall include service charges such as Sanitation Cess, Sewerage Tax or Conservancy Cess etc. levied by local authority.

Note: (i) If any part of municipal or local taxes is met or paid by the tenant, the same shall not be allowed to be deducted while calculating net annual

value.

Note: (ii) It may be noted that the municipal or local taxes are allowed as deduction only in that previous year in which these taxes are actually paid, so on due basis, it cannot be deducted.

(iii) Balance amount is called Net Annual Value (NAV)

1.5.3.2 Annual Rental Value in case of Self-Occupied House Property :

1. Only one House under own Occupation :

The net annual value of one self-occupied house shall be taken as nil if following conditions are fulfilled :

- (i) House is used by an individual owner of HUF for the residential use of the individual or the members of the HUF.
- (ii) House or any part of the house is not actually let out during the previous year or part of that previous year.
- (iii) No other benefit is derived from such a house [Section 23(2)].

2. More than one house under own occupation:

Annual value of one house is taken as nil. And other house/houses are deemed to be let out.

3. House property is partly let-out and partly is under own occupation:

Whole property is treated as let-out house property and no benefit of self - occupancy.

4. House property is used for own business or Profession:

It is not treated under the head house property and NAV is taken as nil. No, rent can be debited under the head Profits and Gains of business or profession.

1.5.4 EXEMPTED HOUSE PROPERTY INCOMES

Under Section 10 of the Income Tax Act 1961 following incomes from house property are exempted from Tax. These incomes are not to be included in the total income of assessee.

These income are:

- 1. Income from property in the vicinity of agricultural land (Sec. 2(l) (c))
- 2. Incomes from house property belong to
 - (a) A local authority
 - (b) An authority constituted for the purpose of planning, development or improvement of cities town and villages Sec. 10 (20A).
 - (c) Scientific research association Sec. 10(2 1).
 - (d) University or other educational institution Sec. 10(22)
 - (e) Hospital or other medical institution. (22A)
 - (f) Games or sports association Sec. 10(23)
 - (g) A registered trade union 10 (42)

3. Income derived from letting of godowns or warehouse for storage or facilitating the marketing of commodities.
4. Income from property held for charitable purpose Sec. 11(1).
5. Income from house property in the hands of a political party (Sec. 13A).
6. Income from property used by the assessee for the purpose of his own business under sec. 22.
7. Income from self-occupied property which could not be used during the previous year.

Deductions allowed u/s 24 (1)

Out of the net annual value computed in accordance with the earlier mentioned provisions following deductions are allowed. These deductions have been grouped into two parts :

(A) For Self-Occupied House

- (a) In case property is acquired or constructed with borrowed capital before 1 April 1999 then deduction of interest on loan taken is allowed. Actual interest paid or payable during the previous year and 1/5th of preconstruction interest (to be explained later under let out house property) or Rs. 30,000 p.a. whichever is less is allowed as deduction. Loss of self-occupied house shall be set off from income of any other head and unadjusted portion shall be allowed to be carried forward.
- (b) Where the property is acquired or constructed with capital borrowed on or after the 1st day of April, 1999 then deduction of interest on loan shall be allowed up to actual interest paid or payable during the previous year plus 1/5th of pre-construction interest (to be explained later under let out house property) or Rs. 2,00,000 p.a. whichever is less.
- (c) In case loan is taken to repair or renovate or reconstruct the property before or after 1.4.1999 interest on such loan taken for repair, or renovation of the house shall be allowed up to actual interest paid or payable during the previous year plus 1/5th pre-construction interest of Rs. 30,000 p.a. whichever is less.
- (d) Owner of more than one house- In case an assessee is self-occupied more than one house then he is liable to pay tax on notional rent. But as per Finance Act 2019, an exemption is given on such levy of income tax on notional rent on a second self-occupied houses.

B. In case of all other house properties

1. Standard Deduction :

30% of net annual value is allowed as deduction every year irrespective of any expenditure.

2. Interest on loan

- (a) Loan must be taken to repair, construct, renovate or purchase the house.
- (b) Interest on mortgage is not allowed unless purpose of loan is connected with house.
- (c) Interest for the period (no limit of time) prior to the completion of house is called Pre-construction Interest (PCI). It is allowed to be deducted over a period of 5 years i.e. 1/5th every year. No deduction after 5 years.
- (d) Interest on delayed payment of interest is not allowed.

Maximum limit of interest on loan: Same amount of interest is allowed to deduct as deduction which is allowed in case of self-occupied house.

1.5.5 TREATMENT OF UNREALISED RENT RECOVERED

Unrealised rent received subsequently to be charged to income tax [Section 25AA]

Where the assessee cannot realise rent from a property let to a tenant and subsequently the assessee has realised any amount, in respect of such rent, the amount so realised shall be deemed to be income chargeable under the head 'Income from house property' and accordingly charged to income-tax as the income of previous year in which such rent is realised whether or not the assessee is the owner of that property in that previous year.

1.5.6 LOSS FROM HOUSE PROPERTY

- (i) Loss from House property can be first set off from any other House Property Income and, balance if any, can be set off from any other head.
- (ii) The balance of unabsorbed loss from house property can be carried forward for 8 Assessment years to be set off against income from house property only.

1.5.7 SELF-CHECK EXERCISE

Ques.1: Compute the income from house Property from information given below for the assessment year 2023-24 :

	Rs
Municipal Rental value	18,000
Rent received during the year	24,000
Municipal Taxes (50% paid by tenant) for the whole year	1,800
Expenses incurred:	
(a) by tenant on repairs	3,000
(b) by tenant on collection charges	1,000

Ques.2 X owns a property. It is given on rent (rent being Rs. 11,000 per month) to a bank. Municipal value of the property is Rs. 1,30,000, fair rent is Rs. 1,40,000 and standard rent is Rs. 1,34,000. Municipal tax paid by X is as follows:

Rs. 26,000 on March 3, 2022.

Rs. 30,000 on May 10, 2022. On May 1, 2022 rent is increased from Rs. 11,000 per month to Rs. 14,000 per month with retrospective effect from April 1, 2021. Arrears of rent 2021-22 are paid on May 1, 2022. Find out the income chargeable to tax for the A.Ys 2022-23 and 2023-24.

1.5.8 SUMMARY

Section 22 of Income Tax Act, 1961 is provided to compute and assess the income from house property, that is, income from houses, buildings, bungalows, godowns etc. Section-10 also explains various incomes from house property which are not taxable under this head. To compute the annual value of house property computation of valuation is described in two situation (a) Annual value of let-out house property, and (b) Annual value of self-occupied house property as discussed in this lesson. Any loss under this head which remains unadjusted can be set off and carry forward for eight succeeding previous years.

1.5.9 GLOSSARY

1. MRV : Municipal Rental Value
2. FRV : Fair Rental Value
3. ERV : Expected Rental Value
4. ARV : Annual Rental Value
5. RRV : Real Rental Value

1.5.10 ANSWERS TO SELF-CHECK QUESTIONS

Ans.1

Computation of Income from house property : Let-out For the A.Y. 2023-24

	Rs.	Rs.
Actual Rent Received	24,000	
Or		
Municipal Rental value	18,000	
Whichever is higher in ARV		24,000
Less Municipal Taxes paid by owner (50% of 1,800)		<u>900</u>
Net Annual Value		23,100
<i>Deduction u/s 24:</i>		
Standard Deduction 30% of NAV		<u>6,930</u>
Income from house property		16,170
By Owner	3000	

By tenant	3000
Collection charges	1000

t. Note : No deduction is allowed for repair or collection charges as paid by the tenant.

Ans.2

Gross Annual Value:	Assessment Years	
	2022-23	2023-24
	Rs.	Rs.
Step I Municipal value or fair rent whichever is higher, subject to maximum of standard rent.	1,34,000	1,34,000
Step II If rent collected is higher than the amount of Step-I, then rent collected will be taken <u>N.A.</u>		<u>1,68,000</u>
Gross Annual Value	1,34,000	1,68,000
Less: Municipal Taxes	<u>26,000</u>	<u>30,000</u>
Net Annual Value	1,08,000	1,38,000
Less : Standard deduction U/S 24 (i.e. 30% of net Annual Value)	<u>32,400</u>	<u>41,400</u>
Income from Property	<u>75,600</u>	<u>96,600</u>

Arrears of rent of the previous year 2020-21 paid on May 1, 2022 Rs.

Gross Annual Value of previous year 2021-22 if rent is

Rs. 14,000 per month	1,68,000
Less: Gross Annual Value considered earlier	<u>1,34,000</u>
Arrears of rent	34,000
Less : 30% of the Rs. 34,000	<u>10,200</u>
Amount Taxable	<u>23,800</u>

Assessment year 2022-23

Income from House Property is = Rs. 75,600

Assessment Year 2023-24

Income from House Property is = Rs. 1,20,400 (96,600+23,800)

Rs. 96,600 income for the A.Y. 2023-24

Rs. 23,800 Arrears of House Property income of A.Y. 2022-23 but received in 2023-24.

1.5.11 EXERCISE

(A) Short Questions :

Ques.1. Write a short notes on:

- (1) Annual Rent Value
- (2) Fair Rental Value
- (3) Expected Rental Value
- (4) Standard Rent

Ques.2. What do you mean by Composite Rent?

Ques. 3. Determine the Annual Rental Value of let-out House Property.

(B) Long Questions :

Ques. 1. Write a detailed note on the deductions given under the head 'Income from House Property' from Gross Annual Rental Value under Section 24.

SELF CHECK EXERCISE

Q.1 An Employer (Mr. R) announced a bonus of 1,00,000 for his employees but due to shortage of funds he could pay Rs. 40,000 only upto 31-3-2023; and Rs. 30,000 on 30-7-2023 and balance on 21-11-2023. For this financial year due date of filing of his return is 31-7-2023. Discuss the status of these items for reducing the tax liability of an employer.

Ans: As per Income tax provisions, amount of bonus paid to employees can be debited by the employers only if paid upto 31st March or before filing of return of income. Therefore in the present case of Rs. 40,000 (paid on 31-3-23) and Rs. 30,000 (paid on 30-7-22) can be debited during the A.Y. 2023-24. However the balance amount of Rs. 30,000 (paid on 21-11-23) is allowed to debit from the income fall in the previous year 2023-24, so deductible from the Return filing in the A.Y. 2024-25.

Q.2 To what extent following expenditure are allowed to deduct from the business income of Mr. Arvind:-

- (a) Entertainment expenditure incurred during the P.Y. ending 31-3-23 is Rs. 50,000.
- (b) Ten items were presented for advertisement during the P.Y. 2022-23 each costing Rs. 2000.
- (c) Income tax deposited in advance for Rs. 10,000 during the P.Y. Rs. 2022-23.

Ans: Mr. Arvind is allowed to deduct business expenses as mentioned below:

- (a) Entertainment expenditure is fully allowed to debit as per sector 37
- (b) Advertisement expenses on distribution of gift items are fully allowed.
- (c) Advance payment of income tax is not allowed to be debited as on expenditure u/s 40 (a)

1.5.12 SUGGESTED READINGS

- (1) The Income Tax Law & Practice, By : Shailinder Sekhon
- (2) Direct Tax Law & Practice, By : Dr. Vinod K. Sighania
- (3) Income Tax Law & Accounts, By : Dr. H. C. Mehrotra.
- (4) Income Tax Law & Practice, By : Mahesh Chandra, S.P.Goyal

Note : Assessment Year is 2023-24.

Previous Year is 2022-23

AGRICULTURE INCOME**Structure of the Lesson :**

- 1.6.0 Objective
- 1.6.1 Introduction and Meaning of agriculture income
- 1.6.2 Income derived from agricultural land by agricultural operations
- 1.6.3 Income derived from agriculture
- 1.6.4 Income derived from marketing process
- 1.6.5 Income from sale of agricultural produce
- 1.6.6 Income from farm building
- 1.6.7 Tests of determine agricultural income
- 1.6.8 Instances of agricultural income
- 1.6.9 Instances of non-agricultural income
- 1.6.10 Partially Integrated Taxation of Non-Agricultural Income with Agricultural Income
 - 1.6.10.1 Computation of tax about the cases covered by the scheme
 - 1.6.10.2 Illustration I and II
- 1.6.11 Computation of Net Agriculture Income
 - Self Check Exercise
- 1.6.12 Summary
- 1.6.13 Glossary
- 1.6.14 Answer to Self- Check Question
- 1.6.15 Exercise
- 1.6.16 Suggested Readings

1.6.0 OBJECTIVE

The main objective of this lesson is to acquaint the students with the latest provisions of tax treatment of agriculture income.

1.6.1 INTRODUCTION AND MEANING OF AGRICULTURE INCOME

Agricultural income is exempted from income tax u/s 10 (1). The Parliament has no power under the Constitution of India to levy tax on agricultural income because entry 82 of the Union List empowers the Parliament to make law for levying tax on income other than agricultural income. However, it is to be noted that with effect from the assessment year 1974-75 the agricultural income has been taken into account in determining the rate of tax applicable to the non-agricultural income

of the assesses. Since agricultural income is exempted from income-tax the person may be interested in associating their incomes with agriculture. The expression "agricultural income" means :

- a. any rent or revenue derived from land which is situated in India and is used for agricultural purposes [Sec. 2 (1A) (b)] and
- b. income attributable to a farm house subject to the conditions that the building is situated on or in the immediate vicinity of the land and is used as a dwelling house, store house or other out-building land is assessed to land revenue or a local rate or, alternatively, the building is situated on or in the immediate vicinity of land which (though not assessed to land revenue or local rate) is situated outside the urban areas, i.e., any area which comprised within the jurisdiction of a municipality or cantonment board having a population of ten thousand or more or in any area within such notified distance [up to eight kilometers-see Notification No. 9477, dated January 6, 1994] from the local limits of such municipality or cantonment board [see.2 (IA) (c)]

Rent or revenue derived from land - According to section 2 (IA) (a), if the following conditions are satisfied, income derived from land can be termed as "agricultural income"

:

- a. rent or revenue should be derived from land.
- b. the land is one which is situated in India.
- c. the land is used for agricultural purposes.
- d. Agriculture not merely includes food and gains.

What does Agriculture Includes?

Agriculture income includes :

- (1) Rent of land
- (2) Income derived from cultivation of land.

Agriculture does not merely imply raising of food and grains for the consumption of men and animals ; it includes all products from the performance of basic as well as subsequent operations on land. These products, for instance may be grain or vegetables or fruits including plantation and groves, grass or pasture for consumption of beasts or articles of luxury such as betel, coffee, tea, spices, tobacco, etc. or commercial crops like cotton, flax, jute, hemp, indigo, etc. All these are products raised from the land. The term "agriculture" cannot be confined merely to the production of food and grains products for human beings but must be understood or for trade and commercial asset would also include forest products such as timber, sal and piyasal trees, casuarina plantation, tendu leaves, horra nuts, etc.

Mere connection with land not sufficient - The mere fact that an activity has

some connection with or is in some way dependent on land is not sufficient to bring it within the scope of the term "agriculture". For instance, breeding and rearing a livestock, dairy farming, cheese and butter-making and poultry farming would not by themselves be agricultural purposes.

1.6.2 INCOME DERIVED FROM AGRICULTURAL LAND BY AGRICULTURAL OPERATIONS [Sec. 2 (1A) (b)]

Section 2 (1A) (b) gives the following three instances of agricultural income :

- a. any income derived by agriculture from land situated in India and used for agricultural purposes ;
- b. any income derived from by a cultivator or receiver of rent-in kind by any process ordinarily employed to render the produce raised or received by him fit to be taken to market or
- c. any income derived from such land by the sale by a cultivator or receiver of rent-in-kind of the produce raised or received by him in respect of which no process has been performed other than a process of the nature described in (b).

The aforesaid income is agricultural income if such income is derived from land which a situated in India and is used for agricultural purposes. Section 2 (1A) (b) does not contemplate sale of commodity different from what is cultivated and processed and where assessee is growing mulberry leaves, feeding them to silk worms and obtaining silk cocoons, income from sale of silk cocoons is not an agricultural income

- 239 ITR 597 (SC).

1.6.3 INCOME DERIVED FROM AGRICULTURE

Any income derived by "agriculture" from land situated in India and used for "agricultural purposes."

1.6.4 INCOME DERIVED FROM MARKETING PROCESS

Sometimes it becomes difficult to find ready market of the crop as harvested. In order to make the produce a commodity which is saleable, it becomes necessary to perform some kind of process on the produce. The income, using by way of enhancement of value of such produce, by performing such process to make the raw product fit for market, is also agricultural income. However, the following conditions must be satisfied :

- a. the process must be one which is ordinarily employed by a cultivator or receiver of rent-in-kind ; and
- b. the process must be applied to render the produce fit to be taken to market.

For instance, tobacco leaves are ordinary dried to make them suitable for sale.

Therefore, the income from the ordinary process employed to dry the tobacco leaves to make them fit to be taken to market, is agricultural income. The ordinary process employed to render the produce fit to be taken to market includes thrashing,

winnowing, cleaning, drying, crushing, boiling and decanting, etc. through the nature of process depends upon quality of the produce and varies from time to time and place to place. Moreover, if marketing process is performed on a produce which can be sold in its raw form (without requiring any process to make it fit for marketing), income derived therefore is partly agricultural and partly non-agricultural. For instance, unginned cotton has a ready market and as such profit attributable to ginning operation is not agricultural income. Similarly, if sugarcane is generally sold in a given area without being subjected to any process, the process of converting sugarcane into gur would not be agricultural process and income attributable to the process of converting sugarcane into gur would not be agricultural income- Brihan Maharashtra Sugar Syndicate Ltd. V. CIT (1946) 14 ITR 611 (Bombay).

1.6.5 INCOME FROM SALE OF AGRICULTURAL PRODUCE

Any income from the sale of any produce (of any land situated in India and used for agricultural purposes) to the cultivator or receiver of rent-in-kind is agricultural income provided the produce is not subjected to any process except process ordinarily employed to make it fit for taking it to market. Where, however, the produce is subject to other process, income arising on sale of such produce is partly agricultural income and partly non-agricultural income.

1.6.6 INCOME FROM FARM BUILDING [Sec. 2 (IA) (c)]

Bona fide annual value of a house property is taxable under section 22. However, income from a house property which satisfies the following, cultivated conditions would be treated as agricultural income and consequently, it would be exempt from tax by virtue of section 10 (1);

- a. the building is occupied by the cultivator or receiver of rent-in-kind ;
- b. it is on or in the immediate vicinity of the land situated in India and used for agricultural purposes;
- c. the cultivator or receiver of rent-in-kind, by reason of his connection with the agricultural land, requires the building as a dwelling house or as a store house of other out-building; and
- d. the land is assessed to land revenue or local rate or alternatively the land (though not assessed to land revenue or local rate) is situated outside "urban areas", i.e. any area which is comprised within the jurisdiction of any municipality distance (i.e. up to a maximum of 8 kilometers) from the limits of any such municipality or cantonment board.

Use of building or land for any purpose other than agriculture. With effect from the assessment year 2001-02, an Explanation has been inserted to clarify that any income from such building or land arising from the use of the building or land for any purpose other than agriculture, shall not be included in the definition of "agricultural Income". For example, if a person has income from using such building or land for

purposes such as letting it out for residential purposes of any business or profession, then, such income shall not be treated as agricultural income.

1.6.7 TESTS OF DETERMINE AGRICULTURAL INCOME

The three tests which must be satisfied to treat a particular income as agricultural income are given below. It is essential that all the following three tests must be fulfilled :

Test (a) - Income derived from land

It is essential that for any income to be termed as agricultural income land must be effective and immediate source of income and not indirect and secondary. (C.I.T. Vs. Kamakshya Narain Singh). As a result, interest on arrears of land revenue, dividend paid by a company out of its profits which included agricultural income also (Bacha Guzdar vs. C.I.T.) and salary paid to a manager for managing agricultural farms (Premier Construction Co. Ltd. Vs. C.I.T.) are not agricultural incomes because in all these cases land is not the effective and immediate source of income.

Test (b) - Land is used for agricultural purposes

To term any income as agricultural income, it is necessary that income must be the result of agricultural operations performed on agricultural land. Agriculture means performance of some basic operations - ploughing, sowing, irrigating and harvesting and some subsequent operations - weeding, digging, pruning, cutting etc. It involves employment of some human skill, labour and energy to get some income from land. Supreme Court in its decision has observed :

- (i) Agriculture in its primary sense denotes the cultivation of the field and it is restricted to the cultivation of land in strict sense of the term meaning thereby tilling of the land, sowing of seeds, planting and similar operations on the land.
- (ii) Operations to be performed subsequently like weeding, digging etc.
- (iii) Agriculture comprises within its scope all produce regardless of its nature. The produce may be grains, vegetables or fruits including plantations, groves and pastures, or articles of luxury such as betel, coffee, tea, spices, etc.

Test (c) - Land is situated in India

To qualify for exemption u/s 10(1) of the Act, it is necessary that agricultural income must be derived from land situated in India. In case income is derived from agricultural land situated outside India or is from any non-agricultural land, it will not be exempted u/s 10(1). It is taxable income under the head "Income from other sources."

1.6.8 INSTANCES OF AGRICULTURAL INCOME

The following are held as agricultural income :

1. Sale of replanted trees;

2. Rent from agricultural land;
3. Compensation received on account of agricultural loss;
4. Flowers income grown up in agricultural farms;
5. Share of profit from agricultural farm;
6. Interest on capital from firm engaged in agricultural business;
7. Plants sold in pots planted in agricultural farms etc.;
8. Seeds sold, produced by way of agricultural means.

1.6.9 INSTANCES OF NON AGRICULTURAL INCOME

The following are held as non-agricultural income :

1. Annuity received by a person a consideration of transfer of agricultural land.
2. Interest on arrears of rent payable in respect of agricultural land.
3. Natural growth income from sale of forest trees, fruits and flowers growing on land naturally and spontaneously and without the intervention of human agency.
4. Salt income produced by flooding the land with sea water.
5. Purchase of standing crop profit accruing thereon and resale it after harvest by a merchant.
6. Remuneration from a company received by a managing agent at a fixed percentage of net profit from a company having agricultural income.
7. Interest received by a money-lender in the form of agricultural produce.
8. Dividend paid by a company out of its agricultural income.
9. Fisheries Income and Royalty Income of mines.
10. Income from butter-making and cheese-making.
11. Income from poultry farming.
12. Income from preservation of agricultural produce in cold storage.
13. Income from stone quarries.
14. Income from mining royalties.
15. Income from land used for storing agriculture produce.
16. Income from self-grown grass, trees or bamboos.

1.6.10 PARTIALLY INTEGRATED TAXATION OF NON-AGRICULTURAL INCOME WITH AGRICULTURAL INCOME

This scheme is applicable only if the following conditions are satisfied :

1. The taxpayer is an Individual, a HUF, a Body of Individuals or an AOPs or an artificial juridical person.
2. The taxpayer has non-agricultural income exceeding the amount of exemption limit i.e. Rs. 3,00,000 in the case of resident citizen (60 years or more), Rs. 2,50,000 in the case of any other individual or every HUF, Rs. 5,00,000 in case of individual of the age of 80 years or more.
3. The agricultural income of the taxpayer exceeds Rs. 5000.

Note: This scheme is not applicable in the case of a firm, company, co-operative and local authority.

1.6.10.1 Computation of tax about the cases covered by the scheme

Under this scheme, income tax will be computed for the A.Y. 2021-22 as per undermentioned manner :

STEP ONE : Net agricultural income is to be computed as if it were chargeable to income tax.

STEP TWO : Agricultural and non-agricultural income of the assessee will then be aggregated and income-tax is calculated on the aggregate income as if such aggregate income were the total income.

STEP THREE: The net agricultural income is then increased by the first slab of income on which tax is charged at nil rate i.e. Rs. 3,00,000 in the case of resident senior citizen (60 years or more), Rs. 5,00,000 in case of individual of the age of 80 years or more, Rs. 2,50,000 in the case of any other individual/HUF for the A.Y. 2021-22. And income-tax is calculated on net agricultural income, so increased, as if such income were the total income of the assessee.

STEP FOUR : The amount of income-tax determined at step II will be reduced the amount of income tax determined under step III.

STEP FIVE : Rebate U/S 88 E shall be deducted if any available.

STEP SIX : Find out balance, Add Surcharge if applicable.

STEP SEVEN : Add 4% Health and education less. The amount so arrived at is the income-tax payable by the assessee.

1.6.10.2 Illustration I and II

1. X Ltd. grows sugarcane to manufacture sugar. The detail of transactions of P.Y. 2022-23 is as follows:

	(Rs. in Lakh)
Cost of cultivation of sugarcane	6,00,000
Market value of sugarcane when sugarcane is transferred to factory	9,00,000
Other manufacturing cost	6,00,000
Sales turnover of sugar	22,00,000
Salary of managing director who looks after agriculture as well as non-agricultural operations of the company	2,00,000

Solution:

Income in this case will be determined as follows -

	Income from manufacturing	Agriculture income
Sales turnover/market value of Sugarcane	22,00,000	9,00,000
Less : Expenses :		
Manufacturing expenses	6,00,000	-
Market value of raw material (i.e. sugarcane)	9,00,000	-
Managing Director's Salary	2,00,000	-
Cultivation Expenses	-	6,00,000
Income	5,00,000	3,00,000

II. X Ltd. is engaged in the business of growing and manufacturing tea in India, the following data is available for the previous year 2022-23 :

	Rs. in Lakh
Sales turnover of tea	45
Less :	
Expenses on growing tea leaves	20
Manufacturing expenses	15
Income [60 per cent of Rs. 10 lakh will be agriculture income and 40 per cent (i.e. Rs. 4 lakh), will be taken as non-agriculture income]	<u>10</u>

1.6.11 COMPUTATION OF NET AGRICULTURE INCOME

For the purpose of computing tax in the case of individuals, Hindu undivided families, etc. having net agricultural income in addition to the non-agricultural income, the net agricultural income for the assessment year 2023-24 will be computed as follows :

Rule 1- Agricultural income of the nature referred in section 2(1A) (a) will be computed on the same basis as is adopted for the computation of income chargeable under the head "income from other sources" under section 57 to 59.

Rule 2- Agricultural income of the nature referred in section 2 (1A) (b) will broadly be computed as if it were income chargeable to tax under the head "Profits and gains of business or profession" and provisions of sections 30 to 32, 36, 37, 40, 40A

[other than sub-sections (3) and (4)], 41, 43, 43 A 43B and 43C will apply accordingly. Rule 3 - Agricultural income of the nature referred in section 2 (1A) (c) will be computed as if it were income chargeable under the head "Income from house

property" under sections 23 to 27.

Rule 4 - Where an assessee derives income from sale of tea grown and manufactured by him in India, 60 per cent of the total income from such business, as computed in accordance with rule 8 of the Income-tax Rules, will be regarded as agricultural income.

Rule 5 - Where the assessee is a member of an association of persons or a body of individuals (other than a Hindu undivided family, a company or a firm) which, in the previous year, has either no income chargeable to tax or has non-agricultural income not exceeding the maximum amount not chargeable to tax in the case of association of persons or body of individuals, but has agricultural income, then the agricultural income or loss of the association or body is to be computed in accordance with these rules and the share of the assessee in the agricultural income or loss so computed will be regarded as agricultural income or loss of the assessee.

Rule 6 - Loss incurred in agriculture will be allowed to be set off against gains from agriculture. No set off will, however, be allowed in respect of an assessee's share in the agricultural loss of an association of persons or a body of individuals.

Rule 7 - Any tax levied by a State Government on agricultural income will be allowed as deduction.

Rule 8 - The unabsorbed loss from agricultural activities during the previous years relevant to the assessment year 2015-16 to 2022-23 will be set off against the agricultural income of the assessment year 2023-24 in chronological order. Likewise, an unabsorbed loss from agriculture during the previous year relevant to the assessment years 2016-17 to 2023-24 will be taken into account in determining the net agricultural income for the purpose of payment of advance tax during the financial year 2023-24. The set off of loss will, in either case, be allowed only if such loss has already been determined. Where a person is succeeded by another person (otherwise than by inheritance), the person (other than the person who has incurred the loss) cannot claim the set off as discussed above.

Rule 9 - Where the net result of computation of agricultural income from various sources is a loss, the loss will be disregarded and the net agricultural income of the assessee shall be taken as nil.

Rule 10 - The net agricultural income of the assessee will be rounded off to the nearest multiple of Rs. 10.

SELF CHECK EXERCISE

Question: I For the assessment year 2023-24, net agricultural income of an assessee is Rs. 86,000 and non-agricultural income is Rs. 12,65,000. The taxpayer contributes Rs. 40,000 towards PPF. Find out the tax if the taxpayer is

- (a) X, an individual (22 years)
- (b) Y, a HUF
- (c) Z, a firm assessed as such
- (d) A Ltd. an Indian Company.

1.6.12 SUMMARY

Section 10(1) exempts agricultural income from tax. The reason of exemption of agricultural income from Central taxation is that the Constitution gives exclusive power to make laws with respect to taxes on agricultural income to the State Legislature. However, in some cases agricultural income is taken into consideration to determine tax on non-agricultural income.

1.6.13 GLOSSARY

1. Agriculture income: Income which is exempted from income tax u/s 10 (1).
2. Non- agricultural income: Income which is not agricultural income and subject to tax.
3. Test to determine Agricultural income: Three tests are prescribed to determine-
 - Test (1) - Income derived from land
 - Test (2) - Land is used for agricultural purposes
 - Test (3) - Land is situated in India
4. Unabsorbed Loss: Loss from agriculture remains unadjusted so carry forward to next years
5. Partial Integrated scheme of taxation: A scheme of adding agricultural income into non agricultural income for tax rate purposes.

1.6.14 ANSWER TO SELF CHECK QUESTION

Solution :

	Rs.
Gross total Income	12,65,000
Less : Deduction U/S 80 C	40,000
Total Income	12,25,000
 I. Case of X and Y (An Individual and HUF) Rs.	
1. Income tax on Rs. 13,11,000 (i.e. agricultural income : 86,000+Non agricultural income Rs. 12,25,000)(see working note-I)	205800
2. Income-tax on agricultural income (Rs. 86,000+ exempted slab of income Rs. 2,50,000)(see working note-II)	<u>4300</u>
3. Income-tax computed at (1) minus income tax computed at (2)	210100
4. Add : Surcharge (Not applicable)	<u>Nil</u>
5. Tax and Surcharge	210100
6. Add : Health and Education Cess (4%)	8404
Tax Payable	<u>218504</u>

II. Case of Z (a firm) and A Ltd.

	Z Rs.	A Ltd. Rs.
Tax on non-agricultural income of Rs. 12,65,000 @ 30% (agricultural income is not considered in the case of firm or company)	3,79,500	3,79,500
Add : Surcharge	<u>Nil</u>	<u>Nil</u>
Tax and Surcharge	3,79,500	3,79,500
Add : Health & Education Cess (4% of tax and surcharge)	15180	15180

WORKING NOTE-I : Tax on Rs. 13,11,000 (Total Income)

On First Rs. 2,50,000	-	Nil Rate= Nil	394680	394680
On next Rs. 2,50,000	-	5%= Rs, 12500		
On Next Rs. 5,00,000	-	10%= Rs. 100000		
On First Rs. 2,50,000	-	30%= Rs. 93300		
Total		Rs= 2,05,800		

WORKING NOTE-II : Tax on agricultural income Rs. 86000

+ exempted slab of Rs. 250000= 3,36,000

On First Rs. 2,50,000	-	Nil Rate= Nil	
On next Rs. 86000@ 5%	-	= Rs, 4300	4300

1.6.15 EXERCISE

(A) Short Questions :

Ques.1. What do you mean by Agricultural Income?

Ques.2. What type of incomes basically deemed to be agricultural incomes?

(B) Long Questions :

1. From the following information compute taxable income and agricultural income for the A.Y. 2023-24 :	Rs.
(1) Income from business letting cycles on hire	40,000
(2) Lease rent received from lands given to tenants for agricultural operations	48,000
(3) Sale of agricultural produce (Landlord is share)	30,000
(4) Sale of agricultural land situated in a village	1,20,000
(5) Fixed deposit interest received from companies on deposits made of sale proceeds of land (gross)	18,000
(6) Dividends (gross) from an Indian Company having rubber plantations	6,000
(7) Salary received as a partner from a tea manufacturing firm	36,000

- | | | |
|------|--|--------|
| (8) | Payment of government tax on agricultural land | 6,000 |
| (9) | Expenses on power, irrigation, cess and farms labour | 10,000 |
| (10) | Purchase of seeds | 1,000 |
| (11) | Tractor hire charges (for agricultural work) | 2,500 |
2. In the following cases calculate the tax liability of an individual for the AY 2023-24 :
- (a) Total Income = Rs. 31,500 (Agricultural income Rs. 50,000)
 - (b) Total Income = Rs. 60,000 (Agricultural income Rs. 3,500)
 - (c) Total Income = Rs. 1,62,000 (Agricultural income Rs. 50,000)

1.6.16 SUGGESTED READINGS

1. Students' guide to Income Tax (A.Y. 2023-24)
Dr. Vinod Singhania,
Dr. Kapil Singhania.
2. The Income Tax Law. Dr. Shailinder Sekhon
Dr. Vinod Singhania,
Dr. Kapil Singhania. (A.Y. 2023-24)
3. Professional Approach to Direct Taxes, Law and Practice,
.By: Dr. Girish Ahuja, and Dr. Ravi Gupta
Bharat's Law house Pvt. Ltd. (A.Y. 2023-24)

Mandatory Student Feedback Form

<https://forms.gle/KS5CLhvpwrpgjwN98>

Note: Students, kindly click this google form link, and fill this feedback form once.