ACG 301

Direct Taxes

SPECIAL GROUP : A - ACCOUNTING GROUP

M. Com (M 17) – Part II
Semester - III

YASHWANTRAO CHAVAN MAHARASHTRA OPEN UNIVERSITY
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INTRODUCTION

The subject 'Direct and Indirect Tax' which is neither in its infancy, nor in its maturity, has become very popular among every 'Person' in the last six decades in India. This book is written according to syllabus prescribed by YCMOU, Nashik. Hence, it will serve as good as text and reference book for these students.

The book attempts to maintain a balance between conceptual and practical approaches to 'Direct and Indirect Tax'. It presents the most contemporary issues in a very pragnatic and readable manner. Following each unit have numerous questions and problems which are design to reinforce concepts and procedures presented in the body of the unit. The coverage of the text material is design to satisfy the need of commerce students.

I am thankful to Head of Commerce Department of YCMOU and there Staff who took lot of efforts to publish this book. I am very much thankful to Mrs.Shubhangi Saraf for assisting me in this book. Also to my parents for there kind co-operation and encouragement in bringing out this book.

Any useful suggestions or modifications would be welcome. I have tried to avoid errors but nevertheless some must have escaped my attention. I will be very thankful if these are pointed out to me.

I am confident, that students will welcome new edition of this book.

With knowledge, hard work, marvelous success is just around the corner.

All The Best!

- Dr. Parag Prakash Saraf

Message from the Vice-Chancellor

Dear Students,

Greetings!!!

I offer cordial welcome to all of you for the Master's degree programme of Yashwantrao Chavan Maharashtra Open University.

As a post graduate student, you must have autonomy to learn, have information and knowledge regarding different dimensions in the field of Commerce & Management and at the same time intellectual development is necessary for application of knowledge wisely. The process of learning includes appropriate thinking, understanding important points, describing these points on the basis of experience and observation, explaining them to others by speaking or writing about them. The science of Education today accepts the principle that it is possible to achieve excellence and knowledge in this regard.

The syllabus of this course has been structured in this book in such a way, to give you autonomy to study easily without stirring from home. During, the counseling sessions, scheduled at your respective study centre, all your doubts will be clarified about the course and you will get guidance from some experienced and expert professors. This guidance will not only be based on lectures, but it will also include various techniques such as question-answers, doubt clarification. We expect your active participation in the contact sessions at the study centre. Our emphasis is on 'self study'. If a student learns how to study, he will become independent in learning throughout life. This course book has been written with the objective of helping in self-study and giving you autonomy to learn at your convenience.

During this academic year, you have to give assignments and complete the Project work wherever required. You have to opt for specialization as per programme structure. You will get experience and joy in personally doing above activities. This will enable you to assess your own progress and thereby achieve a larger educational objective.

We wish that you will enjoy the courses of Yashwantrao Chavan Maharashtra Open University, emerge successful and very soon become a knowledgeable and honorable Master's degree holder of this university.

Best Wishes!

Vice-Chancellor

SYLLABUS - DIRECT TAXES

1) BASIC CONCEPTS

Income Tax, Features of Income Tax, Scope of the Income Tax Act, Objectives of Income Tax, Important Definitions, Concept of Income [Section 2 (24)], Assessment Year [Section 2 (9)], Previous Year [Section 3], Person [Section 2 (31)], Assessee [Section 2 (7)], Deemed Assessee, Gross Total Income [Section 14], Total Income or Taxable Income, Rounded-off, Capital and Revenue Receipts, Capital and Revenue Expenditure, Tax always calculate as per Income Tax Rate declared in Budget, Residential Status, Types of Residential Status, Rules for Determining the Residential Status, Resident and Tax Liability

2) EXEMPTION UNDER SECTION 10

Exemption (Section 10), Agricultural Income [Section 10 (1), Alternative Tax on Agricultural Income, Income to Family Member from HUF [Section 10 (2)], Profit or Income to Partners from Partnership Firm [Section 10 (2A)], Interest on Investment by Foreigner [Section 10 (4)], Leave Travel Concession (LTC) [Section 10 (5)], Income of Foreigner [Section 10 (6)], Allowances paid outside India [Section 10 (7)], Income of Foreign Employee for Services under Co-operative Programme [Section 10 (8 and 9)], Gratuity [Section 10 (10)], Commuted Pension [Section 10 (10 A)], Leave Encashment [Section 10 (10 AA)], Any Amount Received from Provident Fund [Section 10 (11)], Any Amount Received from Superannuation Fund [Section 10 (13)], House Rent Allowance (H.R.A.) [Section 10 (13A)], Special Allowance [Section 10 (14)], Interest on Specific Securities [Section 10 (15)], Scholarship (Education) [Section 10 (16)], Daily Allowances to Parliament Members [Section 10 (17)], Income or Pension of Gallantry Award [Section 10 (18)], Income or Amount of Award given by Government [Section 10 (19)], Income of Local Authority [Section 10 (20)], Income of sports Association [Section 10 (21)], Income of Educational Institute [Section 10 (22)], Income of Medical Institute [Section 10 (23)], Income of Minor [Section 10 (32)], Dividend from Indian Company [Section 10 (34)], Interest on Mutual Fund [Section 10 (35)]

3) INCOME FROM SALARY

Income from Salary, Salary Chargeable Basis [Section 15], Allowances and their Taxability, Perquisites and their Valuation [Section 17 (2)], Perquisites, Gift by Employer to Employee, Medical Facility by Employer, Educational Facility to Children of Employee, Gas, Electricity, Water provided by Employer, Telephone Bill paid by Employer, If Credit Card given, Facility of Health Club, Snacks or Lunch provided, Loan at Lower Rate, Cook, Gardner, Watchman, Servant provided by Employer and Salary paid by Employer, Any Obligation of Employee, Provident Fund, Car provided by Employer to Employee, Other Vehicles (Motor cycle, Scooter or any other Conveyance is provided by the Employer), Transport Facility by a Transport undertaking (not being provided by Railways or by an Airlines), Travelling and Touring Accommodation, Valuation of Perquisites, Deduction u/s 16, Different Meaning of Salary for Different Purposes

4) INCOME FROM HOUSE PROPERTY

Basis of Charge [Section 22], Conditions, Classification of House Property, Gross Annual Value [Section 23 (1)], Steps for Computing Income from House Property, Let Out House Property, Deemed Let Out House Property, Self-Occupied House Property, Net Annual Value (NAV), Deductions from Income of House Property [Section 24]

5) PROFITS AND GAINS FROM BUSINESS OR PROFESSIONS

Profits and Gains of Business and Professions, Business [Section 2 (13)], Profession [Section 2 (36)], Vocation, Expenditure, Income, The Main Rules for Preparation of Trading, Profit and Loss A/c, Expenses/Deductions expressly allowed as deduction from Profit and Gain of business or Profession, Disallowed Expenses, While computing the Income from Business or Profession it is difficult to remember which expenses are allowed and which expenses are not allowed under the Act, Format of Computation of Taxable Income from Business or Profession, Personal Incomes (Disallowed Incomes)

6) CAPITAL GAIN

Basis of Charge [Section 45], Chargeability of Tax, Some Important Definitions, Computation of Capital Gains, Full Value of Consideration, Cost of Acquisition, Deemed Cost of Acquisition, Indexed Cost of Acquisition, Cost of Improvement, Indexed Cost of Improvement, Tax on Capital Gains, Exemptions under the Head 'Capital Gains'

7) INCOME FROM OTHER SOURCES

Last Head of Income Under Gross Total Income, Expenses which are Deductible under the head 'Income from Other Sources [Section 57], Inadmissible Expenses under the Head 'Income from Other Sources' [Section 58], Basis of Charge under the Head 'Income from Other Sources'

8) DEDUCTIONS u/s 80

Deduction in respect of the amount paid or deposited out of income chargeable to tax or otherwise in the various chargeable to tax or otherwise in the various schemes [Section 80 C], Deductions in respect of Contribution to Pension Fund and Annuity Plan [Section 80 CCC], Deduction in respect of amount paid or deposited in a pension scheme [Section 80 (CCD)], Maximum Limit [Section 80 (CCE)], Deduction in respect of Medical Insurance Primia [Section 80 D], Deductions in respect of Maintenance including Medical Treatment of Handicapped Dependents [Section 80 DD], Deduction in respect of Medical Treatment [Section 80 DDB], Deduction in respect of Payment of Interest on Loan taken for Higher Education [Section 80 E], Deduction in respect of Donation to certain Funds and Charitable Institutions [Section 80 G], Deduction in respect of Rent Paid [Section 80 GG], Deduction in respect of certain Donations for Scientific Research or Rural Development [Section 80 GGA], Deduction in respect of Royalty on Patents [Section 80 RRB], Deduction in case of a Person Totally Blind or Physically Handicapped and Resident [Section 80U]

9) GROSS TOTAL INCOME (G.T.I.)

Gross Total Income, Chart Showing the Computation of Taxable Income

10) CARRY FORWARD AND SET OFF

Clubbing of Income, Set off and Carry Forward of Losses

11) TAX PLANNING

Tax Planning (Meaning), Justification of Tax Planning, Nature and Scope of Tax Planning in the Corporate Sector

12) PROCEDURE UNDER INCOME TAX ACT, 1961

UNIT - 1
BASIC CONCEPTS

NOTES

1.0 Introduction
1.1 Objectives
1.2 Income Tax
  1.2.1 Features of Income Tax
  1.2.2 Scope of the Income Tax Act
  1.2.3 Objectives of Income Tax
1.3 Important Definitions
  1.3.1 Concept of Income [Section 2 (24)]
  1.3.2 Assessment Year [Section 2 (9)]
  1.3.3 Previous Year [Section 3]
  1.3.4 Person [Section 2 (31)]
  1.3.5 Assessee [Section 2 (7)]
  1.3.6 Deemed Assessee
  1.3.7 Gross Total Income [Section 14]
  1.3.8 Total Income or Taxable Income
  1.3.9 Rounded-off
1.4 Capital and Revenue Receipts
1.5 Capital and Revenue Expenditure
1.6 Tax always calculate as per Income Tax Rate declared in Budget
1.7 Residential Status
1.8 Types of Residential Status
1.9 Rules for Determining the Residential Status
1.10 Resident and Tax Liability
1.11 Key Concepts
1.12 Summary
1.13 Exercise
1.14 Further Reading and References

CHECK YOUR PROGRESS

Describe features of Income Tax?

1.0 Introduction

Income Tax is tax on income. According to the Constitution of India, income tax is a central subject. Income Tax on all types of income, other than agricultural income is charged and collected by the Central Government. The Income Tax Act, 1961 has been brought into force with effect from 1st April, 1962. It applies to the whole of India (including Jammu and Kashmir). Since then several amendments of far-reaching nature have been made in the Income Tax Act by the Finance Acts of every year. Besides this, amendments have also been made.

1.1 Objectives

After reading this unit, you should be able :

1. To understand basics of Income Tax.
2. To understand A.Y. & P.Y.

NOTES

1.2 Income Tax

1.2.1 Features of Income Tax:

1. Income Tax is charged on the income of previous year, at a rate which is prescribed by the Finance Act for the relevant assessment year.
2. The Finance Act is passed every year by the Parliament in the form popularly known as "Budget".
3. Income Tax is levied on a person in relation to his income of the previous year.
4. The tax payer's liability is determined with reference to his residential status in the previous year or accounting year.
5. Liability to income tax arises only where the total income in the accounting year exceeds the maximum tax free amount prescribed by the Finance Act to that relevant year.
6. The rates of income tax are progressive and incidence of tax increases with the rise in income.
7. It is compulsory to deduct the tax at source and to pay it to the Government Treasury.

CHECK YOUR PROGRESS

Describe Scope of Income Tax?

1.2.2 Scope of the Income Tax Act:

The Income Tax Act, 1961 is applicable to whole of India, including Jammu and Kashmir. The Act broadly covers ?

1. Basis of charging income.
2. Income exempt from income tax.
3. Computation of income under various heads of income.
4. Clubbing of income.
5. Set-off and carry forward of losses.
6. Permissible deductions.
7. Rebates and reliefs.
8. Determination of tax in certain special cases.
9. Tax on dividends distributed by domestic companies.
10. Income Tax Authorities and their powers.
11. Survey, search and seizure.
12. Assessment procedures.
13. Collection and recovery of tax and Tax Deduction at Source (TDS).
14. Payment of advance tax.
15. Refund.
16. Appeal and revisions.
17. Acquisitions of immovable property.
18. Penalty and prosecution.

1.2.3 Objectives of Income Tax:

The objectives of income tax may be summarized as follows:

1. To reduce inequalities in the distribution of income and wealth.
2. To bring out a greater measures of equity between different classes of tax payers.

3. To achieve the twin objectives of higher yields with reduction in inequalities.
4. To accelerate the temp of economic growth and development of the country.
5. To maintain reasonable economic stability in the force of long run inflationary pressure and short run international price movements.
6. To make available of funds for economic development.
7. To reduce extreme inequalities in wealth, income and consumptions standards with undetermined productive efficiency, offence, justice and political stability.
8. To encourage investment in new capital goods.
9. To channelize investment into those sectors which contribute the most of economic growth.

NOTES

1.3 Important Definitions

CHECK YOUR PROGRESS

Explain A.Y. and P.Y.?

1.3.1 Concept of Income [Section 2 (24)]:

Definition of Income under Income Tax Act, is inclusive and it includes ?

1. Profits and gains.
2. Dividend.
3. Charity received to trust.
4. Remuneration.
5. Allowances other than salary.
6. Perquisites provided.
7. Daily allowance to directors.
8. Profit from insurance business.
9. Any casual receipts.
10. Profit from keyman insurance policy.
11. Any gift in excess of ` 50,000 at a time.
12. Profits on sale of a license granted.
13. Interest, salary, bonus, commission or remuneration received by the partner from the firm.

1.3.2 Assessment Year [Section 2 (9)] (A.Y.):

Assessment year means the period of twelve months commencing on the first day of April every year and ending on thirty first March of the subsequent year. It is also called Tax Year, Government Year, Financial Year or Fiscal Year. The total income of a person and his tax liability is accesses in the assessment year as per the provisions applicable to that year. e.g. for the previous year ended on the 31st March, 2016, the assessment year would be 1/4/2016 to 31/3/2017. Thus, the assessment year immediately follows the year in which the income is subject to tax.

1.3.3 Previous Year [Section 3] (P.Y.):

Previous year means the financial year immediately preceding the Assessment Year. The income of the previous year is assessed to tax in the assessment year. It is also called 'earning year', year of the account or accounting

NOTES

year of income.The previous year start from 1st April and concludes on 31st March every year except in case of setting up a new business in that year.

In case of newly set up business or profession or a source of income newly coming into existence, the first previous year will be the period commencing from the date of setting up of the business or profession and ending on the immediately following 31st March, e.g. if a business is newly set up on 15th September, 2015, the previous year is 15-09-2015 to 31-03-2016 and the assessment year will be 2015-16.

1.3.4 Person [Section 2 (31)]:

Income Tax is levied in the income of the person. Person includes:

i. An individual: An individual means a natural human being. It includes a male, a female, minor or major and a lunatic.

ii. A Hindu Undivided Family (HUF): It means a family which consists of all persons lineally descended from a common ancestor and includes their wives and unmarried daughters.

iii. Company: Company is an incorporated association created by law having common seal and perpetual succession. Under Income Tax only two companies are there :

- **a) Indian Company:** A company which is registered under Indian Company Act, 1956 is known as Indian Company.
- **b) Foreign Company:** A company which is registered under, other than Indian Company Act is known as Foreign Company.

iv. Firm: Firm means partnership firm. When two or more persons carrying business and distribute the profits between them is known as partnership firm.

v. An Association of Person (AOP): When two or more persons join hands for a common purpose with a view to earn an income but do not constitute a partnership whether incorporated or not, they may be assessed as an Association of Persons. An AOP may consist of non-individuals.

vi. Body of Individuals (B.O.I.): Means conglomeration of individuals who carry on some activity with the object of earning some income. It would consist of only of individuals entities like companies or firms cannot be members of a Body of Individuals.

vii. A Local Authority: It means any Municipal Committee or District Board.

viii. Every Artificial Juridicial Person: The term artificial juridical person covers all such persons who cannot be included under any of the first six categories and register under any Act.

CHECK YOUR PROGRESS

Describe Person U/S 2 (31)?

1.3.5 Assessee [Section 2 (7)]:

Assesse means a person by whom any tax or any other sum of money is payable under Income Tax Act and includes:

a) Every person in respect of whom, any proceeding under the Act has been taken for the assessment of his income or of the income of any other person in respect of which he is assessable.

b) Every person is deemed to be an assessee and an assessee in default under any provisions of this act.

In short, assessee is a person by whom tax or any other sum of money is payable under this act. The other sum of money includes fine, penalty and interest.

1.3.6 Deemed Assessee:

A person is liable to pay tax on his own income. But sometimes he is also liable to pay tax on other's income. That time, he is known as deemed assessee. e.g.

1. After the death of a person, his legal representative is treated as an assessee for that income of the deceased person on which tax has not been paid.
2. A person representing a Minor or Lunatic is treated as an assessee for the income of the minor or lunatic.

NOTES

1.3.7 Gross Total Income [Section 14]:

Gross Total Income means the total income computed in accordance with the provisions of the Income Tax Act before making any deduction under Section 80 C to 80 U or under section 280-U. Under the Income Tax Act, the various types of income liable to tax have been classified under five heads:

i. Income from salaries.

ii. Income from house property.

iii. Profits and Gains from business or profession.

iv. Capital gain

v. Income from other sources.

CHECK YOUR PROGRESS

What is GTI?

1.3.8 Total Income or Taxable Income:

The total income of an assessee is gross total income as reduced by the amount permissible as deduction under Section 80 C to 80 U.

The scheme of computation of total income and tax liability thereon can be easily understood with the help of following chart:

Computation of Income under Various Heads		
(a) Income from Salaries	xxx	
(b) Income from House Property	xxx	
(c) Income from Business or Profession	xxx	
(d) Capital Gains	xxx	
(e) Income from Other Resources	xxx	
Total (i.e. (a) + (b) + (c) + (d) + (e))		**xxx**
Less : Adjustment on account of set-off and carry forward of losses		xxx
Add : (1) Inclusion of income under Section 60, 61, 64, 66 to 69 D	xxx	
(2) Income of any other persons to be added	xxx	xxx
Gross Total Income		**xxx**
Less : Deductions under Section 80 C to 80 U		xxx
Total Income or Taxable Income		xxx
Tax on Total Income		xxx
Less : Relief under Section 89, 90 and 91		xxx
Balance		xxx
Add : Surcharge (if applicable)		xxx
Tax and Surcharge Payable		xxx
Add : Education Cess on it		xxx
Total Tax Liability		**xxx**

1.3.9 Rounded-off:

Rounded-off Income [288 (a)] means income always rounded nearest ` 10 and Rounded off Income Tax [288 (b)] means income tax always rounded to nearest.

NOTES

1.4 Capital & Revenue Receipt

Income Tax is charged on revenue receipts unless they are expressly exempt, whereas capital receipts are exempt from tax unless they are expressly taxable e.g. capital gains taxable under Section 45. There are no hard and fast rules in regard to capital and revenue receipts. One type of receipts may at one time be capital and at another time it may be revenue receipts.

CHECK YOUR PROGRESS

Distinguish between Capital & Revenue Receipts?

- **Distinction between Capital and Revenue Receipts :**

No.	Points	Capital Receipts	Revenue Receipts
1.	Nature	An amount received as fixed capital is a capital receipt.	An amount received as a circulating capital is a revenue receipt.
2.	Substitution of source of income	A receipt is substitution of a source of income is a capital receipt e.g. VRS compensation.	A receipt in substitution of an income is a revenue receipt. e.g. reward received by an employee for his goods services.
3.	Compensation	An amount received as a compensation for the surrender of certain rights under an agreement is capital receipt.	An amount received under an agreement as compensation for loss of future profits is a revenue receipt.
4.	Coverage	Whether a particular receipt is a capital or revenue, depends upon the nature of its receipt in the hands of the receiver.	If a person receives an amount as an income, it will be a revenue receipt even if the payer has paid it out of capital.
5.	Mode of Receipt	Even if the amount is received in instalment. It may be treated as capital receipt.	Even if the amount is received as a lumpsum payment it may be treated as revenue receipt.
6.	Sale proceeds of assets	If any asset is used in business or is kept as an investment, the sale proceeds thereof will be capital receipt.	If any asset has been purchased for resale at a profit, the proceeds thereof is revenue receipts.
7.	Profits on devaluation	Profit on devaluation or appreciation of currency which was kept as investment is capital receipt.	Profit on devaluation or appreciation of currency which was kept for sale or conversion is Revenue Receipts.
8.	Grants or Subsidies	Grants or subsidies received from Govt. for specific purposes e.g. for any development scheme are capital receipt	Grants or subsidies received from the Govt. for assisting the trader in his business are revenue receipt.
9.	Insurance money	Insurance money received for capital assets is capital receipt.	Insurance money received for atrading asset e.g. Stock in trade is Revenue Receipt.

NOTES

1.5 Capital & Revenue Expenditure

Expenditures are of two types: Capital and Revenue. Capital expenditure is not deductible from the gross income of business in order to arrive at the taxable income but the revenue expenditure is deductible.

- **Distinction between Capital and Revenue Expenditure**

No.	Points	Capital Expenditure	Revenue Expenditure
1.	Purpose	Expenses on purchase and installation of assets is capital expenditure.	Expenses on meeting day to day fixed requirements including goods purchased for resale are revenue expenses.
2.	Asset Acquisition Income Earning	Expenditure incurred for the acquisition of a source of income is capital expenditure e.g. purchase of plant and machinery.	An expenditure incurred for the purpose of earning an income is a revenue expenditure e.g. purchase of goods, payment of wages etc.
3.	Earning capacity/ Maintenance	An expenditure incurred for increasing the earning capacity of a business by improving it's a capital expenditure.	An expenditure incurred or maintaining a fixed asset in a good condition is a revenue expenditure.
4.	Treatment in Accounts	Normally, expenditure incurred in relation to a fixed asset such as land and building, plant and machinery etc. is added to the cost of respective asset in Balance Sheet.	Normally, an expenditure incurred in relation to stock in trade is a revenue expenditure and is charged off to Profit and Loss A/c.
5.	Duration of Benefits	Capital expenditure produce benefits for several previous years.	Revenue expenditure gives benefit for one previous year only.
6.	Frequency or Recurrence	Usually, capital expenditure is a non-recurring.	Revenue expenditure is normally a recurring item.
7.	Carry forward	These expenses are carry forward to the next period (year).	These expenses are not carry forward to the next period (year).
8.	Deduction	These expenses are not deducted from the profit of the business but they show the financial position of the business.	These expenses are deducted from the profit of the business during The year.
9.	Relation with share loan or debentures	Expenditure incurred in obtaining capital by issuing shares is capital expenditure	Expenditure incurred in relation to loans and debentures is revenue expenditure.

CHECK YOUR PROGRESS

Distinguish between Capital & Revenue Expenditure?

NOTES

1.6 Tax always calculates as per Income Tax Rate declared in Budget

1. General Assessee: Who is not senior citizen. Tax rates are :

1st	2,50,000	Nil
Next	2,50,000	10%
Next	5,00,000	20%
Remain		30%

Education cess is applicable 3%.

2% primary, 1% secondary & 0.5% for Pradhanmantri Swacchata Abhiyan

Problem 1.1:

Mr. X gets Rs.10,00,000 during the previous year 2015-2016. Find out his tax liability.

Mr. X
Statement showing Tax Liability

Taxable Income (P.Y. 2015-16)		**AY 2016-17**
		10,00,000
1st 2,50,000	Nil	Nil
Next 2,50,000	10%	25,000
Next 5,00,000	20%	1,00,000
Remain	30%	
		1,25,000
Add : Surcharge	Not Applicable	-
		1,25,000
Add : Education Cess	3%	3,750
		1,28,750

Tax Liability = **1,28,750**

Problem 1.2 :

Mr. X gets ` 8,40,000 during previous year 2015-16. Find out their tax liability for A.Y. 2016-17.

Mr. X
Statement showing Tax Liability

(P.Y. 2015-16)		**AY 2016-17**
Taxable Income		8,40,000
1st 1,60,000	Nil	25,000
Next	10%	
Next	20%	68,000
Remain 40,000	30%	
		93,000
Add : Surcharge	Not Applicable	-
Add : Education Cess	3%	2,790
		95,790

Tax Liability ` **95,790**.

2. Senior Citizen: A person who completes the age of 65 not attempt 65. Tax rates are:

1st	3,00,000	Nil
Next	2,00,000	10%
Next	5,00,000	20%
Remain		30%

Educational Cess is 3% on tax.

Problem 1.3 :

Mr. Jayram gets 8,50,000/- in the previous year whose age is 70 years. Find their tax liability.

Mr. Jayram
Statement showing Tax Liability

(P.Y. 2015-16)		**AY 2016-17**
Taxable Income		8,50,000
1st 3,00,000	Nil	Nil
Next 2,00,000	10%	20,000
Next 3,50,000	20%	
Remain	30%	70,000
		90,000
Add : Surcharge	Not Applicable	-
Add : Education Cess	3%	2,700
		92,700

Tax Liability **= 92,700**.

Problem 1.4 :

Shrimati Narayani age 66 years gets 6,00,000 in previous year. Find out her tax liability.

ShrimatiNarayani (Senior citizen)
Statement showing Tax Liability

(P.Y. 2015-16)		**AY 2016-17**
Taxable Income		6,00,000
1st 2,40,000	Nil	Nil
Next 2,60,000	10%	20,000
Next 1,00,000	20%	20,000
		40,000
Add : Surcharge	Not Applicable	-
Add : Education Cess	3%	1,200
		41,200

Tax Liability **= 41,200**.

1. Partnership Firm :

30% of net profit of business

Surcharge - N.A.

Education Cess - 3%.

NOTES

2. Co-operative Society :

Tax is on Net Profit :

1st 10,000	10%
Next 10,000	20%
Remain	30%
Surcharge	Not Applicable
Education Cess	3%

3. Company :

(i) Indian Company : 30% tax.

Surcharge 5% if income of previous year exceeds 1 crore. But not exceeds Rs.10 crores and if income exceed Rs.10 crore then surcharge is 10%

Education cess 3%.

(ii) Foreign company : Tax on profit 50%.

Surcharge 2% if income in previous year exceeds 1 crore. But upto Rs.10 crore if it exceeds Rs.10 crore then surcharge is 5% on total income.

Education cess 3%.

4. Local Authority, Association of Person, Body of Individual:

10% on profit.

Surcharge - Not Applicable.

Education Cess 3%

5. Capital Gain :

(i) Short-term capital gain: 15% tax.

(ii) Long-term capital gain: 20% tax.

Surcharge Not Applicable

Education Cess - 3%

6. Casual Receipts :

(i) Winning from lottery (ii) Winning from card games

(iii) Winning from gamble (iv) Winning from races including horse races

(v) Winning from camel races etc.

Tax is 30%

Surcharge : Not Applicable.

Education Cess - 3%.

1.7 Residential Status

The income tax liability of an assessee depends upon his residential status. For instance, whether an income accrued to an individual outside India, is taxable in India or not, depends upon the residential status of the individual. Similarly, whether an income earns by foreign national in India (or outside India) is taxable in India or not depends on the residential status of the individual, rather than on his citizenship. Therefore, the determination of the residential status of a person is very significant in order to find out his tax liability.

NOTES

1.8 Types of Residential Status

On the basis of residence, all the assesses are classified into two classes :

(a) Resident of India (ROI).

(b)Non-resident of India (NRI).

The first category i.e. resident in India (for individuals and HUFs) is further classified into two types:

i. Resident and Ordinary Resident or

ii. Resident and not Ordinary Resident.

1.9 Rules for Determining Residential Status

There are separate rules for determining the residential status of different kinds of assessees. The different kinds of assessees are individual, Hindu undivided families, firms, association of persons, companies, local authorities and artificial juridical persons.

CHECK YOUR PROGRESS

Describe conditions for Residential Status of Individual?

(A) Residential Status of an Individual (Section 6) :

Resident of India? u/s 6 (1) an individual is said to be resident of India in any previous year, if he satisfies at least one of the following basic conditions :

a) He is in India in the previous year for a period of 182 days or more 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 4 years immediately preceding the previous year.

Exceptions: The aforesaid rule of resident is subject to the following exceptions, by virtue of explanation.

a) to Section 6 (1) the period of 60 days refer to in

b) above has been extended to 182 days in following cases :

1. An Indian citizen, who leaves India during the previous year for the purpose of employment, outside India or an Indian citizen who leaves India during the previous year as a member of the crew of an Indian ship.

2. Indian citizen or a person of Indian origin. A person is deemed to be of Indian origin, if he or either of his parents or any of his grandparents was born in undivided India.

Resident and Ordinary Resident: Under Section 6 (6), a resident individual is treated as resident and ordinarily resident in India, if he satisfies the following two additional conditions:

a) He has been resident in India at least 2 out of 10 previous year immediately preceding the relevant previous year and

b) He has been in India for a period of 730 days or more during 7 years immediately preceding the relevant previous year.

In brief, it can be said that, an individual becomes resident and ordinarily resident in India if he satisfies at least one of the basic conditions and the two additional conditions given above.

Resident but not Ordinary Resident:An individual who satisfies at least one of the basic conditions but does not satisfy the two additional conditions (given above) is treated as a resident but not ordinarily resident of India.

Non-resident:An individual is non-resident of India during the previous year, if the satisfied none of the basic conditions laid down in Section 6 (1) above. In the case of non-resident additional conditions are not relevant.

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(B) Residential Status of Hindu Undivided Family [Section 6 (2)]:

A Hindu Undivided Family (like an individual) is either resident in India or non-resident of India. A resident HUF is either ordinarily resident or not ordinarily resident.

Resident: A HUF is said to be resident of India, if the control and management of its affairs is wholly or partly situated in India.

Ordinarily Resident : A resident HUF is 'ordinarily resident' in India, if the Karta or manager of the family is resident in India at least 2 years out of 10 previous years and is in India for 730 days or more during the 7 years immediately preceding the relevant previous year.

CHECK YOUR PROGRESS

Describe conditions for Residential Status of HUF?

Resident but not ordinarily resident : If the Karta or manager of resident family is not resident in India at least 2 out of 10 immediately preceding previous year or is not present in India for at least 730 days in 7 immediately previous year as aforesaid, the family will be regarded as resident but not ordinarily resident in India.

Non-resident: A HUF is non-resident of India if its control and management is wholly situated outside India.

(C) Residential Status of Firm or an Association of Persons [Sec. 6 (4)]:

A partnership firm or an association of persons is said to be resident of India, if the control and management of its affairs are wholly or partly situated within India during the relevant previous year. It would be treated as non-resident of India if the control and management of its affairs are situated wholly outside India.

(D) Residential Status of a Company [Section 6 (3)]:

An Indian Company is always resident of India. A foreign company is resident in India only if during the previous year control and management of its affairs is situated wholly in India.

A foreign company is treated as non-resident if during the previous year, the control and management of its affairs is either wholly or partly situated out of India.

A company can never be 'ordinarily' 'not ordinarily' resident of India.

(E) Residential Status of every other person:

Every other person is resident of India if control and management of his affairs is wholly or partly, situated within India during the relevant previous year. If control and management of its affairs is wholly situated outside he is treated as non-resident.

NOTES

1.10 Resident & Tax Liability

Following chart highlights the provision of tax incidence in brief.

Income	Whether tax incidence arises or not		
	Resident or Resident and ordinarily resident	**Resident not ordinarily resident**	**Non resident**
1. Income received or deemed to be received in India whether accrued in India or outside India e.g. profits from business in Iran received in India.	Yes	Yes	Yes
2. Income accruing or arising or deemed to accrue or arise in India whether received in India or outside India	Yes	Yes	Yes
3. Income received and accrued or arising outside India from a business controlled in or from a profession set up in India	Yes	Yes	No
4. Income received and accrued or arise outside India from a business controlled from outside India or a profession set up outside India	Yes	No	No
5. Income (not being from a business/profession) received and accrued outside India	Yes	Yes	No
6. Income earned and received outside India and remitted to India during the previous year.	No	No	No

1.11 Key Concepts

Assessment year means the period of twelve months commencing on the first day of April every year and ending on thirty first March of the subsequent year.

Previous year means the financial year immediately preceding the Assessment Year.

1.12 Summary

Income tax is a tax on income. It is charged on the income of previous year, at a rate which is prescribed by the finance act for the relevant assessment year. It helps to reduce inequalities in the distribution of income and wealth. Assessment year means the period of 12 months commencing on the 1st April every year and ending on 31st March of subsequent year. Previous year means

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the financial year immediately preceding the Assessment year. The term 'Person' includes an individual, HUF, firm, company, association of persons, body of individuals, local authority and every artificial juridical person. An assessee means a person who is liable to pay tax. An amount received as fixed capital is capital receipt and an amount received as circulating capital is a revenue receipt.

Section 6 of Income Tax Act, 1961 describes provisions related to residential status of an assessee. Residential status is necessary because if assessee is Resident of India then only he is liable to pay tax at a low rate while non-resident pay tax at higher rate. Residential status can be classified as Resident of India, ordinarily resident, resident but not ordinarily resident and non-resident. Individual and HUF are classified into all categories. But firm, company, AOP, BOI can classify under two heads only i.e. resident of India and non-resident of India.

1.13 Exercise

1. Write brief notes on 'Income Tax'.
2. What are the features of Income Tax?
3. What are objectives of Income Tax?
4. Write short notes on :
   - (i) Income
   - (ii) Assessment Year
   - (iii) Person
   - (iv) Deemed Assessee
   - (v) Gross Total Income
   - (vi) Taxable Income
   - (vii) Rounded-off
   - (viii) Capital and Revenue Expenditures
5. Write distinction between Capital Receipts and Revenue Receipts.
6. State the tax rates of (for A.Y. 2016-17).

   General assessee, Senior citizen, Partnership firm,Co-operative Society, Company.
7. What is the residential status of an individual?
8. Give brief note on 'Resident and Tax Liability'.

● **Fill in the blanks**

1) Income Tax is tax on _____.
   (wealth, income, expenses, transaction)
2) The Finance Act is passed every year by the Parliament in the form popularly known as "_____".
   (Budget, Estimate, Statement, Report)
3) It is compulsory to deduct the tax at source and to pay it to the _____
   (State Government, Central Government, Government Treasury, Government officer).
4) _____ means the period of twelve months commencing on the first day of April every year and ending on thirty first March of the subsequent year.
   (Financial year, Previous year, Assessment year, Accounting year)
5) _____ means the financial year immediately preceding the Assessment Year.
   (Previous year,Financial year, Assessment year, Accounting year)

NOTES

6) An_____ means a natural human being. It includes a male, a female, minor or major and a lunatic.
(individual, Association of Persons, Body of individual, firm)

7) _____ is an incorporated association created by law having common seal and perpetual succession.
(individual, Association of Persons, Body of individual, Company)

8) _____means a person by whom any tax or any other sum of money is payable under Income Tax Act.
(Individual, Assessee, Firm, Company)

9) Sometimes person is also liable to pay tax on other's income, he is known as _____.
(Individual, Assessee, Firm, Deemed assessee)

10) The total income of an assessee is _____as reduced by the amount permissible as deduction under Section 80 C to 80 U.
(gross total income, net income, total deduction,gross receipts)

11) Capital expenditure is not deductible from the _____ of business in order to arrive at the taxable income but the revenue expenditure is deductible.
(net income, total deduction, gross expenditure, gross income)

12) Expenses on purchase and installation of assets are _____.
(Revenue expenditure, Capital expenditure, Revenue receipts, Capital receipts)

13) Income of Local Authority, Association of Person, Body of Individual is chargeable to tax at the rate of _____.
(10%, 20%, 30%, 50%)

14) Long-term capital gain is chargeable to tax at the rate of _____.
(10%, 20%, 30%, 50%)

15) The income tax liability of an assessee depends upon his_____.
(Residential status, citizenship, employment, income)

16) A resident HUF is 'ordinarily resident' in India, if the Karta or manager of the family is resident in India at least 2 years out of 10 previous years and is in India for _____or more during the 7 years immediately preceding the relevant previous year.
(182 days, 730 days, 800 days, 750 days)

(**Answers:** 1) income, 2) Budget, 3) Government Treasury, 4)Assessment year, 5)Previous year, 6)individual, 7)Company, 8)Assessee, 9) Deemed assessee, 10)gross total income, 11)gross income, 12) Capital expenditure, 13) 30%, 14)20% 15) residential status, 16) 730 days)

1.14 Further Reading and References

1) Students Guide To Income Tax by Vinod Singhania
2) Taxman
3) Income Tax Bare Act

UNIT - 2
EXEMPTION UNDER SECTION 10

NOTES

2.0 Introduction
2.1 Objectives
2.2 Exemption (Section 10)
2.3 Agricultural Income [Section 10 (1)
2.3.1 Alternative Tax on Agricultural Income
2.4 Income to Family Member from HUF [Section 10 (2)]
2.5 Profit or Income to Partners from Partnership Firm [Section 10 (2A)]
2.6 Interest on Investment by Foreigner [Section 10 (4)]
2.7 Leave Travel Concession (LTC) [Section 10 (5)]
2.8 Income of Foreigner [Section 10 (6)]
2.9 Allowances paid outside India [Section 10 (7)]
2.10 Income of Foreign Employee for Services under Co-operative Programme [Section 10 (8 and 9)]
2.11 Gratuity [Section 10 (10)]
2.12 Commuted Pension [Section 10 (10 A)]
2.13 Leave Encashment [Section 10 (10 AA)]
2.14 Any Amount Received from Provident Fund [Section 10 (11)]
2.15 Any Amount Received from Superannuation Fund [Section 10 (13)]
2.16 House Rent Allowance (H.R.A.) [Section 10 (13A)]
2.17 Special Allowance [Section 10 (14)]
2.18 Interest on Specific Securities [Section 10 (15)]
2.19 Scholarship (Education) [Section 10 (16)]
2.20 Daily Allowances to Parliament Members [Section 10 (17)]
2.21 Income or Pension of Gallantry Award [Section 10 (18)]
2.22 Income or Amount of Award given by Government [Section 10 (19)]
2.23 Income of Local Authority [Section 10 (20)]
2.24 Income of sports Association [Section 10 (21)]
2.25 Income of Educational Institute [Section 10 (22)]
2.26 Income of Medical Institute [Section 10 (23)]
2.27 Income of Minor [Section 10 (32)]
2.28 Dividend from Indian Company [Section 10 (34)]
2.29 Interest on Mutual Fund [Section 10 (35)]
2.30 Key Concepts
2.31 Summary
2.32 Exercise
2.33 Further Reading and References

CHECK YOUR PROGRESS

Describe the provisions of Agricultural Income?

2.0 Introduction

Certain exemptions are given by Income Tax Act which also known as direct exemptions. Section 10 of Income Tax is exemption section.

2.1 Objectives

After reading this unit, you should be able :

1. To understand direct exemption from Income Tax.
2. To make aware about exemption limit of Income Tax.
3. To know about allowances and their exemption limit.

2.2 Exemption [Section 10]

Items given in Section 10 gives exemption from income, so called as exempted section.

2.3 Agricultural Income [Section 10 (1)]

In India, Agricultural Income is total exempted because Constitution of India does not give any power to charge tax on agricultural income.

Section 2 (1A) defines Agricultural income and it includes :

1. Any amount or revenue derived from land.
2. Any income from process which make prouse marketable.
3. Any income from farm house.

The detail explanation of above is as follows :

1. Income derived from land : Any income received from land if fulfill following three conditions is agricultural income.

i. Income derived from land.

ii. Land must be situated in India.

iii. Agricultural activity must be carried on it.

Agricultural activity by farmer is important to find out whether such income is agricultural or not. Agricultural activity includes leveling, digging, sowing, irrigating, fertilizing, pesticiding, cutting and polishing.

Any income due to natural process for which agricultural activity is not carried on is not agricultural income.

Dairy, poultry, fishery, are activity related to agriculture but income from it is not agricultural income.

2. Any process to make prouse marketable: Prouse means raw crop. Any process carried on for making prouse marketable is agricultural activity and income derived from it is agricultural income.

3. Income from farm house: House in a farm is farm house and income from it is agricultural income. Any house become farm house if following three conditions are satisfied :

(i) House must be immediate vicinity of agricultural land.

(ii) That house is used for dwelling or storing of material.

(iii) That house is not within 8 km from urban area.

Urban area means a place where the population exceeds 10,000.

Only above three income are treated as agricultural income and which is exempted from tax.

2.3.1 Alternative Tax on Agricultural Income:

A separate method is used to find out alternative tax on agricultural income. Alternative tax is applicable when following two conditions are satisfied:

(i) Agricultural income of an assessee must exceeds 5,000 and

(ii) Other than agricultural income must exceed exemption limit.

CHECK YOUR PROGRESS

What is Alternative Tax on Agricultural Income?

NOTES

[according to class of assessee) - General Assessee - 2,50,000 and Senior Citizen - 3,00,000.

When both aforesaid conditions are satisfied then alternative tax can find out by using following three steps :

Step I : Take addition of agricultural income with other than agricultural income and find out tax agricultural + Other income.

Step II : Take addition of agricultural income with exemption limit.

Exemption limit + Agricultural Income

Step III : Alternative tax is equal to tax under Step I - Tax under Step II.

Alternative tax = Tax I ? Tax II

PROBLEMS

Problem 1:

Mr. Hari, a farmer whose agricultural income was 1,50,000 and income from other sources 2,40,000 then calculate for alternative tax.

Solution :

(i) Agricultural income must exceeds 5,000 and

(ii) Other than agricultural income must exceeds exemption limit.

i.e. Rs.2,50,000 but here Non-agricultural income does not exceeds exemption limit.

Hence both conditions are not satisfied. So, alternative tax is not aplicable.

Problem 2:

Miss Leena is a agriculturist gets 2,00,000/- as agricultural income and 1,70,000 as income from other sources. Find out alternative tax on agricultural income.

Solution :

For Alternative Tax :

(i) Agricultural income must exceed 5,000.

(ii) Other than agricultural income must exceed exemption limit.

Miss Leena gets 2,00,000 as agricultural income which exceeds of 5,000.

But her income from other sources is 1,70,000 which does not exceed exemption limit 2,50,000.

Hence, both conditions are not satisfied. So alternative tax is not applicable.

Problem 3:

Ramu 64 years old gets 2,00,000 as agricultural income and 5,00,000 as income from other source. Find out alternative tax on agricultural income.

Solution :

For Alternative Tax :

(i) Agricultural income must exceed 5,000 and

(ii) Other than agricultural income must exceed exemption limit.

Ramu satisfies both the conditions so alternative tax is applicable.

Step I :

Agricultural Income + Other Income

= 2,00,000 + 5,0,000

= 7,00,000

Particulers	Rate	Tax
1st 3,00,000	Nil	
Next 2,00,000	10%	20,000
Next 2,00,000	20%	40,000
Total		**60,000**

Step II :

Exemption Limit + Agricultural Income
= 3,00,000 + 2,00,000
= 5,00,000

Particulers	Rate	Tax
1st 3,00,000	Nil	
Next 2,00,000	10%	20,000
Total		**20,000**

Step III :

Alternative Tax = Tax I - Tax II
= 60,000 - 20,000
= 40,000.

Alternative Tax 40,000.

2.4 Income to Family Member from HUF [Section 10 (2)]

According to constitution doubled taxation strictly prohibited. HUF is separate assessee and they have to pay tax on their income. After payment of tax if remaining amount is distributed among family members is totally exempted in the hand of family member because doubled taxation is not allowed.

2.5 Profit or Income to Partners from Partnership Firm [Section 10 (2A)]

In India, double taxation strictly prohibited. Partnership firm is separate assessee. If firm paid tax on profit of partnership firm and remaining amount distributed among partners is totally exempt.

2.6 Interest on Investment by Foreigner [Section 10 (4)]

Any interest on investment by foreigner in ?
1. Government Securities
2. Government Bond.

3. Any amount credited into RBI is totally exempt from income tax.

NOTES

2.7 Leave Travel Concession (LTC) [Section 10 (5)]

Any amount paid by employer for traveling within India for employee and their family members are allowed as exemption.

Such exemption is only for traveling expenses of shortest route (journey) between two places. If employer paid lodging and boarding charges they are not exempted under the act. For different travel conveyance exemption is,

Bus	-	Volvo ticket
Train	-	A.C. first class
Ship	-	Normal ticket
Air	-	Economy ticket

Such exemption is allowed ones in 4 year.

CHECK YOUR PROGRESS

Give the Provisions of LTC?

2.8 Income of Foreigner [Section 10 (6)]

Any income of foreigner in India is exempt from tax if his stay in India is not more than 90 days. Such rule is applicable to crew (captain of the ship), to research student and foreign players.

2.9 Allowances paid outside India [Section 10 (7)]

Any allowances paid outside India to employee of India for their services as co-operative assistance agreement is totally exempt in India.

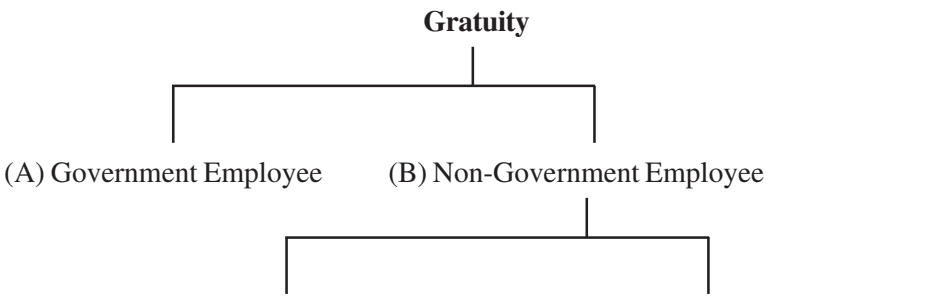
2.10 Income of Foreign Employee for Services Under Co-Operative Programme [Section 10 (8 & 9)]

Any person who provides services in India under co-operative assistance programme is totally exempted under Section 10 (8 and 9).

2.11 Gratuity [Section 10 (10)]

Gratuity means award or reward given by employer to employee on retirement for their continuous service. Gratuity is lumpsum amount which given by employer to employee on retirement.

Exemption of Gratuity is classified under two heads :



NOTES

(A) Government Employee :

Any person who provide services under Central Government, State Government or local authority is Government Employee.

For Government Employee 100% exemption to gratuity is applicable.

(B) Non-Government Employee :

(i) Gratuity Act, 1972 is applicable : An employer other than specified above is non-government employee. Gratuity Act, 1972 is applicable to any organisation where more than 10 employees are working. When Gratuity Act, 1972 is applicable the exemption is least of following three :

1. 15/26 x Last drawn salary x Number of yrs completed (consider fraction)
2. 10,00,000.
3. Actual Gratuity Received.

For this calculation,

Salary = Basic + D.A. (forming part)

CHECK YOUR PROGRESS

Give the Provisions of Gratuity?

* For D.A. forming part portion or retirement benefit part is not given then D.A. is not forming part.

For finding completed years fractions have to be considered. If service is in month and equal to or below 6 months then earlier year considered for calculation.

If service provide in months is more than 6 months then next year is considered for calculation.

Example :

1. 24 years and 4 months = 24 years.
2. 23 years and 6 months = 24 years.
3. 28 years and 6 months and 15 days = 29 years.
4. 31 years, 11 months = 32 years.

(ii) If Gratuity Act, 1972 is not applicable -

Exemption is list of following three.

1. ½ Average Salary x Completed years only.
2. 10,00,000.
3. Actual gratuity receive.

Here, average salary means last 10 months average.

When all emoluments are constant, average calculation is not required.

Salary = Basic + D.A. (Forming part) + % Commission on turnover

Completed years means Fraction not to be consider.

e.g. 24 years 4 months - 24 years.
24 years 6 months - 24 years.
24 years 11 months - 24 years.

Problem 2.1:

Mr. X working with ABC Co. retire on 31st December, 2010 after completing a service of 25 years and 10 months. On retirement he receive 2,90,000 as gratuity.

His salary details are as follows :

Basic	8,000 per month
Dearness Allowance (D.A.)	2,000 per month (75% forming part)
Bonus	10,000 per annum

Commission	3,000 per month
Other	2,000 per month

Find out exemption under Section 10 (10) for Gratuity Act, 1972 is applicable.

NOTES

Solution :

X is non-government employee.

Exemption is least of following three :

1. 15/26 Last drawn salary x Number of years completed (consider fraction)

2. 10,00,000.

3. Actual Gratuity Received

Here, Salary = Basic + D.A. (forming part)

(i) Salary = 8,000 + 75% of 2,000

= 8,000 + 1,500

= 9,500

(ii) Number of years completed = 25 years and 10 month

i.e. 26 years

1. 15/26 x 9,500 x 26

= 1,42,500.

2. 10,00,000.

3. 2,90,000

Least amount is 1,42,500. So exemption u/s 10 (10) is 1,42,500.

Gratuity Received	2,90,000
Less : Exempt	1,42,500
Taxable Gratuity	**1,47,500**

Taxable Gratuity 1,47,500

Problem 2.2:

Mr. X retired from Excellent Co. where Gratuity Act, 1972 is applicable. He retires after completion of service of 29 years 5 months. On retirement he get gratuity 4,50,000. On retirement his salary is as follows :

Basic Salary	15,000 p.m.
D.A.	4,000 p.m.
(75% not forming part)	
Commission	2,000 p.m.
Other	3,000 p.m.

Find out gratuity exemption u/s 10 (10).
Is your answer any different, if X is Government employee?

Solution :

Mr. X is non-government employee.
Gratuity Act, 1972 is applicable.
Exemption u/s 10 (10) is least of following three :

1. 15/26 x Last drawn salary x Number of years completed (consider fraction)

2. 10,00.000.

3. 4,50,000 (Actual gratuity received.)

(i) Salary = Basic + D.A. (forming part)

= 15,000 + ` 1,000

= 16,000

(ii) Number of years completed = 29 years 5 months i.e. 29 years.

1. 15/26 x 16,000 x 29 = 2,67,692

2. 10,00,000.

3. 4,50,000 (Actual received).

Least amount is 2,67,692

Gratuity Received	4,50,000
Less : Exempt	2,67,692
Taxable Gratuity	**1,82,308**

Taxable Gratuity 1,82,308

If X is Government employee then u/s 10 (10) gratuity received to Government employee is 100% exempted. So amount received 4,50,000 to Mr. X as gratuity is totally exempted.

Problem 2.3:

Mr. X working with Pragati Ltd., Pune for 30 years and 10 months and retired on 31st July, 2009. On retirement he gets 4,30,000 as gratuity.

On retirement his salary details are as follows :

Basic	12,500 p.m.
D.A.	5,500 p.m. (100% forming part)
Bonus	20,000 p.a.
Commission	600 p.m.

Find out exemption u/s 10 (10) when,

(1) Mr. X working where Gratuity Act, 1972 is applicable.

(2) Mr. X is Government employee.

Solution :

(1) Mr. X is non-Government employee and Gratuity Act, 1972 is applicable :

Exemption u/s 10 (10) is least of following three :

1. 15/26 x Last drawn salary x Number of yrs completed (consider fraction)

2. 10,00,000.

3. Actual gratuity received.

(i) Salary = Basic + D.A. (forming part)

= 12,500 + 5,500

= 18,000

(ii) Number of years completed = 30 years and 10 months i.e. 31 years

1. 15/26 x 18,000 x 31 years

= 3,21,923.

2. 10,00,000.

3. Actual gratuity received 4,50,000.

Least amount is 3,21,923.

NOTES

	Gratuity Received	4,30,000
Less :	Exempt	3,21,923
	Taxable Gratuity	**1,08,077**

Taxable Gratuity 1,08,077

(2) If X is Government Employee :

Under Section 10 (10) gratuity received to Government employee is 100% exempted so amount received ` 4,30,000 to Mr. X as gratuity is totally exempted.

(ii) When employee is non-government and Gratuity Act, 1972 is not applicable :

Exemption is least of following three :

1. ½ x Salary last drawn x Completed years service only
2. 10,00,000.
3. Actual gratuity received

Here, Salary = Basic + D.A. (forming part) + % commission on turnover.

Problem 2.4:

Mr. X retired on 31st December 2009 after completion of service 26 years and 10 months on retirement he gets gratuity 5,50,000. His salary emoluments are:

Basic	12,000 p.m.
D.A.	5,000 p.m. (60% forming part)
Commission	4,000 p.m.
% Commission	2,000 p.m.
Bonus	25,000 p.a.

Find out exemption under section 10 (10) if ?

(i) X is Government employee.

(ii) X is non-government employee and Gratuity Act, 1972 is applicable.

(iii) X is non-government employee and Gratuity Act, 1972 is not applicable.

Solution :

(i) X is Government employee :

For Government employee any gratuity received on retirement is totally exempt. So amount received as gratuity ` 5,50,000 is totally exempted.

(ii) X is non-government employee and Gratuity Act, 1972 is applicable :

Exemption is least of following three :

1. 15/26 x Last drawn salary x Number of years provide (consider fraction)
2. 10,00,000.
3. Actual Gratuity received

Here, Salary = Basic + D.A. (forming part)
= 12,000 + 3,000 (60% of 5,000)
= 15,000

Number of years service provided = 26 years and 10 months i.e. 27 years.

1. 15/26 x 15,000 x 27 years
= 2,33,654
2. 10,00,000

3. Actual received 5,50,000

Least amount is 2,33,654

	Gratuity received	5,50,000
Less :	Exempted	2,33,654
	Taxable Gratuity	**3,16,346**

Taxable Gratuity 3,16,346

(iii) X is non-government employee and Gratuity Act, 1972 is not applicable:

Exemption is least of following three :

1. ½ x Last drawn salary x Completed years only

2. 10,00,000

3. Actual received

Here, Salary = Basic + D.A. (forming part) + % commission

= 12,000 + 3,000 (60% of 5,000) + ` 2,000

= 17,000

Number of years service provided = 26 years and 10 months i.e. 26 years.

1. ½ x 17,000 x 26 years

= 2,21,000

2. 10,00,000.

3. Actual received 5,50,000.

	Least amount is 2,21,000	
	Gratuity received	5,50,000
Less :	Exempted	2,21,000
	Taxable Gratuity	**3,29,000**

Taxable Gratuity Rs. 3,29,000

2.12 Commuted Pension [Section 10 (10 A)]

Any monthly amount received to employee from employer is pension which is always taxable in the hands of employee whether government or not.

Exemption u/s 10 (10A) is related to commuted pension. Commuted pension is lumpsum payment in lieu of periodical payment of pension.

Exemption is as follows :

1. **Government Employee :** In case of government employee total value of commuted pension is exempted.
2. **Non-government employee and gratuity received:** If commuted pension received to non-government employee and he also gets gratuity, exemption is 1/3 of full value of pension.
3. **Non-government employee and gratuity not received:** Exemption is 1/2 of full value of pension.

Problem 2.5:

Mr. X retired from ABC Co. and gets 2,40,000 as 40% commuted pension. Find out exemption u/s 10 (10A) if :

1. X is Government employee.

2. X is non-government employee and gets gratuity 1,50,000.

NOTES

3. X is non-government employee and no gratuity received.

Solution :

1. X is Government employee :

In case of Government employee full value of commuted pension is exempted u/s 10 (10A) so amount received 2,40,000 is totally exempted.

2. X is non-government employee and gratuity received :

Exemption is 1/3 of full value of pension.

Full value is

40% = 2,40,000
100% = ?
2,40,000 / 40 x 100
= 6,00,000

	Commuted pension received	2,40,000
Less :	Exempted u/s 10 (10A)	2,00,000
	1/3 of 6,00,000	
	Taxable Pension	**40,000**

Taxable Pension 40,000

CHECK YOUR PROGRESS

Give the Provisions of Commuted Pension?

3. X is non-government employee and no gratuity received :

Exemption is 12 of full value of pension.

Full value 6,00,000.

	Commuted pension received	2,40,000
Less :	1/2 of 6,00,000	3,00,000
	Taxable Pension	-

Taxable Pension Nil

Problem 2.6:

Mr. X retired from ABC Co. after completion of service of 28 years 10 months on retirement 70% commuted pension received 3,50,000. Find out exemption u/s 10 (10A) if :

1. X is Government employee.
2. X is non-government employee and gratuity received.
3. X is non-government employee and gratuity not received.

Solution :

1. X is Government employee :

For government employee any amount of commuted pension received is totally exempted. So amount received 3,50,000 is exempted.

2. X is non-government employee and gratuity received :

Exemption is 1/3 of full value of commuted pension.

Full value is,

70% = 3,50,000
100% = ?
= 3,50,000 / 70 x 100
= 5,00,000

Commuted pension received	3,50,000
Less : Exemption u/s 10 (10A)	1,66,667
[1/3 of 5,00,000]	
Taxable Pension	**1,83,333**

Taxable Pension 1,83,333

3. X is non-government employee and gratuity not received :

Exemption is 1/2 of full value of commuted pension.

Full value 5,00,000.

Commuted pension received	3,50,000
Less : Exemption u/s 10 (10A)	2,50,000
1/2 of 5,00,000	
Taxable Pension	**1,00,000**

Taxable Pension 1,00,000

Exemption u/s 10 (10A) is applicable to commuted pension only. Any monthly pension received is fully taxable.

2.13 Leave Encashment [Section 10 (10AA)]

Leave encashment means sale of leave credited during the service. If such leave encashment is in continuation of service, it is 100% taxable. But when leave encashment is at retirement, the exemption is available to following criteria :

1. Government employee: Any leave encashment received to government employee on retirement is totally exempt.

2. Non-government employee: Any leave encashment received to non-government employee is exempted least of following four :

1. Number of days credit / 30 days x Average salary
2. 10 x Average salary
3. 3,00,000
4. Actual leave encashment received

Here, salary is Basic + DA (forming part) + % commission on turnover.

* Maximum number of days allowed to credit 30 days every year.

Problem 2.7

Mr. X retired from ABC Co. on 31st December, 2009. On that day his leave account show credit balance 225 days. He sold the leave ` 2,90,000 and salary details are as follows :

Basic	14,000 p.m.
D.A.	4,000 (75% forming part)
Bonus	30,000
Commission	2,000 p.m.

NOTES

Find out exemption u/s 10 (10AA) if :

1. X is Government employee.

2. X is not government employee.

Solution :

1. X is Government employee :

For government employee any amount received on retirement is totally exempt. So amount received 2,90,000 is fully exempted.

2. X is non-government employee :

For non-government employee exemption is least of following four :

(i) Number of days credited / Average salary x 30 days

(ii) 10 x Average salary

(iii) 3,00,000.

(iv) Actual leave encashment received.

Salary = Basic + D.A. (forming part) + % Commission

= 14,000 + 3,000

= 17,000

Exemption is,

(i) 225 / 30 x 17,000 = 1,27,500

(ii) Average salary x 10

17,000 x 10 = 1,70,000

(iii) 3,00,000

(iv) 2,90,000

Least amount is 1,27,500. So exempted.

Actual leave encashment received	2,90,000
Less : Exemption u/s 10 (10AA)	1,27,500
Taxable Leave Encashment	**1,62,500**

Taxable Leave Encashment 1,62,500

Problem 2.8:

Mr. John retired from XYZ Co. On retirement leave credited 75 days which he sold for 1,50,000. On retirement his salary details are as follows :

Basic	12,000 p.m.
D.A.	2,000 p.m. (40% not forming part)
Commission	600 p.m.
% Commission	400 p.m.
Fees	300 p.m.
Other	800 p.m.

Find out exemption u/s 10 (10 AA) if :

1. John is government employee.

2. John is non-government employee.

Solution :

1. John is Government employee :

For government employee any amount received on retirement is totally exempt.

2. John is non-government employee :

For non-government employee exemption is least of following four :

(i) Number of days credit / 30 x Average salary

(ii) 10 x Average salary

(iii) 3,00,000.

(iv) Actual Leave Encashment Received

Salary = Basic + D.A. (forming part) + % Commission
= 12,000 + 1,200 + 400
= 13,600

Exemption is :

(i) 75 / 30 x 13,600 = 34,000.

(ii) 10 x 13,600 = 1,36,000.

(iii) 3,00,000

(iv) 1,50,000

Least amount is 34,000. So exempt :

Actual leave encashment received	1,50,000
Less : Exemption u/s 10 (10AA)	34,000
Taxable Leave Encashment	**1,16,000**

Taxable Leave Encashment 1,16,000

2.14 Any Amount Received from Providend Fund [Section 10 (11)]

Any amount received to employee on retirement from Statutory Provident Fund (SPF) is totally exempted in the hands of any person. (No criteria of government or non-government employee).

2.15 Any Amount Received from Super Annuation Fund [Section 10 (13)]

Any amount received on retirement from super annuation fund is totally exempted to any person.

2.16 House Rent Allowance (HRA) [Section 10 (13A)]

Allowance means extra amount received for specific purpose. Normally, allowance is given in addition to salary. House Rent Allowance is given for payment of house rent at business place. For this exemption, assessee classified under two heads :

1. BCDM Criteria :

If a person working at Mumbai, Kolkata, Delhi and Chennai (Metropolitan Cities) then, exemption is least of the following three :

(i) 50% of salary.

(ii) Actual rent paid - 10% of salary.

(iii) Actual H.R.A. received.

NOTES

For this calculation,

Salary = Basic + D.A. (forming part) + % Commission

In following two conditions, H.R.A. exemption is not applicable.

1. When person reside in his own house.

2. When calculation in 2 [Actual Rent paid - 10% of Salary] gives negative answer.

2. Other than BCDM :

When person reside other than BCDM, then exemption for H.R.A. is least of following three:

(i) 40% of salary.

(ii) Actual Rent paid - 10% of salary.

(iii) Actual H.R.A. received.

Here, Salary is Basic + D.A. (forming part) + % Commission

In following two conditions, exemption is not applicable.

1. If person reside in his own house.

2. Answer of calculation 2 (Actual rent paid ? 10% of salary is negative).

The exemption of Section 10 (13A) is depend on the place of work, not where the worker is reside.

CHECK YOUR PROGRESS

Give the Provisions of HRA?

Problem 2.9:

Mr. W working with Pragati Ltd., Pune. His salary details are as follows :

Basic	20,000 p.m.
D.A.	2,000 p.m. (100% forming part)
Bonus	50,000
Commission	3,000 p.m.
H.R.A.	4,000 p.m.
Actual Rent Paid	5,000 p.m.

Find out exemption u/s 10 (13A).

Solution :

Mr. X working at Pune. So other than BCDM. Exemption is least of following three :

1. 40% of salary.

2. Actual Rent paid - 10% of salary.

3. Actual H.R.A. received.

Here, Salary = Basic + D.A. (forming part) + % Commission

= (20,000 12) + (2,000 12)

= 2,40,000 + 24,000

= 2,64,000

Exemption :

1. 40% of 2,64,000 = 1,05,600			1,05,600
2. Actual Rent Paid (5,000 x 12)		60,000	
Less : 10% of 2,64,000		26,400	
			33,600
3. Actual H.R.A. received (4,000 x 12)			48,000

Least amount is 33,600. So exempt.

Actual H.R.A. received (4,000 12)	48,000
Less : Exemption u/s 10 (13A)	33,600
Taxable Amount	**14,400**

Taxable amount 14,400

Problem 2.10:

Mr. X working with ABC Co. Mumbai from last 5 years. His residency place is Thane. He gets following salary :

Basic	12,000 p.m.
D.A.	3,000 p.m.
(50% forming part)	
Commission	500 p.m.
% Commission	1,000 p.m.
Other	3,000 p.m.
H.R.A.	4,000 p.m.
Actual Rent Paid	4,500 p.m.

Find out exemption u/s 10 (13A).

Solution :

X is working with ABC Co. Mumbai. So BCDM criteria and exemption is least following three :

1. 50% of salary.
2. Actual rent paid - 10% of salary.
3. Actual H.R.A. received.

Salary = Basic + D.A. (forming part) + % Commission

= 1,44,000 + 18,000 + 12,000

(12,000 x 12) (3,000 x 12 x 50%) + (1,000 x 12)

= 1,74,000

Exemption is :

1.	50% of 1,74,000			87,000
2.	Actual Rent Paid (4,500 x 12)		54,000	
	Less : 10% of 1,74,000	17,400	36,600	
3.	Actual H.R.A. received (4,000 x 12)			48,000
	Least amount is 36,600. So exempt.			36,600

Actual H.R.A. received	48,000
Less : Exemption u/s 10 (13A)	33,600
Taxable Amount	**11,400**

Taxable amount 11,400

2.17 Special Allowance [Section 10 (14)]

Any amount received for special purpose in addition with salary is special allowance and exemption is depend upon two types :

1. Exemption depend upon actual expenditure :

NOTES

Under this head six items are considered and exemption is actual expenditure incurred for that purpose. These items are :

i. Travelling Allowance
ii. Transfer Allowance
iii. Daily Allowance
iv. Helper Allowance
v. Research Allowance
vi. Washing or Dress Allowance.

2. Standard Exemption :

This exemption does not depend upon expenditure but certain specific amount fixed by government allowed as deduction.

(i) Children Education Allowance: Exemption is 100 p.m. per child upto maximum two children.

How much received must be compared with standard.

(ii) Children Hostel Allowance: Exemption is actual allowance received or 300 p.m. per child upto maximum two children.

(iii) Transport Allowance: Any amount paid to driver or cleaner for specific journey and exemption is least of following two :

70% of allowance or 10,000 p.m. which is lower or less.

(iv) Conveyance Allowance :

(a) In case of normal person maximum exemption is 800 p.m.

(b) In case of abnormal person (handicapped, blind etc.) maximum exemption is 1,600 p.m.

(v) Special compensatory hilly allowance : Exemption is varied from 300 to 7,000 per month.

(vi) Boarder Area Allowance : Exemption is upto 700 per month.

(vii) Underground Allowance : Exemption is limited upto 800 per month.

(viii) Tribal area or Scheduled area allowance : Exempted from tax upto 200 per month.

CHECK YOUR PROGRESS

What are Special Allowances?

2.18 Interest on Specific Securities [Section 10 (15)]

Any securities issued by Central Government, State Government or combination of both governments then interest on it totally exempted from income tax.

2.19 Scholarship (Education) [Section 10 (16)]

Any amount received as education scholarship is totally exempted from tax whether such amount used for education or not.

2.20 Daily Allowances to Parliament Member [Section 10 (17)]

Any daily allowances received to state legislative or parliament member is totally exempted from tax.

2.21 Income or Pension of Galantri Award [Section 10 (18)]

Any gallantry award such as Veer Chakra, Paramveer Chakra or any related to defence is totally exempt. Exemption is for :

(i) Award amount

(ii) Pension

(iii) Family pension.

NOTES

2.22 Income or Amount of Award Given by Government [Section 10 (19)]

Any award given by Central or State Government such as 'Bharat Ratna, 'Padmashri' etc. then any amount received as award is totally exempted.

2.23 Income of Local Authority [Section 10 (20)]

Any income of local authority i.e. municipal corporation, gram panchayat is totally exempted. Only one income is chargeable if they sold water to any other local authority.

2.24 Income of Sports Association [Section 10 (21)]

Any organisation or association which create or form for promotion of sport then any income received is totally exempted from tax.

2.25 Income of Educational Institute [Section 10 (22)]

Any institute which form for promotion of educational facility is totally exempted under act. Any amount received to such institute is exempt.

2.26 Income of Medical Institute [Section 10 (23)]

Any amount received to medical institute or organisation who form for the promotion of medical knowledge is totally exempt.

2.27 Income of Minor [Section 10 (32)]

Any income of minor (not completed age of 18) is taxable under the Act.

Any income due to skill of minor then exemption is 1,500 and remaining amount taxable.

When income received to minor without any skill is added to income of father or mother whose income is more.

2.28 Dividend from Indian Company [Section 10 (34)]

Any dividend given by Indian company to shareholder after 1-4-2003 is totally tax free because on that dividend company pays tax on it.

2.29 Interest on Mutual Fund [Section 10 (35)]

Any interest on mutual fund units is totally exempted after 1-4-2003.

NOTES

2.30 Key Concepts

Certain exemptions are given by Income Tax Act which also known as direct exemptions. **Section 10 of Income Tax is exemption section.**

In India, **Agricultural Income** is total exempted because Constitution of India does not give any power to charge tax on agricultural income.

2.31 Summary

Section 10 of Income Tax Act, 1961 is related with Exempted Income. Exempted income is that income on which the income tax is not chargeable. According to Section 10 (1) Agricultural Income is totally exempted. Income to family member from HUF, profit or income to partners from partnership firm, leave travel concession, interest on investment by foreigners are such exempted income. For Gratuity [Section 10 (10)] and commuted pension [Section 10 (10A)], there are two criteria i.e. government employee and non-government employee. Leave encashment [Section 10 (10AA)] means sale of leaves credited during the service. For this also the criteria of government and non-government is applicable. House Rent Allowance [Section 10 (13A)] is given for payment of house rent at business place. For calculation of HRA BCDM criteria is applicable. Some special allowances like traveling, transfer, daily, helper, research and washing allowance exemption depends upon actual expenditure. So for calculation of taxable income, Section 10 is very important.

2.32 Exercise

1. Give short notes on:
   (a) Agricultural Income
   (b) Alternative Tax on Agricultural Income
   (c) Gratuity
   (d) Commuted Pension
   (e) Leave Encashment
   (f) House Rent Allowance
2. Give any ten items which are exempted from tax u/s 10.

- **Fill in the blanks**

1) _____ is total exempted because Constitution of India does not give any power to charge tax on agricultural income.

   (Salary, Agricultural Income, Pension, Gratuity)

2) House in a farm is _____ and income from it is agricultural income.

   (Guest house, Tent house, farm house, agricultural house)

3) A separate method is used to find out _____ on agricultural income.

   (alternative tax, direct tax, indirect tax, optional tax)

4) For Alternative Tax Agricultural income must exceed _____and other than agricultural income must exceed exemption limit.

   (10000, 5000, 50000, 200000)

NOTES

5) Any amount distributed among family members of HUF is totally _____ in the hand of family member because doubled taxation is not allowed.

(exempted, taxable, chargeable, grantable)

6) Any allowances paid outside India to _____ of India for their services as co-operative assistance agreement is totally exempt in India.

(employer, resident, employee, person)

7) _____means award or reward given by employer to employee on retirement for their continuous service.

(Pension, Salary, Gratuity, Compensation)

8) For Government Employee _____exemption to gratuity is applicable.

(10%, 100%, 50%, 25%)

9) _____is lumpsum payment in lieu of periodical payment of pension.

(Commuted pension, Salary, Gratuity, Compensation)

10) If commuted pension received to non-government employee and he also gets gratuity, exemption is _____ of full value of pension.

(1/3, 25%, 1/2, 1/4)

11) When person reside other than BCDM, then exemption for H.R.A. is least of ___ of salary, actual Rent paid - 10% of salary or actual H.R.A. received.

(40%, 50%, 100%, 60%)

12) Any amount paid to driver or cleaner for specific journey and exemption is least 70% of allowance or _____ p.m. which is lower or less.

(800, 10000, 6000, 5000)

13) Any income due to skill of minor then exemption is _____and remaining amount taxable.

(2000, 1500, 3000, 4500)

(**Answers:** 1) Agricultural Income, 2) farm house, 3) alternative tax, 4) 5000, 5) exempted, 6) employee, 7) Gratuity, 8) 100%, 9) Commuted pension, 10) 1/3, 11) 40%, 12) 6000, 13) 1500)

2.33 Further Reading and References

1) Students Guide To Income Tax by Vinod Singhania
2) Taxman
3) Income Tax Bare Act

UNIT 3
INCOME FROM SALARY

NOTES

3.0 Introduction
3.1 Objectives
3.2 Income from Salary
3.3 Salary Chargeable Basis [Section 15]
3.4 Allowances and their Taxability
3.5 Perquisites and their Valuation [Section 17 (2)]
- 3.5.1 Perquisites
- 3.5.2 Gift by Employer to Employee
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- 3.5.10 Loan at Lower Rate
- 3.5.11 Cook, Gardner, Watchman, Servant provided by Employer and Salary paid by Employer
- 3.5.12 Any Obligation of Employee
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- 3.5.14 Car provided by Employer to Employee
- 3.5.15 Other Vehicles (Motor cycle, Scooter or any other Conveyance is provided by the Employer)
- 3.5.16 Transport Facility by a Transport undertaking (not being provided by Railways or by an Airlines)
- 3.5.17 Travelling and Touring Accommodation
- 3.5.18 Valuation of Perquisites

3.6 Deduction u/s 16
3.7 Different Meaning of Salary for Different Purposes
3.8 Key Concepts
3.9 Summary
3.10 Exercise
3.11 Further Reading and References

3.0 Introduction

Any amount received from employer is chargeable to tax under the head 'Income from Salary'.

3.1 Objectives

After reading this unit, you should be able :

1. To understand chargeability of salary.
2. Be clear about allowances and perquisites.
3. To know about diductions from salary and calculations.

3.2 Income from Salary

Salary:

Any amount paid by employer to employee for contribution of service after specific interval is known as 'salary'. Salary is remuneration for continuous service provided. For charging any income under the head of salary the relationship between two person must be employer and employee. Without such relation amount cannot be chargeable under the head salary.

According to Section 17 (1) of Income Tax Act, 1961, salary is inclusive term and it includes :

1. Wages and Salary.
2. Leave Salary.
3. Bonus.
4. Commission.
5. Leave encashment in service.
6. Advance salary.
7. Any allowance.
8. Perquisites.
9. Monthly pension.
10. Gratuity.
11. Annuity etc.

CHECK YOUR PROGRESS

What is Charging Base of Salary?

3.3 Salary Chargeable Basis [Section 15]

Salary always charged on due or receipt which is earlier so any advance salary received chargeable in the year of receipt.

1. Due Basis: Under this principle the income from salary is taxable when it becomes due e.g. salary for the month of March 2016 has become due in 2015-16 but paid in April 2016 will be included in total income of the P.Y. 2015-16.

2. Receipt Basis: Under this principle the income from salary is taxable when it is received by the employee e.g. the salary for the month of March 2016 paid in April 2016 will be included in total income and taxable in theAssessment Year 2016-17.

However, it may be noted that salary once taxed on a particular basis cannot again be taxed on another basis.

3.4 Allowances and their Taxability

Allowances: Allowance means any additional payment by employer to employee for specific purpose.

Allowances may be classified in three groups :

A. Fully taxable allowances.

B. Tax free or fully exempted allowances.

C. Partially exempted allowances.

The tax treatment of different allowances is given below :

(A) Fully Taxable Allowances:

NOTES

The following allowances are fully taxable and so included in the salary income of the assessee.

i. **Dearness allowance:** This is an allowance given on account of high prices and it is always taxable fully.

ii. **Fixed medical allowance:** It is always chargeable to tax.

iii. **Tiffin allowance:** It is taxable.

iv. **City compensatory allowance:** This allowance is given in big city due to high cost of living.

v. **Overtime allowance:** This allowance is given for overtime work.

vi. **Entertainment allowance:** This allowance firstly included in salary and then deduction is allowed u/s 16 (ii).

vii. **Non-practising allowance:** It is given to the doctors employed by the Government.

viii. **Other allowances:** Other allowances are such as project allowance, warden allowance, washing allowance, family allowance, servant allowance, etc.

(B) Tax Free or Fully Exempted Allowance:

The following allowances are fully exempted from tax and so not included in salary income:

i. **Foreign allowance:** This allowance is paid by the Government of India to its citizen employees for being posted outside the country.

ii. **Allowance from U.N.O. paid to its employee.**

iii. **Allowance to High Court Judges:** Any allowance paid to a Judge of High Court and Supreme Court Judge under Section 22A (2) and 23 (B) respectively are not taxable.

(C) Partially Exempted or Partially Taxable Allowance:

Partially exempted allowances means of which some part of it is taxable and some part of it is exempted from tax. The untaxable amount is computed as per the income tax rules and then it is deducted from the amount of allowance actually received. The balance amount is added in salary income.

1. House Rent Allowance [Section 10 (13A)]:

House Rent Allowance is given for payment of house rent at business place. For this exemption, assessee classified under two heads:

i. BCDM Criteria : If a person working at Mumbai, Kolkata, Delhi and Chennai (Metropolitian cities), then exemption is least of following three :

1. 50% of salary.

2. Actual rent paid (-)10% of salary.

3. Actual H.R.A. received

For this calculation,

Salary = Basic + D.A. (forming part) + % Commission

In following two conditions H.R.A. exemption is not applicable:

1. When person reside in his own house.

2. When calculation of 2nd i.e. (Actual Rent paid (-)10% of Salary) gives negative answer.

NOTES

(ii) Other than BCDM criteria : When person reside other than BCDM then exemption for H.R.A. is least of following three :

1. 40% of salary.
2. Actual rent paid (-)10% of salary.
3. Actual H.R.A. received.

Here, Salary = Basic + D.A. (forming part) + % Commission

In the following two conditions, exemption is not applicable.

1. When person reside in his own house.
2. When answer of calculation 2 (Actual Rent paid (-)10% of salary) is negative.

The exemption of Section 10 (13A) is depended on the place of work, not where the worker is reside.

2. Specific/Notified Special Allowances [Section 10 (14)] :

There are certain specific allowances which are exempt either in full or upto certain limit prescribed in the rules. These allowances are of two types :

(A) Special Allowances (Exemption depends upon actual expenditure by the employee) [Section 10 (14) (1)] :

The following allowances are exempt under Section 10 (14) (1) to the extent the amount is utilized or spent for the specified purpose for which the allowance is received.

CHECK YOUR PROGRESS

What are Special Allowances?

i. **Travelling Allowance/Transfer Allowance:** Any allowance granted to meet the cost of travel on tour or on transfer.

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

iii. **Helper Allowance:** The allowance to meet the expenditure on helper.

iv. **Research Allowance:** The allowance granted to encouraging the academic research.

v. **Uniform Allowance:** The allowance to meet the expenditure incurred on the purchase or maintenance of uniform.

vi. **Conveyance Allowance:** Conveyance allowance is granted to meet the expenditure on conveyance in performance of duties of an office. It is exempted from tax. An expenditure for covering the journey between office and residence is not treated as expenditure in performance of duties of the office. So such expenditure is not exempted from tax.

vii. **Vehicle Allowance:** This allowance is granted to meet expenditure incurred for vehicle used for official duties.

(B) Special Allowance to meet the Personal Expenses [Section 10 (14) (2)]

Under this exemption is not depended upon expenditure, but certain specific amount fixed by Government allowed as deduction.

i. **Tribal Area or Scheduled Area Allowance:** Exempted from tax upto 200 per month.

ii. **Allowance for Transport Employees (working in Transport System):** Exemption is 70% of such allowance or 10,000 p.m. which is lower or less.

iii. **Children Education Allowance:** Exemption is 100 p.m. per child maximum upto two children. How much received must be compared with standard.

iv. **Hostel Expenditure Allowance:** Any allowance granted to an employee

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to meet the hostel expenditure on his child. Exemption is actual allowance receive or 300 p.m. per child maximum upto two children.

v. **Transport Allowance:** Transport allowance is granted to an employee to meet his expenditure for covering the journey between the place of his residence and place of his duty. Exemption is :

a. In case of normal person maximum exemption is 800 p.m.

b. In case of abnormal person (i.e. blind or handicapped etc.) maximum exemption is 1,600 p.m.)

vi. **Underground Allowance:** Underground allowance is granted to an employee who is working in underground coal mines.

Exemption is limited upto 800 per month.

vii. **Special Compensatory Hilly Allowance:** Exemption is varied from 300 to 7000 per month.

viii. **Compensatory Field Area Allowance:** Exempt to the extent of 2,600 per month.

CHECK YOUR PROGRESS

Give the Provisions of Gift by Employer to Employee?

3.5 Perquisites and their Valuation [Section 17 (2)]

3.5.1 Perquisites

'Perquisites' is defined as any casual emolument, fees or profits attached to an office or position in addition to salary or wages. Perquisites may be in cash or kind. Perquisites are included in salary income only if they are received by an employee from his employer. All perquisites are not taxable. They are taxable subject to certain exemption and certain limits as provided in the Act and income tax rules.

3.5.2 Gift by Employer to Employee

If gift given by employer to employee in terms of cash or cash convertible then such gifts are 100% taxable.

If gift is given in terms of things or goods then exemption is aggregate 5,000 per year.

Immovable Property Gifted by Employer to Employee after used in office

For charging value of that property, following rules are important:

No.	Particulars	Electronic Items (Computer, Printer, Electronic Diary)	Vehicles (two and four wheeler only)	Other
1.	Rate of depreciation	50%	20%	10%
2.	Method of depreciation	Written Down Value Method	Written Down Value Method	Fixed (Straight Line Method
3.	Year consider	Completed years only	Completed years only	Completed years only

First less depreciation from asset and then add remaining amount in salary in that year when property is gifted.

3.5.3 Medical Facility by Employer

There are four types of medical facility by employer to employee:

i. By appointment of one doctor at factory premises and provide monthly medical facility free of charge. It is 100% exempted from tax.

ii. Give authority to any doctor to provide medical facility to employee and taken medical treatment from him is 100% exempted from tax.

iii. Any expenditure incurred by employer or reimbursement of expenses by employer is exempted maximum upto 15,000.

iv. Medical facility provided outside India is exempted according to limit fixed by RBI. If no limit fixed by RBI then no exemption. For such outside exemption the income of assessee must not exceed 2,00,000 in previous year.

3.5.4 Educational Facility to Children of Employee

Such facility means allow children to take education in employer's institute.

In such a case exemption is 1,000 per month per child and there is no maximum limit of children. For ascertaining taxable portion first find out cost of same education in another institute. If it exceeds 12,000, then exceed portion should be treated as salary of employee.

CHECK YOUR PROGRESS

Give the Provisions of Educational Facility?

3.5.5 Gas, Electricity, Water provide by Employer

All examples are of used in house and for that two possibilities are their:

i. Employer is manufacturer: In such a case, the cost of manufacture treated as salary.

ii. Purchase from other: If such a service purchase from other than actual amount paid to purchase the service is treated as salary and chargeable to tax.

3.4.6 Telephone Bill paid by Employer

Any bill of telephone including mobile is paid by employer on behalf of employee is totally exempted from income tax. So no value adds to salary.

But if telephone bill of office and private use is given separate then office exp. exempt and private exp. taxable.

3.5.7 If Credit Card given

Any expenditure incurred for providing credit card to employee is added to salary.

Expenses incurred by employer	xxxx
Less : Amount recovered from employee	xx
Value of perk (Add to salary) (If it is positive)	xxxx

3.5.8 Facility of Health Club

Any amount paid by employer for providing health club facility is added to value of salary. If any recovery from employee deducted from expenditure incurred by employer.

Expenses incurred by employer	xxxx
Less : Amount recovered from employee _____	xx
Value of perk (Add to salary) (If it is positive)	xxxx

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3.5.9 Snacks or Lunch provide

i. Snacks provide anywhere = Totally exempt.
ii. Lunch provide at remote place = Totally exempt.
iii. Lunch provide in factory or office (normal area) :

Expenditure incurred for lunch	xxx
Less : 50 per lunch	xx
	xxx

3.5.10 Loan at Lower Rate

Any loan given by employer to employee at concessional rate then value of perquisite is

State Bank of India Standard Rate (-) Actual Rate charged by employee.

3.5.11 Cook, Gardner, Watchman, Servant provide by Employer and Salary paid by Employer

Any salary paid by employer to cook, gardener, watchman or servant added to salary of employee.

3.5.12 Any Obligation of Employee

Any obligation of employee borne or paid by employer is 100% taxable.

CHECK YOUR PROGRESS

Give the Provisions of Providend Fund?

3.5.13 Provident Fund

Any fund for providing lumpsum amount on retirement is known as Provident Fund. In India, Provident Fund are classified under three heads :

1. Statutory Provident Fund (S.P.F.)
2. Recognised Provident Fund (R.R.F.)
3. Unrecognised Provident Fund (U.R.P.F.)

For any provident fund following concepts are more important.

i. **Employee's Contribution:** The amount which deducted from salary for provident fund is contribution by employee.

ii. **Employer's Contribution:** The amount which given by employer normally which is equal to employees contribution is employer's contribution.

iii. **Interest on Provident Fund:** Monthly employer and employee contribution deposited into the bank upto retirement of employee and on that amount bank give interest is known as interest on provident fund.

iv. **Maturity Value:** The accumulated value (Contribution + Interest received) on retirement is known as Maturity value.

Particulars	Statutory Provident Fund (S.P.F.)	Recognised Provident Fund (R.P.F.)	Unrecognised Provident Fund (U.R.P.F.)
1. Employer's Contribution	Fully exempt	Exempt upto 12% of salary	For the time being exempt
2. Employee's Contribution	Useful for deduction u/s 80C (Investment)	Useful for deduction u/s 80C (Investment)	Deduction u/s 80C is not applicable.
3. Interest on Provident Fund	Fully exempt	Exempt upto9.5%	For the time being exempt
4. Maturity Value	Fully exempt (100%) U/S 10(11)	Fully exempt (100%)	Half (50%) exempt.

Here, Salary = Basic + D.A. (forming part) + % Commission on turnover

3.5.14 Car provided by Employer to Employee

Value of perquisite for car provide to employee is depend upon ownership of car and maintenance cost bear by whom.

i. If car own by employee and maintenance cost also by employee : In any condition no value should be added to salary of employee.

ii. If car own by employee and maintenance by employer :

1. Fully use for office = No value.

2. Fully use for domestic purpose = Actual maintenance expenditure incurred by employer added to salary.

3. How much portion is used for office is not known :

Car below 1600 cc = 1,800 per month.
Car above 1600 cc = 2,400 per month
If driver or chauffeur is provide = 900 p.m.
Actual Expenses by Employer - Value as per rule.

iii. If car own by employer and maintenance cost also by employer :

1. Use for office purpose = No value.

2. Use for domestic/personal purpose = 10% of value of car + Actual maintenance expenses.

3. How much portion for office is not given :

Car below 1600 cc = 1,800 p.m.
Car above 1600 cc = 2,400 p.m.
If driver or chauffeur is provide = 900 p.m.

iv. If car own by employer and maintenance cost by employee :

1. Use for office. No value.
2. Car use for house = 10% of cost of car.
3. How much portion use for office is not known

Below 1600 cc = 600 p.m.
Above 1600 cc = 900 p.m.
If driver or chauffeur provide = 900 p.m.

3.5.15 Other Vehicles (Motor cycle, Scooter or any other Conveyance is provided by the employer

When employees owns any automotive conveyance (other than car) and running and maintenance charges are met or reimbursed by employer then ?

1. It is used for office = No value.

2. It is used partly for official and partly for private purpose = Actual expenditure incurred by the employer less ` 900 per month or higher sum if certain conditions are satisfied and amount recovered from employee.

3.5.16 Transport facility by a Transport undertaking (not being provided by Railways or by an Airlines)

Valuation = Value at which such benefit is offered to the public ? Amount recovered from the employee (i.e. cost to the employer).

3.5.17 Travelling and Touring Accommodation

Any other expenses paid by employer for any holiday availed by employee or any member of household

Valuation is,

A. Where such facility is available uniformly to all employees.

Valuation = Cost to the employer.

B. Where such facility is not available uniformly to all employees = Value at which such facilities are offered by other agencies to the public.

NOTES

CHECK YOUR PROGRESS

Give the Provisions of Car Provided by Employer?

NOTES

3.5.18 Valuation of Perquisites

Perquisites means allow employee to use the property free of cost or at concessional rate. Normally perquisites are of four types:

1. Rent free accommodation.
2. Furnished Rent free accommodation.
3. Concessional furnished accommodation.
4. Residential accommodation provided at hotel.

In case of Government employee value of perquisite is licence fees which received.

For non-government employee valuation of perquisites is on certain basis.

Salary for perk valuation/Perquisites valuation = Basic + DA (forming part) + Commission + Bonus + Fees + Taxable Allowances + Any money chargeable under the Act.

1. Rent Free Unfurnished Accommodation:

Any flat or house provided by employer to employee free of cost are covered under this head. For such valuation two different criteria's are applicable:

i. **The house which provided owned by employer:** Value of perk consider in salary on the basis of population of that place, where house is provided.

Population	Value of Perk
1. Population exceeds 25 lakhs	15% of salary
2. Population is below 25 lakhs but exceeds 10 lakhs	10% of salary
3. Population is less than 10 lakhs	7.5% of salary

ii. **If employer provide house which is not owned by himself but taken on rented basis :** In this category no population base is applicable and value of perk is ?

15% of salary or

Actual rent paid by employer which is lower or less.

PROBLEM

Problem 3.1:

Mr. X working with Indus Ltd., Chennai whose salary details are :

Basic	20,000 p.m.
D.A.	6,000 p.m. (50% forming part)
Bonus	20,000 p.a.
Commission	1,000 p.m.
Taxable Allowance	600 p.m.

Rent free accommodation at Chennai.

The accommodation provides which is owned by employer.

Find out value at rent free unfurnished accommodation.

Solution :

X is non-government employee.

House provide is owned by employer.

Population is above 25 lakhs.

Salary = Basic + DA (forming part) + Commission + Bonus + Fees + Taxable Allowances + Any Money Chargeable under Act

NOTES

Basic Salary (20,000 x 12)	2,40,000
D.A. (3,000 x 12)	36,000
Bonus	20,000
Commission (1,000 x 12)	12,000
Taxable Allowance (600 x 12)	7,200
	3,15,200

Value of rent free accommodation is 15% of salary.

= 15% of 3,15,200

= 47,280

Value of rent free accommodation 47,280 (15% of 3,15,200).

2. Rent Free Furnished Accommodation :

Accommodation with furniture is known as furnished accommodation. Furnished accommodation is combination of Furniture + Accommodation.

For this calculation first find out value of house as per above and then add the value of furniture in it.

In case of furniture, owned by employer = 10% of original cost of furniture is taken as value.

If furniture is taken on rented basis, then actual rent paid by employer for furniture is treated as cost.

Problem 3.2:

X is employee of PQR Ltd. Salary details are :

Basic	2,00,000
D.A.	40,000 (100% forming part)
Bonus	20,000
Taxable Allowance	12,000

Furnished accommodation provides to X which company purchase on rented basis. Rent paid is 6,000 p.m. House also include a furniture owned by company.

Original cost 45,000 (out of 45,000 a furniture of 15,000 is second hand).

Find out value of rent free furnished accommodation.

Solution :

X is non-government employee.

Flat provided which taken by employer on rented basis.

Value of accommodation is 15% of salary or actual rent paid which is lower or less.

Salary = Basic + D.A. (forming part) + Commission + Bonus + Fees + Taxable allowances + Any money chargeable under the Act

= 2, 00,000 + 40,000 + 20,000 + 12,000

NOTES

= 2,72,000

Value is,

i. 15% of ` 2,72,000 = 40,800.

ii. Actual rent paid 6,000 12 = 72,000.

Least amount is 40,800.

Furniture also provide which is owned by employer.

So 10% of original cost i.e. 10% of 45,000

= 4,500

Value of accommodation	40,800
Add : Value of Furniture	4,500
Value of furnished accommodation	45,300

Furniture - whether new or second hand is immaterial.

Value of rent free furnished accommodation 45,300.

CHECK YOUR PROGRESS

What are Deduction U/S 16?

3. Furnished Accommodation at Concession :

At concession means not free but minimum charges are recovered from employee. To find out the value of this, following steps are important.

Step - I : Find out value of house as per above.

Step - II : Find out value of furniture as per above.

Step - III : Step I + Step II

Step - IV : Concessional rate means give at minimum rate. Total recovered amount.

Step - V : Step 3 - Step 4.

The answer amount add into salary.

4. Resident facility provided at Hotel :

If employer allow employee to reside at hotel, here maximum 15 days allow to reside at hotel.

1. 24% of salary or
2. Actual amount paid to hotel which is lower or less.

3.6 Deduction U/S 16

In case of salary three different deductions are allowed :

i. Standard Deduction [Section 16 (1)] : Not applicable.

ii. Entertainment Allowance [Section 16 (2)] : If entertainment allowance receive to Government employee then only exemption is allowed least of following three :

1. 20% of basic salary.
2. 5,000.
3. Actual entertainment allowance received. First this allowance add into salary.

If entertainment allowance received first this allowance is added into salary. If entertainment allowance received to other than government employee then 100% taxable.

iii. Professional Tax : Tax for profession or service is professional tax. Exemption is full amount paid as professional tax.

1. If professional tax paid by employer = First add it to salary and then take deduction.
2. If professional tax paid by employee = Take only deduction

3.7 Different Meaning of Salary for Different Purposes

NOTES

1. Rent free house or Concession in rent:

Salary = Basic salary + D.A. (forming part) + Commission + Bonus + Fees + All Taxable Allowances + Any money chargeable under Act

2. House Rent Allowance :

Salary = Basic Pay + D.A. (forming part) + % Commission

3. Qualifying amount for Contribution to R.P.F.:

Salary = Basic Pay + D.A. (forming part) + % Commission (Same as for House Rent Allowance)

4. Entertainment Allowance:

Salary = Basic Salary

5. Gratuity, when 1972 Act not applicable:

Salary = Basic Pay + D.A. (forming part) + % Commission

(Same as for House Rent Allowance)

6. Gratuity Act 1972 is applicable:

Salary = Basic + D.A. (forming part)

* If there is the percentage of forming part is not given then it is assumed that 100% not forming part.

PROBLEMS OF INCOME FROM SALARY

Problem 3.3:

Mr. Milind is employed in a firm of Mumbai and he furnished the following particulars of income for the year 2015-2016.

1. Basic salary 15,000 p.m.
2. Dearness Allowance 6,000 p.m. (Out of this 2,000 p.m. consider for retirement benefits).
3. Bonus 40,000.
4. Entertainment Allowance 1,000 p.m.
5. Interest on R.P.F. at 13% 39,000.
6. Employer's contribution to R.P.F. is 15% of salary.
7. He is provided with furnished accommodation at Mumbai by the employer. Cost of furniture is 50,000. Rent paid for accommodation by Mr. Milind is 2,000 p.m.
8. Hospital Bills reimbursed by the employer 12,000.
9. He bas been provided with the facility of sweeper, watchman and servant, who are paid by the employer 1,500 p.m., 1,800 p.m. and 1,700 p.m. respectively.
10. He has been provided with a 1800 cc car for both official and private

purpose. Running and maintenance expenses are borne by the employer.

11. Gas, electricity and water bills paid by employer 12,000.

12. Professional tax paid 2,500.

NOTES

Compute his taxable income from salary for the assessment year 2016-17.

Solution:

Computation of Taxable Income of Mr. Milind from Salary
For the Assessment Year 2016-17

Particulars	Amount	Amount
1. Basic Salary (15,000 12)		1,80,000
2. Dearness Allowance (6,000 12)		72,000
3. Bonus		40,000
4. Entertainment Allowance (1,000 12)		12,000
5. Interest Credited to RPF Balance @ 13%	39,000	
Less : Exempted from tax at 9.5% 39,000 x 9.5% / 13%	28,500	10,500
6. Contribution to RPF at 15% (15% of 2,04,000)	30,600	
Less : Exempted from tax at 12% of salary i.e. 2,04,000 (Note 1)	(-) 24,480	6,120
7. Accommodation of Concessional Rent (Note 2)		19,400
8. Reimbursement of Medical Bill	12,000	
Less : Exempted from tax upto 15,000	(-) 12,000	Nil
9. Domestic Servants		
(a) Sweeper (1,500 12)	18,000	
(b) Watchman (1,800 12)	21,600	
(c) Servant (1,700 12)	20,400	60,000
10. Motor Car perks taxable in the hand of employee w.e.f. A.Y. 2010-11 (Note 3)		28,800
11. Gas, Electricity and Water Bills		12,000
Gross Salary		4,40,820
Deductions (u/s 16)		
1. Standard deduction	N.A.	
2. Entertainment Allowance	N.A.	
(N.A. for private sector employee)		
3. Professional Tax	2,500	(-)2,500
Income from Salary		**4,38,320**

Working Note:

1. Salary for Contribution to R.P.F.:

Salary = Basic Pay + D.A. (forming part) + % Commission
= 1,80,000 + 24,000
= 2,04,000

2. House Accommodation:

House is owned by the employer:

Population of Mumbai is more than 25,00,000, therefore, the valuation = 15% of salary.

Salary = Basic Salary + D.A. (forming part) + Bonus + Commission + Fees + All Taxable Allowances + Any money chargeable under the Act

= 1,80,000 + 24,000 + 40,000 + 12,000

= 2,56,000

Valuation = 15% of Salary i.e. 15% of 2,56,000

= 38,400 (w.e.f. A.Y. 2008-2009)

Valuation of Furniture = 10% of Cost of Furniture

= 10% of 50,000

= 5,000

Valuation with Furniture = 38,400 + 5,000

= 43,400

Valuation with Furniture	43,400
Less : Rent paid (2,000 x 12)	24,000
Value added in the salary	**19,400**

3. Valuation of Motor Car :

As FBT is abolished motor car becomes taxable in the hands of the employee.

i. Car is owned by the employer

ii. Maintenance and running expenses are borned by the employer and

iii. C.C. exceeds 1,600 so,

Valuation = 2,400 x 12 = 28,800

Problem 3.4:

Mrs. Narayani working as 'Accountant' in Super India Ltd. Pune has given you the following details of her emoluments for the F.Y. 2015-2016.

Basic Salary	1,80,000
D.A.	40% of Basic Salary
H.R.A.	10% of Basic Salary
C.C.A.	5% of Basic Salary
Educational Allowance	2% of Basic Salary
Conveyance Allowance	12,000
(for going to office and back to residence)	

Mrs. Narayani has got one son studying in Vth standard. She stays in a rented flat by paying monthly rent 3,000. She is provided with a car of 1200 c.c. for official and personal use.

The entire expenditure of the car is borne by the employer. A chauffeur is also provided with the car. A medical expenditure of 12,500 is reimbursed by the employer.

NOTES

Mrs. Narayani has contributed 35,000 to the recognized Provident Fund. An equal amount is contributed by the employer also. Interest @ 15% has been credited to her recognized Provident Fund account amounting to 13,500.

You are required to compute income taxable under salary of Mrs. Narayani for the A.Y. 2016-2017.

Solution :

Computation of Taxable Income under Salary of Mrs. Narayani
For the A.Y. 2016-17

Particulars	Amount	Amount
1. Basic Salary		1,80,000
2. D.A. (40% of Basic Salary i.e. 40% of 1,80,000)		72,000
3. H.R.A. (10% of Basic Salary)	18,000	
Less : Exempted from Tax (Note 1)	10,800	7,200
4. City Compensatory Allowance (5% of Basic Salary)		9,000
5. Educational Allowance (2% of Basic Salary)	3,600	
Less : Exempted from Tax (100 12 1)	(-)1,200	2,400
6. Motor Car (Note 2)		32,400
7. Conveyance Allowance (Note 3)		12,000
8. Reimbursement of Medical Expenses	12,500	
Less : Exempted upto 15,000	(-)	Nil
	12,500	
9. Employers Contribution to RPF	35,000	
Less : Exempted from tax at 12% of Salary	(-)	
(Note : No.4)	30,240	4,760
10. Interest credited to R.P.F. at 15%	13,500	
Less : Exempted from Tax at 9.5%	(-)8,550	4,950
13,500 x 9.5% / 15%		
Gross Salary		3,24,710
Deductions u/s 16		
1. Standard Deduction	N.A.	
(w.e.f. A.Y. 2006-2007)		
2. Entertainment Allowance	-	
3. Professional Tax	-	-
Taxable Income from Salary		**3,24,710**

Working Notes :

1. H.R.A. :

Mr. Narayani working at Pune. So other than BCDM criteria is applicable. So exemption is least of following three :

(i) 40% of Salary.
(ii) Actual rent paid - 10% of Salary.
(iii) Actual H.R.A. received.

Here, Salary = Basic + D.A. (forming part) + % Commission
= 1,80,000 + 72,000

= 2,52,000

So exemption is,

(i) 40% of salary (40% of 2,52,000)		1,00,800
(ii) Actual Rent paid (3,000 x 12)	36,000	
Less : 10% of Salary (10% of 2,52,000)	(-) 25,200	10,800
(iii) Actual HRA received		18,000

Least amount is 10,800, so exempted from tax.

It is assumed that D.A. is 100% forming part.

2. Motor Car :

Taxable in the hands of employee as FBT is abolished w.e.f. A.Y. 2015-16.

Valuation is,

(i) Car is owned by employer.

(ii) Maintenance and running expenditure are borned by employer.

(iii) Below 1600 cc

(iv) Chauffeur is provided.

Valuation = (1,800 x 12) + (900 x 12)

= 21,600 + 10,800

= 32,400

3. Conveyance Allowance:

This allowance is granted to meet the expenditure on conveyance in performance of duties of an office. An expenditure for covering the journey between office and residence is not treated as expenditure in performance of duties of the office and consequently, such expenditure is not exempt from tax.

4. Employer's Contribution to R.P.F.:

Salary = Basic + D.A. (forming part) + % Commission

= 1.80,000 + 72,000

= 2,52,000

= 12% of 2,52,000

= Rs.30,240

Problem 3.5 :

Mr. Akshay is a General Manager of A Textile Company of Delhi. He has submitted the following particulars of his income for the financial year 2015-2016.

(i) Basic Salary 1,10,000 (Annual).

(ii) D.A. 2,000 per month (500 p.m. enters into retirement benefits).

(iii) Education Allowance for two children at 130 p.m. per child.

(iv) Commission on Sales 20,000.

(v) Entertainment Allowance 800 p.m.

(vi) Travelling Allowance for his official tours 40,000
[Actual expenditure on tours amounted to 27,000).

(vii) He was given cloth worth 2,000 by his employer free of cost.

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(viii) He resides in the Bungalow of the company. Its fair rent is 2,000 p.m. He pays 11,000 p.a. as rent for the house. A watchman and a cook have been provided by the company who were paid 400 per month each.

(ix) He has been provided with a motor car of 1.8 litre engine capacity power for his official as well as personal use. Running and maintenance expenses are borne by the company. A driver is provided with car.

(x) The company has contributed 15,000 to his RPF. Interest on RPF was @ 13% p.a. amounted to 16,250. Professional tax paid 2,500.

Compute his income from salary for the assessment year 2016-17.

Solution :

Computation of Taxable Income from Salary of Mr. Akshay
For the Assessment Year 2016-17

Particulars		Amount	Amount
1.	Basic Salary		1,10,000
2.	Dearness Allowance (2,000 x 12)		24,000
3.	Education Allowance (130 x 12 x 2)	3,120	
	Less : Exempted from Tax (100 x 2 x 12)	(-)2,400	720
4.	Commission on Sales		20,000
5.	Entertainment Allowance (800 x 12)		9,600
6.	Travelling Allowance	40,000	
	Less : Exempted (Actual Expenditure)	(-)	13,000
7.	Cloth given at free of cost	27,000	
	(Gift in kind exempted upto 5,000)		Nil
8.	Value of accommodation provided at concessional rent (Note 1)	23,898	
	Less : Rent paid	(-) 11,000	12,898
9.	Value of facility of cook (400 x 12)		4,800
10.	Value of facility of watchman (400 x 12)		4,800
11.	Motor Car (Note 2)		39,600
12.	Employer's contribution to RPF (Note 3)	15,000	
	Less : Exempted upto 12% of Salary	(-) 13,920	1,080
13.	Interest credited to RPF at 13%	16,250	
	Less : Exempted at 9.5%	(-)	
	16,250 x 9.5% / 13%	11,875	4,375
	Gross Salary		**2,44,873**
	Less : Deductions u/s 16		
1.	Standard deduction	N.A.	
2.	Entertainment allowance (Note 4)	-	
3.	Professional Tax	2,500	(-)2,500
	Income from Salary		**2,42,373**

Working Note:

1. Valuation of Accommodation:

The accommodation is owned by the employer.

The population of Delhi is more than 25 lakhs. Therefore, the valuation of 15% of salary.

Salary = Basic Pay + D.A. (forming part) + Bonus + Commission + Fees + All Taxable Allowances + Any money chargeable under the Act

= 1,10,00 + 6,000 (500 12) + 20,000 + 720 + 9,600 + 13,000

= 1,59,320

15% of 1,59,320 = 23,898

2. Motor Car :

i) Motor car own and maintain by employer

ii) Car is above 1600 CC

ii) Chauffeur is provided

iv) Valuation of car

= (2,400 x 12)+ (900 x 12)

= 28,800 + 10,800

= 39,600

3. Contribution to RPF:

Salary = Basic + D.A. (forming part) + % Commission

= 1,10,000 + 6,000 = 1,16,000

= 12% of 1,16,000

= 13,920.

4. Mr. Akshay is private sector employee. So he is not entitled to get deduction for entertainment allowance (w.e.f. A.Y. 2002-03).

Problem 3.6:

Mr. Guru, a director of Alfa India ltd., Delhi receive the following salary and perquisites from his employer during the previous year 2015-16.

1. Basic pay 66,000.
2. Profit Bonus 18,000 and D.A. 2,000 p.m. [enters into retirement benefit].
3. Commission on Sales at 4% of turnover of 18,50,000.
4. Advance salary of April to July 2014, 22,000.
5. Employer's contribution towards recognized provident fund 18,000.
6. Interest credited to R.P.F. account @13% 13,000.
7. A rent free furnished house in Delhi (rent of unfurnished house paid by employer 84,000, rent of furniture 18,000).
8. He has been provided free services of a gardner salary 4,000 p.a., free services of cook - salary 3,600 p.a. and free services of watchman salary 9,000 p.a.
9. Mr. Guru's 2 children are studying in the school run by the employer. The cost of education in similar institution per student is 1,000 p.a.
10. Electricity bill paid by employer 3,000 p.a.
11. He has been provided 1,800 cc car for both official and private purpose. The assessee pay the running and maintenance expenses for the personal use of car.

NOTES

12. The assessee is provided with free lunch during working days (in all 250 lunches 70 each).
13. He received 17,000 by way of reimbursement of the hospital bill by the employer.
14. He paid Life Insurance Premium 15,000 p.a.
15. He paid Professional Tax 2,500 p.a.

Compute his taxable income from salary for A.Y. 2016-17.

Solution :

Computation of Income from Salary of Mr. Guru
For Assessment Year 2016-17

Particulars	Amount	Amount
1. Basic Salary		66,000
2. Bonus		18,000
3. D.A. (2000 x 12)		24,000
4. Commission on sale at 4%		74,000
5. Advance Salary		22,000
6. Employers contribution to RPF	18,000	
Less : Exempted at 12% of salary (Note 1)	(-)19,680	
7. Interest Credited to R.P.F. at 13%)	13,000	
Less : Exempted from tax at 9.5%	(-) 9,500	3,500
8. Value of Rent free accommodation (Note 2)		45,300
9. Watchman Service		9,000
10. Gardner Service		4,000
11. Cook Service		3,600
12. Electricity Bill paid by Employer		3,000
13. Reimbursement of Hospital Bill	17,000	
Less : Exempted from Tax (Note 3)	(-) 15,000	2,000
14. Education facility cost in other institute (1,000 x 2x12)	24,000	
Less : Exemption (1,000 x 2 x 12)	(-) 24,000	-
15. Motor Car (900 x 12)		10,800
16. Free Lunch (250 x 70)	17,500	
Less : Exemption (250 x 50)	(-) 12,500	5,000
Gross Salary		**2,90,200**
Less : Deduction u/s 16		
1. Standard Deduction	N.A.	
2. Entertainment Allowance	-	
3. Professional Tax	2,500	(-) 2,500
Income from Salary		**2,87,700**

Working Note:

1. Contribution to R.P.F.:

Salary = Basic + D.A. (forming part) + %Commission
= 66,000 + 24,000 + 74,000
= 1,64,000

2. Value of Rent Free Accommodation at Delhi:

The accommodation is not owned by the employer, so the valuation of accommodation is least of following amount:

Rent paid by the employer or

15% of the salary.

Rent paid by employer 84,000.

Salary = Basic + D.A. (forming part) + Bonus + Commission + Fees + All taxable allowance + Any money chargeable under the Act

= 66,000 + 24,000 + 18,000 + 74,000

= 1,82,000

15% of 1,82,000 = 27,300

Least amount is 27,300

Value of Furniture = Original Cost

Because Furniture is taken on hired basis.

Value of Furniture 18,000.

Value of rent free furnished Accommodation is :

Value of accommodation	27,300
Value of Furniture	18,000
	45,300

3. It is assumed that Mr. Guru has taken a treatment in private hospital.

4. Deduction for L.I.P. paid is allowed from GTI u/s 80C and not Income from Salary u/s 16.

5. Valuation of Motor Car :

1800 CC car provided by the employer is used for both official and private purpose.

The assessee pay the running and maintenance expenses of private use.

So valuation = (900 x 12)

= 10,800

Problem 3.7:

Mr. Taxman, is employed in Taxplan Ltd., Pune as an Accountant. During the previous year 2015-16 he has received the following emolument.

Basic salary 12,500 p.m.

D.A. 30% of basic salary (Applicable for retirement benefits).

City Compensatory Allowance 850 p.m.

Children Education Allowance 300 p.m.

(Mr. Taxman is having two sons and one daughter studying in the school).

H.R.A. 1,500 p.m.

He contributed 2,000 p.m. towards his Recognised Provident

Fund and equal amount is contributed by employer.

During the year, the interest credited to his Recognised Provident

Fund A/c @ 12% p.a. amounted to 14,400.

He received 18,000 by way of reimbursement of the hospital bill

in respect of his wife.

He has paid 3,300 as professional tax.

NOTES

He has taken a L.I.P. of 1,00,000 in respect of his wife by paying an annual premium of 14,800.

He stays in a rental house at Pune by paying rent 3,000 p.m.

You are required to compute the taxable income from salary of Mr. Taxman for the A.Y. 2016-17.

Solution :

Computation of Taxable Income from Salary of Mr. Taxmann

Particulars	Amount	Amount
1. Basic Salary (12,500 x 12)		1,50,000
2. D.A. (30% of Basic Salary i.e. 30% of 1,50,000)		45,000
3. City Compensatory Allowance (850 x 12)		10,200
4. Children Education Allowance (300 x 12)	3,600	
Less : Exempted from tax (100 x 12 x 2)	(-) 2,400	1,200
5. H.R.A. (1,500 x 12)	18,000	
Less : Exempted from tax (Note 1)	(-) 16,500	1,500
6. Employer's Contribution to R.P.F. (2,000 x 12)	24,000	
Less : Exempted from tax (Note 2)	(-) 23,400	600
7. Interest credited to R.P.F. balance @12%	14,400	
Less : Exempted @ 9.5%		
14,400 x 9.5% / 12%	(-) 11,400	3,000
8. Reimbursement of Hospital Bill	18,000	
Less : Exempted from Tax upto 15,000	(-) 15,000	3,000
Gross Salary		**2,14,500**
Less : Deductions u/s 16		
1. Standard Deduction	N.A.	
2. Entertainment Allowance	-	
3. Professional Tax	3,300	- 3,300
Income from Salary		**2,11,200**

Working Note :

1. HRA Calculation :

Mr. Taxman working at Pune. So other than BCDM criteria.

Exemption is least of following three :

1. 40% of salary.
2. Actual rent paid - 10% of salary.
3. Actual HRA received.

Here, Salary = Basic + D.A. (forming part) + % Commission
= 1,50,000 + 45,000
= 1,95,000

Exemption is,

1.	40% of 1,95,000		78,000
2.	Actual Rent paid (3,000 x 12)	36,000	
	Less : 10% of 1,95,000	19,500	16,500
3.	Actual HRA received (1,500 x 12)		18,000

Least amount is 16,500 so exempted.

2. Contribution to R.P.F :

Salary = Basic + D.A. (forming part) + % Commission
= 1,50,000 + 45,000
= 1,95,000
12% of 1,95,000 = 23,400

NOTES

3. L.I.P. premium is an item of an investment and it deduct u/s 80C.

Problem 3.8:

From the following particulars of Mr. Ambre an employee of RIL company, find out his taxable income from salary for the A.Y. 2016-17.

1. Basic salary 20,000 p.m.
2. Dearness Allowance 6,000 p.m. (part of the salary).
3. Bonus @ 20% of salary (Basic + DA).
4. Entertainment allowance 9,000 p.m.
5. Employer's contribution to R.P.F. @ 13%.
6. Interest credited on R.P.F. balance @ 16% 24,000.
7. Free furnished quarter is provided by the employer at Mumbai. Fair rent 5,000 p.m., Cost of Furniture 30,000.
8. Gas, Electricity and Water charges 5,000 per annum paid by the employer.
9. Reimbursement of educational expenses 10,000.
10. Reimbursement of medical expenses 12,000 per annum.
11. His contribution to R.P.F. 4,000.
12. A motor car (cc of the engine is 18 liters) is provided to Mr. Ambre. The motor car is used both for the private and official work. Expenses on maintenance of private use are borne by Mr. Ambre.
13. Insurance premium on his own policy 4,200 p.a. and on his wife's policy 3,600 p.a. are paid by the employer.

Solution :

Computation of Income from Salary of Mr. Ambre for the Assessment Year 2016-17

Particulars	**Amount**	**Amount**
1. Basic Salary		2,40,0000
2. Dearness Allowance (6,000 x 12)		72,000
3. Bonus (20% of Salary) (20% of 3,12,000)		62,400
4. Entertainment Allowance (9,000 x 12)		1,08,000
5. Employer's Contribution to R.P.F. at 13% (Note 1)	40,560	
Less : Exempted at 12%	(-) 37,440	3,120
6. Interest on R.P.F. at 16%	24,000	
Less : Exempted at 9.5%	(-) 14,250	9,750
24,000 x 9.5% / 16%		
7. Rent Free Furnished Quarter at Mumbai (Note 2)		76,530
8. Gas, Electricity and Water Charges		5,000
9. Reimbursement of Medical Expenses	12,000	
Less : Exempted upto 15,000	(-) 12,000	
10. Reimbursement of Educational Expenses (Note 3)		10,000
11. Motor Car (900 x 12) (Note 4)		10,800
12. Insurance Premium paid by the employer		
(4,200 + 3,600)		7,800
Gross Salary		**6,05,400**

NOTES

Less : Deduction u/s 16		
1. Standard Deduction	N.A.	
2. Entertainment Allowance for Private Sector	N.A.	
3. Professional Tax	-	
Income from Salary		**6,05,400**

Working Notes :

1. Contribution to R.P.F :

Salary = Basic + D.A. (forming part) + % Commission

= 2,40,000 + 72,000

= 3,12,000

Contribution exempted upto 12% of salary i.e.

12% of 3,12,000 = 37,440

2. Valuation of Rent Free Furnished House :

Valuation = Valuation without Furniture + Valuation of Furniture

House is owned by the employer. The population of Mumbai is more than 25,00,000. Valuation without Furniture = 15% of salary.

Salary = Basic + D.A. (if part of salary) + Bonus + Fees + Commission + All Taxable Allowances + Any other money chargeable under the Act

= 2,40,000 + 72,000 + 62,400 + 1,08,000 + 7,800

= 4,90,200

Valuation = 15% of Salary = 73,530

Valuation of Furniture = 10% of Original Cost

= 10% of 30,000 = 3,000

Valuation with Furniture = 76,530

3. Reimbursement of Education Expenses or fees of family members or child is a taxable perquisite. Therefore, it will not be included in salary for the purpose of valuation of accommodation.

4. Motor Car :

(i) Provided by the employer.

(ii) Exceeds 1600 cc.

(iii) Used for official and private purposes.

(iv) Expenses on maintenance of private use are borne by employee.

So, the valuation = 900 p.m.

= 900 x 12

= 10,800

3.8 Key Concepts

Salary is chargeable to tax on due or receipt which is earlier.
Allowance means extra amount paid for specific purpose.
Perquisite means value of service provide by employer.

3.9 Summary

'Salary' means any amount paid by employer to employee for continuation of service after specific interval. According to Section 17 (1), 'Salary' includes wages, bonus, commission, allowances, perquisites, pension, gratuity etc. Salary is always charged on due or receipt basis whichever is earlier. 'Allowances' means any additional payment by employer to employee for specific purpose. Allowances classified in three groups i.e. fully taxable allowance, tax free allowance, partially exempted allowance. 'Perquisites' means allow employee to use the property at free of cost. Perquisites include gift by employer, medical facility, educational facility, snacks or lunch, facility of health club, telephone bill paid etc. The valuation of motor car and rent free accommodation are important. There are some deductions from salary u/s 16. They are standard deduction, entertainment allowance and professional tax. The meaning of salary is different for different purpose.

3.10 Exercise

1. Give the definition of salary/concept of salary.
2. What are chargeable basis of salary ?
3. Write fully taxable allowances.
4. Write tax-free or fully exempted allowances.
5. Write partially exempted allowances.
6. Write short note on :
   (i) Allowances
   (ii) Perquisites
   (iii) Provident Fund
7. What are deduction from salary u/s 16 ?

- **Fill in the blanks**

1) Any amount paid by employer to _____ for contribution of service after specific interval is known as 'salary'.
   (government, employee, charity, any person)
2) _____always charged on due or receipt which is earlier so any advance salary received chargeable in the year of receipt.
   (Profit, Salary, Insurance Claim, Gain)
3) _____means any additional payment by employer to employee for specific purpose.
   (Salary, Perquisite, Allowance, Tax)
4) _____Allowance is given for payment of house rent at business place.
   (Travelling, House Rent, Dearness, Special)
5) When person reside other than BCDM, then exemption for H.R.A. is least of ___ of salary, actual Rent paid - 10% of salary or actual H.R.A. received.
   (40%, 50%, 100%, 60%)
6) _____is granted to meet the expenditure on conveyance in performance of duties of an office.
   (Conveyance allowance, Helper allowance, Daily allowance, Travelling allowance)
7) In case of normal person maximum exemption of transport allowance is

NOTES

_____ p.m.

(1000, 1600, 800, 1200)

8) '_____' is defined as any casual emolument, fees or profits attached to an office or position in addition to salary or wages.

(Salary, Perquisite, Allowance, Tax)

9) If gift is given by employer to employee in terms of things or goods then exemption is aggregate ` _____ per year.

(5,000, 50000, 10000, 25000)

10) Any expenditure incurred by employer or reimbursement of expenses by employer is exempted maximum upto ` _____.

(15,000, 25,000, 50,000, 30,000)

11) Interest on Statutory Provident Fund is _____exempt.

(9.5%, partly, fully, 12%)

12) If _____ receive to Government employee then only exemption is allowed.

(entertainment allowance, conveyance allowance, helper allowance, daily allowance)

13) Any fund for providing lumpsum amount on retirement is known as _____

(Mutual fund, Provident Fund, Employee fund, Recognized fund)

14) In case of educational facility exemption is _____ per month per child and there is no maximum limit of children.

(2000, 5000, 1000, 10000)

15) _____ allowance is given in big city due to high cost of living.

(Tiffin, City compensatory, Helper, Transport)

(**Answers:** 1) employee, 2) Salary, 3) Allowance, 4) House Rent, 5) 40%, 6) Conveyance allowance, 7) 800, 8) Perquisites, 9) 5,000, 10) 15,000, 11) fully, 12) entertainment allowance, 13) Provident Fund, 14) ` 1,000, 15) City compensatory)

3.11 Further Reading and References

1) Students Guide To Income Tax by Vinod Singhania
2) Taxman
3) Income Tax Bare Act

UNIT 4
INCOME FROM HOUSE PROPERTY

4.0 Introduction 4.1 Objectives
4.2 Basis of Charge [Section 22] 4.3 Conditions
4.4 Classification of House Property
4.5 Gross Annual Value [Section 23 (1)]
4.6 Steps for Computing Income from House Property
4.6.1 Let Out House Property
4.6.2 Deemed Let Out House Property
4.6.3 Self-Occupied House Property
4.7 Net Annual Value (NAV)
4.8 Deductions from Income of House Property [Section 24]
4.9 Key Concepts 4.10 Summary
4.11 Exercise 4.12 Further Reading and References

NOTES

4.0 Introduction

Annual value of any building own by assessee is chargeable to tax under the head 'Income from House property'.

CHECK YOUR PROGRESS

Describe Classification of House Property?

4.1 Objectives

After reading this unit, you should be able :

1. To know about Gross Annual Value (GAV)
2. To know about Net Annual Value (NAV)
3. To understand deductions u/s. 24

4.2 Basis of Charge [Section 22]

Under the head income from house property, the basis of charge is the annual value of property.

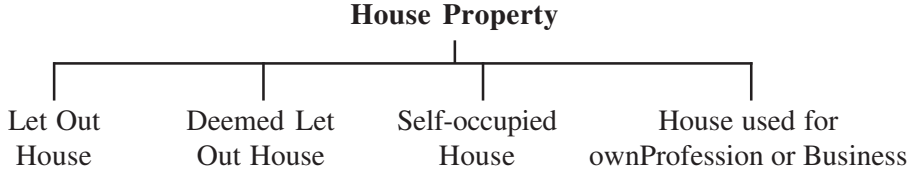
4.3 Conditions

The following conditions must be satisfied to charge a rental income under the head Income from House Property.

1. **The property should consist of any buildings or lands appurtenant thereto:** Rental income of a vacant plot (not appurtenant to building) is not chargeable to tax under the head 'Income from House Property'. It is taxable under the head income from other sources or profits and gains of business.
2. **The assessee should be owner of the property:** Annual value of property is assessed to tax in the hands of the owner even, if he is not in receipt of income.
3. The property should not be used by the owner for the purpose of any business or profession carried on by him, the profits of which are chargeable to tax.

4.4 Classification of House Property

For Income Tax purpose the house property may be classified as under:



NOTES

4.5 Gross Annual Value [Section 23 (1)]

The gross annual value depends upon the following seven factors:

(A) Municipal Value (M.V.): The value of property declared by municipal corporation for charging municipal tax is municipal value. It is also called as Municipal Record Value.

(B) Fair Rent (F.R.): The value of similar property in same locality is fair rental value.

(C) Standard Rent (S.R.): The rent which declared under Standard Rent Control Act is standard rent. The owner cannot be expected to get a rent higher than the standard rent fixed under the Rent Control Act.

(D) Annual Rent: Rent of the previous year or that part of the previous year when the property is available for letting it out.

(E) Unrealised Rent: It is the rent which the owner cannot be realized.

(F) Loss of rent because of vacancy: Where the property is let out but was vacant during the whole or any part of previous year and owing to such vacancy there is loss of rent.

(G) Actual rent received or receivable: Annual Rent - (Unrealised Rent + Rent pertaining to vacancy period)

CHECK YOUR PROGRESS

What is GAV?

4.6 Steps for Computing Income from House Property

Steps for Computing Income from House Property:

Step I :	Fair Rental value or Municipal value which is higher but not more than standard Rent under Rent Control Act`	xxx
Step II :	Annual Rent - Unrealised Rent	xxx
Step III :	Step I or Step II which is higher	xxx
Step IV :	Vacancy Allowance. (Proportionate to Annual Rent)	xxx
Step V :	Gross Annual Value (GAV) (Step III - Step IV)	
Less :	Municipal tax paid by landlord only	xxx
	Net Annual Value (NAV)	**xxx**
Less :	Deduction u/s 24	
	24(1) Standard deduction (30% of NAV)	(xxx)
	24(2) Interest on Housing Loan	(xxx)
	Income from House Property	**xxx**

* Only one S.O.P shows negative income (if housing loan for it is taken).

Problem 1:

From following details find out income from house property.

M.V.	2,10,000
F.R.V.	2,40,000
Standard Rent	2,20,000
Annual Rent	3,00,000
Vacancy Allowance	2 months
Unrealise Rent	20,000
Ground Rent	15,000

Municipal tax paid

By Tenant	10,000
By Landlord	12,000
Insurance	15,000
Interest on Housing Loan	42,000
Status of Property - Let out	

Solution :

Statement showing Income from House Property

Step I :	M.V. or F.R.V. which ever is higher but not more S.R.	2,10,000 2,40,000 2,20,000	2,20,000
Step II :	Annual Rent Unrealise Rent (3,00,000 - 20,000)		2,80,000
Step III :	Step I or Step II whichever is higher		2,80,000
Step IV :	Vacancy Allowance 3,00,000 x 2 / 12		50,000
	Gross Annual Value		
	GAV (Step III - Step IV)		2,30,000
Less :	Municipal tax paid by landlord		12,000
	Net Annual Value (NAV)		2,18,000
Less :	Deduction u/s 24		
	24(1) Standard deduction (30% of NAV)		65,400
	24(2) Interest on Housing Loan		42,006
Income from House Property			**1,10,600**

Problem 2 :

Mr. Suresh having three houses. Find out income from house property.

Particulars	House		
	I	II	III
M.V.	2,40,000	3,00,000	2,80,000
F.R.V.	2,60,000	2,80,000	2,50,000
S.R.	3,00,000	3,20,000	2,60,000
Annual Rent	3,60,000	3,00,000	3,00,000
Unrealised Rent	20,000	-	30,000
Vacancy Allowance	2.5 Mths	-	1 Mths
Municipal Tax paid by Landlord	20,000	30,000	14,000
Insurance	16,000	14,000	20,000
Interest on Housing Loan	40,000	36,000	30,000
Ground Rent	12,000	14,000	12,000
Status	LOP	SOP	LOP

NOTES

Solution :

Income from House II (SOP)

Particulars	
Net annual Value	Nil
Less : Deduction u/s 24	
24(1) Standard deduction	-
24(2) Interest on Housing Loan	36,000
Income of SOP	**(-) 36,000**

Income from Let Out Property House I and III

Particulars	Hs. I	Hs. II
Step I : M.V. or F.R.V. which higher not more S.R.	2,60,000	2,60,000
Step II : A.R. - Unrealise Rent	3,40,000	2,70,000
Step III : Step II or Step III which is higher	3,40,000	2,70,000
Step IV : Vacancy Allowance	75,000	25,000
GAV Step III - Step IV	2,65,000	2,45,000
Less : Municipal tax by landlord	20,000	(14,000)
Net Annual Value	2,45,000	2,31,000
Less : Deduction u/s 24		
24(1) Standard Deduction (30% of NAV)	73,500	(69,300)
24(2) Interest on Housing Loan	40,000	(30,000)
Income from House Property	**1,31,500**	**1,31,700**

Mr. Suresh
Income from House Property

House I (LOP)	1,31,500
House II (SOP)	(36,000)
House III (LOP)	1,31,700
	2,27,200

4.6.1 Let Out House Property

Determination of Gross Annual Value (GAV) :

Step I : Find out the reasonable expected rent (E.R.)

(a) Where the Standard Rent is not applicable: Reasonable Expected Rent is the M.V. or F.R. whichever is higher.

(b) Where the Standard Rent (S.R.) is applicable: Reasonable Expected Rent is the least of the following two:

(i) M.V. or F.R. whichever is higher.

(ii) Standard Rent.

For example :

1. M.V. = 40,000

   F.R. = 46,000

   S.R. = Not applicable. Find out expected rent.

   Reasonable Expected Rent = M.V. or F.R. which is higher

   = 46,000

Reasonable Expected Rent Rs. 46,000

2. M.V. = 40,000

   F.R. = 46,000

   S.R. = 45,000

   Find out expected rent.

   Reasonable expected rent is least of following two :

(i)	M.V. or F.R. which is higher	46,000
(ii)	Standard Rent (S.R.)	45,000

Reasonable Expected Rent Rs. 45,000

Step II : Find out rent actually received.

Actual Rent Received (A.R.R.) = Annual Rent - (Unrealised Rent + Loss due to vacancy)

Annual Rent - Rent for 12 months

Step III : Find out Gross Annual Value

(a) If the actual rent received is more than the expected rent then (A.R.R. > E.R.).

Gross Annual Value = Actual Rent Received

(b) If the actual rent received is less than the expected rent (A.R.R. < E.R.), then

Gross Annual Value = E.R. - Loss due to vacancy

4.6.2 Deemed Let Out House Property

In case of deemed let out property,

Gross Annual Value = Expected Rent

4.6.3 Self-Occupied House Property

One self occupied property always exempted from Income Tax. Self-occupied property exempted means its net annual value taken as nil.

From that Net Annual Value only one deduction is allowed i.e. interest on housing loan with certain limitation. So self-occupied property always shows negative income.

4.7 Net Annual Value (NAV)

After getting Gross Annual Value by deducting municipal taxes from it, you get Net Annual Value. Municipal taxes paid by landlord are only consider for ascertaining Net Annual Value. If municipal taxes paid by tenant then it not to be consider municipal taxes are allowed on payment basis only.

NOTES

CHECK YOUR PROGRESS

What is NAV?

NOTES

4.8 Deductions from Income of House Property [Section 24]

There are two different deduction from income from house property :

1. Standard Deduction [Section 24 (1)] :

Standard deduction is allowed from Net Annual Value. Standard deduction is 30% of NAV. Once you get standard deduction no other expenses are allowed as deductions. So repairing charges, ground rent paid, insurance premium, land revenue expenses are not allowed as deductions.

2. Interest on Borrowed Capital [Section 24 (2)]:

If property is L.O.P., then no limitation for deduction of interest.

But when property is S.O.P. then interest deduction having limitations :

(i) If property is S.O.P. and loan taken before 1-4-1999 and if construction should not be completed within three years from the end of the financial year, then interest deduction allowed. Actual interest paid or ` 30,000 which is lower or less.

(ii) If property is S.O.P. and loan taken on or after 1-4-1999 and construction should be completed within three years from the end of the financial year, then interest deduction allowed. Actual interest paid or 2,00,000 which is lower or less.

(iii) If loan taken for repairs, then date of loan is immaterial and maximum deduction is allowed. Actual interest paid or 30,000 which is lower or less.

CHECK YOUR PROGRESS

Describe Deduction U/S 24?

Format for Computation of Income from House Property (Let Out and Deemed Let Out) For the Assessment Year 2016-17

Particulars	Amount	Amount
Gross Annual Value		xxx
Less : Municipal Tax paid by landlord		xxx
Net Annual Value		xxx
Less : Deductions u/s 24		
Standard Deduction u/s 24 (1)	xxx	
30% of Net Annual Value)		
Interest on Borrowed Capital u/s 24 (2)	xxx	xxx
Income from House Property		xxx

Format for Computation of Income from House Property (Self-occupied) For the Assessment Year 2016-17

Particulars	Amount	Amount
Net Annual Value		Nil
Less : Deductions u/s 24		
Standard deduction u/s 24 (1)	N.A.	
(30% of Net Annual Value)		
Interest on Borrowed Capital u/s 24 (2)	xxx	(- xxx)
Income from House Property		**(- xxx)**

PROBLEMS ON INCOME FROM HOUSE PROPERTY

Problem 4.1:

Mr. Sushant has occupied two houses for his personal purpose, the details of which are given as follows :

Particulars	House I	House II
Municipal Valuation	90,000	45,000
Fair Rent	1,20,000	60,000
Standard Rent	1,00,000	66,000
(Under Rent Control Act)		
Fire Insurance)	1,500	1,500

Municipal taxes 10% of municipal valuation. Mr. Sushant pays 5,000 annually as annuity on House II. He has spent 10,000 and 15,000 on repairing in respect of House I and II respectively.

You are required to compute income from house property for the A.Y. 2016-17.

Solution :

Computation of Taxable Income from House Property of Mr. Sushant For the Assessment Year 2016-17

Particulars	Self-occupied	Deemed Let out
Gross Annual Value	Nil	60,000
Less : Municipal tax paid by landlord (10% of M.V.)	Nil	4,500
Net Annual Value	-	55,500
Less : Deductions u/s 24		
1. Standard Deduction (u/s 24 (1)) (30% of N.A.V.)	-	16,650
2. Interest on borrowed capital u/s 24 (2)	-	- **-16,650**
Income from House Property	**Nil**	**38,850**

Income from House Property = House I (S.O.P.) + House II (Deemed to

= Nil + 38,850

Income from House Property 38,850

Working Note :

Mr. Sushant has occupied two houses.

The M.V. of first house is more than second. So, House I is S.O.P. and House II is deemed let out.

The G.A.V. of House I (S.O.P.) is nil.

So, we calculate the G.A.V. of House II (deemed let out).

Gross Annual Value :

(i) First find out Expected Rent : S.R. is applicable, so expected rent is least of following two :

NOTES

M.V. or F.R. which is higher (45,000 and 60,000)	60,000
Standard Rent	66,000
Expected Rent is least amount i.e.	60,000
In case of deemed let out property.	
G.A.V. = Expected Rent.	
So, G.A.V. of House II	60,000

Problem 4.2 :

Mr. Ram has occupied two houses for his residential purposes. From the following particulars determine the income from house property for the A.Y. 2016-17.

Particulars	**House 1**	**House 2**
(a) Municipal Valuation	1,20,000	60,000
(b) Fair Rent	1,70,000	64,000
(c) Standard Rent under Rent Control Act	1,30,000	72,000
(d) Municipal Taxes paid	10%	10%
(e) Fire Insurance	4,000	3,000
(f) Annual Charges	6,000	2,000
(g) Interest on loan for construction of house	1,41,600	7,000

Computation of Income from House Property of Mr. Ram
For the Assessment Year 2016-17

Particulars	**House I (S.O.P.)**	**House II (Deemed Let Out)**
Gross Annual Value	Nil	64,000
Less : Municipal tax paid by landlord	Nil	6,000
Net Annual Value	Nil	58,000
Less : Deductions u/s 24		
1. Standard Deduction u/s 24 (1) (30% of N.A.V.)	N.A.	17,400
2. Interest on Borrowed Capital u/s 24 (2)	1,41,600	7,000
	- 1,41,600	**- 24,400**
Income from House Property	**- 1,41,600**	**33,600**

Income from House Property = Income from House 1 + Income from House 2

= (- 1,41,600) + 33,600

= (- 1,08,000)

Loss from House Property (-1,08,000)

Working Note :

In this problem, type of house is not given.

M.V. of House 1 is more than House 2.

So, we consider House 1 as S.O.P. and House 2 as L.O.P.

1. House 1 : House 1 is considered as S.O.P. So, Net Annual Value of this house is nil.

2. House 2 : House 2 is considered as deemed let out. So first, we find out Gross Annual Value.

Gross Annual Value = Expected Rent

Standard Rent is applicable. So Expected Rent is least of following two :

(i)	M.V. or F.R. which is higher	64,000
	(60,000 or 64,000)	
(ii)	Standard Rent	72,000
	Least amount is	64,000
	So, Expected Rent	64,000
	So, Gross Annual Value	64,000

It is assumed that the loan is taken after 1st April, 1999 and the construction is completed within 3 years.

Municipal tax is calculated of Municipal value.

Loss from House Property : Loss from L.O.P. or S.O.P. (due to interest on loan) can be set off against income from any other head. Unadjusted loss can be carried forward for 8 succeeding year.

Problem 4.3 :

Mr. Sudhakar owns three houses, particulars of which are as follows :

Particulars	**House 'A' (Let Out)**	**House 'B' (S.O.P.)**	**House 'C' (S.O.P.)**
1. Municipal Valuation	3,60,000	4,80,000	6,00,000
2. Fair Rent	3,70,000	4,70,000	6,20,000
3. Standard Rent	3,80,000	4,65,000	6,30,000
4. Annual Rent	3,78,000	4,50,000	6,25,000
5. Unrealised Rent of the P.Y.(2015-16)	15,700	N.A.	N.A.
6. Period of Vacancy	1 Month	N.A.	N.A.
7. Municipal taxes at 10% of M.V.	Paid By Tenants	Not Paid upto31/3/15	Paid By Sudhakar
8. Construction completed on	10/4/2003	10	10/5/2002
9. Loan taken for construction on	16/11/99	10/10/02	2/11/99
10. Interest paid on loan	1,70,000	15/7/98	1,55,000
		1,53,000	

Find out the income from House Property for the A.Y. 2016-17.

NOTES

Solution :

Computation of Income from House Property of Mr. Sudhakar
For the A.Y. 2016-17

Particulars	House 'A' (Let Out)	House 'B' (Deemed Let Out)	House 'C' (S.O.P.)
Gross Annual Value	3,38,500	4,65,000	Nil
Less : Municipal Tax paid by landlord	N.A. as Paid by Tenant	N.A. as not paid upto 31 Mar	N.A.
Net Annual Value	3,38,500	4,65,000	Nil
Less : Deductions u/s 24			
1. Standard deduction u/s 24 (1) (30% of N.A.V.)	1,01,550	1,39,500	N.A.
2. Interest on borrowed capital u/s 24 (2)	1,70,000	1,53,000	1,55,000
	2,71,550	2,92,500	(-1,55,000)
Income from H.P.	**66,950**	**1,72,500**	**(-1,55,000)**

Income from House Property = Income from House A + House B + House C

= 66,950 + 1,72,500 + (- 1,55,000)

= 84,450

Income from House Property 84,450

Working Note :

Mr. Sudhakar occupied two houses for his own residence. As per Section 23 (2) one house will be treated as self-occupied and another house will be treated as 'Deemed Let Out'.

M.V. of House C is more than house 'B'.

So, House C is S.O.P. and House B is deemed let out.

1. GAV of House 'A' = House 'A' is L.O.P.

First find out expected rent. S.R. is applicable. So, E.R. is least of following two :

(i) M.V. or F.R. which is higher 3,70,000
(3,60,000) (3,70,000)

(ii) Standard Rent 3,80,000

Least amount is 3,70,000

Expected rent is 3,70,000

Now, we will find out Actual Rent Received :

A.R.R. = Annual Rent - (Unrealised Rent + Loss due to vacancy)

= 3,78,000 - (15,700 + 31,500)

= 3,78,000 - 47,200

A.R.R. = 3,30,800

Loss due to vacancy is calculated on basis of annual rent.

Period of vacancy	=	1 month
Annual rent	=	3,78,000
3,78,000 / 12 x 1	=	31,500

Here, A.R.R. is less than E.R.

So, G.A.V. = E.R. - Loss due to vacancy

= 3,70,000 - 31,500

= 3,38,500

G.A.V. of House A 3,38,500

2. GAV of House 'B' :

House 'B" is deemed let out.

GAV = E.R.

S.R. is applicable. So, E.R. is least of following two :

(i) M.V. or F.R. which is higher 4,80,000

(4,80,000) (4,70,000)

(ii) Standard Rent 4,65,000

Least amount is 4,65,000

E.R = 4,65,000

G.A.V = 4,65,000

3. House 'C' is S.O.P. So G.A.V. is nil.

4. Interest on loan taken from SOP is deductiable upto Rs.2,00,000 when loan is taken on or after 1-4-1999.

Problem 4.4 :

Mr. Ashok owns a building which consists of three identical units. Mr. Ashok uses Unit 1 for his own residence and unit 2 for his business. Unit 3 is let out for residential purposes. Mr. Ashok provides the following particulars in respect of the house for the A.Y. 2016-17.

1. Fair rent for each unit is 60,000.
2. Actual rent received for unit 3 is 72,000 p.a.
3. Municipal taxes levied for the entire house were 18,000. Out of which an amount of 15,000 has been actually paid.
4. On 1st April, 2006 Mr. Ashok borrowed an amount of 5,00,000 for the construction of the house at the rate of interest of 12% p.a.
5. The construction of the property was completed on 21st April, 2008.

Calculate the Income from House Property of Mr. Ashok for the A.Y. 2016-17.

NOTES

Solution :

Computation of Income from House Property of Mr. Ashok
For the A.Y. 2016-17

Particulars	**Unit 1 (S.O.P.)**	**Unit 3 (Let Out)**
Gross Annual Value	Nil	72,000
Less : Municipal Tax paid by Landlord (1/3rd of 15,000)	Nil	5,000
Net Annual Value	Nil	67,000
Less : Deduction u/s 24		
1. Standard deduction u/s 24 (1) (30% of N.A.V.)	N.A.	20,100
2. Interest on borrowed capital u/s 24 (2)	28,000	28,000
	(-28,000)	(-48,100)
Income from House Property	**(-28,000)**	**18,900**

Income from House Property = Income from Unit 1 + Unit 2

= (-28,000) + 18,900

Loss from House Property 9,100

Working Note :

1. Unit 1 is used for his own residence.

   So Unit 1 is S.O.P.

   GAV = Nil

2. Unit 2 is used for his business.

   Income/Loss of such property/Unit is not chargeable under 'Income from House Property'. All expenses such as municipal taxes, (on paid or due basis), repairs, interest on loan etc. will be charged to business income.

3. Unit 3 is L.O.P.

   First, we find out Expected Rent.

   Here, M.V. or S.R. are not given.

   So, E.R. = F.R.

   Expected Rent 60,000.

   Actual Rent Received 72,000.

   A.R.R. > E.R.

   So, G.A.V. = Actual Rent Received

   GAV of Unit 3 72,000.

4. Interest for preconstruction period 1/4/2006 to 31/3/2008 at 12% on

5,00,000	=	1,20,000
1/5th of 1,20,000	=	24,000
(+) Interest for P.Y. (at 12% on 5,00,000)	=	60,000
Total interest allowed for deduction		84,000
Per unit 1/3rd for 84,000	=	28,000

Problem 4.5:

Mayur owns two houses. He has furnished the following particulars for the financial year 2015-2016.

First House : Its municipal valuation is 1,00,000. He uses it for his residence. He has paid fire insurance premium 2,000 and municipal taxes 10,000. He has also paid interest on housing loan 16,000.

Second House : Its Municipal valuation is 60,000 and has let out at a rent of 6,000 p.m. He has made the following payments in respect of his house. Municipal Taxes 6,000, Repairs 10,000, Legal Expenses for getting the house vacated 5,000, Annual Charges 30,000. The house remained vacant for two months. 20,000 could not be recovered from the defaulting tenant during this year.

Compute his taxable income from the house property for the A.Y. 2016-17.

Solution :

Computation of Income from House Property of Mayur
For the Assessment Year 2016-17

Particulars	**House I (Self-occupied)**	**House II (Let Out)**
Gross Annual Value	Nil	48,000
Less : Municipal Tax paid by Landlord	Nil	(-) 6,000
Net Annual Value	Nil	42,000
Less : Deductions u/s 24		
1. Standard deduction u/s 24 (1)	N.A.	12,600
30% of Net Annual Value)		
2. Interest on borrowed capital u/s 24 (2)	16,000	-
	(-) 16,000	(-) 12,600
Income from House Property	**(-) 16,000**	**29,400**

Loss/Income from House Property = Income from House I + House II

= (-) 16,000 + 29,400

= 13,400

Income from House Property 13,400

Working Note :

1. House I is used for own residence. So, it is self-occupied property. So Gross Annual Value of House I is nil.
2. House II is let out property. So we can find out the Gross Annual Value.
   (i) Find out Expected Rent : S.R. is not applicable. So, Expected Rent is M.V. or F.R. which is higher.

   M.V 60,000

   F.R. N.A.

   So, Expected Rent 60,000.

   (ii) Find out Actual Rent Received :

   Actual Rent Received = Annual Rent - (Unrealised Rent + Loss due to vacancy)

NOTES

= (6,000 x 12) - (20,000 + 6,000 x 2))

= 72,000 - (20,000 + 12,000)

= 72,000 - 32,000

= 40,000

Actual Rent Received = 40,000

(iii) Here, A.R.R. < E.R.

So, G.A.V. = E.R. - Loss due to vacancy

= 60,000 - 12,000

= 48,000

Gross Annual Value of House II 48,000.

Problem 4.6:

Ashutosh owns three houses for his residential purposes. The following are the details of these houses.

Particulars	House I	House II	House III
1. Municipal Valuation	82,000	50,000	70,000
2. Fair Rent	75,000	60,000	65,000
3. Standard Rent Under Rent Control Act.	70,000	70,000	65,000
4. Municipal Taxes	8,200	6,000	7,000
5. Repairs	8,000	6,000	-

Ground Rent is paid @ 10% of Net Annual Value in respect of each house. Interest paid on capital borrowed for renewal of house property No. 1 and 3 amounting to 38,000 and 32,000 respectively the loan was taken on 1st June 2000.

You are required to determine taxable income from house property of Mr. Ashutosh for the A.Y. 2016-17.

Solution :

Computation of Income from House Property of Mr. Ashutosh

Particulars	House I (S.O.P.) Let Out)	House II (Deemed Let Out)	House III (Deemed
Gross Annual Value	Nil	60,000	65,000
Less : Municipal Tax paid by landlord	Nil	6,000	7,000
Net Annual Value	Nil	54,000	58,000
Less : Deductions u/s 24			
1. Standard deduction u/s 24 (1) (30% N.A.V.)	N.A.	16,200	17,400
2. Interest on borrowed capital (u/s 24 (2))	30,000	-	32,000
	(-) 30,000	(-) 16,200	(-) 49,400
Income from House Property	**(-)30,000**	**37,800**	**8,600**

Income/Loss from House Property = Income from House I + House II + HouseIII

= (-) 30,000 + 37,800 + 8,600

= 16,400

Income from House Property 16,400

NOTES

Working Note :

In this problem the type of house property is not given. The M.V. of House I is more than House II and III. So, House I is self-occupied and House II and III are deemed let out.

1. G.A.V. of House I : House I is S.O.P. So, G.A.V. of this is Nil.
2. G.A.V. of House II : House II is deemed let out.

(i) First we find out Expected Rent. S.R. is applicable, so E.R. is least of following two :

M.V. or F.R. which is higher (50,000) (60,000)	60,000
Standard Rent	70,000
Least amount is	60,000
So, Expected Rent	60,000

In case of deemed let out property, G.A.V. = E.R.

So, G.A.V. of House II = 60,000

3. G.A.V of House III : House III is deemed let out.

(i) First we find out expected rent. S.R. is applicable. So, E.R. is least of following two :

M.V. or F.R. which is higher (70,000) (65,000)	70,000
Standard Rent	65,000
Least amount is	65,000
So, E.R. =	65,000

In case of deemed let out property, G.A.V. = E.R.

So, G.A.V. of House III is 65,000

* The loan is taken for renewal of house. If the house property is self-occupied, then maximum ceiling of 30,000 is applicable. The maximum ceiling for interest on borrowed capital is not applicable to the L.O.P. or deemed let out.

Problem 4.7 :

Mr. Ram owns two houses and both are occupied by him for his own residence. He has given the following information. As a Income Tax Consultant give your advice to Mr. Ram which house should be treated as self-occupied.

Particulars	House I	House II
Municipal Valuation	100000	126000
Fair Rent	110000	120000
Standard Rent	90000	128000
Annual Rent	120000	132000
Municipal Taxes	18000	24000
Interest on Loan	36000	180000
Date of Loan	1st April 98	Dec. 1998
Date of Completion of Construction	May 2001	April 2000

NOTES

Option I : First we consider House 'I' as S.O.P. and House 'II" as deemed let out.

Particulars	House I (S.O.P.)	House II (Deemed Let Out)
Gross Annual Value	Nil	1,26,000
Less : Municipal tax paid by landlord	N.A.	24,000
Net Annual Value	Nil	1,02,000
Less : Deduction u/s 24		
1. Standard deduction u/s 24 (1)		
(30% of Net Annual Value)	N.A.	30,600
2. Interest on borrowed capital u/s 24 (2)	30,000	1,80,000
	(- 30,000)	(-2,10,600)
Income from House Property	**(-30,000)**	**(-1,08,600)**

Income/Loss from House Property = House I + House II

= (-30,000) + (1,08,600)

= (-1,38,600)

Loss from House Property (-1,38,600)

Working Note :

Option I : House I is S.O.P and House II is deemed let out.

1. G.A.V. of House I ; House I is S.O.P. So, G.A.V. of House I is nil.

2. G.A.V. of House II : House II is deemed let out. So, G.A.V. = E.R.

(i) First we find out Expected Rent : S.R. is applicable. So, E.R. is least of following two :

M.V. or F.R. which is higher	1,26,000
(1,26,000) (1,20,000)	
Standard Rent	1,28,000
Least amount is	1,26,000
So, E.R. is	1,26,000.
So, G.A.V. of House II is	1,26,000.

Option II : House I is deemed let out and House II is S.O.P.

1. G.A.V. of House I : House I is deemed let out. So, G.A.V. = E.R.

(i) First, we find out Expected Rent : S.R. is applicable.

So, E.R. is least of following two :

M.V. or F.R. which is higher	1,10,000
(1,00,000) (1,10,000)	
Standard Rent	90,000
Least amount is	90,000
So, E.R is	90,000
So, G.A.V. of House I is	90,000

2. G.A.V. of House II : House II is S.O.P. So, G.A.V. of House II is nil.

NOTES

Option III : We consider House 'I' as deemed let out and House 'II' as S.O.P.

Computation of Income from House Property of Mr. Ram For the A.Y. 2016-17

	House 'I' (Deemed Let Out)	House 'II' (S.O.P.)
Gross Annual Value	90,000	Nil
Less : Municipal tax paid by landlord	18,000	N.A.
Net Annual Value	72,000	Nil
Less : Deductions u/s 24		
1. Standard deduction u/s 24 (1) (30% of N.A.V.)	21,600	N.A.
2. Interest on borrowed capital u/s 24 (2)	36,000	30,000
	- 57,600	(- 30,000)
Income from House Property	**14,400**	**(- 30,000)**

Income/Loss from House Property = House I + House II

= 14,400 + (- 30,000)

= (-15,600)

Loss from House Property (-15,600)

Advice :

Under Option I, Loss from House Property is 1,38,600 and under Option II Loss from House Property 15,600.

In this case the municipal valuation, fair rent, standard rent or the annual value of House II is greater than House I, still it is beneficial to treat house II as deemed let out and House I as self-occupied.

The loss of 1,38,600 can be carried forward for subsequent year or can be set-off against income under any other head of income and the tax liability will be reduced accordingly.

There is no maximum ceiling on deduction for interest paid/payable on loan taken for the construction and etc. of house property which is let out/deemed let out.

4.9 Key Concepts

Property use for own purpose is self occupied property.
Property use for letout is known as letout property.

4.10 Summary

The second head of GTI is Income from House Property. The basis of charge House property is annual value of property. House property may be classified as let out, deemed let out, self-occupied and house used for own profession or business. The important terms of house property are municipal value, fair rent, standard rent, annual rent, unrealised rent, actual rent received and loss due to vacancy. First, we calculate GAV and then deduct from it municipal tax, we get Net Annual Value. Deductions u/s 24 are for House Property. Standard deduction

u/s 24 (1) and Interest on borrowed capital u/s 24 (2).

4.11 Exercise

NOTES

1. What is the basis of charge of house property?
2. What are the types of house property?
3. How we calculate Gross Annual Value for

   (i) Self-occupied

   (ii) Let Out Property

   (iii) Deemed Let Out Property
4. What are deductions from house property?
5. Give short note on 'Net Annual Value'.

- **Fill in the blanks**

1) Under the head income from house property, the basis of charge is the _____of property.

   (annual value, average value, actual value, nominal value)

2) The value of property declared by Municipal Corporation for charging municipal tax is _____.

   (fair value, municipal value, annual value, actual value)

3) The owner cannot be expected to get a rent higher than the _____fixed under the Rent Control Act.

   (actual rent, standard rent, municipal rent, fair rent)

4) Actual rent received or receivable = _____ ? (Unrealised Rent + Rent pertaining to vacancy period)

   (Annual Rent, Standard Rent, Municipal Rent, Fair Rent)

5) Reasonable Expected Rent is the Municipal Value or _____ whichever is higher.

   (Annual Rent, Standard Rent, Actual Rent, Fair Rent)

6) _____ self occupied property always exempted from Income Tax.

   (Two, One, Three, Five)

7) Self-occupied property exempted means its _____taken as nil.

   (net annual value, gross annual value, fair value, municipal value)

8) Standard deduction is allowed from Net Annual Value. Standard deduction is _____of NAV.

   (50%, 20%, 30%, 40%)

9) If loan taken for repairs, then date of loan is immaterial and maximum deduction is allowed. Actual interest paid or _____ which is lower or less.

   (30,000, 150,000, 200,000, 50,000)

10) If property is L.O.P., then no limitation for deduction of_____.

(municipal tax, interest, expenses, rent)

11) First, we calculate GAV and then deduct from it_____, we get Net Annual Value.

(municipal tax, interest, expenses, rent)

12) In case of deemed let out property, Gross Annual Value = _____

(Standard Rent, Expected Rent, Municipal Rent, Unrealized Rent)

13) Once you get _____no other expenses are allowed as deductions.

(standard deduction, interest deduction, tax deduction, rent deduction)

14) If municipal taxes paid by _____then it not to be consider.

(tenant, landlord, department, employer)

15) _____is the rent which the owner cannot be realized.

(Standard Rent, Expected Rent, Municipal Rent, Unrealized Rent)

(**Answers:** 1) annual value, 2) municipal value, 3) standard rent, 4) Annual Rent, 5) Fair Rent, 6) One, 7) net annual value, 8) 30%, 9) 30,000, 10) interest, 11) municipal tax, 12) Expected Rent, 13) standard deduction, 14) tenant, 15) Unrealized Rent)

NOTES

4.12 Further Reading and References

1) Students Guide To Income Tax by Vinod Singhania
2) Taxman
3) Income Tax Bare Act

NOTES

UNIT - 5
PROFITS AND GAINS FROM BUSINESS OR PROFESSIONS

5.0 Introduction 5.1 Objectives
5.2 Profits and Gains of Business and Professions
5.3 Business [Section 2 (13)] 5.4 Profession [Section 2 (36)]
5.5 Vocation 5.6 Expenditure
5.7 Income
5.8 The Main Rules for Preparation of Trading, Profit and Loss A/c
5.9 Expenses/Deductions expressly allowed as deduction from Profit and Gain of business or Profession
5.10 Disallowed Expenses
5.11 While computing the Income from Business or Profession it is difficult to remember which expenses are allowed and which expenses are not allowed under the Act
5.12 Format of Computation of Taxable Income from Business or Profession
5.13 Personal Incomes (Disallowed Incomes)
5.14 Key Concepts 5.15 Summary
5.16 Exercise 5.17 Further Reading and References

CHECK YOUR PROGRESS

Define Business?

5.0 Introduction

Any gain arise from business activity hold by assessee chargeable to tax under the head 'Profits and gains of business and professions.'

5.1 Objectives

After reading this unit, you should be able :

1. To know about allowable Expenses and Incomes
2. To know about certain limited deductions.
3. To know about Assume Income.

5.2 Profits and Gains of Business and Professions

Third head of income is 'Profits and gains of Business and Professions'.

5.3 Business [Section 2 (13)]

Business means the purchase and sale or manufacture of a commodity with a view to make profit. It includes any trade, commerce or manufacture or any adventure or concern in the nature of trade. It is important that the intention of purchase or manufacture of goods should be to sell at a profit.

5.4 Profession [Section 2 (36)]

Profession means the activities for earning livelihood which require intellectual skill or manual skill, e.g. the work of a lawyer, doctor, auditor, engineer

and so on, are in the nature of profession.

5.5 Vocation

Vocation means activities which are performed in order to earn livelihood, e.g. brokerage, insurance agency, music, dancing, etc. The rules for the assessment of business, profession or vocation are the same.

According to Income Tax Act any profit or gain from business or profession chargeable to tax means profit derived from trading, profit and loss a/c is chargeable to tax. Under this chapter, we consider the rules regarding which expenses and incomes are allowed or disallowed.

5.6 Expenditure

Outflow of cash is expenditure.

Expenditures are classified under two heads:

(i) Revenue Expenditures: The expenditures incurred repetitively or consistently.

(ii) Capital Expenditures: The expenditure incurred once a while.

5.7 Income

Inflow of cash is Income.

5.8 The Main Rules for Preparation of Trading, Profit and Loss A/c

1. Trading, profit and loss a/c must be for business.
2. It must be for one year only (previous year).
3. It must record all revenue expenditures and revenue incomes.
4. Personal or individual expenses are not recorded.

5.9 Expenses/Deductions Expressly Allowed as Deduction from Profit and Gain of Business or Profession

1. **Expenses in respect of business premises [Section 30]:** The following deductions are allowed:
   (a) Rent, rates, taxes, repairs and insurance for premises used for the purpose of the business or profession.
   (b) Any sum paid on account of land revenues, local taxes or municipal taxes.
   (c) Insurance premium in respect of goods held in stock.
2. **Repairs and insurance of machinery, plant and furniture [Section 31]:** Current repairs and insurance of machinery, plant and furniture used for the purposes of the business or profession.
3. **Depreciation [Section 32]:** Depreciation is an allowable expenditure subject to the following conditions.
   (a) The assessee is the owner of the asset.
   (b) The asset is used for the business purposes.
   (c) The asset is used in the relevant previous year.

NOTES

Depreciation is allowed on tangible assets (i.e. building, machinery, plant etc) and also on intangible assets (i.e. know how, patent, Trade mark etc. @ 25%) acquired on or after 1.4.1998. Depreciation is to be allowed as per income tax rules. It is to be allowed on the written down value of the assets. w.e.f. 1.4.2009.

Depreciation on New Plant and Machinery: In the case of any new machinery or plant (other than ships and air craft). Which has been acquired and installed after 31st March 2005 by an assessee, a further sum equal to 20% of the actual cost of such machinery or plant shall be allowed as deduction.

4. **Expenditure for research and development [Section 35]:** If Research and development expenses for personal business, then all revenue expenses are allowed.

   For own research and development any capital expenditure incurred (purchase of land and building) is totally disallowed.

   If any donation given for research to any approved institute, university or government department then deduction is cumulative 125% of donation given.

CHECK YOUR PROGRESS

Give the list of Allowed Expenses?

5. **Expenditure on government approved programme :** Any expenditure incurred for development of society under any government approved scheme total expenditure are allowed. For such allowance a certificate of chartered Accountant is essential.
6. **Tele-communication license fees :** If any expenses incurred for renewal of license if totally allowed.

   In case of Tele-communication license, the expenditure incurred distribute according to their life (period allowed). e.g. Expenditure incurred for Tele-communication license ` 20,000 and life of the licence is 8 years. So expenditure charges each year is ` 20 000 8 years = ` 2,500.
7. **Purchase of patent or copy rights (Section 35 A) :** A manufacturing design or right to manufacture is known as patent.

   If patent purchase after 1.4.98. then depreciation 25% is allowed.

   If patent purchase before 1-4-98, then such expenditure can be distributed over 14 years commencing from the previous year in which the expenditure is incurred.
8. **Expenditure of know how/purchase of know-how (secret formula):** If know-how purchase after 1-4-98, then 25% depreciation is applicable.

   If know-how purchase before 1.4.98, then that expenditures are equally distribute in 8 years.
9. **Amortisation of preliminary expenses:** Any expenses incurred before commencement of business, department or branch. Such expenses are allowed to be distributed over 5 years equally.
10. **Advertisement Expenses:** Any advertisement expenditure who's benefit for short period for e.g. advertisement in newspaper, calendars, pamphlets, diary etc. are allowed expenses.
11. **Expenses on Rural Development Programme :** Any expenditure incurred by business for rural development programme is allowed as deduction.

    For such deduction a certificate of chartered Accountant is important.
12. **Expenditure for Natural Resources conservation programmes :** Any expenditure incurred by business for natural conservative sources is allowed as deduction.
13. **Payment under voluntary retirement scheme (V.R.S.) :** Any amount given to employee for voluntary retirement benefit under any V.R.S. scheme, the lumpsum amount paid charge to each year 1/5 distribute total exp. in five equal annual installments beginning from the year in which such part payment

is made to employee.

14. **Expenditure on family planning promotion:** Any expenditure incurred for the promotion of family planning.

    If it is revenue then 100% allowed

    If it is capital then 1/5th allowed in a year.

    When revenue or capital is not given then such expenses are treated as capital expenditure and 1/5 allowed in each year.

15. **Other deductions allowed:** The following other deductions are allowed:
    1. Insurance premium on property.
    2. Insurance premium on health of the employees.
    3. Bonus or commission paid to any employee.
    4. Interest on borrowed capital.
    5. Contribution to employees recognized provident fund.
    6. Contribution to Approved Gratuity Fund and superannuation Fund upto 8.33% of salary.
    7. Bad debts.
    8. Interest on bank loan (loan must be for business purpose).
    9. Any legal charges or fees.
    10. Write off bad debts.
    11. Insurance premium for group insurance.
    12. Traveling Expenses.
    13. Traveling Expenses abroad for study or research.
    14. Sales tax, excise duty paid upto the date of filing the Income Tax Return and expenses incurred in connection with sale tax proceeding including appeals.
    15. Any tax, duty, cess or fees paid for carrying on the business or profession is allowed e.g. sales tax, purchase tax, value added tax, Banking cash transaction tax, professional tax, central excise and custom duties, local tax, service tax, Entry tax etc.
    16. Legal expenses for maintenance of right of business.
    17. Advertisement expenditure incurred for launching of new product.
    18. Registration expenses of trade mark.
    19. Maintenance of guest house.
    20. Interest on money borrowed for payment of dividends, interest or non-payment of sales tax is deductible.
    21. Discount on issue of zero coupon bonds are to be allowed on prorata basis.
    22. Expenditure for promoting social/economic welfare or uplift of the public (Section 35 AC).
    23. Securities transaction tax paid in respect of the taxable securities transactions, if the income arising from such taxable securities is included under the head 'profits and gains of Business/Profession (w.e.f. 1/4/2009).

CHECK YOUR PROGRESS

Give the list of Disallowed Expenses?

5.10 Disallowed Expenses

The following expenses are not allowed to be debited to profit and loss account which is prepared for calculation of taxable income from profits and gains of business or profession:

1. **Advertisement Expenses:** Permanent type of advertisement e.g. permanent sign board, wall painting, electric sign board, lighting effects are totally disallowed.

NOTES

Any advertisement given in political souvenir, magazine, brochure etc. is totally disallowed.

2. **Any payment in cash in excess of Rs 20,000:** According to RBI rules and guidelines issued by Income Tax department, any payment in excess of 20,000 must be required by account payee cheque or demand draft.

   If such amount paid in cash or by bearer cheque then total amount paid in cash is disallowed.

   If amount paid is result of two or more claims then such expenditure is allowed if any claim not exceed ` 20,000.

   Any claim exceed ` 20,000 and total amount paid by cash is totally disallowed.
3. Excessive payments to relatives as defined in section 2 (41).
4. Interest, royalties, fees for technical services payable outside India without deduction of tax.
5. Income tax.
6. Fringe Benefit tax
7. Wealth tax
8. Gift tax
9. Salary payable outside India without tax deduction.
10. Mere provision for gratuity (without any payment)
11. Reserve for doubtful debts (it is only a provision hence not allowed).
12. Drawings of proprietor/partner.
13. Personal expenses of proprietor/partner.
14. Capital expenditure.
15. Penalties paid by the assessee for breach of law.
16. Litigation expenses of registration of shares.
17. Insurance premium paid by partnership firm on life Insurance policies of its partners.
18. Personal expenses.
19. Salary or rent to proprietor.
20. Interest on capital.
21. Any Royalty paid outside India without TDS.
22. Any charity, donation, reserve, provision.
23. Any fine and penalty
24. Asset purchase.
25. Installation charges of assets.
26. In case of partnership firm, interest paid on capital in excess of 12%.
27. Life Insurance Premium.

5.11 While Computing the Income form Business or Profession it is Difficult to remember which Expenses are Allowed and which Expenses are not allowed under the Act therefore, while Solving the example apply the following General Rules

(i) All types of revenue expenses related to business are allowed for deductions.
(ii) The expenses should be in respect of a business or profession carried on by the assessee and the profits and gains of which are to be computed and assessed.
(iii) The expenses should not be a personal expenses of the assessee. e.g. Gifts and Presents.
(iv) The expenses should have been paid out or expanded wholly and exclusively for the purpose of such business or profession.
(v) The expenses should not be in the nature of capital expenditure.
(vi) The expenses should relate to the previous year concerned.
(vii) Penalty, fine, interest paid/payable under direct taxes e.g. Income tax are not allowed.
(viii) Any type of penalty, fine under sales tax act, Customs Act or Factories Act are not allowed.
(ix) Interest and expenses relating to sales tax, customs and excise are deductible e.g. interest for late payment of sales tax.

5.12 Format of Computation of Taxable Income from Business or Profession

Particulars		
Profit as per profit and loss A/c		xxxx
Add : (i) Expenses or losses not allowed but claimed/ charged to P & L A/c.		
e.g. Household expenses, Income tax, LIC, Bad debts reserve, Interest on capital, personal expenses etc.	xxx	
(ii) Incomes taxable as business income but not credited to Profit and Loss A/c		
e.g. Interest received on business investments, sale of assets used for scientific research	xxx	
(iii) Expenses in excess of the allowed amount charged to P & L A/c	xxx	
e.g. Excess salary paid to relatives		
(iv) Under valuation of closing stock	xxx	
or over valuation of opening stock		xxxx
		xxxx
Deduct :		
(i) Expenses or losses allowed but not debited to Profit and Loss A/c e.g. Depreciation	xxx	
(ii) Income not taxable as business income but credited to the Profit and Loss A/c e.g. Dividends, profit on Sale of investments, Rent form house property.	xxx	
(iii) Income exempt from tax but credited to Profit and Loss A/c. e.g. Grants and subsidies	xxx	
(iv) Over valuation of closing stock and under valuation of opening stock.	xxx	
		xxxx

Taxable Income From Business **xxxx**

Note 1 : If instead of profit there is loss as per the Profit and Loss Account, the above rules shall be reversed, i.e. items to be added shall be deducted and those to be deducted shall be added.

Note 2 : The same rules will apply to Income and Expenditure Account.

NOTES

5.13 Personal Incomes (Disallowed Incomes)

1. Interest on investment
2. Dividend received
3. Personal receipt
4. Profit on sale of personal asset
5. Dividend received on units
6. Rent received (personal property)

CHECK YOUR PROGRESS

Give the list of Disallowed Incomes?

Discuss the tax implications in the following situations:

1. Personal expenses 6,000 were debited to the Profit and Loss A/c.

* Personal expenses not allowed to charge to P & L A/c. Here, profit reduces by 6,000. So while calculating Profit as per Income Tax ` 6,000 should be added.

2. Rent paid for Premises 10,200 was by mistaken written on the credit side of P & L A/c.

o Rent paid for premise is allowed deduction but is wrongly recorded at credit side of P & L so it increases profit by 10,200. Now correct treatment is deduct 20,400 from net profit for ascertaining correct profit.

3. Loss of 70,000 on account of embezzelement by an employee.

* According to Income Tax Act any embezzlement by employee is allowed deduction. So 70,000 allowed to debit 70,000 to P & L A/c.

4. Furniture costing 15,000 was purchased and debited to P & L A/c. The profit was then calculated to 1,00,000. The furniture was put to use for more than 200 days.

* Only revenue expenditure allowed to charge to P & L A/c. No capital expenditure allow to charge to P & L.

* Here purchase of furniture charge is disallowed so net profit increases by 15,000. Asset use more than 182 days so total full year charge to P&L A/c i.e. 10% on 15,000 so net effect profit increases by 13,500.

So, correct profit now	1,00,000
+ Capital Expenses	13,500
	1,13,500

5. Office expenses 3,500 and audit fee 4,000 was not debited to P&L A/c and N.P. was 4,50,000.

* According to I.T. Act, Office Expenses and Audit Fee both are allowed expenses but not recorded so allowed to reduce profit by 7,500.

`

N.P.	4,50,000
Less : Expenses allowed but not recorded	7,500
Profit as per I.T. Act	4,.42,500

6. A company whose N.P. as per P & L is 5,00,000/- has debited to P & L A/c a sum of 3,00,000 as one time compensation under VRS approved by competent authority.

* For V.R.S. compensation total amount not allowed as deduction but only 1/5 i.e. 20% of amount paid allowed as deduction. So N.P. as per P & L A/c was 5,00,000 and Disallow Expenses 80% of 3,00,000 is 2,40,000. So N.P. as I.T. Act, 7,40,000.

7. Mr. John purchase shares of public listed company on 28/02/05 for 1,00,000 and sold the same through share broker on 1/03/06 for 1,70,000.

* In case of shares 12 months period is considered to find out short-term or long-term. Here shares are long-term asset but indexation not applicable. So long-term capital gain is 70,000.

8. A company has reported a net loss 50,000 in its P & L A/c for year ended 31/03/06. P & L A/c debited R.D.D. 1,50,000 and bad debts written off 15,000.

* Bad debts written off is allowed expenditure but any provision is disallowed so R.D.D. is disallowed. Now profit is,

Loss	- 50,000
Add : Disallowed Expenses record to P & L	1,50,000
Profit of business	1,00,000

PROBLEMS ON PROFITS AND GAINS FROM BUSINESS OR PROFESSIONS

Problem 5.1 :

The following is the Profit and Loss A/c for the financial year ending on 31st March 2016 furnished by Miss Pradnya:

Profit and Loss A/c

Particulars	Amount	Particulars	Amount
To Salary	1,20,000	By Gross Profit	2,80,000
To Advertisement	8,000	By Interest on Fixed deposit	17,000
To Repairs	12,400	By dividend	7,000
To Fire Insurance	1,500	By Bad Debts Recovered	12,400
To Depreciation	18,000	By Commission	18,000
To Wealth Tax	4,500		
To Sales Tax	10,000		
To Banking Cash Transaction Tax	2,000		
To Reserve for future losses	3,000		
To R.D.D.	4,000		
To Bad Debts	1,000		
To Net Profit	1,50,000		
	3,34,400		**3,34,400**

Other Information :

1. Repairs include 8,400 as repairing to the residential house.
2. Allowable amount of depreciation is 15,000.
3. Sales tax included 750 as penalty and 570 as interest for late payment of sales tax charged by the sales tax Authority.

NOTES

4. Bad debts recovered were written-off in the year 2007-08 or and admitted by the Income tax Department.

You are required to compute taxable income of Miss Pradnya from business for the A.Y. 2016-17.

Computation of Taxable Income from business of Miss Pradnya
For the Assessment Year 2016-17

Particulars	Amt. Rs.	Amt. Rs.
Net Profit as per Profit and Loss A/c		1,50,000
Add : Disallowed expenses debited to P&L A/c		
(i) Repairs to the residential house	8,400	
(ii) Excess Depreciation (18,000 - 15,000)	3,000	
(iii) Wealth Tax	4,500	
(iv) Penalty charged by Sales Tax Authority	7,50	
(v) Reserve for Future Losses	3,000	
(vi) R.D.D.	4,000	23,650
		1,73,650
Less : Disallowed Incomes Credited to P&L A/C		
(i) Interest on Fixed Deposit	17,000	
(ii) Dividends	7,000	- 24,000
Taxable Income form Business		**1,49,650**

Note : Interest for late or non-payment of sales tax is deductible.

Taxable Income From Business 1,49,650

Problem 5.2

The following is the profit and loss account of Mr. Universe, Pune for the financial year ending on 31st March, 2016.

Profit and Loss Account

Particulars	Amount	Particulars	Amount
To Salary	1,60,000	By Gross Profit	4,20,000
To Rent and Taxes	60,000	By Commission	42,000
To Commission	16,000	By Sundry receipt	4,200
To Advertisement	15,000	By interest on fixed deposit	35,000
To R.D.D.	8,000	By Gift from friend	2,900
To Depreciation	20,000		
To Legal Expenses on I.T. Proceeding	2,000		
To Conveyance	8,400		
To Stationery	15,200		
To Bonus	16,000		
To Contribution to R.P.F.	12,500		
To Interest on Capital	13,000		
To Net Profit	1,58,000		
	5,04,100		**5,04,100**

Additional Information:

(a) Depreciation allowable under Income Tax Rule is amounted to 18,000.

(b) Rent and taxes includes 8,000 as property tax on residential house of Mr. Universe.

(c) Advertisement includes 12,000 as the cost of permanent signboard fixed on the premises.

(d) Sundry receipts 4,000 are in respect of recovery of personal loan given to a friend of Mr. Universe.

(e) Contribution by the employer to R.P.F. due on 31/3/2016, 4,000 was deposited on 25/6/2016.

You are required to compute taxable income from business for the A.Y. 2016-17.

Solution :

Computation of income from business of Mr. Universe
For the A.Y. 2016-17

Particulars	**Amount**	**Amount**
Net Profit as per Profit and Loss A/c		1,58,000
Add : Disallowed expenses debited to P&L A/c		
(i) Rent and taxes (property tax)	8,000	
(ii) Advertisement (sign board-capital expenses)	12,000	
(iii) R.D.D.	8,000	
(iv) Depreciation (Excess)	2,000	
(v) Interest on Capital	13,000	43,000
		2,01,000
Less : Disallowed Incomes credited to P&L A/c		
(i) Sundry Receipts (personal loan)	4,000	
(ii) Interest on fixed deposit	35,000	
(iii) Gifts from a friend	2,900	-41,900
Taxable Income from Business		**1,59,100**

Note : Employees contribution to R.P.F. is deductible if payment is made or deposited on or before the due date of submission of return of income.

Taxable Income from Business 1,59,100

Problem 5.3

The following is the profit and loss Account for the year ended on 31st March 2016 furnished by Mr. Vijay.

NOTES

Profit and Loss A/c

Particulars	Amount	Particulars	Amount
To Salary	39,000	By Gross Profit	1,00,000
To Advertisement	4,000	By Sundry Receipts	4,200
To Fire Insurance	1,750	By Gift from father	12,500
To Office Expenses	2,250	By Interest on bank deposits	3,000
To Depreciation	7,900	By Bad Debts recovered (not allowed as deduction earlier)	2,700
To Bonus	6,400		
To Income Tax	4,300		
To Sales Tax	2,250		
To Interest on bank loan	2,800		
To R.D.D.	1,750		
To Net Profit	50,000		
	1,22,400		**1,22,400**

Additional Information :

(i) Salary includes 2,100 paid to a domestic servant.

(ii) Advertisement includes 275 as expenditure incurred for selling household furniture.

(iii) Allowable depreciation as per income tax rules is 7,000.

(iv) Sale tax includes 250 as penalty for not filing return in time.

(v) Bank loan is for business purposes.

You are required to compute taxable income from business for the assessment year 2016-17.

Solution :

Computation of Income from business of Mr. Vijay
For the Assessment Year 2016-17

Particulars	Amount	Amount
Net Profit as per Profit and Loss A/c		
Add : Disallowed expenses debited to profit and loss A/c		50,000
(i) Salary paid to domestic servant	2,100	
(ii) Advertisement (Selling household furniture)	275	
(iii) Depreciation (Excess)	900	
(iv) Income Tax	4,300	
(v) Sales Tax (Penalty)	250	
(vi) R.D.D.	1,750	9,575
		59,575
Less : Disallowed incomes credited to P&L A/c		
(i) Gift from father	12,500	
(ii) Interest on bank deposits	3,000	
(iii) Bad debts	2,700	-18,200
Taxable Income from Business		**41,375**

Taxable Income from Business 41 375

Problem 5.4:

The following is the Receipts and Payments Account of medical practitioner for the year ending March 31, 2016.

Receipts	Amount	Payments	Amount
Balance b/d	1,10,000	Clinic Rent	15,000
Visiting Fees	65,000	Staff Salaries	80,000
Consultation Fees	65,000	Rent and Taxes	5,000
Sales of Medicines	25,000	Electricity and water	4,000
Operation Theatre Rent	15,000	Purchase of Medical Books	4.000
Interest and Dividend	20,000	(Annual Publ.)	
		Purchase of Medicines	30,000
		Motor Car exp.	15,000
		Medical Association Membership Fees	5,000
		Audit Fees	20,000
		Staff welfare Expenses	2,000
		Diwali Expenses	1,000
		Entertainment expenses	6,000
		Purchase of surgical Equipments	30,000
		Balance c/d	83,000
	3,00,000		**3,00,000**

Additional Information :

1. Depreciation allowable under Income Tax Rules is amounted to 4,500 on surgical equipment and 6000 for motor car (for professional use).
2. One-third of motor car expenses relate to his personal use.

Compute the taxable income from profession for the A.Y. 2016-2017.

Solution :

Computation of Taxable Income from Profession
For the Assessment Year 2016-17

Particulars	Amount	Amount
Revenue Receipts (Professional earning)		
(i) Visiting fees	65,000	
(ii) Consultation Fees	65,000	
(iii) Sales of Medicines	25,000	
(iv) Operation theatre Rent	15,000	1,70,000
Less : Revenue Payments (Expenses allowed)		
(i) Clinic Rent	15,000	
(ii) Staff salaries	80,000	
(iii) Rent and Taxes	5,000	
(iv) Electricity and water	4,000	
(v) Purchase medical books	4,000	
(vi) Purchase of medicines	30,000	
(vii) Motor car Expenses (2/3 of 15,000)	10,000	
(viii) Medical Association Membership Fees	5,000	
(ix) Audit Fees	20,000	
(x) Staff welfare expenses	2,000	
(xi) Diwali expenses	1,000	
(xii) Entertainment Expenses	6,000	
(xiii) Depreciation on surgical equipment (15% on 30,000)	4,500	

NOTES

(xiv) Depreciation on Motor car (professional use)	6,000	
		1,92,500
Loss from Profession		(- 22,500)

Loss from profession (-22 500)

Problem 5.5 :

Mr. Ashish is the proprietor of a business. His profit and loss Account for the year ending on 31st March, 2016 is as follows -

Particulars	Amount	Particulars	Amount
To Establishment	9,600	By Gross Profit	1,01,680
To Rent, Rates and Taxes	5,800	By Interest on Govt.securities	10,800
To General charges	1,500	By Rent from House property	10,800
To Household Expenses	3,460		
To Commission	3,000		
To discount and Allowance	900		
To Provision for Bad Debts	2,400		
To Postage and Telegrams	540		
To Law charges	900		
To Advertising	3,100		
To Gifts and presents to employees	300		
To Fire Insurance premium (for goods)	720		
To Sales Tax paid	2,900		
To Repairs and Renewals (for house property)	960		
To Loss on sale of Motor car (used for private purposes)	3,600		
To Life Insurance premium	3,580		
To Wealth tax	1,480		
To Interest on Capital	700		
To Audit Fees	600		
To Interest on bank loan	2,760		
To Provision for depreciation	5,000		
To Provision for income tax	7,800		
Net Profit	61,680		
	1,23,280		**1,23,280**

Other Information :

(a) Actual Bad debts written off during the year 1,100.
(b) Amount of Income tax actually paid during the year is 8,400.
(c) Depreciation allowable as per Income Tax Rules is 3,400.
(d) Advertising exp. include 1,100 spent on special advertising campaign to open a new shop in the market.
(e) Law charges are in connection with protection of a trademark.
(f) Mr. Ashish carries on his business in a rented premises, half of which is used as his residence. Rent, rates and taxes include 4,800 paid as rent of the premises during the year.

(g) Bank loan is taken for business purposes.

Compute the business income of Mr. Ashish for the A.Y. 2016-17.

NOTES

Solution :

Computation of Income from business of Mr. Ashish
For the A.Y. 2016-17

Particulars	Amount	Amount
Net profit as per Profit and Loss Account		61,680
Add : Disallowed expenses debited to P&L A/c		
(i) Rent of one half premises	2,400	
(ii) Household expenses	3,460	
(iii) Provision for bad debts	2,400	
(iv) Repairs and Renewals for house property	960	
(v) Loss on sale of Motor car	3,600	
(vi) Life Insurance Premium	3,580	
(vii) Wealth tax	1,480	
(viii) Interest on Capital	700	
(ix) Provision for depreciation	5,000	
(x) Provision for Income Tax	7,800	
(xi) Gifts and Presents	300	31,680
		93,360
Less : Expenses allowed but not charged toP&L A/c		
(i) Bad debts	1,100	
(ii) Depreciation	3,400	- 4,500
		88,860
Less : Incomes under other heads but credited to profit and loss A/c		
Interest on Govt. securities	10,800	
	10,800	- 21,600
Income from Business		**67,260**

1. Expenses incurred on special advertising campaign to open a new shop in the market are allowed as these are incurred for better marketing of the goods.
2. Law charges are incurred for the maintenance of an existing trademark and hence they are allowed.
3. Repairs and renewals are not for business premises, hence not allowable as business expenditure.
4. Gifts and presents to employees are not allowable expenses/deductions.
5. Income tax, though actually paid is not admissible expenses.

Income from Business 67 260

NOTES

Problem 5.6 :

Mr. Ram is advocate and has prepared the following income and expenditure account for the year ending 31-3-2016.

Income and Expenditure Account

Particulars	Amount	Particulars	Amount
Office Expenses	1,00,000	Audit fees	7,05,000
Employee's salary	50,000	Gift from Father-in-law	50,500
Magazines	6,000	Dividend	80,000
Personal expenses	1,70,000	Profit on sale of Investment	64,500
Donation to N.D.F.	5,000	Law consultancy fees	5,00,000
Interest	7,000		
Income Tax	1,33,000		
Car Expenses	20,000		
Net Surplus	9,10,000		
	14,00,000		**14,00,000**

You are required to compute his professional income for the assessment year 2016-17 considering the following points :

1. The car is used equally for official and personal purposes.
2. 10,000 domestic servant's salary is included in employees salary.

Solution :

Computation of Income from profession of Mr. Ram.
For the Assessment Year 2016-17

Particulars	Amount	Amount
Net surplus as per Income and Expenditure Account		9,10,000
Add : Disallowed Expenses		
(i) Domestic Servants Salary		
10,000		
(ii) Personal Expenses	1,70,000	
(iii) Donation to N.D.F.	5,000	
(iv) Income Tax	1,33,000	
(v) Car Expenses	10,000	3,18,000
		12,28,000
Less : Receipts/Incomes under other heads		
(i) Gift from father-in-law	50,500	
(ii) Dividend	80,000	
(iii) Profit on sale of Investment	64,500	- 1,95,000
Income from profession		10,33,000

Income from profession 10,33,000

NOTES

Problem 5.7 :

The following is the Profit and Loss account of Mr. Businessman for the year ending on 31st March, 2016.

Profit and Loss Account

Particulars	Amount	Particulars	Amount
To Salary	1,25,000	By Gross Profit	3,00,000
To General expenses	12,500	By Commission	30,000
To Conveyance	1,250	By Sundry Receipt	3,000
To Postage	125	By gift from a friend	12,000
To Depreciation	25,000	By Interest on fixed deposits	23,075
To Computer Stationery	2,500	By Bad Debts recovered	10,000
To Construction of canteen	15,700		
To Donation to an education Institute	10,500		
To Sales tax	25,000		
To R.D.D.	2,500		
To Net profit	1,58,000		
	3,78,075		3,78,075

Additional Information :

(i) Salary includes 12,500 paid to Mr. Businessman.

(ii) General expenses include 5,850 as the gift given to a friend on his marriage ceremony.

(iii) Depreciation allowed as per income tax rules is amounted to 22,000.

(iv) Sales tax included 2,500 as penalty for evasion of sales tax.

Compute taxable income from business of Mr. Businessman for the assessment year 2016-17.

Solution :

Computation of Income from Business of Mr. Businessman.
For the Assessment year 2016-17

Particulars	Amount	Amount
Profit as per Profit and Loss A/c		1,58,000
Add : Disallowed expenses debited to P&L A/c		
(i) Salary to proprietor	12,500	
(ii) General expenses (gift to friend)	5,850	
(iii) Depreciation (Excess) (25,000 - 22,000)	3,000	
(iv) Penalty for evasion of sales tax	2,500	
(v) Construction of canteen (capital expenditure)	15,700	
(vi) Donation to an educational Institute	10,500	
(vii) R.D.D.	2,500	52,550
		2,10,550
Less : Income under other heads credited to P&L A/c		
(i) Gift from a friend	12,000	
(ii) Interest an Fixed deposits	23,075	- 35,075
Income from business		1,75,475

Income from business 1,75,475

NOTES

Problem 5.8 :

The following is the profit and loss account for the year ended on 31st March 2016, furnished by Mr. Abhishek.

Profit and Loss Account

Particulars	Amount	Particulars	Amount
To Salary	78,000	By Gross profit	2,00,000
To Advertisement	8,000	By Sundry receipt	8,400
To Fire insurance	3,500	By Gift from a father	25,000
To Office expenses	4,500	By Interest on bank deposits	6,000
To Depreciation	15,800	By Bad debts recovered	5,400
To Bonus	12,800	(not allowed as deduction earlier)	
To Income tax	8,600		
To Sales tax	4,500		
To Interest on bank loan	5,600		
To Interest on Income tax	3,500		
Net Profit	1,00,000		
	2,44,800		**2,44,800**

Other Information :

1. Salary includes 4,200 paid to a domestic servant.
2. Advertisement includes 550 as expenditure incurred for selling household furniture.
3. Allowable depreciation as per I.T. Rules is 14,000.
4. Sales tax includes 500 as penalty for not filing returns in time.
5. Bank loan is for business purposes.

You are required to compute taxable income from business for the A.Y. 2016-17 of Mr. Abhishek.

Solution : Computation of Income from business of Mr. Abhishek

For the Assessment Year 2016-17

Particulars	Amount	Amount
Net Profit as per Profit and Loss A/c		1,00,000
Add : Disallowed expenses debited to P&L A/c		
(i) Salary to domestic servant	4,200	
(ii) Advertisement (Household exp.)	550	
(iii) Depreciation (Excess) (15,800 - 14,000)	1,800	
(iv) Income Tax	8,600	
(v) Sales tax penalty	500	
(vi) Interest on Income tax	3,500	+ 19,150
		1,19,150
Less : Income under other heads but credited to Profit & Loss A/c		
(i) Gifts from father	25,000	
(ii) Interest on bank deposits	6,000	
(iii) Bad debts recovered (as not allowed earlier)	5,400	
		- 36,400
Income from business		**82,750**

Income from business 82,750

Problem 5.9:

Following is the Profit and Loss Account of a Merchant.

To Rent	6,000	By Gross Profit	52,300
To Salary to staff	5,400	By interest from debtors	2,800
To Diwali Pujan Expenses	200	By Rent from property	2,400
To Interest on loan	12,500	By Sundry incomes	1,000
To Sundry expenses	5,500	By Commission	3,700
To Bad debts	600		
To Charity	100		
To Reserve for bad debts	200		
To Rates	600		
To Entertainment	850		
To Loss by theft	1,400		
To Net profit	29,450		
	62,800		**62,800**

Other information :

1. Rent includes 1,200 of a shop belonging to the assessee himself.
2. Salary of staff includes salary of 2,400 of a son, who is B.Com. student and who casually helps in the business.
3. A loan of 6000 @ 15% p.a. is taken from his wife out of funds advanced by him and interest is included in interest on loan.
4. Sundry expenses include 900 being expenses incurred on pilgrimage to Hardware.
5. Entertainment includes 150 spent on tea of some guest of a local M.L.A.
6. Loss by theft took place when a pretended customer stole a necklace worth 800, were stolen from his house in the night by de-locking.
7. He earned 4,000 in gold smuggling not shown in books.
8. Rates include 400 for the property let. Compute the Merchant's Business Income.

Solution :

Computation of Income from business of Mr. Merchant
For the Assessment year 2016-17

Particulars	**Amount**	**Amount**
Net profit as per Profit and Loss A/c		29,450
Add : Disallowed expenses debited to P&L A/c		
(i) Charity	100	
(ii) Reserve for Bad Debts	200	
(iii) Rent paid to self	1,200	
(iv) Salary to son	2,400	
(v) Interest on loan from wife (funds advanced by him) (6,000 @ 15%)	900	
(vi) Pilgrimage Expenses	900	
(vii) Expenses on Tea to guest	150	
(viii) Loss by theft stolen from house	800	
(ix) Rates of Let Out Property	400	7,050
		36,500
Less : income not taxable under this head :		
(i) Rent from property	2,400	2,400
(a) Business Profit		34,100
(b) Add : Smuggling business income		4000
Profit and gains of Business or Profession		38,100

Income from business 38,100

NOTES

Notes :

1. Loss by theft from shop during working hours is a revenue loss, hence allowed.
2. Income may be legal or illegal it is taxable if declared.

5.14 Key Concepts

Expenditure allowed by income tax act is allowed expenditure while others are disallowed.

5.15 Summary

Third head of income is 'Profit and Gain from Business or Profession'. There are three main concepts i.e. Business, profession and vocation. The rules for assessment of business, profession and vocation are same. Expenditure means outflow of cash and income means inflow of cash. Expenditures are classified as revenue and capital expenditure. There are some expenses which are expressly allowed as deductions from profit and gain of business premises, depreciation, repairs and insurance of machinery, plant and furniture etc. All personal expenses are disallowed expenses. All types of revenue expenditures are allowed expenses and all capital expenditures are disallowed expenses. Personal income treated as disallowed income.

5.16 Exercise

1. Give short note on:
   (i) Business
   (ii) Profession
   (iii) Vocation
2. List out expenses/deductions expressly allowed as deduction from profit and gain from business or profession.
3. List out disallowed expenses.
4. List out disallowed incomes.

- **Fill in the blanks**

1) _____means the purchase and sale or manufacture of a commodity with a view to make profit.

(Business, Profession, Trading, Manufacturing)

2) _____ means the activities for earning livelihood which require intellectual skill or manual skill.

(Business, Profession, Trading, Vocation)

3) _____ means activities which are performed in order to earn livelihood.

(Business, Profession, Trading, Vocation)

4) _____is allowed on tangible assets and also on intangible assets.

(Depreciation, Expenditure, Appreciation, Income)

5) If Research and development expenses for personal business, then all _____are allowed.

(expenses, capital expenses, revenue expenses, depreciation)

6) If any donation given for research to any approved institute, university or government department then deduction is cumulative _____of donation given.

(150%, 125%, 200%, 100%)

7) Preliminary expenses are allowed to be distributed over ____ years equally.

(10, 5, 7, 8)

8) Any revenue expenditure incurred for the promotion of family planning is _____ allowed.

(150%, 125%, 200%, 100%)

9) Any capital expenditure incurred for the promotion of family then _____ allowed in a year.

(1/5th, 1/4th, 1/2, 1/3rd)

10) Any payment in excess of _____ must be required by account payee cheque or demand draft.

(35,000, 25,000, 20,000, 50,000)

11) In case of_____, interest paid on capital in excess of 12% will be disallowed.

(HUF, partnership firm, individual, company)

12) _____ expenses not allowed to charge to P & L A/c.

(Advertisement, Personal, Research, Business)

13) Sales tax, excise duty paid upto the date of filing the _____and expenses incurred in connection with sale tax proceeding including appeals.

(Income Tax Return, VAT Return, TDS Return, CST Return)

(**Answers:** 1) Business, 2) Profession, 3) Vocation, 4) Depreciation, 5) revenue expenses, 6) 125%, 7) 5, 8) 100%, 9) 1/5th, 10) 20,000, 11) partnership firm, 12) Personal, 13) Income Tax Return)

5.17 Further Reading and References

1) Students Guide To Income Tax by Vinod Singhania
2) Taxman
3) Income Tax Bare Act

UNIT 6
CAPITAL GAIN

NOTES

6.0 Introduction
6.1 Objectives
6.2 Basis of Charge [Section 45]
6.3 Chargeability of Tax
6.4 Some Important Definitions
6.5 Computation of Capital Gains
6.6 Full Value of Consideration
6.7 Cost of Acquisition
6.8 Deemed Cost of Acquisition
6.9 Indexed Cost of Acquisition
6.10 Cost of Improvement
6.11 Indexed Cost of Improvement
6.12 Tax on Capital Gains
6.13 Exemptions under the Head 'Capital Gains'
6.14 Key Concepts
6.15 Summary
6.16 Exercise
6.17 Further Reading and References

CHECK YOUR PROGRESS

What is the Chargeability of Captial Gain?

6.0 Introduction

Capital gain means any profit or gain arising from the transfer of a capital asset. It is treated as income of the previous year in which the transfer takes place. Capital receipts are not taxable. But gains or profits from transfer of certain asset is treated as income chargeable to income tax use as.

6.1 Objectives

After reading this unit, you should be able :

1. To know about Long Term Capital Gain.
2. To know about Short Term Capital Gain.
3. Deductions under Capital Gain.

6.2 Basic of Charge [Section 45]

Any profit or gain arising from the transfer of a capital asset is chargeable to tax under the hear Capital gains in the previous year in which the transfer took place. Capital gains tax liability arises only when the following conditions are satisfied:

1. There must be a capital asset.
2. The capital asset must have been transferred by the assessee.
3. Such transfer takes place during the previous year.
4. There must be profits or gains on such transfer.

6.3 Chargeability Tax

The following gains are chargeable to tax under the head 'Capital Gain'

1. Any profits or gains arising from the transfer of a capital asset effected in the previous year shall be chargeable to income-tax under the head 'Capital Gain' [Section 45 (1)].
2. Capital gain an receipt of compensation from insurance company for damage or destruction etc. of capital asset [Section 45 (1A0] (w.e.f. A.

Y. 2000-01)

3. Capital gains on the conversion of a capital asset into stock in trade [Section 45 (2)].
4. Capital gain on transfer of a capital asset by a partner member to a firm (AOP) BOI as capital contribution shall be chargeable to tax in the hands of the partner member [Section 45(3)].
5. Capital gain on transfer of a capital asset by a firm/AOP/BOP to partner member on dissolution or otherwise shall be chargeable to tax as the income of the firm/AOP/BOI.
6. Capital gains on the compulsory acquisition of an assets by the Government.
7. Capital gain on conversion of debentures into shares.
8. Capital gains on distribution of assets by companies in liquidation [Section 46].
9. Capital gain on transfer of business.

NOTES

6.4 Some Important Definitions

1. Capital Assets [Section 2(14)]: 'Capital Asset' means property of any kind held by an assessee, whether or not connected with his business or profession but does not include the following:

(i) Stock-in-trade, row materials or consumable stores held for the purposes of business or profession.

(ii) Agricultural land in India which is not urban agricultural land or not situated in any specified area.

(iii) Gold deposit bonds issued under the gold deposit scheme 1999 by the Central Government.

(iv) Personal effects of movable nature such as furniture, vehicles, held for personal use by the assessee or any dependent member of his family. However, Jewellery archaeological collections, drawings, paintings and any work of art are capital asset.

2. Short Term capital Asset [Section 2 (42A0] : Short term capital asset means capital asset held by an assessee for not more than 36 months, immediately prior to its date of transfer. However, the following assets are treated as short term capital assets if they are held by on assessee for not more than 12 months.

(i) Equity or preference shares in a company.

(ii) Securities (like debentures, Government Securities) listed in a recognized stock exchange in India.

(iii) Units of U.T.I.

(iv) Units of mutual fund specified under section 10(23D).

3. Long-term capital asset [Section 2(29A)]: Asset other than short term capital asset is regarded as long term capital asset. In other words, if the asset is held by the assessee for more than 36 months (12 months in case of shares, units) will be treated as a long term capital asset.

4. Short Term Capital Gains [Section 2 (42B)] : 'Short-Term Capital Gains' means capital gain arising from transfer of short term capital asset is called as short term capital gain.

For tax purpose S.T.C.G. is classified as -

(a) S.T.C. G. arising from sale/transfer at listed securities and

(b) S.T.C.G. arising from the transfer of short term capital assets other than listed securities.

5. Long Term Capital Gains [Section 2(29B)] : 'Long-Term Capital Gains' means capital gain arising from transfer of long term capital asset.

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For tax purpose long term capital gain is classified as:

(a) L.T.C.G. arising from sale/transfer of an equity shares in a company or a units of an equity oriented funds. (listed securities) and

(b) L.T.C.G. arising from the transfer of L.T.C. assets other than listed securities.

6. Transfer of Capital Asset: Transfer, in relation to a capital asset, includes sale, exchange or relinquishment (to surrender) of the capital asset or extinguishment of any rights there in or the compulsory acquisition there of under any law.

In case where the asset is converted by the owner into stock in trade, such conversion is also a transfer of capital assets.

However certain transactions are not regarded as transfer e.g.

(i) Distribution of assets by HUF to its family members at the time of total or partial partition.

(ii) Distribution of assets by a company to its shareholders an liquidation.

(iii) Transfer under a will or an irrecoverable trust or a gift or deemed gift.

(iv) Transfer of capital asset by a company to its wholly owned Indian subsidiary company and vice versa but not as stock in trade.

(v) Any transfer, in a scheme of amalgamation, of a capital asset by the amalgamating company to the amalgamated company (Indian company).

(vi) Transfer of assets by the banking company to the banking institution.

CHECK YOUR PROGRESS

How you Compute Capital Gain?

6.6 Computation of Capital Gains

[A] Computation of Short Term Capital Gains

(i.e. gains arising from the transfer of a short term capital assets)		
Full consideration on transfer (selling price)		xxx
Less : 1. Cost of Asset	xxx	
2. Cost of improvement to the asset	xxx	
3. Expenditure on transfer of assets	xxx	
		xxx
Short Term Capital Gain		**xxx**
Less : Exemption uls 54/54B/54D/54G		xxx
Short term Capital gain (Chargeable to tax)		**xxx**

[B] Computation of Long Term Capital Gain :

(i.e. gains arising from the transfer of a long term capital assets)		
Full consideration on sale or transfer		xxx
Less : 1. Indexed cost of Acquisition	xxx	
2. Indexed cost of improvement	xxx	
3. Expenditure on sale/transfer	xxx	xxx
Long Term Capital Gain		xxx
Less : Exemption under section 54B/54D/54EC/54F/54G	xxx	xxx
Long Term Capital Gain (Chargeable to tax)		xxx

6.6 Full Value of Consideration

It means the total price, the transferor of asset receives for giving up his right on the capital asset transferred. The full value means the whole price paid without any deduction.

NOTES

6.7 Cost of Acquisition

The cost of acquisition of an asset is the value for which it was acquired by the owner. The cost includes any expenditure of capital nature incurred for completing or acquiring the title to the property.

6.8 Deemed Cost of Acquisition

Where the capital assets became the property of the assessee under a gift or will or on the distribution of the assets on partition of H.U.F., the cost of acquisition of such assets shall deemed the cost of acquisition to the previous owner or its fair market value as on 1-4-1981 at the option of the assessee.

CHECK YOUR PROGRESS

What is Indexed Cost of Acquisition?

6.9 Indexed Cost of Acquisition

In case of long term capital gains, the amount to be deducted from the full value of the consideration includes Indexed cost of acquisition and improvement.

Indexed cost of acquisition means the amount which bears to the cost of acquisition, the same proportion as cost Inflation Index for the year in which the asset is transferred bears to the cost Inflation Index for the first year in which the asset was held by the assessee or for the year beginning an April 1981, whichever is later. The indexed cost of acquisition is computed as under:

Cost of acquisition or Fair Market Value as on 1-4-81 to assessee or previous owner, whichever is more

$$\text{Indexed cost of acquisition} = \frac{\text{Cost of acquisition or Fair market value as on 1-4-81 to assessee or previous owner whichever is more}}{\text{It for the year of purchase or 1981-82 if value of 1-4-81is taken}}$$

CII = Cost Inflation Index

6.10 Cost of Improvement

The cost of improvement means capital expenditure incurred for increasing the value of asset. All expenses of capital nature incurred in making any addition/ alteration to the capital assets are included in the cost of improvement.

6.11 Indexed Cost of Improvement

Indexed cost of improvement means the amount which bears to the cost

NOTES

of improvement, the same proportion as cost Inflation Index for the year in which the asset is transferred beans to the cost inflation Index for the year in which the improvement to the asset takes place. It is computed as under

$$\text{Indexed cost of improvement} = \frac{\text{Cost of improvement incurred by assessee or previous owner}}{\text{CIT for the year of improvement}} \times \text{CII for the year inwhich asset is transferred}$$

Cost Inflation Index

Previous Year	Cost Inflation Index
1981-82	100
82-83	109
83-84	116
84-85	125
85-86	133
86-87	140
87-88	150
88-89	161
89-90	172
90-91	182
91-92	199
92-93	223
93-94	244
94-95	259
95-96	281
96-97	305
97-98	331
98-99	351
99-2000	389
2000-01	406
2001-02	426
02-03	447
03-04	463
04-05	480
05-06	497
06-07	519
07-08	551
08-09	582
09-10	632
2010-11	711
2011-12	785
2012-13	852
2013-14	939
2014-15	1024
2015-16	1081

NOTES

6.12 Tax on Capital Gains

(a) Tax on short term capital gain [Section 111A]: S.T.C.G. is taxable like any other income. But short term capital gain arising from the equity shares or units of an equity funds and if such transaction is chargeable to securities transaction tax. The income tax payable an such S.T.C.G. is 10% (15%).

(b) Tax an Long Term Capital Gain [Section 112]: If income under other heads are taxable, the L.T.C.G. is taxable at a flat rate of 20%, L.T.C.G. on sale or transfer of equity shares/units of an equity funds chargeable to securities transaction tax is exempted from tax.

6.13 Exemptions under the head 'Capital Gains'

(a) Capital Gains arising from Transfer of Residential House [Section 54]: Section 54 provides exemption to capital gains arising from the transfer of a residential house property (being building or lands appurtenant there to the income of which is chargeable under the head 'Income from house property) Under this section only an individual or a HUF can claim exemption.

(b) Capital Gains arising from transfer of load used for Agricultural Purpose [Section 54B]: Exemption U/s 54B is available an transfer of agricultural land, provided the taxpayer is an individual and he transfer an agricultural land which was used by tax payer or his parents for agricultural purposes for a period of two years immediately preceding the date of transfer.

(c) Capital Gains on compulsory Acquisition of land and Buildings forming part of Agricultural Undertaking [Section 54D] : The amount of exemption under this section is equal to the amount of capital gains generated on transfer by way of compulsory acquisition of land or building or the amount invested in new land and building, provided that the taxpayer may an individual, HUF, Firm, Company or any other person and such land or building was used by the assessee for the purpose of agricultural undertaking for at least two years preceding the date of compulsory acquisition.

(d) Capital Gains on Investment in Certain Bands [Section 54EC] : The amount of exemption under this section is the amount of capital gains generated on transfer of capital asset, or the amount invested in it, provided that the assessee may an individual firm, company or any other person and the asset transferred should be along term capital asset.

(e) Capital gain on transfer of assets in case of shifting of industrial undertaking from urban areas. [Section 54G].

(f) Capital gain on transfer of certain listed securities/units not to be charged to tax an certain cases. [Section 54ED].

(g) Long term capital gains on transfer of assets other than a residential house. [Section 54F].

Problems on 'Capital Gain'

Problem 6.1 :

X sells his house, the sale proceeds are 5,80,000 in 2015-16. The house was acquired in 1985-86 for 18,000. The cost of improvement is 70,000 in the year 1991-92. Calculate capital gains. Cost inflation index was

2015-2016 : 1081

1991 - 92 : 199

1985 - 86 : 133

(M.B.A. December, 2007)

Solution :

NOTES

Computation of Capital Gains of Mr. X

Particulars	**Rs.**	**Rs.**
(a) Sale Consideration	5,80,000	
Less : Expenses Incurred	-	Nil
(b) Net Consideration		**5,80,000**
Less : (i) Indexed cost of acquisition		
Rs. 18,000 x 1081 / 133	1,46,300	
(ii) Indexed cost of improvement		
Rs. 70,000 x 1081 / 199	3,80,251	5,26,551
Gross Capital Gain		53,449
Less : Exemption U/s 54 (cost of new house or capital gain whichever is lower)		Nil
Net Capital Gain		53,449

Net Capital Gain = 53,449

Problem 6.2:

'X' sells the following capital assets during the previous year 2015-16.

	Shares	Self Generated good will	House Property
Sale Consideration	6,30,000	15,00,000	3,15,700
Year of Acquisition	1991 - 92	N.A.	1983.84
Cost of Acquisition	2,90,000	Nil	18,000
Cost of Improvement Incurred in 1989-90	-	-	10,000

Compute the capital Gain for A.Y. 2016-17 (C.II for 2015-16 = 1081, 91-92 = 199, 83-84 = 116, 89-90 = 172)

Solution :

Computation of Capital Gain

For the Assessment Year (2016-17)

	Shares	Self Generated good will	House Property
Sale consideration	6,30,000	15,00,000	3,15,700
Less :			
(i) Indexed cost acquisition	15,75,327	Nil	1,67,741
(ii) Indexed cost of Improvement	Nil	Nil	62,849
Long Term Capital Gain/(Loss)	**(-9,45,327)**	**15,00,000**	**85,110**

Income Under the Heads 'Capital Gain' = (15,00,000 + 85,110 - 9,45,327)

= 6,39,783

Income from Capital Gain =6,39,783

Working notes :

1. Indexed Cost of Acquisition (shares) :

$$= 2,90,000 \times \frac{\text{Cost Inflation Index for 2015-16}}{\text{Cost Inflation Index for 1991-92}}$$

$$= 2,90,000 \times 1081 / 199$$

$$= 15,75,327$$

2. Indexed cost of Acquisition (House Property) :

$$= 18,000 \times \frac{\text{Cost Inflation Index for 2015-16}}{\text{Cost Inflation Index for 1983-84}}$$

$$= 18,000 \times 1081 / 116$$

$$= 1,67,741$$

3. Index Cost of Improvement :

$$= 10,000 \times \frac{\text{Cost Inflation Index for 2015-16}}{\text{Cost Inflation Index for 1989-90}}$$

$$= 10,000 \times 1081 / 172$$

$$= 62,849$$

Problem 6.3:

Mr. Shamrao purchased a house property for ` 3,00,000 an 1st May 1975. The following expenses are incurred by him for making addition and alteration to the house property.

(I) Cost of construction of first floor in 1979-80 ` 3,60,000.

(II) Cost of construction of second floor in 1984-85 ` 4,40,000.

(III) Renovation of the property in 1997-98 2,50,000. Fair market value of the property on 1st April 1981 is 7,20,000. The house property was sold in November 2015 for ` 95,50,000 by incurring expenditure of ` 1,60,000 on transfer. The cost inflation index for 1981-82, 1984,85, 1997-98 and 2015-16 were 100,125, 331, and 1081 respectively.

Compute the taxable capital gain for assessment year 2016-17.

Solution :

Computation of taxable L.T.C.G. for A.Y. 2016-17 of Mr. Shamrao

Sale proceeds of property		95,50,000
Less : Exp. on transfer		-1,60,000
Net Sale Proceeds		**93,90,000**
Less : (i) I.C.A. (7,20,000 x 1081/100)	77,83,200	
(ii) I.C.T. (Second floor) (4,40,000 x1081/125)	38,05,120	
(iii) Indexed Cost of Renovation (2,50,000 x 1081/331)	8,16,465	1,24,04,785
L.T.C.L.		**(-30,14,785)**

I.C.A. Indexed Cost of Acquisition

I.C.I. Indexed Cost of Improvement

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Working Note :

Cost of Acquision upto 1st Apritl 1981 or fair market value as on 1-4-81 whichever is higher is to be taken as has.

(a) Cost of Acquisition = Purchase price 3,00,000 + Addition during 1979-80 3,60,000 = 6,60,000.

OR

(b) Fair Market value as on 1-4-81 = 7,20,000

Highest value is 7,20,000

Long term capital loss 30,14,785

Problem 6.4:

From the following particulars find out capital gain in the hands of Mr. Rajkumar.

	Cost of Acquisition	F.M. Value on 1-4-1981	Consideration or sales
1. Goodwill	-	40,000	4,00,000
2. Tenancy Right	-	1,00,000	6,00,000
3. Route permit	-	50,000	5,00,000
4. Shares acquired in 1978	70,000	50,000	4,00,000

Relevant Index is 497

Solution :

Statement showing Taxable Capital Gain

Particulars	Goodwill	Tenancy Right	Route Permit	Shares
Value of consideration	4,00,000	6,00,000	5,00,000	4,00,000
Less : Indexed cost of asset 70,000 x 497 / 100	-	-	-	3,47,900
Long Term Capital Gain	**4,00,000**	**6,00,000**	**5,00,000**	**52,100**

Total capital Gain = 4,00,000 + 6,00,000 + 5,00,000 + 52,100 = 15,52,100.

Total Capital gain 15,52,100

Problem 6.5:

On April 25, 2015 Rambhau Patil sold an Urban Agricultural Land for 70,00,000, which had been used for Agricultural purposes for several years. He acquired that land in 1979 for ` 2,50,000. The market value of such land as on April, 1, 1981 was ` 5,00,000. He purchased rural Agricultural land for ` 8,00,000 on June 25, 2015, which was sold for ` 12,50,000 on January 18, 2016. A sum of ` 11,50,000 was also invested by him in purchase of residential property on July 25, 2015. He did not own any house property before this date. The new house property was sold on March 28, 2016 for ` 13,00,000. Compute his taxable Capital Gains for the Assessment Year 2016-17.

Cost inflation Index for F.Y. 2015-16 =1081.

Solution :

Computation of Capital Gain For A.Y. 2016-17

Particulars	
Value of sale consideration of Urban Agricultural Land	70,00,000
Less : Indexed cost of acquisition 5,00,000 x 1081 / 100	54,05,000
Gross L.T.C.G. (A)	**15,95,000**
Less : Exempted U/s 54	
(i) Agricultural Land (Rural - sec. 54B)	8,00,000
(ii) Residential house (Section 54F)	2,62,035
(13,95,000 11,50,000/39,50,000)	
Gross L.T.C.G. (B)	**10,62,035**
Long term Capital Gain (A-B)	5,32,965
Assessment year 2016-2017	
Sale consideration of House property	13,00,000
Less : Cost of acquisition	11,50,000
S.T.C.G.	**1,50,000**
L.T.C.G. (previously exempted u/s 54F) become taxable as the house property is transferred within three years.	4,06,139
Total Capital Gain	**5,56,139**

Note :

1. Agricultural Land (Rural) sold on 18th Jan, 2016 for 12,50,000. There will be no capital gain on the transfer of rural agricultural and although sold within three years from the date of its acquisition, as it is not a capital assets for capital gain purpose.
2. No change in provisions for A.Y. 2013-14. A.Y. 2014-15 and 2015-16.
3. Exemption u/s 54F = LTCG/Net sales consideration x cost of aquisition

   = 15,95,000/70,00,000 x 11,50,000

   = 2,62,035

Problem 6.6:

Nakul is a resident of India. He furnishes the following information for the previous year ended 31-3-2016.

1. Capital Gain 21,000 from a house which he purchased two years before the date of sale 21-08-2015.

2. On 31-1-2016 he sold equity shares of TISCO Ltd. For 9,50,000 through recognized stock exchange, which were purchased by him on 1-4-86 for 2,10,000 (CIT 1986 = 140)

3. He sold an agricultural land for 2,55,000 on 30-8-2014. The land was owned by him for last six years and was purchased for 60,000. The land is situated in a village having population of 4,500.

4. On 1-2-2016 he sold a flat for 10,00,000 which was purchased by him on 1981 for Rs.90,000 Compute his taxable in come from capital gains for the A.Y. 2016-17 (Current CIT = 1081)

NOTES

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Solution :

Computation of income from capital gain of Mr. Nakul for the A.Y. 2016-17

Particulars	
(i) S.T.C.G. from sale of house property (House held less than 36 months)	21,000
(ii) L.T.C.G. from sale of TISCO Ltd. shares (exempted note)	
(iii) Agricultural land not on capital assets. No capital Gain on sale	Nil
(iv) **L.T.C.G. on sale of flat**	
Sale consideration (Fair market value is taken)	10,00,000
Less : Indexed Cost of Acquisition 90,000 x 1081 / 100	9,72,900
L.T.C.G.	**27,100**
Taxable income from capital gain	
(a) Short term capital gain	21,000
(b) Long term capital gain	27,100
Total Capital Gain	**48,100**

Note : If the shares of Public Ltd. company had been sold through recognized stock exchange and securities transaction tax had been paid there on at the time of sale L.T.C.G. there on would be exempt u/s 10(38) Here it is assumed that securities transaction tax has been paid.

Total capital gain 48,100

Problem 6.7 :

Mr. Rambhau sells agricultural land situated within the municipal limits of Pune for 60,00,000 on 4th July, 2005, which was purchased by him on 1st March,1988 for 8,00,000. On 15th July, 2006 he purchased agricultutal land in rural are a for ` 8,60,000 and deposited 21,60,000 in a deposit account for availing exemption u/s 54B. He purchased another agricultural land (situated within the limit of Pune Municipal corporation) an 30th June, 2007 for 1694,000 by withdrawing from the deposit. Amount left in the deposit account is withdrawn on 10th July, 2007. The agricultural land in rural area is transferred on 1st April, 2008 for 9,80,000 and the land in Pune is transferred on 17th July, 2008 for 17,40,000. Determine the amount of capital gains.

Cast inflation index for different assessment year : 1987-88-150, 2005-06-497, 2007-08-551.

Solution :

Assessment year 2006-07	
Sale proceeds	60,00,000
Less : Indexed cost of acquisition 8,00,000 x 497 / 150	26,50,667
Balance (A)	**33,49,333**
Less : Exemption u/s 54B	
(i) Cost of Rural Agricultural land purchased 15-7-2006	8,00,000
(ii) Amount deposited (C.G. deposit a/c scheme 1988)	21,60,000
Balance (B)	30,20,000
Long term capital gain (A-B)	**3,29,333**
Assessment year 2008-09	
Amount deposited (withdrawn)	21,60,000
Less : Amount utilized for purchasing agricultural land (urban)	- 16,94,000
L.T.C.G. (utilized amount)	**4,66,000**

Assessment year 2009-10

	Agri. Land in Rural area	Agri. Land in Urban area
Sale proceeds	9,80,000	17,40,000
Less : Cost of acquisition (New assets transferred within 3 years)	8,60,000	16,94,000
S.T.C.G.	**Not taxable**	**46,000**
Add : Exempted L.T.G. (A.Y. 2008-09) becomes taxable as the urban agricultural land at Pune is transferred within 3 years		16,94,000
Total S.T.C.G.		**17,40,000**

Note : As the agricultural land in rural area is not a capital assets and consequently capital go in on its transfer is not chargeable to tax.

Total short term capital gain 17 40 000

Problem 6.8 :

From the following information compute the capital gains for the A.Y. 2016-17.

	House I	House II
Date of Purchase	May 1977	Dec. 1980
Cost of acquisition	1,90,000	2,50,000
Cost of additional construction in 1980	10,000	25,000
Fair Market value an 1st April, 1981	1,75,000	3,50,000
Cost of additional construction (1994-95)	51,800	77,700
Sale proceeds of property in 2015-16	22,00,000	50,00,000

Cost inflation index are :

1981- 82 = 100

1994 - 95 = 259

2015 - 16 = 1081

Solution :

Computation of Capital Gains

House I : Selling price		22,00,000
Less : (i) Indexed cost of acquisition (note -1)	21,62,000	
(ii) Indexed cost of improvement in 1994-95 (51,800 x 1081 / 259)	2,16,200	23,78,200
L.T.C. Loss		**(-1,78,200)**

Note 1 : Indexed cost of acquisition has been calculated as under :

(Cost of acquisition + additional construction before 1-4-81) or fair market value as on 1-4-81 whichever is more = (1,90,000 + 10,000) or 1,75,000 whichever is more i.e. 2,00,000. Hence, ICA = 2,00,000 x 1081 / 100 = 21,62,000.

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Computation of capital gain

House II selling price		50,00,000
Less : (i) Indexed cost of acquisition	37,83,500	
(ii) Indexed cost of improvement in 1994-95 (77,700 x 1081 / 259)	3,24,300	- 41,07,800
L.T.C. Gain		**8,92,200**

Note 2 : Indexed cost of acquisition has been calculate as under :

(cost of acquisition + additional construction before 1-4-81) or fair market value as an 1-4-81 whichever is more = (2,50,000 + 25,000) or 3,50,000 whichever is more i.e. 3,50,000

Hence, ICA = 3,50,000 x 1081 / 100 = 37,83,500

Note 3 : Capital expenditure incurred prior to 1-4-1981 will not be added to arrive at the cost of acquisition as fair market value as an 1-4-1981 includes in it.

Note 4 : Actual cost of acquisition is ignored as it is lower than fair market value as on 1-4-1981.

Total long term capital gain = 8,92,200 - 1,78,200

= 7,14,000

Problem 6.9 :

Mr. Sahdeo sells shares in a private ltd. company on 10th July 2015 for 16,10,000 which was purchased an 15th June 1985 for 1,20,000. Expenses an sale 10,000. On 10th July 2015, he owns one residential u/s 54F. Sahdeo deposits 12,00,000 in Capital Gain Deposit Account scheme on 13th July 2015. By withdrawing from the Deposit Account, he purchased a residential house property in Pune on 6th July 2016 for 9,60,000 Ascertain -

(a) The amount of Capital Gain chargeable to tax for the A.Y. 2016-17.

(b) Tax treatment of the unutilized amount.

(c) Tax treatment if the new house sold before 6-7-2018.

(d) When can be withdraw the unutilized amount.

(e) What Sahdeo has to do to ensure that exemption u/s 54F is never taken back.

CII 1985-86 = 125, 2015-16 = 1081 assumed.

Solution :

(a) Capital Gain for A.Y. 2016-17.

Sale consideration consideration	16,10,000
Less : Expenses on sale	- 10,000
Net sale	**16,00,000**
Less : I.C.A. 1,20,000 x 1081 / 125	10,37,760
Gross L.T.C.G.	5,62,240
Less : Exemption u/s 54F 12,00,000 x 5,62,240 / 16,00,000	- 4,21,680
	1,40,560

(b) Tax treatment of unutilized amount :

Note 1 : In this case Sahadeo has not fully utilized the deposit account for acquiring a residential house property. Out of 12,00,000 deposited for acquiring the house, it is utilized to the extent of 9,60,000. The tax treatment of 2,40,000 being the unutilized amount will be as follows :

Deposited	12,00,000
Utilised	
(a) Unutilised amount	9,60,000
(b) Net sale consideration	2,40,000
(c) Original capital gain	16,00,000
(d) National L.T.C.G. = a / b	10,43,200

Effective exemption u/s 54F 7,82,400 - 1,56,480 = 6,25,920.

1,56,480 will be chargeable to tax as L.T.C.G. after the expiry of 3 years from the date of transfer of share i.e. 9th July 2011. Consequently, it will be taxable for the A.Y.2012-13.

(c) It Sahdeo sells the new house at Pune before 6th July 2013 (before 3 years) then 6,25,920 (exempted u/s 54F) will be taken as L.T.C.G. of the year in which the house is sold (i.e.) During 6-7-2010 to 6-7-2013).

(d) The unutilized amount 2,40,000 can be will drawn at any time after 6th July 2011.

(e) It Sahdeo purchases any other residential house before 10th July 2010, or constructs any other house before 10th July 2011 then, 6,25,920 (exemption u/s 54F) will be deemed as L.T.C.G. of the year in which another house is purchased or constructed so he do not do like this.

6.14 Key Concepts

Property hold for less than 36 months is short term property and more than 36 months is long term property.

Index value is useful for long term capital gain.

6.15 Summary

Fourth head of Income is capital gain. Capital gain means any profit or gain arising from transfer of a capital asset. Short term capital asset means capital asset held by an assessee for not more than 36 months and gain arising from it is short term capital gain. Long term capital asset means capital asset held by an assessee for more than 36 months and gain. Full value of consideration, cost of acquisition, indexed cost of acquisition, cost of improvement and indexed cost of improvement are another important concepts.

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6.16 Exercise

1. What is 'Basis of charge for income from capital Gain?
2. What gains are chargeable to tax under the head 'Capital Gain'?
3. Write short note on

   (i) Capital Gain (ii) Capital Asset (iii) Short term capital asset (iv) Long term capital assets (v) Short term Capital Gain (vi) Long term capital gain (vii) Transfer of capital assets (viii) Full value of consideration (ix) Cost of acquisition (x) Indexed cost of acquisition (xi) Cost of improvement (xii) Indexed cost of improvement.
4. What is tax structure of Capital Gain?

- **Fill in the blanks**

1) _____means any profit or gain arising from the transfer of a capital asset.

   (Capital gain, Revenue gain, Other income, Miscellaneous income)

2) Capital gain is treated as income of the previous year in which the _____takes place.

   (purchase, transfer, conversion, registration)

3) '_____' means property of any kind held by an assessee, whether or not connected with his business or profession

   (Capital Asset, Stock in trade, Fixed assets, Capital liabilities)

4) _____means capital asset held by an assessee for not more than 36 months, immediately prior to its date of transfer.

   (Stock in stock, Long term capital assets, Short term capital asset, Capital liabilities)

5) Where the asset is converted by the owner into stock in trade, such conversion is also a _____of capital assets.

   (purchase, transfer, sale, registration)

6) The _____means the whole price paid without any deduction.

   (full value, net value, market value, fair value)

7) The _____includes any expenditure of capital nature incurred for completing or acquiring the title to the property.

   (purchase price, cost, value, market price)

8) In case of long term capital gains, the amount to be deducted from the full

value of the consideration includes _____and improvement.

(Indexed cost of acquisition, purchase cost, market value, cost of conversion)

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9) All expenses of _____incurred in making any addition/alteration to the capital assets are included in the cost of improvement.

(revenue nature, cost, capital nature, acquisition)

10) If income under other heads are taxable, the L.T.C.G. is taxable at a flat rate of _____.

(10%, 15%, 30%, 20%)

11) _____ provides exemption to capital gains arising from the transfer of a residential house property.

(Section 54B, Section 54, Section 54EC, Section 54D)

12) Exemption U/s 54B is available an transfer of_____, provided the taxpayer is an individual.

(residential house property, agricultural land, bonds, machinery)

(**Answers:** 1) capital gain, 2) transfer, 3) Capital Asset, 4) Short term capital asset, 5) transfer, 6) full value, 7) cost, 8) Indexed cost of acquisition, 9) capital nature, 10) 20%, 11) Section 54, 12) agricultural land)

6.17 Further Reading and References

1) Students Guide To Income Tax by Vinod Singhania
2) Taxman
3) Income Tax Bare Act

UNIT 7
INCOME FROM OTHER SOURCES

NOTES

7.0 Introduction 7.1 Objectives
7.2 Last Head of Income Under Gross Total Income
7.3 Expenses which are Deductible under the head 'Income from Other Sources [Section 57]
7.4 Inadmissible Expenses under the Head 'Income from Other Sources' [Section 58]
7.5 Basis of Charge under the Head 'Income from Other Sources'
7.6 Key Concepts 7.7 Summary
7.8 Exercise 7.9 Further Reading and References

7.0 Introduction

The residual head of income. Income which not chargeable under earlier four heads are chargeable under this head.

CHECK YOUR PROGRESS

Give the list of Income from Other Sources?

7.1 Objectives

After reading this unit, you should be able :

1. To know about residual head of Income Tax.
2. To know about Deductions under Other Sources.

7.2 Last Head of Income Under Gross Total Income

Last head of income under gross total income is 'Income from other source'. The income which is not chargeable in any other head chargeable to tax under the head of 'Income from Other Source'. Following are the main source of it.

1. **Dividend :** A share of profit of a company an equity share is dividend. Dividend received from Indian company or domestic company is totally exempted from tax. Dividend received on units from U.T.I. (Unit Trust of India) is also 100% exempted.
2. **Interest :** Interest received from any post office scheme, government scheme, state government scheme is totally exempt. But interest received from bank, fixed deposit, recurring deposit is totally taxable.
3. **Family Pension :** Any pension received to deceased employee to family members is family pension and exemption from it is :
   (i) 15,000 or
   (ii) 1/3rd of pension
   which is lower or less.
4. **Rent for Machine :** Any machine let out and rent received from it chargeable to tax under the head of income from other sources. Any expenses incurred for maintenance of machine or upkeep of machine is charge to tax as deduction.
5. **Winning from Lottery, Card Games, Gamble, Races including Horse Races etc. :** All are known as casual receipts and chargeable to tax under the head of income from other source. On casual receipts flat 30% tax charged for which a person who gives it liable to deduct and deposit.
6. **Contribution to Provident Fund (employee):** Employee's part of contribution to provident fund is not deposited by employer is chargeable to tax under the head of income from other source.
7. Any sum received under a keyman insurance policy including bonus if

not taxable as salary or business income.

8. Any specified properties including sum of money exceeding 50,000 received without consideration by an individual or H.U.F. from person other than relatives on or after 1-4-2006 subject to certain exceptions e.g. gift received from any relatives, shall be chargeable to tax.

9. Interest received on compensation or enhanced compensation u/s 145 A (2) (w.e.f. 1-4-2010 i.e. A.Y. 2010-11): Besides the following income is also chargeable under the head 'Income from Other Sources':

(a) Income from subletting.
(b) Interest on bank deposit and loans.
(c) Income from royalty (if it is not an income from business).
(d) Director's fee.
(e) Agricultural income from a place outside India.
(f) Director's commission for standing as a guarantor to bankers.
(g) Directors commission for underwriting shares of new company.
(h) Examination fees received by a teacher from a person other than his employer.
(i) Rent of plot of land.
(j) Insurance commission.
(k) Annuity payable under a will, contract trust deed.
(l) Salaries/remuneration paid or payable to a Member of Parliament.
(m) Interest on employee's contribution to unrecognized provident fund when it becomes due for payment.
(n) Income from undisclosed source.
(o) Gratuity paid to a director who is not an employee of the company.
(p) Annuity payable to the lender of a trade mark.
(q) Assessment fees for answer sheets.

CHECK YOUR PROGRESS

What are the Expenses which are Deductible under the head of 'Income from Other Source' ?

7.3 Expenses which are Deductible under the head 'Income From Other Sources' [Section 57]

(a) In respect of dividend income and interest income any reasonable expenditure incurred by way of commission or remuneration for realization of such income is deductible.
(b) In respect of any sum collected from employees towards the Welfare Fund Contribution deduction shall be allowed to the extent the amount is remitted within the relevant due date.
(c) In respect of family pension a sum equal to 33.33% of the pension or ` 15,000 whichever is less shall be allowed as deduction.
(d) In respect of income earned by ways of lease rental on letting of machinery, plant and furniture with or without building the following shall be deducted : (a) Repairs, (b) Insurance, (c) Depreciation.
(e) Any other expenditure incurred by the assessee not being capital expenditure but laid out or expended wholly or exclusively for the purpose of making or earning any income chargeable under this head of income can be claimed.

7.4 Inadmissible Expenses under the head 'Income from Other Source' [Section 58]

(a) Personal expenses.

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(b) Wealth tax.
(c) Expenses of the nature described in Section 40 A.
(d) Interest and salary payable outside India, if tax has not been paid or deducted at source.
(e) No deduction shall be allowed in respect of winnings from lotteries, crossword puzzles, card games, races including horse race, gambling, betting etc.

7.5 Basis of Charge Under the head 'Income from Other Sources'

The following income shall be charged to tax only under the head 'Income from Other Sources':

(a) Dividend income covered by sub-clauses (a) to (e) of clause (22) of Section 2.
(b) Income by way of winnings from lotteries, crossword, puzzles, races including horse race, card games and other games of any sort, gambling, betting, etc. It requires to mention here that such winnings are chargeable to tax u/s 115 BB of a flat rate of 30%.
(c) Any sum of money, the aggregate value of which exceeds 50,000 received from any person without consideration, by an individual or Hindu Undivided Family.

However, exemption is granted in respect of any sum of money received :

(i) From any relative or
(ii) On the occasion of marriage of an individual or
(iii) Under a will or by way of inheritance or
(iv) in contemplation or deaths of the payer or
(v) from a local authority, or
(vi) from any fund, foundation, university other educational institution, hospital, medical institution, any trust or institution referred to in Section 10 (23 c), or
(vii) from charitable institutions registered u/s 12 AA.

PROBLEM ON 'INCOME FROM OTHER SOURCE'

Problem 7.1 :

Shri. Hari Gopal is a Member of Parliament from Pune. During the previous year 2015-16 he had the following incomes :

1. As a member of parliament he received a salary of 30,000 p.m. and daily allowance of 40,000 for attending various sessions.
2. He held the following investments :

   (a) 10% preference shares in Pune Sugar Works Ltd. of the face value of 10,000.

   (b) 2,000 equity shares of 10 each in Tata Finlay Ltd. The company declared and paid a dividend at 15% on 15th February, 2016.

   (c) 10% fixed deposit of 2,00,000 is held by him in Indian Banks Interest is credited annually.

   (d) He received dividend of 1,000 from a co-operative society.
3. He won 8,000 in crossword puzzles.

4. On 1st September, 2012, he purchased a plot of land for constructing his house. On account of shortage of funds, he could not get this house constructed and hence let out the plot at 3,000 p.m. from 1st Nov. 2015.

5. He has let machinery and furniture and also building to Mr. Krishna Gopal at a monthly rent of 10,000. He spent 3,000 on the repair of machinery, furniture and building during the previous year. Depreciation allowable in respect of these assets for the previous year was 20,000.

   The bank charged 40 as commission on collection of dividends from various companies. Compute the taxable income of Shri. Hari Gopal under the head 'Income from Other Sources'.

Solution :

Computation of Taxable Income of Shri. Hari Gopal
For the A.Y. 2016-17

Particulars		
Income from Other Sources		
1. Salary as Member of Parliament (30,000 12)		3,60,000
2. Daily Allowance (exempted from tax)		-
3. Dividend on Preference Shares		-
4. Final Dividend on Equity Shares (exempted)		-
5. Dividend from Co-operative Society (No. T.D.S.)		1,000
6. Interest on Fixed Deposit		20,000
7. Winning from crossword, puzzles fully taxable		8,000
8. Income from plot of land for 5 months		15,000
9. Rental income from machinery, furniture and building		1,20,000
Less : Admissible Expenses		5,24,000
(i) Bank Commission on Collection of Dividend (Note 3)	Nil	
(ii) Repair Expenses	3,000	
(iii) Depreciation	20,000	23,000
Income from Other Sources		**5,01,000**

Income from Other Source 5,01,000

Note :

1. Winning from crossword, puzzles is causal income. Basic exemption is not allowed w.e.f. A.Y. 2003-04.
2. Daily allowance for attending session is exempt u/s 10 (17).
3. Dividend on shares of Indian Companies are exempted from tax w.e.f. 2004-05 and so, the bank commission on collection as dividend is not allowed.

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Problem 7.2 :

Mr. Ashish holds the following securities on April 1, 2015 :

8,00,000, 5% A.P. Govt. Loan (date of payment of interest January 1)

40,000, 6% Non-listed debentures of XYZ Ltd. (Dates of payment of interest June 11 and December 11 every year).

25,000, 8% debentures of ABC Ltd. (date of payment of interest : June and December is every year).

On 1-12-2015, Mr. Ashish sells 25,000, 8% debentures of ABC Ltd.

Calculate the Taxable Income of Mr. Ashish for the A.Y. 2016-17 on the assumption that his business income is 5,60,000.

Solution :

Computation of Taxable Income of Mr. Ashish
For the A.Y. 2016-17

Particulars	
A.P. Government Loan (+)	40,000
(8,00,000 x 5 / 100)	
Debentures of XYZ Ltd.	2,400
(40,000 x 6 / 100)	
(+) Debentures of ABC Ltd.	1,000
(Interest accrued on June 15th, 2015	
(25,000 x 8 / 100 x 1 / 2	
Interest on securities taxable under the head 'Income from Other Sources	43,400
Business Income	5,60,000
Gross Total Income	6,03,400
Less : Deductions	Nil
Net Income	**6,03,400**

Net Income 6,03,400

7.6 Key Concepts

Casual income is chargeable at flat rate 30%.

7.7 Summary

The fifth and last head of income is 'Income from Other Sources'. All those incomes which are not chargeable to tax under any other head, chargeable to tax under his head. Such incomes are dividend, interest on securities, family pension, rent for machine, royalty, casual receipts, contribution to provident fund etc. Personal expenses and wealth tax are inadmissible expenses.

7.8 Exercise

1. Give atleast 10 examples of income chargeable to tax under the head 'Income from Other Sources'.
2. Give expenses which are deductible under the head 'Income from Other Source'.
3. State 'Inadmissible Expenses under the head 'Income from Other Sources.
4. What is Basis of charge under the head 'Income from other source' ?

● **Fill in the blanks**

1) _____received from Indian company or domestic company is totally exempted from tax.
(Commission, Interest, Dividend, Profit)
2) Pension received to deceased employee to family members is family pension and exemption from it is ` _____ or 1/3rd of pension which is lower or less.
(20,000, 18,000, 50,000, 15,000)
3) On casual receipts flat _____ tax charged for which a person who gives it liable to deduct and deposit.
(60%, 30%, 50%, 20%)
4) Any sum of money, the aggregate value of which exceeds ` _____received from any person without consideration, by an individual or HUF chargeable to tax.
(20,000, 18,000, 50,000, 15,000)
5) In respect of dividend income and interest income any reasonable expenditure incurred by way of commission or remuneration for _____of such income is deductible.
(realization. claim, deposit, aggregate)
6) The income which is not chargeable in any other head chargeable to tax under the head of '_____'.
(Salary, Income from house property, Income from Other Source, Professional income)
7) _____received from bank, fixed deposit, recurring deposit is totally taxable.
(Commission, Interest, Dividend, Profit)
8) _____part of contribution to provident fund is not deposited by employer is chargeable to tax under the head of income from other source.
(Employee's, Employer's, Company's, Trust's)

(**Answers:** 1) Dividend, 2) 15,000, 3) 30%, 4) 50,000, 5) realization, 6) Income from Other Source, 7) Interest, 8) Employee's)

7.9 Further Reading and References

1) Students Guide To Income Tax by Vinod Singhania
2) Taxman
3) Income Tax Bare Act

UNIT 8
DEDUCTIONS u/s 80

NOTES

8.0 Introduction
8.1 Objectives
8.2 Deduction in respect of the amount paid or deposited out of income chargeable to tax or otherwise in the various chargeable to tax or otherwise in the various schemes [Section 80 C]
8.3 Deductions in respect of Contribution to Pension Fund and Annuity Plan [Section 80 CCC]
8.4 Deduction in respect of amount paid or deposited in a pension scheme [Section 80 (CCD)]
8.5 Maximum Limit [Section 80 (CCE)]
8.6 Deduction in respect of Medical Insurance Primium [Section 80 D]
8.7 Deductions in respect of Maintenance including Medical Treatment of Handicapped Dependents [Section 80 DD]
8.8 Deduction in respect of Medical Treatment [Section 80 DDB]
8.9 Deduction in respect of Payment of Interest on Loan taken for Higher Education [Section 80 E]
8.10 Deduction in respect of Donation to certain Funds and Charitable Institutions [Section 80 G]
8.11 Deduction in respect of Rent Paid [Section 80 GG]
8.12 Deduction in respect of certain Donations for Scientific Research or Rural Development [Section 80 GGA]
8.13 Deduction in respect of Royalty on Patents [Section 80 RRB]
8.14 Deduction in case of a Person Totally Blind or Physically Handicapped and Resident [Section 80U]
8.15 Key Concepts
8.16 Summary
8.17 Exercise
8.18 Further Reading and References

8.0 Introduction

Deduction form GTI which also known as indirect exemption.

8.1 Objectives

After reading this unit, you should be able :

1. To know about various deductions from GTI.
2. To know about certain calculations.

8.2 Deduction in respect of the amount paid or deposited out of income chargeable to tax or otherwise in the various schemes (Section 80 C)

Gross Qualifying Amount : Gross Qualifying Amount is the aggregate of the following payments :

1. **Life Insurance Premium :** Premium paid by an assessee for insurance on his own life or on the life of the spouse or any child including married daughter 20% of sum assured or amount of insurance premium paid whichever is

lower eligible for deduction.

2. Contribution to (i) Public Provident Fund (in the name of individual or spouse or any child of such individual subject to minimum ` 500 and maximum ` 70,000). (ii) Statutory Provident Fund, (iii) Recognised Provident Fund, (iv) Approved Superannuation Fund by an employee. This does not include repayment of loan or advance.
3. Any sum paid to purchase National Savings Certificate.
4. Interest accrued on National Saving Certificates.
5. Contribution made by an individual for participating in the unit linked insurance plan of UTI i.e. ULIP or United Linked Plan of the LIC mutual fund.
6. Any sum paid for notified annuity plan of the LIC or any other insurer e.g. New Jeevan Dhara and Jeevan Akshay Plans of LIC.
7. Any subscription, to notified units of any Mutual Fund covered u/s 10 (23 D) or the specified company of the UTI.
8. Contribution to notified pension fund set up by Mutual Fund or by the UTI or by National Housing Bank.
9. Any sum paid (including interest) as subscription to the home loan account scheme of National Housing Bank.
10. Any instalment or part payment of the amount due under any self financing authority engaged in the construction and sale of house property on ownership basis.
11. Any repayment of loan (principal) taken for purchasing or construction of a new residential house property.
12. Payment made for stamp duty, registration fees and other expenses for the purpose of transfer of house property to assessee.
13. Term deposits for a period of not less than five years with schedule banks.
14. Any sum paid as tuition fees (excluding the payment towards any development fees or donation or payment of similar nature/of the time of admission.
15. Deposit with post office.
16. Postal office insurance.
17. Any pension scheme.

Deduction is actual investment or 1,50,000 which is lower or less.

8.3 Deductions in respect of contribution to pension fund and annuity plan [Section 80 (CCC)]

Amount paid or deposited by an individual in an annuity plan of the LIC or any other insurer for receiving pension.

The deduction is amount paid or 1,50,000 whichever is lower.

Any additional investment of 20,000 with infrastructure bond is allowed. At that time maximum deduction available under 80C is 1,20,000.

8.4 Deductions in respect of amount paid or deposited in a pension scheme [Section 80 (CD)]

Any amount paid by an individual, employed by central government or any other employer in his account under a pension scheme notified by the Central Government shall be allowed as deduction in the computation of his total income.

Deduction is amount deposited or 10% of salary which is lower.

Salary = Basic + D.A. (if the terms of employment so provides).

8.5 Maximum Limit [Section 80 (CCE)]

(Newly inserted w.e.f. A.Y. 2006-07]. The aggregate amount of deduction u/s 80 C, 80 CCC and 80 CCD shall not in any case exceed 1,50,000.

NOTES

8.6 Deduction in respect of Medical Insurance Premium [Section 80 D]

The insurance premium on mediclaim insurance policy covering assessee, spouse, dependent parents and children, paid by the tax payer. The amount of premium must be paid by any mode other than cash and out of income chargeable to tax.

For this deduction premium must be paid by cheque :

Deduction is,

For an individual = Maximum 25,000 and additional 25,000 for parents

For senior citizen = Maximum 30,000 and additional 30,000 for parents

8.7 Deductions in respect of maintenance including medical treatment of handicapped dependents [Section 80 DD]

An expenditure incurred by the tax payer for the medical treatment (including nursing), training and rehabilitation of handicapped dependent or mentally retarded dependent relative.

Deduction is,

If below 80% handicapped 75,000.

If above 80% handicapped (severe disability).

1,25,000.

8.8 Deduction in respect of medical treatment [Section 80 DDB]

If an resident individual or H.U.F. has incurred some expenditure for medical treatment of a specified diseases or ailments (e.g. Cancer, AIDS, Chronic Renal Failure, Neurological Diseases) of the assessee himself or a dependent relative or the member of HUF is eligible for deduction. The assessee shall have to submit a certificate in prescribed form from a prescribed authority.

Deduction is,

For general actual expenses or 40,000 which is lower/less.

For senior citizen actual expenses or 60,000 which is lower/less.

8.9 Deduction in respect of payment of interest on loan taken for higher education [Section 80 E]

If loan is taken for higher education and repaid then the deduction is only the amount of interest of repayment loan. Only interest allowed as deduction. If principal amount repaid no deduction allowed.

8.10 Deduction in respect of donation to certain funds and charitable institutions [Section 80 G]

This section allows deduction in respect of amounts given as charitable donations and it is allowed to all types of assessee.

1. No limit donations : i.e. The whole amount quality for deduction. Such donations can be further classified as (i) Deduction allowed @ 100% of qualifying amount and (ii) Deduction allowed @ 50% of qualifying amount.

2. With limit donations : i.e. the qualifying amount for deduction shall not exceed 10% of gross total income. Such donations can further be classified as:

(i) Deduction allowed @ 100% of qualifying amount and

(ii) Deduction allowed @ 50% of qualifying amount.

NOTES

(A) No limit (without any qualifying limit) donations where deduction is allowed @ 100% of donation are as under :

1. The National Defence Fund set-up by the Central Government.
2. The Prime Minister's National Relief Fund.
3. The Prime Minister's America Earthquake Relief Fund.
4. The Africa (Public Contributions India) Fund.
5. The National Foundation for Communal Harmony.
6. A University or Educational Institution of National eminence as may be approved by the authority prescribed u/s 80 G.
7. The Maharashtra Chief Minister's Relief Fund or Chief Minister's Earthquake Relief Fund, Maharahstra.
8. Zilla Saksharta Sumitis.
9. Any Fund set up by State Government to provide medical relief to the poor.
10. The Andhra Pradesh Chief Minister's Cyclone Relief Fund.
11. Any fund set up by the State Government of Gujarat exclusively for providing relief to the victims of earthquake in Gujarat.

(B) No limit donations where deduction is allowed @ 50% are as under:

1. Jawahar Lal Nehru Memorial Fund.
2. Prime Minister's Drought Relief Fund.
3. National Children's Fund.
4. Indira Gandhi Memorial Trust.
5. Rajiv Gandhi Foundation.

(C) With limit donations where deduction is allowed @ 100% qualifying amount:

Donation to the Government or to any such local authority, institution or for approved association to be utilized for the purpose of promoting family planning.

(D) With limit donations where deduction is allowed @ 50% of qualifying amount:

1. The Government or any local authority to be utilized for charitable purpose other than family planning.
2. Any other fund or institution which is established in India for a charitable purpose fulfilling certain conditions.
3. Any authority dealing with and satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages.

Notes :

1. Donation should not be given in kind.
2. Donation should not be given for the benefit of any particular religion

8.11 Deduction in respect of rent paid [Section 80 GG]

An assessee is allowed a deduction in respect of payment of rent for any accommodation occupied by him for the purpose of his own residence.

Amount of deduction is least of the following :

(a) 2,000 p.m.

(b) 25% of adjusted total income.

(c) The excess of actual rent paid over 10% of adjusted total income.

Adjusted total income : GTI - (LICG + STCG taxable u/s 111 A + Deduction u/s 80 CCC to 80 U except 80 GG + Income under Section 115 A).

NOTES

8.12 Deduction in respect of certain donations for scientific research or rural development [Section 80 GGA]

Deduction is allowed to all assessee not having any income chargeable under the head "Profits and Gains or Business or Profession" [Section 80 GGA].

Amount of Deduction = 100% of the amount paid.

8.13 Deduction in respect of royalty on patents [Section 80 RRB]

The deduction is available to an individual who is resident in India and is patentee or co-patentee in receipt of any income by way of royalty in respect of patent registered on or after 1-4-2003 under the Patents Act, 1970 and his gross total income includes royalty. Amount of deduction is 100% of such royalty income or 3,00,000 whichever is less.

8.14 Deduction in case of a person totally blind or physically handicapped and resident [Section 80U]

The deduction is available to an individual who is resident in India and is a person with disabilities. A resident individual who is totally blind or suffers from permanent physical disability (not less than 40%) or subject to mental retardation is entitled to a deduction of 75,000. Where such individual is a person with severe disability (80% or more) the amount of deduction is allowed 1,25,000.

8.15 Key Concepts

Deductions from GTI, first added and then deducted so called as indirect exemption.

8.16 Summary

After calculating Gross Total Income, there are some deductions u/s 80. Section 80 C is related with investment. Section 80 D for medical insurance premium and 80 DD for maintenance including medical treatment of handicapped dependents. Section 80 DDB is for medical treatment. Section 80 E is payment of interest on loan taken for higher education and 80 G is for donation. Deduction in respect of rent paid (Section 80 GG), deduction in respect of donation for scientific research and rural development [Section 80 GGA], deduction in respect of royalty on patent (Section 80 RRB), deduction in respect of physically handicapped person [Section 80 U] are other deductions.

8.17 Exercise

1. State the deductions allowed u/s 80 to an individual assessee.
2. What is charitable donations ? State the provisions u/s 80 for donations.
3. Write short notes on :
   - (a) Deduction u/s 80 C
   - (b) Deduction u/s 80 CCC
   - (c) Deduction u/s 80 CCD
   - (d) Deduction u/s 80 D
   - (e) Deduction u/s 80 DD
   - (f) Deduction u/s 80 DDB
   - (g) Deduction u/s 80 E
   - (h) Deduction u/s 80 G
   - (i) Deduction u/s 80 GG
   - (j) Deduction u/s 80 GGA
   - (k) Deduction u/s 80 RRB
   - (l) Deduction u/s 80 U

UNIT - 9
GROSS TOTAL INCOME (G.T.I.)

NOTES

9.0 Introduction 9.1 Objectives
9.2 Gross Total Income
9.3 Chart Showing the Computation of Taxable Income
9.4 Key Concepts 9.5 Summary
9.6 Exercise 9.7 Further Reading and References

9.0 Introduction

Total of five heads of income is gross total income. Income tax always calculate on GTI.

9.1 Objectives

After reading this unit, you should be able :

1. To know about GTI. 2. To know about deductions from GTI.

9.2 Gross Total Income

According to Income Tax Act, there are five heads of income i.e.

1. Income from salary. 2. Income from House Property.
3. Profits and gains of business and profession.
4. Capital gains. 5. Income from other sources.

Total of all five heads is known as Gross Total Income. Every head has its own deduction. So under GTI net taxable income of each head should be considered.

9.3 Chart Showing the computation of Taxable Income

Particulars		
(A)	**Income from Salary**	
	(i) Basic pay xxx	
	(ii) Taxable Allowances xxx	
	(iii) Value of Perquisites xxx	
	Gross Salary	**xxx**
Less :	Deductions u/s 16	
	(i) Entertainment Allowance xxx	
	(ii) Professional Tax xxx	xxx
	Income from Salary	**xxx**
(B)	**Income from House Property**	
	(i) Self-occupied Property	
	Annual Value Nil	
	Less : Interest on Loan xxx	(-xxx)
	Loss from Self-occupied Property	**(-xxx)**
	(ii) Income from Let Out Property	
	Gross Annual Value	xxx
	Less : Municipal Taxes	(-xxx)
	Net Annual Value	**xxx**
	Less : Deductions u/s 24	
	(a) Standard deduction xxx	
	(30% of Net Annual Value)	
	(b) Interest on Loan xxx	(-xxx)
	Income from Let Out Property	xxx
	Income from House Property (i + ii)	**xxx**
(C)	**Income from Business or Profession**	
	Profit as per Profit and Loss Account :	xxx

NOTES

Add :	(i) Expenses Debited to Profit and Loss A/c but not allowed (inadmissible expenses)	xxx	
	(ii) Income taxable as business income but not credited to Profit and Loss A/c	xxx	
Less :	(i) Expenses allowed but not debited to P & L A/c	xxx	
	(ii) Income not taxable as business income but credited to Profit and Loss A/c	xxx	(xxx)
	Income from Business/Profession		**xxx**
(D)	**Capital Gains**		
	(i) Short-term Capital Gain		xxx
	(ii) Long-term Capital Gain	xxx	
	Less : Deduction u/s 54	xxx	(-xxx)
	Capital Gain		**xxx**
(E)	**Income from Other Sources**		
	Gross Total Income (A + B + C + D + E)		(xxx)
	Less : Deductions allowed u/s 80C to 80U		
	Total Income		**xxx**

PROBLEMS ON GROSS TOTAL INCOME

Problem 10.1 :

Mr. Ashok Kumar, who is handicapped (not severe) given you the following information of his income for the year ending 31st March, 2016. You are required to compute his total income and tax payable by him for the A.Y. 2016-17.

(i) Gross Salary 1,42,000
(ii) Income from House Property 52,180
(iii) Income from Other Sources 7,950
(iv) He paid 3,500 as Life Insurance Premium on the policy of his wife, deposited in Public Provident Fund 5,000, contributed to R.P.F. 7,500 and purchased N.S.C. of 10,000.
(v) Professional Tax paid 1,800.

Solution :

Computation of Total Income of Mr. Ashok Kumar
For A.Y. 2016-17

Particulars			
1.	**Income from Salary**		
	Gross Salary		1,42,000
	Less : Deduction u/s 16	N.A.	
	(i) Standard deduction	N.A.	
	(ii) Entertainment Allowance	1,800	-1,800
	(iii) Professional Tax		
	Income from Salary		**1,40,200**
2.	**Income from House Property**		52,180
3.	**Income from Other Sources**		7,950
	Gross Total Income (1 + 2 + 3)		2,00,330
	Less : Deduction u/s 80		
	1. Qualifying Savings u/s 80	26,000	(1,01,000)
	2. Physically handicapped (u/s 80 U)	75,000	
	Total Income		**99,330**
	Tax Payable		Nil

NOTES

Note :

Qualifying Savings for deduction u/s 80 C

L.I.P. (wife)	3,500
Deposited in P.P.F.	5,000
Contribution to R.P.F.	7,500
Purchase to N.S.C.	10,000
	26,000

Problem 10.2 :

Mr. Babasaheb has given the following particulars of his income for the A.Y. 2016-17.

1. Profit of business 10,60,000 including 80,000 received as compensation for termination of an agency.
2. One third share of profit from firm 30,000.
3. Long-term capital gain on sale of share 32,000 (shares sold on 25-7-2015). Securities Transaction Tax has been paid.
4. Winning from lottery of Maharashtra Government (Gross) 50,000.
5. Interest on Tax free Government Securities 30,000.
6. Profit from the Business of Dairy Farming 16,000.
7. Interest received on deposits in a partnership firm in which he is a partner 4,500 (Gross).
8. Interest receivable on 10% Bonds of Central Government is 18,400. The right to receive interest on these securities was transferred 3 years back to his son aged 22 years to meet the cost of his education.

   He paid 15,200 for Life Insurance Premium and deposited 16,000 in Public Provident Fund on 15th May, 2015.

   Calculate the total income and tax liability for the Assessment Year 2016-17.

Solution :

Computation of Total Income and Tax Liability of Mr. Babasaheb
For A.Y. 2016-17

Particulars			
(A)	**Income from Business**		
	(i) Profit from Business (10,60,000 - 80,000)		9,80,000
	(ii) Profit from Dairy Farming		16,000
	(iii) Profit from Firm		Exempted
	(iv) Interest on deposits in a Partnership firm		4,500
	Total Income from Business		**10,00,500**
(B)	Long-term Capital Gain on Sale of Shares (u/s 10 (38)		Exempted
(C)	Income from Other Sources		
	(i) Winning from Lottery		50,000
	(ii) Interest on tax-free Government Securities (Exempted)		-
	(iii) Interest on Central Government Bonds (to be clubbed)		18,400
	Total Income Other Sources		68,400
	Gross Total Income		**10,68,900**
	Less : Deduction u/s 80 C		
	L.I.P.	15,200	
	P.P.F.	16,000	-31,200
	Total Income		**10,37,700**

Note :

1. Compensation for termination of an agency is a capital receipts. Not to be included in business income/profits.

NOTES

Tax on Total Income = 10,37,700.

1.	On winning from Lottery at 30% on 50,000			15,000
2.	On the balance of other income of 9,87,700			
	1st 2,50,000	Nil	-	
	Next 2,50,000	10%	25,000	
	Next 4,87,700	20%	97,540	
				1,22,540
				1,37,540
Add :	Surcharge (N.A.)			
	Education Cess (3%)			3,676
	Total Tax			**1,41,666**

Problem 10.3 :

Mr. Suraj is working in Mahindra Ltd., Delhi. He has furnished following details of his income for the year 2016-17.

1. Basic Salary 18,000 p.m.
2. D.A. 7,200 p.m.
3. Bonus 1,00,000.
4. Transport Allowance 1,000 p.m.
5. Entertainment Allowance 600 p.m.
6. H.R.A. 2,500 p.m. (Actual Rent paid 3,000 p.m.)
7. Personal Medical bill reimbursed by employer ` 20,000.
8. His contribution to R.P.F. 22,000 and employer contribute an equal amount.
9. Interest credited to R.P.F. (12%) 9,000.
10. Income from Business 45,000.
11. Short-term Capital Gain 25,000.
12. Interest on Securities 7,000.
13. Income from Units of UTI 4,500.
14. Interest on Bank Deposits 6,500.
15. Donation paid to Government 5,000.
16. Life Insurance Premium paid 18,000.
17. Professional tax paid 2,500.

Solution :

Computation of Taxable Income and Tax Liability of Mr. Suraj
For A.Y. 2016-17

Particulars			
(A)	**Income from Salary**		
	Basic (18,000 x 12)		2,16,000
	D.A. (7,200 x 12)		86,400
	Bonus		1,00,000
	Transport Allowance (1,000 x 12)	12,000	
	Less : Exemption u/s 10 (14)	12,000	
	Entertainment Allowance	(600 x 12)	7,200
	H.R.A. (2,500 x 12)	30,000	
	Less : Exemption u/s 10 (13 A)	5,760	24,240
	Medical Bill reimbursed	20,000	
	Less : Exempt	20,000	
	Contribution to R.P.F.	22,000	
	Less : Exemption	36,288	
	(12% of 3,02,400)		Nil
	Interest credited to R.P.F. (12%)	9,000	
	Less : Exemption (9.5%)	7,125	1,875
	Gross Salary		**4,35,715**

	Less : Deduction u/s 16			
	(i) Standard deduction u/s 16 (1)			
	(ii) Entertainment Allowance u/s 16 (2)			
	(iii) Professional Tax u/s 16 (3)		2,500	
	Income from Salary			**4,33,215**
(B)	**Income from House Property**			-
(C)	**Profits and Gains of Business and Profession**			45,000
(D)	**Capital Gain**			
	Short-term Capital Gain			25,000
	Long-term Capital Gain			-
(E)	**Income from Other Source**			
	Interest on Securities		7,000	
	Income from Units of U.T.I. (Totally exempt)			
	Interest on Bank Deposit		6,500	13,500
	Gross Total Income (A + B + C + D + E)			**5,16,715**
	Less : Deduction u/s 80			
	1. Investment (80C)			
	L.I.C. Premium	18,000		
	Contribution to R.P.F.	22,000	40,000	
	2. Donation 80 (G)			
	Donation to Government (100% applicable)		5,000	(45,000)
	Taxable Income			**4,71,715**
	Tax 1st 2,50,000 Nil		-	
	Next 2,21,715 10%		22,172	
	Total		**22,172**	
	Add : 3% Education Cess		665	
			22,837	
	Less : Advance Tax on TDS		-	
	Taxable Payable		22,840	
				22,840

Working Note :

Exemption of H.R.A. :

Working place Delhi. So, BCDM. HRA is least of following :

1. 50% of salary.
2. Rent paid - 10% of salary.
3. Actual H.R.A. received.

Salary = Basic + D.A. (forming part) + % Commission
= 2,16,000 + 86,400
= 3,02,400

1. 50% of 3,02,400		1,51,200
2. Rent paid (3,000 x 12)	36,000	
Less : 10% of 3,02,400	30,240	5,760
3. Actual HRA received		30,000

Least amount is 5,760

It is assumed that, D.A. is 100% forming part.

Problem 10.4 :

Shrimati Punekar, a computer engineer working in IBM Ltd., Pune has provided you following information in respect of 2015-16.

1. Basic salary 20,000 p.m.
2. D.A. 5,000 p.m.
3. Transport Allowance 2,000 p.m.

NOTES

4. C.C.A. 750 p.m.

During the year she has contributed 3,500 p.m. to U.R.P.F. and equal amount is contributed by company.

She has been provided a rent free accommodation at Pune by the company.

During the year she received interest 24,000 and family pension from software Ltd. 2,400 p.m.

She owns a flat at Satara for which she had borrowed 5,00,000 on 31st March, 2004. During the year she had paid interest 38,000 and repay the principal amount of housing loan 52,000.

She has taken L.I.C. policy for her son living at Satara by paying 14,000 as premium.

She has invested 15,000 in N.S.C. and 10,000 in P.P.F.

Company deducted tax at source 50,000 and professional tax 2,500.

Compute her taxable income and tax liability for A.Y. 2016-17.

Solution :

Computation of Taxable Income and Tax Liability of Shrimati Punekar For A.Y. 2016-17

Particulars			Amt.	Amt.
(A)	**Income from Salary**			
	Basic pay (20,000 x 12)		2,40,000	
	D.A, (5,000 x 12)		60,000	
	Transport Allowance (2,000 x 12)	24,000		
	Less : Exemption (1600 x 12)	19,200	4,800	
	C.C.A. (750 x 12)		9,000	
	Contribution to U.R.P.F. (employer for the time being exempt)			
	Value of Rent free accommodation (Note 1)		47,070	
	Gross Salary		**3,60,870**	
	Less : Deductions u/s 16			
	Professional Tax u/s 16 (3)		2,500	
	Income from Salary			**3,58,370**
(B)	**Income from House Property (S.O.P)**			
	Net Annual Value		Nil	
	Less : Deductions u/s 24			
	Interest on housing loan u/s 24 (2)		-38,000	
	Loss from House Property			**(-38,000)**
(C)	**Profits and Gains of Business**			
(D)	**Capital Gain**			
	Short-term Capital Gain			
	Long-term Capital Gain			
(E)	**Income from Other Source**			
	Interest		24,000	
	Family Pension (2,400 x 12)	28,800		
	Less : Exemption (Note 2)	9,600	19,200	
	Income from Other Source			**43,200**
Gross Total Income (A + B + C + D + E)				**3,63,570**
	Less : Deductions u/s 80			
	Investment 80 (C)			
	L.I.C.	14,000		
	N.S.C.	15,000		
	P.P.F.	10,000		
	Repayment of Housing Loan	52,000	91,000	-91,000
	Taxable Income			**2,72,570**

Tax on it			
1st 2,50,000	Nil		
Next 22,570	10%	2,257	
Add : 3% Education Cess		67.71	
Total		**2,325**	
Less : Advance tax/TDS		50,000	
Tax Refundable		47,675	
Rounded off		47,680	
Tax Refundable			**47,680**

Working Note :

1. Valuation of Rent Free Accommodation :

Flat is owned by company.

Population of Pune is more than 25,00,000.

Value is 15% of Salary.

Salary for Perk = Basic + D.A. (forming part) + Bonus + Fees + Commission + Taxable + Any money chargeable under the Act

= 2,40,000 + 60,000+ 4,800 + 9,000

Salary = 3,13,800

Value is 15% of 3,13,800 = 47,070

2. Exemption from Family Pension :

Least of following two :

15,000 or

1/3rd of 28,800 i.e. 9,600

Least amount is 9,600 so exempted.

Problem 10.5 :

Ramesh is the proprietor of a business. His Profit and Loss Account for the year ending 31st March, 2016 is as follows :

Particulars		**Particulars**	
To Establishment Expenses	2,40,000	By Gross Profit	4,17,180
To Rent, Rate and Taxes	48,000	By Interest on Government Securities	7,120
To General Charges	7,500	(Gross)	
To Household Expenses	28,000	By Rent from House Property	96,000
To Commission	18,000	By Dividend from Domestic Company	15,000
To Discount and Allowance	4,000		
To Provision for Bad Debt	12,000		
To Postage and Telegrams	2,500		
To Law Charges	7,500		
To Advertising	15,800		
To Gifts and Presents (Personal)	1,200		
To Fire Insurance Premium (for goods)	4,000		
To Sales Tax	14,800		
To Repairs and Renewals	3,000		
To Loss on Sale of Motor Car (Used for private purpose)	2,500		
To Life Insurance Premium	4,000		
To Donation to Rayat Shikshan Sanstha	10,000		
To Public Provident Fund	5,000		
To Wealth Tax	3,000		
To Interest on Capital	4,500		
To Audit Fee	5,000		
To Interest on Bank Loan	7,000		

To Provision for Depreciation	25,000		
To Provision for Income Tax	15,000		
To Net Profit	48,000		
	5,35,300		**5,35,300**

NOTES

The following further information is given :

(a) Actual Bad Debts incurred during the year amounted to 6,000.
(b) Income tax actually paid during the year is 8,000.
(c) Depreciation allowable is 24,000 as per Income Tax Rules.
(d) Advertising Expenses include 10,000 spent on special advertising campaign to open an another new shop in the market.
(e) Law Charges are in connection with trade mark.
(f) Ramesh carries on his business from rented premises, half of which is used as his residence, rent, rates and taxes include 8,000 paid as rent of the premises during the year.
(g) Municipal Tax paid for let out house property 4,500.

Compute total income of Ramesh for the A.Y. 2016-17.

Solution :

Computation of Total Income of Ramesh
For A.Y. 2016-17

Particulars		**Amt.**	**Amt.**
(A)	**Income from Business**		
	Profit as per Profit and Loss A/c		48,000
Add :	Disallowed Expenditure Profit and Loss A/c		
	Rent and Taxes (half rent)	4,000	
	Household Expenses	28,000	
	Provision for Bad Debts	12,000	
	Gifts and Present's	1,200	
	Loss on Sale of Motor	2,500	
	L.I.P.	4,000	
	Donation to Rayat Shikshan Sanstha	10,000	
	P.P.F.	5,000	
	Wealth Tax	3,000	
	Interest on Capital	4,500	
	Provision for Income Tax	15,000	
	Provision for Depreciation	25,000	1,14,200
			1,62,200
Less :	(i) Receipts under other heads but credited to Profit and Loss A/c		
	Interest on Government Security	7,120	
	Rent from	96,000	
	Dividend from Domestic Company	15,000	-1,18,120
	(ii) Expenses allowed but not debited to Profit and Loss A/c		
	Depreciation	24,000	
	Bad Debts	6,000	-30,000
	Income from Business (i + ii)		14,080
(B)	**Income from House Property**		
	Gross Annual Value	96,000	
Less :	Municipal Taxes	-4,500	
	Net Annual Value	91,500	
Less :	Deductions u/s 24		

	(i) Standard deduction (30% of N.A.V.)	-27,450	
	Income from House Property		64,050
(C)	**Income from Other Sources**		
	Interest on Government Securities	7,120	
	Dividend from Domestic Company (Exempted)	Nil	7,120
	Gross Total Income (A + B + C)		**85,250**
	(14,080 + 64,050 + 7,120)		
Less :	Deduction u/s 80		
	(i) Qualifying Savings (u/s 80 C)	9,000	
	(ii) Donation 50% of ` 10,000 (80 G)	5,000	-14000
	Total Income		**71,250**

Notes :

1. Qualifying Savings for deduction u/s 80 C
   L.I.P. + P.P.F. = 4,000 + 5,000 = 9,000
2. Tax on total income nil.

Problem 10.6 :

Mr. Prakash Mohite has given the following particulars of his income and savings for the financial year ending on 31-3-2016.

(i) Gross salary 3,03,000.
(ii) Profits from business 1,50,000.
(iii) Interest on Government Securities 3,800.
(iv) Dividends received from an Indian Company 5,600.
(v) Income from House Property 15,000.
(vi) He paid professional tax 2,500 and Income Tax 32,000.
(vii) He paid 10,200 for Life Insurance Premium, deposited in Public Provident Fund 10,000, invested 5,000 in National Savings Certificates and made F.D. for 5 years in State Bank of India 50,000.
Compute the Income Tax Liability of Mr. Prakash Mohite for the A.Y. 2016-17.

Solution :

Computation of Taxable Income and Tax Liability of Mr. Prakash Mohite
For A.Y. 2016-17

Particulars		**Amt.**	**Amt.**
(A)	**Income from Salary**		
	Gross Salary		3,03,000
Less :	Deduction u/s 16		
	Professional Tax	+2,500	2,500
	Income from Salary		3,00,500
(B)	**Income from House Property**		15,000
(C)	**Income from Business**		1,50,000
(D)	**Income from Other Sources**		
	Interest on Government Securities	3,800	
	Dividend from Indian Company (Exempted)	-	3,800
	Gross Total Income (A + B + C + D)		4,69,300
Less :	Deductions u/s 80		
	(i) Qualifying Savings Section 80 C (Note 3)	75,200	
	(ii) Interest and Dividends 80 L (Note 2)	N.A.	
	Total Income		**3,94,100**
	Tax on Total Income		
	1st 2,50,000 Nil		Nil

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	Next 1,44,100	10%	14,410
			14,410
Add :	3% Education Cess		432
	Total Tax Payable		14,842
Less :	Income Tax paid		(-) 32,000
	Total Tax Liability (Refundable)		**17,158**

Notes :

1. Dividends from domestic company is exempted from tax w.e.f. A.Y. 2004-05.
2. Section 80 L is omitted w.e.f. A.Y. 2006-07.
3. Qualifying amount for deduction u/s 80 C.

L.I.P.	10,200
P.P.F.	10,000
N.S.C.	5,000
F.D. in State Bank of India (w.e.f. 1-4-2006)	50,000
Total	75,200

9.4 Key Concepts

Income tax is annual tax which chargeable to every person on gross total income.

9.5 Summary

Gross Total Income is the summation of five heads :

(i) Income from salary.

(ii) Income from house property.

(iii) Profit and Gain of business.

(iv) Capital Gain.

(v) Income from other sources.

After calculating G.T.I, there are same deductions u/s 80. Then, we get total income. After getting total income, tax is calculated according to the category of assessee i.e. General, Lady assessee or senior citizen. Then, we deduct TDS from it and we get total tax liability of an assessee.

9.6 Exercise

1. Give short note on 'Gross Total Income'.
2. Give format which showing computation of taxable income.

9.7 Further Reading and References

1) Students Guide To Income Tax by Vinod Singhania

2) Taxman

3) Income Tax Bare Act

UNIT - 10
CARRY FORWARD AND SET OFF

NOTES

10.0 Introduction
10.1 Objectives
10.2 Clubbing of Income
10.3 Set off and Carry Forward of Losses
10.4 Key Concepts
10.5 Summary
10.6 Exercise
10.7 Further Reading and References

10.0 Introduction

Losses of head of income are allowed to carry forward and set off against different heads for certain period.

10.1 Objectives

After reading this unit, you should be able :

1. To know about limit for carryforward.
2. To know about set off.

10.2 Clubbing of Income

The clubbing of income means the income of other person is included in the total income of the assessee while computing the tax payable by him, as if the income had been earned by the assessee and not by such other person. In the following instances the income of other person is clubbed in the hands of the assessee :

1. **Transfer of Income without transfer of assets [Section 60] :** When a person transfers income without transferring the ownership of the assets, such income is taxable in the hands of the person transferring the income.
2. **Transfer of assets which is revocable [Section 61] :** The income earned by a person from the assets which are transferred by a revocable transfer, is included in the income of the person who makes the revocable transfer.
3. **Remuneration to spouse [Section 64 (1) (ii)] :** The remuneration received by individual from a concern in which his spouse holds a substantial interest, shall be clubbed in the hands of spouse except when the salary, commission, fees. etc. paid to the individual are solely or purely for application of technical or professional knowledge and experience of the individual.
4. **Income from assets transferred to spouse [Section 64 (1) (iv)] :** When an individual transfers asset to his/her spouse directly or indirectly, otherwise than for adequate consideration or in connection with an agreement to live apart all income arising from such asset will be clubbed in the hands of the transferor.
5. **Income from assets transferred to son's wife [Section 64 (i) (vi)] :** If a person transfers assets without adequate consideration to son's wife, directly or indirectly on or after May 31, 1973, income arising from such assets will be included in the total income of the transferor.

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6. **Income from assets transferred to any person for the benefit of spouse [Section 64 (i) (vii)] :** If a person transfers the assets to another person or AOP, directly or indirectly, for inadequate consideration, for the immediate or deferred benefits of his or her spouse, income arising directly or indirectly, from such asset is included in the total income of the transferor to the extent of such benefits.
7. **Income from assets transferred to any person for the benefit of son's wife [Section 64 (1) (viii)] :** If a person transfers the assets to another person or AOP, directly or indirectly, for inadequate consideration, for the immediate benefits of son's wife, income arising directly or indirectly, from such asset is included in the total income of the transferor to the extent of such benefits.
8 **Income of minor child [Section 64 (IA)] :** Any income that arises or accrues to the minor shall be clubbed in the income of one of his parents, who has greater income excluding the income to be clubbed under this section. If the marriage of the parents does not subsist, then it shall be included in the income of the parent who is maintaining the minor in the relevant previous year.
9. **Conversion of self acquired property into joint family property and subsequent partition [Section 64 (2)] :** If member of HUF converts his self acquired property into joint family property, entire incomes arising from such property shall be included in the income of the transferor. If there is partition subsequently amongst the members, then income received from the part of the converted property which is allotted to the spouse of individual shall be included in his income.
10. **Clubbing of negative income :** u/s 64 income in the above cases is clubbed in the hands of another person. The income herein includes the 'loss' as loss is a negative income of the person. So if in the above cases the computed income of the person is a loss, then such loss is included in the income of the another person.

10.3 Set Off and Carry forward of Losses

The procedure of setting off of losses and their carrying forward can be summarized as follows :

[A] Inter source Adjustment under the same head of income.
[B] Inter head Adjustment in the same assessment year. (Applied if a loss can not set off under step A).
[C] Carry Forward of a loss to be set off fully or partly after the above steps. (If loss can not be set off under step A and B).

[A] Inter source Adjustment [Section 70] : If an assessee suffers loss from one source of income in a year, he has right to set off such loss against the income from another source under the same head of income. This rule has the following exceptions :

1. Losses from speculation business can be set off only against the profit from a speculation business.
2. Losses from business of owning and maintaining race horses can be set off only against the profit from such business/activity. If can not be set off against the income from any other sources.
3. Long term capital losses can be set off only against L.T.C.G.
4. Losses can not be set off against casual receipts

Other points

(a) The first two losses cannot be set off against another source of income.
(b) Losses from non-speculation business or other business can be set off

against income from speculation business or non speculation business.

(c) S.T.C.L. can be set off against any capital gain.

(d) Loss from a house property can be set off against income from any other house property.

(e) Income exempt from tax u/s 10, loss from such source cannot be set off against income chargeable to tax.

[B] Inter-Head Adjustment [Section 71] : If any head of income other than capital gains shows loss for any assessment year. Such loss can be set off against another heads of income in the same assessment year. This rule has following 5 exceptions :

1. The business or profession loss can not be set off against the income from salaries [Section 71 (2A)]
2. Loss under the head capital gains cannot be set off against income, under other heads of income [Section 71 (3)]
3. Losses from speculation business can be set off only against the profit from a speculation business i.e. It can not be set off against any other head of income.
4. Losses from owning and maintaining race horses can not be set off against any other income.
5. Loss can not be set off against casual receipts.

Other points : Before adjusting loss under section 71, one has to set off loss under section 70. Bearing/considering the aforesaid five cases, any loss can be set off against income under other heads of income for the same year. e.g.

(a) loss under the head income from house property can be set off against business income, capital gains, salary income or income from other sources.

(b) Business loss can be set off against income from house property, business or capital gains.

(c) A loss under the head income from other sources (except loss from owning and maintaining race horses and losses from speculation business) can be set off against income from salary, house property, business or capital gains.

(C) Carry forward of losses : If a loss can not be set off either under the same head or under the income from another head, it will be carried forward for setting off against income of the next year. The loss under the head income from business or profession, income from house property and under the head capital gains are allowed to be carried forward. Losses under the head salaries, income from other sources can not be carried forward.

Other Points

(a) Carry forward and set off of loss from house property [Section 71 (B)] : If the loss from house property is not fully adjusted under other heads of income in the same assessment year, then the balance loss shall be allowed to be carried forward and set off in subsequent 8 years against income from house property.

(b) Carry forward of business or profession loss [Section 72] : The loss of one business can be carry forward and set off against income of any business or profession in a subsequent year. The loss can not be carried forward for more than 8 years.

(c) Carry forward and set off speculation business loss [Section 73] : The loss from speculation business can be carried forward upto 4 assessment year immediately following the assessment year for which the loss was first computed. Such loss can be set off only against the income from speculation business.

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(d) Loss of any specified business [Section 73A] : Loss of any specified business referred to section 35AD shall not be set off except against profits and gains of any other specified business and shall be carried forward to the following assessment year and it shall be set off against the profit and gains of any other specified business.

(e) Carry Forward and set off of capital loss [Section 74] : The whole capital loss of any assessment year shall be carried forward to the following assessment year and it shall be set off against any income under the head capital gains. Such loss can be carried forward for 8 assessment year.

(f) Carry forward and set off of loss from owning and maintaining race horses [Section 74A] : Such loss can be carried forward to next year and set off only against income from the activity of owning and maintaining of race horses. The loss can be carried forward for 4 assessment year.

(g) Brought forward losses must be set off in the immediately succeeding years.

10.4 Key Concepts

Intersource and interhead set off is allowed. Carry forward is possible for next 8 years.

10.5 Summary

Clubbing of income means the income of other person is included in the total income of the assessee while computing the tax payable by him, as if the income had been earned by the assessee and not by such other person. The procedure of setting off and carry forward of losses can be summarized as (A) Inter source adjustment under the same head of income (B) Inter head adjustment in the same assessment year and (C) Carry forward of a loss to be set off fully or partly after the above steps.

10.6 Exercise

1. Give brief note on :

(a) Clubbing of income

(b) Inter source adjustment

(c) Inter-Head adjustment

(d) Carry forward of losses.

10.7 Further Reading and References

1) Students Guide To Income Tax by Vinod Singhania
2) Taxman
3) Income Tax Bare Act

UNIT - 11
TAX PLANNING

NOTES

11.0 Introduction 11.1 Objectives
11.2 Tax Planning (Meaning) 11.3 Justification of Tax Planning
11.4 Nature and Scope of Tax Planning in the Corporate Sector
11.5 Key Concepts 11.6 Summary
11.7 Exercise 11.8 Further Reading and References

11.0 Introduction

By using all tax rules when liablity of income tax reduces is Tax Planning.

11.1 Objectives

After reading this unit, you should be able :

1. To know about Tax Planning.
2. To know about Tax Avoidance
3. To know about Tax Evasion.

11.2 Tax Planning (Meaning)

Tax planning can be defined as an arrangement of one's financial and economic affairs by taking complete legitimate benefits of all deductions, exemptions, allowances and rebates so the tax liabilities reduce to minimum. Tax planning is a wider term and includes tax management. It emphasizes on minimization of tax burden.

11.3 Justification of Tax Planning

(i) Reduction of tax liability : One main objective of tax planning is the reduction of the tax liability of the taxpayer and it saves the earnings.

(ii) Minimization of litigation : Due to proper tax planning the chances of unscrupulous litigation are certainly minimized and the tax payer may be saved from the hardships.

(iii) Productive investment : Proper tax planning guides the ways and means of productive investment of the earnings.

(iv) Healthy growth of economy : A saving of earnings be legally sanctioned devices is the prime factor for the healthy growth of the economy of a nation and its people.

(v) Economic stability : Under tax planning, taxes legally due or paid without any headache either to the taxpayer or to the collector.

The planning creates economic stability of the nation and its people by even distribution of income resources.

11.4 Nature and scope of Tax Planning in the Corporate Sector

Tax planning may be effective in every area of business management in the corporate sector. Some of the important areas i.e. scope of the tax planning is as follows

[A] Tax Planning with Reference to Setting up of a New Business or Tax Planning Considerations in Relation to Business

In the case of setting of a new business one has to take the following decisions :

1. Location of new business : Tax planning is relevant from location point of view. There are certain locations which are given special tax treatment. Some of these are free trade zone, special economic zone, industrially backward

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state or district etc.

2. **Nature of new business :** Many tax incentives are available under the act which are directly co-related to the nature of business. So, tax planning is also relevant while deciding upon the nature of business. Some of the tax incentives are :- venture capital companies, Tea Coffee and Rubber Development Account, telecommunication services etc.
3. **Forms of business organization and the pattern of its ownership :** Among other consideration, tax incentives play important role while selecting a suitable form of organization for a new business.

[B] Tax Planning with Reference to Specific Financial Management Decisions

Many tax provisions affect financial management decisions, some of these provisions are given below :

(i) Capital Structure : While selecting a capital structure, the tax planner should properly balance risk, cost of capital to be raised, control and tax consideration. An optimum capital structure is one which maximizes shareholders return.

(ii) Dividend Pay : Dividend declared, distributed or paid after 31st March 2003 is not taxable in the hands of the shareholders. On such dividend the company has to pay dividend tax u/s 115-0.

[C] Tax Planning with Reference to Specific Managerial Decisions

Tax provisions affecting various managerial decisions are given below :

(i) Make or buy : Many costing and non costing considerations guide the decisions relating to make/manufacture or buy from the market. The following tax consideration one has to keep in mind while taking 'make or buy' decision.

(a) Establishing a new Unit : If the decision to manufacture a part of component involves setting up a separate industrial unit, then tax incentives available u/s 10A, 10B, 80IB has to keep in mind.

(b) Export : If 'make or buy' decision is taken for exporting goods, then tax incentives available u/s 10B (for 100%. EOU) has to keep in mind.

(ii) Lease or purchase : If asset is purchased, the assesses can claim depreciation. Besides, interest on capital borrowed to purchase assets can also be claimed as deduction. If however, asset is obtained on lease, deduction can be claimed in respect of lease rentals and lease management fees tax saving in both situations have to be studied.

(iii) Purchase by Installment vs. Hire : If an asset is purchased by installments, then the tax payer can claim depreciation and interest payable on unpaid purchase price. In the case of obtaining an assets on hire deduction can be claimed in respect of hire charges. By comparing the tax saving and present value of cash outflows a correct decision can be taken.

11.5 Key Concepts

Tax planning, Tax evasion and Tax avoidance are totaly diferent.

11.6 Summary

Tax planning means reduce of tax liability by using proper income tax rules.

11.7 Exercise

1. What do you mean by Tax planning ?
2. What is justification of tax planning
3. State nature and scope of tax planning.

11.8 Further Reading and References

1) Students Guide To Income Tax by Vinod Singhania
2) Taxman
3) Income Tax Bare Act

UNIT 12
PROCEDURE UNDER INCOME TAX ACT, 1961

12.0	Introduction 12.1 Objectives	12.5	Key Concepts
12.2	Return under income tax act 1961	12.6	Summary
12.3	Best Judgement Assessments	12.7	Exercise
12.4	Advancement Payment of Tax	12.8	Reading & References

12.0 Introduction

The procedure use for disclosure of income is fix by income tax department. Which has to be follow by all assessees in specific manner.

12.1 Objectives -

After reading this unit, you should be able : 1. To know about various procedure under Income Tax Act.

12.2 Return under Income Tax Act 1961

Return mean's disclose income in front of income tax department. Every person who registered under Income Tax Act.

New ITR Form's	Subject
ITR - 1	For individuals having income from salary and interest.
ITR - 2	For individuals and HUF not having business/profession income.
ITR - 3	For individuals/HUFs being partner in firm and not carrying out business or profession under and proprietorship.
ITR - 4	For HUFs/Individuals having income from a proprietary business or profession.
ITR - 5	For firm, AOPs and BOIs.
ITR - 6	For companies other than companies claiming exemption under Section 11.
ITR - 7	For person including companies required to furnish return under Section 139 (4A)/(4B)/(4C)/(4D).
ITR - 8	Return for fringe benefits.
ITR - V	Where the data of the return of income/fringe benefits in forms ITR - 1, ITR - 2, ITR - 3, ITR - 4, ITR - 5, ITR - 6, ITR - 8 transmitted electronically without digital signature.

According to the status of Assessee specific time limit is apply for submission of return which are -

Different Situation	Due Date of Submission of Return
1. Where the assessee is a company.	September 30
2. Where the assessee is a person other than a company. 2.1 In case where Account of the Assessee are required to be audited under any law.	September 30
2.2 Where the assessee is a "working partner" in a firm whose account are required to be audited under any law.	September 30
2.3 In any other case.	July 31

The information asked in form must be given completely if information not given in detail, the return is defective. Following are main reason for defective return.

1. Return form has not been duly filled.
2. Annexuresm Statements, Account are not attached.

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Return by whom to be signed [Section 140]

The return of income or fringe benefits is required to be signed and verified.

Different Assessees	Who should sign the return
Individuals	By the individual himself or where the individual concerned is absent from India by the individual himself or by some duly authorized by him on his behalf and where the individual is mentally incapacitated from attending to his affairs, by his guardian or a person competent to act on his behalf and where for any other reason, it is not possible for the individual to sign the return, by any person duly authorized by him in this behalf.
Hindu Undivided Family	By the karta or where the karta is absent from India or is mentally incapacitated from attending to his affairs by any other adult member of the family.
Company	By the Managing Director thereof or where, for any unavoidable reason, such Managing Director is not able to sign or where there is no Managing Director by any other Director of company.
Firm	By the managing partner thereof or where for any avoidable reason, such managing partner is notable to sign or where there is no managing partner by any partner thereof not being a minor.
Limited Liability Partnership	By the designated partner thereof or where for any unavoidable reason such designated partner is not able to sign or where there is no designated partner, by any partner thereof. (Applicable from the Assessment year 2010 - 2011 onwards)
Local Authority	By the Principal Officer thereof.
Political Party	By the Chief Executive Officer of such Party.
Any Other Association	By any member of Association or the Principle Officer thereof.
Any Other Person	By the person or by some other person competent to act on his behalf.

What is Self-assessment [Section 140 A]

Before submitting the aforesaid return, he is supposed to find out whether any tax and/or interest is payable. For this purpose tax and/or interest shall be calculated as follows :

Find out income tax surcharge education cess and secondary and higher education cess as per return of income.		XXX
Add : Interest Under Section 234 A or 115 week for late submission of return of income or Fringe benefit.	XXXX	
Under Section 234 B for non-payment or short payment of advance tax or fringe benefit. Under Section 234 C for non-payment or short payment of different instalments of advance tax.	XXXX	XXXX
Total Tax and Interest		**XXXX**
Less : Advance tax, tax deducted at source, tax collected at source, MAT credit and relief Under Sections 90/90A/91A		XXXX
Self assessment tax payable Under Section 140 A.		XXXX

What is Best Judgement Assessments [Section 144]

The Assessing Officer, after considering all relevant material which he has gathered, is under an obligation to make an assessment of the total income or loss to the best of his judgement in the following cases.

Case - 1 : If any person fails to make a return required under Section 139 (1) and has not made a return or a revised Return Under Sub-section (4) or (5) of that section.

Case - 2 : If any person fails to comply with all the terms of a Notice under Section 142 (1) or fails to comply with the direction requiring him to get his accounts audited in term of Section 142 (2A).

Case - 3 : If any person, after having filed a return, fails to comply with the term of a Notice under Section 143 (2) requiring his presence or production of evidence and document.

Case - 4 : If the Assessing Officer is not satisfied about the correctness or the completeness of the accounts of the Assessee or if no method of Accounting has been regularly employed by the Assessee.

Advancement Payment of Tax :

Every person is liable to pay advance tax, if advance tax payable is ` 10,000 or more. All items of income are liable for payment of advance tax. From the assessment year 2011-12 an assessee, who has opted for the scheme of computing business income under Section 44 AD on presumptive basis at the rate of 8 percent of turnover, shall be exempted from payment of advance tax related to such business.

When Advance Tax Payment Become Due :

Advance tax is payable as follows :

	In case of Corporate Assessee	**In case of Non Corporate Assessee**
On or before June 15 of the previous year.	Upto 15% of advance tax payable.	-
On or before September 15 of previous year.	Upto 45% of advance tax payable.	Upto 30% advance tax payable.
On or before December 15 of previous year.	Upto 75% of advance tax payable.	Upto 60% of advance tax payable.
On or before March 15 of the previous year.	Upto 100% of advance tax payable.	Upto 100% of advance tax payable.

Deduction and Collection of Tax at Source :

When and how tax is to be deducted at source from salary :

The summarised provision of Section 192 are given below :

Who is the payer	Employer
Who is the recipient	Employee
Payment covered	Taxable salary of the employee
At what time tax has to be deducted at source	At the time of payment
Maximum amount which can be paid without tax deduction at source	The amount of exemption limit. - 2,50,000 - 3,00,000 - 5,00,000 For the assessment yrs.
Rate of tax deduction at source	Normal rate applicable to an individual
When the provision are not applicable	-
Is it possible to get the payment without tax deduction or with lower tax deduction	The employee can make an applicable in Form No. 13 to the Assessing Officer to get a certificate of lower tax deduction

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Interest Payable by Assessee :

Interest is payable by the assessee under the Income Tax Act in the circumstances enumerated below :

1. Rate of interest.	1% per month (simple interest).
2. Period for which interest is payable.	Commencing on the date immediately following the date for filing the return of income and ending : (a) The date of furnishing the return. (b) The date of completion of Assessment Under Section 144.
3. Amount in which interest is payable.	It is find out as under : 1. Find out the tax on total income as determined under Section 143 (1) or an Assessment under Section 143 (3) or Section 147. 2. From the tax so determined, advance tax paid tax deducted or collected at source. Relief under Section 90/90A/ 91 and MAT credit.

12.5 Key Concepts

The form which use to submit the information about income in previous year is known as income tax returns.

12.6 Summary

The procedure use for disclosure of income is fix by income tax department. Which has to be follow by all assessees in specific manner.

12.7 Exercise

1. Describe different form of returns?
2. Describe different dates of returns?
3. Describe slabs for advance tax?

12.8 Further Reading and References

1) Students Guide To Income Tax by Vinod Singhania
2) Taxman
3) Income Tax Bare Act