

PRACTICE MANUAL
Intermediate (IPC) Course

PAPER 4 : TAXATION

Part - I : Income-tax

[As amended by the Finance Act, 2013]

Assessment Year 2014-15

[Relevant for May, 2014 & November, 2014
Examinations]

VOLUME – II



BOARD OF STUDIES
THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

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This Practice Manual has been prepared by the faculty of the Board of Studies. The objective of the Practice Manual is to provide teaching material to the students to enable them to obtain knowledge and skills in the subject. Students should also supplement their study by reference to the standard text books. In case students need any clarifications or have any suggestions to make for further improvement of the material contained herein, they may write to the Director of Studies.

All care has been taken to provide interpretations and discussions in a manner useful for the students. However, the Practice Manual has not been specifically discussed by the Council of the Institute or any of its Committees and the views expressed herein may not be taken to necessarily represent the views of the Council or any of its Committees.

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A WORD ABOUT PRACTICE MANUAL

The Board of Studies has been instrumental in imparting theoretical education for the students of Chartered Accountancy Course. The distinctive characteristic of the course i.e., distance education, has emphasized the need for bridging the gap between the students and the Institute and for this purpose, the Board of Studies has been providing a variety of educational inputs for the students. Bringing out a series of subject-wise Practice Manuals is one of the quality services provided by the Institute. These Practice Manuals are highly useful to the students preparing for the examinations, since they are able to get answers for all important questions relating to a subject at one place and that too, grouped chapter-wise.

Income-tax constitutes Part I of Intermediate (IPC) Paper 4: Taxation. Volume II is the Practice Manual of Part I: Income-tax, which is divided into ten chapters in line with Volume I, namely, the Study Material on Income-tax. This will help the students to correlate the Practice Manual with the Study Material and facilitate in complete revision of each chapter. This Practice Manual has been prepared on the basis of the provisions of law as amended by the Finance Act, 2013, and applicable for A.Y.2014-15.

In this edition of the Practice Manual, all the questions have been adapted and answered on the basis of the provisions of income-tax law as amended by the Finance Act, 2013, which are relevant for the A.Y. 2014-15, being the assessment year applicable for students appearing in May, 2014 and November, 2014 examinations.

This Practice Manual contains a wide range of questions on income-tax and includes questions set at the past examinations at PE-II, PCC & IPCC levels as well as other important questions. Solving questions in the Practice Manual would, therefore, facilitate in thorough understanding of the provisions discussed in Volume I, i.e., the Study Material. In this edition of the Practice Manual, "Key Points" have been included at the beginning of each chapter, which would aid the students in answering the questions and solving the problems contained in that chapter. It would also facilitate quick revision of the chapter.

The Practice Manual also contains a matrix showing the topic-wise distribution of examination questions to make the students aware of the weightage given to the various chapters in the examination. The Practice Manual will serve as a useful and handy reference guide while preparing for Intermediate (IPC) Examination. It will guide the students to improve their performance in the examinations and also help them to work upon their grey areas and plan a strategy to tackle problems in income-tax. For further clarification/guidance, students may send their queries at priya@icai.in

Happy Reading and Best Wishes!

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Paper – 4: Taxation

Statement showing topic-wise distribution of Examination Questions along with Marks

Chapter	Term of Examination												Total Marks	Avg. Marks				
	Nov 2009		May 2010		Nov. 2010		May 2011		Nov. 2011		May 2012				Nov 2012		May 2013	
	Q	M	Q	M	Q	M	Q	M	Q	M	Q	M			Q	M	Q	M
PART-I : INCOME TAX																		
1						7(a)(ii)	4										4	0.5
2			3	10			2(a)(i)	4	6(a)(i)	4					2(a)	8	26	3.25
3	4(c)	4	4(b)	4	4	2(a)(i) 4(a)(ii)	4 4	1(b)	5								21	2.625
4														6(a)	8	7(a)(iii)	12	2.5
Unit-1					7(a)(i) 5(a)	4 8			2(a)	8	7(a)	8			3(a)	8	36	4.5
Unit-2	2(b)	6			7(a)(iii)	4					2(a)(iii)	4					14	1.75
Unit-3			2(a)	6	6(a)	8	7(a)(iii) 6(a) 2(a)(ii)	4	1(a) 4(a) 7(a)(i)	5 8 4	6(a)	8	4(a)	8	7(a)(ii)	4	67	8.375

Unit- 4	Capital Gains	2(c) 4(b)	6 4	2(b)	6	2(a)(ii) 1(b)	4 5	5(a)	8	3(a)	8	3(a)	8	3(a) 7(a)(iii)	8 4	6(a)	8	69	8.625
Unit- 5	Income from Other Sources	2(a)	6					7(a)(ii)	4	6(a)(ii)	4						14	1.75	
5	Income of other Persons included in Assessee's Total Income								1(a)	1(a)	5	2(a)(ii) 5(a)	4 8	2(a)	8	5(a)	8	33	4.125
6	Set-off and Carry Forward of Losses	4(d) 3	4 10			1(a)	5		4(a)	4(a)	8			5(a)	8	4(a)	8	43	5.375
7	Deductions from Gross Total Income								5(a)	5(a)	8							8	1
8	Computation of Total Income and Tax Payable	1	16	1	16	3(a)	8	3(a)	8	1(b)	5	1(a) 4(a)	10 8	1(a)	10	1(a)	10	91	11.375
9	Provisions concerning Advance Tax and TDS	4(a)	4	4(a)	4	4(a)(i)	4		7(a)(ii)	7(a)(ii)	4			7(a)(i)	4	7(a)(i)	4	24	3
10	Provisions for filing of Return of Income			4(c)	4			7(a)(i)	4	7(a)(iii)	4	2(a)(i)	4	7(a)(ii)	4			20	2.5

Note: 'Q' represents question numbers as they appeared in the question paper of respective examination. 'M' represents the marks which each question carries.

The question papers of all the past attempts of IPCE/Intermediate (IPC) Examinations can be accessed from the BOS Knowledge Portal on the Institute's website www.icai.org

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Basic Concepts of Indirect taxes

UNIT – 1: INTRODUCTION

KEY POINTS			
What is a tax?	Tax is money that people have to pay to the Government, which is used to provide public services.		
Direct tax v. Indirect Tax	Direct Tax	Indirect Tax	
	<p>Direct tax is imposed directly on the taxpayer and paid directly to the Government by the persons on whom it is imposed. Its burden cannot be shifted.</p> <p><i>E.g.: Income-tax and Wealth tax.</i></p>	<p>The incidence of indirect tax is borne by the consumers who ultimately consume the product or the service, while the immediate liability to pay the tax may fall upon manufacturer or provider of service or seller of goods.</p> <p>Its burden can be shifted by the taxpayer to someone else.</p> <p><i>E.g.: Excise Duty, Customs Duty, Service Tax, Central Sales Tax (CST), Value Added Tax (VAT), etc.</i></p>	
Constitution of India	<ul style="list-style-type: none"> ◆ Power to levy and collect taxes whether, direct or indirect emerges from the Constitution of India. ◆ In case any act, rule, notification or order is not in conformity with the Constitution, it is called <i>ultra vires</i> the Constitution and is illegal and void. 		
Seventh Schedule to Article 246 of Constitution	Union List (List I)	State List (List II)	Concurrent List (List III)
	It contains the matters in respect of which the Parliament (Central	It contains the matters in respect of which the State Government has	It contains the matters in respect of which both the Central & State Governments

1.2 Indirect Taxes

	Government) has the exclusive right to make laws.	the exclusive right to make laws.	have power to make laws.
	Taxation Entries: 82 to 92C	Taxation Entries: 45 to 63	No head of taxation
	Taxes under Union List: Income-tax, Customs Duty, Service Tax, Central Excise Duty, Central Sales Tax etc.	Taxes under State List: State Level VAT, State Excise Duties	

Question 1

Mr. A's service tax liability for half year ended on March 31, 2014 is ₹ 50,000. However, Mr. A has suffered unexpected loss in his business and is short of cash. Therefore, he decides not to pay service tax for the said half year. Examine whether Mr. A's contention is valid.

Answer

No, Mr. A's contention is not valid as tax is **not a voluntary payment** or donation, but an enforced contribution, exacted pursuant to legislative authority. Thus, Mr. A will have to **compulsorily** pay service tax of ₹ 50,000 for half year ended on March 31, 2014 in accordance with the applicable provisions of service tax law irrespective of his financial position.

Question 2

Goods are imported at a port city. State Government of the port city intends to levy customs duty on such imported goods as they have landed at a port which comes under its (State Government's) jurisdiction. Examine whether the State Government's stand is correct in law.

Answer

No, the State Government's stand is not correct in law. Power to levy customs duty is vested with Central Government by virtue of Entry 83 of Union List of Seventh Schedule to Article 246 of Constitution of India. Union List or List-I contains the matters in respect of which Parliament (Central Government) has the exclusive right to make laws.

Question 3

Examine with reasons whether following statements are true or false:

- (i) *A State Government and the Central Government together can make laws in respect of taxes covered under Concurrent List.*

- (ii) *In case of a Union Territory, Parliament can make laws in respect of a matter included in State List.*

Answer

- (i) **False.** Since, there is no head of taxation in Concurrent List (List – III), there does not arise any question of State Government and the Central Government together making laws in respect of any tax.
- (ii) **True.** Parliament has a further power to make any law for any part of India not comprised in a State even if such matter is included in State List.

Question 4

Examine the validity of following statements:

- (i) *Central Government is empowered to make laws in respect of excise duty leviable on liquors (meant for human consumption) containing alcohol.*
- (ii) *Taxes on intra-State sale or purchase of goods are covered under Entry 92A of Union List of the Constitution.*

Answer

- (i) **Invalid.** Duties of excise on alcoholic liquors meant for human consumption are covered under Entry 51 of State List (List II). Thus, only State Governments are authorized to make laws in respect of such excise duty.
- (ii) **Invalid.** Taxes on intra-State sale or purchase of goods are covered under Entry 54 of State List of the Constitution. Entry 92A of Union List of the Constitution covers central sales tax.

Exercise

1. *Differentiate between direct and indirect taxes.*
2. *Enumerate different types of direct and indirect taxes.*
3. *Explain the salient features of indirect taxes.*
4. *Write a short note on various Lists provided under Seventh Schedule to the Constitution of India.*
5. *Which Governmental bodies control and administer direct and indirect taxes in India?*

UNIT – 2 : CENTRAL EXCISE DUTY

For the sake of brevity, Central Excise Act, 1944 and Central Excise Tariff Act, 1985 has been referred to as CEA and CETA respectively in the key points given below.

KEY POINTS											
What is excise duty?	Excise duty is a tax upon manufacture of goods and not upon sale of goods.										
Constitutional provisions	Central excise duty is levied vide Entry 84 of the Union List.										
	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 15%;">Entry 84 includes excise duty on</td> <td> <ul style="list-style-type: none"> ❖ Tobacco ❖ Other goods manufactured or produced in India ❖ Medicinal and toilet preparations containing alcohol, opium, Indian hemp or other narcotic drugs and narcotics </td> </tr> <tr> <td>Entry 84 excludes excise duty on</td> <td> <ul style="list-style-type: none"> ❖ Alcoholic liquors for human consumption ❖ Opium, Indian hemp and other narcotic drugs and narcotics </td> </tr> </table>	Entry 84 includes excise duty on	<ul style="list-style-type: none"> ❖ Tobacco ❖ Other goods manufactured or produced in India ❖ Medicinal and toilet preparations containing alcohol, opium, Indian hemp or other narcotic drugs and narcotics 	Entry 84 excludes excise duty on	<ul style="list-style-type: none"> ❖ Alcoholic liquors for human consumption ❖ Opium, Indian hemp and other narcotic drugs and narcotics 						
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Entry 84 excludes excise duty on	<ul style="list-style-type: none"> ❖ Alcoholic liquors for human consumption ❖ Opium, Indian hemp and other narcotic drugs and narcotics 										
Applicable excise duties	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 15%;">Basic Excise Duty (CENVAT)</td> <td> <ul style="list-style-type: none"> ❖ Leviable u/s 3(1)(a) of CEA at the rates specified in First Schedule of CETA ❖ Applicable on majority of goods ❖ General rate: 12% </td> </tr> <tr> <td>National Calamity Contingent duty (NCCD)</td> <td> <ul style="list-style-type: none"> ❖ Leviable u/s 136 of the Finance Act, 2001 ❖ Applicable on pan masala, branded chewing tobacco, cigarettes, domestic crude oil and mobile phones </td> </tr> <tr> <td>Additional Duty of Excise</td> <td> <ul style="list-style-type: none"> ❖ Leviable u/s 85 of the Finance Act, 2005 by way of surcharge ❖ Applicable on pan masala and certain specified tobacco products </td> </tr> <tr> <td>Education Cess</td> <td> <ul style="list-style-type: none"> ❖ Leviable on excisable goods manufactured in India ❖ Rate: 2% of the aggregate duties of excise levied on such goods </td> </tr> <tr> <td>Secondary and Higher Education</td> <td> <ul style="list-style-type: none"> ❖ Leviable on excisable goods manufactured in India ❖ Rate: 1% of the aggregate duties of excise </td> </tr> </table>	Basic Excise Duty (CENVAT)	<ul style="list-style-type: none"> ❖ Leviable u/s 3(1)(a) of CEA at the rates specified in First Schedule of CETA ❖ Applicable on majority of goods ❖ General rate: 12% 	National Calamity Contingent duty (NCCD)	<ul style="list-style-type: none"> ❖ Leviable u/s 136 of the Finance Act, 2001 ❖ Applicable on pan masala, branded chewing tobacco, cigarettes, domestic crude oil and mobile phones 	Additional Duty of Excise	<ul style="list-style-type: none"> ❖ Leviable u/s 85 of the Finance Act, 2005 by way of surcharge ❖ Applicable on pan masala and certain specified tobacco products 	Education Cess	<ul style="list-style-type: none"> ❖ Leviable on excisable goods manufactured in India ❖ Rate: 2% of the aggregate duties of excise levied on such goods 	Secondary and Higher Education	<ul style="list-style-type: none"> ❖ Leviable on excisable goods manufactured in India ❖ Rate: 1% of the aggregate duties of excise
	Basic Excise Duty (CENVAT)	<ul style="list-style-type: none"> ❖ Leviable u/s 3(1)(a) of CEA at the rates specified in First Schedule of CETA ❖ Applicable on majority of goods ❖ General rate: 12% 									
	National Calamity Contingent duty (NCCD)	<ul style="list-style-type: none"> ❖ Leviable u/s 136 of the Finance Act, 2001 ❖ Applicable on pan masala, branded chewing tobacco, cigarettes, domestic crude oil and mobile phones 									
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	Cess	(excluding education cess) leviable on such goods
Levy of duty		
Application of central excise law	CEA and CETA apply to <ul style="list-style-type: none"> ♣ whole of India (including Jammu and Kashmir) and ♣ also extends to designated areas in the Continental Shelf and Exclusive Economic Zone of India (EEZ) 	
Taxable event	<ul style="list-style-type: none"> ◆ Taxable event for levy of excise duty is manufacture. However, all manufacturing processes do not attract levy of excise duty unless some basic conditions are met. ◆ Excise duty is not concerned with ownership or sale. 	
Charge of excise duty [Section 3]	Excise duty is leviable when the following four conditions are satisfied cumulatively: <ul style="list-style-type: none"> ♣ There is a manufacture ♣ Such manufacture is in India (excluding SEZ) ♣ Such manufacture results in 'goods', and ♣ Such goods are excisable goods Other propositions of charging section: <ul style="list-style-type: none"> ◆ No distinction between excisable goods produced by Government and those produced by others, with regard to payment of excise duty. ◆ Excise duty leviable on goods sold by an EOU in DTA = Total customs duties leviable under the Customs Act/other applicable law on like goods produced/manufactured outside India, if imported into India. <ul style="list-style-type: none"> ▪ Value of such goods is determined in accordance with Customs Act, 1962 if the duty to be levied is based on the value of such goods (ad valorem). ▪ Where in respect of any such like goods, customs duty is leviable at different rates, then, highest of those rates is taken. 	
Goods, Excisable goods, Non-excisable goods, Non-dutiable goods, Exempted goods		
Goods	<ul style="list-style-type: none"> • Two fundamental aspects of the term 'goods' are that they should be (a) 'moveable' and (b) 'marketable'. Marketability	

	<ul style="list-style-type: none"> ◆ Explanation to section 2(d) of CEA provides that 'goods' includes any article, material or substance which is being capable of brought and sold for a consideration and such goods shall be deemed to be marketable. ◆ Even one purchaser is enough for establishing marketability. ◆ Actual sale is not necessary for being marketable. ◆ Marketability is a question of fact to be decided on the basis of the facts of each case. ◆ Goods of short-shelf life will be deemed to be marketable only if they are capable of being brought and sold during that period.
Excisable goods	<ul style="list-style-type: none"> ◆ Excisable goods are the 'goods' which are specified in the First Schedule and the Second Schedule to the Central Excise Tariff Act, 1985 as being subject to a duty of excise and includes salt [Section 2(d) of CEA]. ◆ Since Nil rate is a rate of duty, goods specified in the Tariff as being subject to Nil rate of duty are also excisable goods.
Non-excisable goods, Non-dutiable goods, Exempted goods	<ul style="list-style-type: none"> ◆ Goods not specified in the Tariff or the goods against which no rate (i.e, blank rate) has been specified in the Tariff are non-excisable goods. ◆ Non-dutiable goods are excisable goods but are not liable to duty either on account of rate of duty being 'NIL' in the Tariff or on account of 100% exemption granted by any exemption notification. ◆ Exempted goods are excisable goods which have been exempted from payment of duty by way of an exemption notification.
Manufacture	
Definition of manufacture [Section 2(f) of CEA]	<p>Manufacture includes any process,</p> <ul style="list-style-type: none"> (i) incidental or ancillary to the completion of a manufactured product; (ii) which is specified in relation to any goods in the Section or Chapter Notes of the Schedule to the Central Excise Tariff Act, 1985 as amounting to manufacture; or (iii) which, in relation to goods specified in the Third Schedule, involves packing or repacking of such goods in a unit container or labelling or re-labelling of containers including the declaration or alteration of retail sale price on it or adoption of any other treatment on the goods to render the product marketable to consumer

	and the term manufacturer shall be construed accordingly and shall include not only a person who employs hired labour in the production or manufacture of excisable goods, but also any person who engages in their production or manufacture on his own account.
Judicial interpretation	An activity or process would amount to "manufacture" if it leads to emergence of a new commercial product, different from the one with which the process started. In other words, it must be an article with different name, character or use.
Deemed manufacture	Clauses (ii) and (iii) of the definition of manufacture as provided in section 2(f) of CEA are termed as 'deemed manufacture'. The aforesaid definition gives a wider meaning to the expression "manufacture" as several processes which would not ordinarily be understood as amounting to manufacture are specifically included therein.
Levy of excise duty on captive consumption	<ul style="list-style-type: none"> ◆ Intermediate goods produced will be chargeable to duty if they arise in the course of manufacture/production, are moveable and marketable in such intermediate stage, listed in the Tariff, and are subject to duty of excise in the Tariff. ◆ However, if duty is payable on final product, excise duty is exempted on intermediate product used in manufacture of such final products.
Assembly <i>vis a vis</i> manufacture	<ul style="list-style-type: none"> ◆ Assembly would not amount to manufacture in as much as an already manufactured item may be put in a readily usable form. ◆ However, if the assembly results in new commercial commodity with a distinct name, character and use, then it would amount to manufacture.
Dutiability of waste and scrap	<ul style="list-style-type: none"> ◆ Waste/scrap can be 'excisable goods' if they are known in commercial parlance, are marketable and specified in Central Excise Tariff. ◆ Since excise duty is leviable on manufacture, waste and scrap (which are excisable goods) actually generated in the course of manufacture alone is chargeable to duty and waste and scrap generated without any process is not liable to excise duty. ◆ Waste of exempted goods is exempt from excise duty.
Manufacturer	
Who is a manufacturer?	<p>A person carrying out manufacture in terms of any of the three clauses of section 2(f) of CEA is the manufacturer. Following are also included in the definition of manufacturer:</p> <ul style="list-style-type: none"> ♣ a manufacturer who manufactures through hired labour

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	♣ a manufacturer who manufactures on his own account
Raw material supplier/ Brand name owner <i>vis a vis</i> manufacturer	<ul style="list-style-type: none"> ◆ Person carrying out actual manufacturing process is manufacturer even if raw material is supplied by someone else and goods have been manufactured as per his specifications. ◆ Person actually undertaking manufacturing process is the manufacturer and not the brand name owner under whose brand name, such person manufactures the final product. ◆ If the relationship between raw material supplier/brand name owner and person carrying out actual manufacturing process is that of a principal and agent, raw material supplier will be the manufacturer. ◆ A person supplying raw material/brand name owner will be considered as hiring job worker only if he supervises and controls the activities of the job worker. ◆ If manufacturer is a dummy or fake unit, then raw material supplier or the brand name owner will be deemed to be the actual manufacturer.
Collection of duty	
Time for payment of duty	<ul style="list-style-type: none"> ◆ Taxable event for levy of excise duty is manufacture, but collection thereof is postponed to the stage of removal. ◆ Excisable goods cannot be removed from the place of manufacture or from warehouse (when the goods are stored in warehouse) without payment of duty whether for consumption, or export, or manufacture of any other commodity in or outside the place of manufacture until the excise duty leviable thereon has been paid in the prescribed manner.
Person liable to pay duty	<ul style="list-style-type: none"> ◆ Every person who produces or manufactures any excisable goods, or who stores such goods in a warehouse is liable to pay excise duty. ▣ Exception: Where molasses are produced in a Khandsari sugar factory, the person who procures such molasses (not the person who produces the same) for use in the manufacture of any commodity is liable to pay duty on such molasses.
Relevant date for determination of rate of duty	<ul style="list-style-type: none"> ◆ For excisable goods other than khandsari molasses, relevant date is the date when such goods are removed from the factory or the warehouse. ◆ For khandsari molasses, relevant date is the date of receipt of such molasses in the factory of the procurer of such molasses.

	<ul style="list-style-type: none"> ◆ In case of captive consumption, relevant date is the date on which the goods are issued for such use. 	
Some special aspects	<ul style="list-style-type: none"> ◆ When there is a change in rate of duty between date of manufacture and date of removal, duty will be leviable at the rate prevalent on the date of removal. ◆ Non-excisable goods will not be chargeable to duty even though subsequent to manufacture but before removal such goods are bought within the purview of the Tariff or are made chargeable to a specified rate of duty under the Tariff. ◆ Exempted goods will be chargeable to duty at the time of removal (at rate prevalent on the date of removal) if, subsequent to manufacture but before removal, the exemption from duty is withdrawn. 	
Classification of excisable goods		
Concept	<ul style="list-style-type: none"> ◆ Classification of excisable goods is essential for determining applicable rate of duty and eligibility to exemptions. ◆ CETA is based on Harmonised System of Nomenclature (HSN). ◆ The First Schedule to CETA specifying rate of CENVAT has Sections which are divided into Chapters. A Chapter is further divided into headings and sub-headings. 	
Eight digit classification system	<ul style="list-style-type: none"> ◆ Excisable goods are classified by using 8-digit system. Description with eight digits is termed as 'tariff item'. ◆ First two digits refer to Chapter Number of the Tariff, Next two digits refer to heading of the goods in that Chapter, Next two digits indicate Chapter sub-heading and Last two digits refer to the Chapter sub-sub-heading. 	
Trade parlance theory	If a product is not adequately classified in CETA, it should be classified according to its popular meaning or meaning attached to it by those dealing with it, i.e., in commercial sense.	
Rate of duty	<ul style="list-style-type: none"> ◆ Rate of duty in respect of each tariff entry is specified in CETA. ◆ Effective rate of duty is ascertained by considering the exemption(s) available in respect of a particular item. 	
Valuation of excisable goods		
Basis of computing duty payable	Specific duty	❖ Duty payable on units like length, weight, volume etc
	Compounded levy scheme	❖ Optional duty payable on the basis of specified factors relevant to production of the goods

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		covered under the scheme at specified rates for specified period.
	Duty based on capacity of production	<ul style="list-style-type: none"> ❖ Mandatory duty payable on notified goods on the basis of production capacity, without any reference to the actual production. ❖ Goods are notified having regard to the nature of the process of manufacture or production of excisable goods of any specified description, the extent of evasion of duty in regard to such goods etc.
	Duty based on value	<ul style="list-style-type: none"> ♣ Duty payable on the basis of Tariff Value [Section 3(2) of CEA] ♣ Duty payable on the basis of Retail Sale Price [Section 4A of CEA] ♣ Duty payable on the basis of Transaction Value [Section 4 of CEA]
Tariff value [Section 3(2)]		<ul style="list-style-type: none"> ◆ Central Government fixes/alters tariff values in respect of notified goods. Duty payable is a percentage of such tariff value. ◆ Different tariff values may be fixed for different classes or descriptions of the same excisable goods. ◆ Different tariff values may also be fixed for same class or description of the goods but produced or manufactured by different classes of producers or manufacturers or sold to different classes of buyers. ◆ Tariff values may be fixed on the basis of wholesale price or average price of various manufacturers as the Government may consider appropriate.
Retail sale price (RSP) based valuation [Section 4A]	Applicable in respect of excisable goods	<ul style="list-style-type: none"> ♣ which are notified by Central Government as goods in relation to which duty will be paid on the basis of RSP less abatements, if any; and ♣ declaration of RSP on package of such goods is required under Legal Metrology Act, 2009.
		Definition of RSP: Retail sale price has been defined to mean the maximum price at which the excisable goods in packaged form may be sold to the ultimate consumer and includes all taxes, local or otherwise, freight, transport charges, commission payable to dealers, and all charges towards advertisement, delivery, packing, forwarding and the like, as the case may be, and the price is the sole consideration for such

	<p>sale.</p> <p>However, if the provisions of the Act, rules or Legal Metrology Act, 2009 require the retail sale price to exclude any taxes, local or otherwise, the retail sale price shall be construed accordingly.</p> <p>Value = RSP printed on the package – Abatement, if any, notified by the Government</p> <ul style="list-style-type: none"> ◆ More than one RSP on package of excisable goods - Maximum of such price to be deemed as the RSP. ◆ Different RSPs on different packages meant for sale in different areas - Each such RSP to be the RSP in the relevant area. ◆ RSP increased after clearance from the place of manufacture - Increased RSP to be deemed as the RSP. ◆ RSP declaration is not mandatory on wholesale packages, packaged commodities for institutional/ industrial consumers, agricultural farm produce etc.
<p>Transaction value [Section 4]</p>	<ul style="list-style-type: none"> ◆ Residual method of valuation – If goods cannot be valued by any of the methods described above, they are to be valued as per provisions of section 4. ◆ Assessable value of the excisable goods shall be the 'transaction value' if following conditions are satisfied:- <ul style="list-style-type: none"> ➤ Price is the sole consideration for the sale i.e., assessee must not receive any other sum either by way of money or by way of any other assistance for the manufacture of goods. ➤ Assessee and buyer of the goods are not related persons. ➤ Goods have been sold by assessee for delivery at the time and place of removal. <p>Definition of Transaction Value</p> <ul style="list-style-type: none"> ♣ Transaction value means the price actually paid or payable for the goods, when sold, and includes in addition to the amount charged as price, ♣ any amount that the buyer is liable to pay to, or on behalf of, the assessee, by reason of, or in connection with the sale, whether payable at the time of the sale or at any other time, including, but not limited to, ♣ any amount charged for, or to make provision for, advertising or publicity, marketing and selling organization expenses, storage,

1.12 Indirect Taxes

	<p>outward handling, servicing, warranty, commission or any other matter; but does not include</p> <p>♣ the amount of duty of excise, sales tax and other taxes, if any, actually paid or actually payable on such goods.</p>				
	<table border="1"> <thead> <tr> <th>Inclusions in transaction value</th> <th>Exclusions from transaction value</th> </tr> </thead> <tbody> <tr> <td> <ul style="list-style-type: none"> ➤ Outward handling upto place of removal ➤ All forms of packing (special, general, protective, etc.) ➤ Dharmada or charity ➤ Design, development and engineering charges specific to goods produced ➤ Bought out essential items if the same are fitted to the main article at the time of removal. ➤ Consultancy charges relating to design, layout, etc. of final product done upto place of removal ➤ Testing & inspection charges ➤ Erection, installation and commissioning charges resulting in movable property ➤ Pre-delivery inspection charges and after sales service charges collected by the manufacturer ➤ Freight from factory to depot if sale is from depot </td> <td> <ul style="list-style-type: none"> ➤ Durable/reusable packing as it is amortized and included in the cost of product itself ➤ Optional bought out items and accessories ➤ Independent testing done by the buyer himself or through a third party ➤ All forms of discount if actually passed on to the buyers. ➤ Notional interest on deposits, advances unless it can be proved that price has been lowered on account of receipt of such advance from the buyer ➤ Interest on delayed payment of receivables ➤ Bank charges for collection of sale proceeds ➤ Delayed payment charges ➤ Outward freight from factory/depot to place of customer. ➤ Transit insurance </td> </tr> </tbody> </table>	Inclusions in transaction value	Exclusions from transaction value	<ul style="list-style-type: none"> ➤ Outward handling upto place of removal ➤ All forms of packing (special, general, protective, etc.) ➤ Dharmada or charity ➤ Design, development and engineering charges specific to goods produced ➤ Bought out essential items if the same are fitted to the main article at the time of removal. ➤ Consultancy charges relating to design, layout, etc. of final product done upto place of removal ➤ Testing & inspection charges ➤ Erection, installation and commissioning charges resulting in movable property ➤ Pre-delivery inspection charges and after sales service charges collected by the manufacturer ➤ Freight from factory to depot if sale is from depot 	<ul style="list-style-type: none"> ➤ Durable/reusable packing as it is amortized and included in the cost of product itself ➤ Optional bought out items and accessories ➤ Independent testing done by the buyer himself or through a third party ➤ All forms of discount if actually passed on to the buyers. ➤ Notional interest on deposits, advances unless it can be proved that price has been lowered on account of receipt of such advance from the buyer ➤ Interest on delayed payment of receivables ➤ Bank charges for collection of sale proceeds ➤ Delayed payment charges ➤ Outward freight from factory/depot to place of customer. ➤ Transit insurance
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Price-cum-duty	
What is price-cum-duty?	<p>Price actually paid for the goods sold + Money value of the additional consideration = Price-cum-duty - Sales tax and other taxes actually paid = Price-cum-duty deemed to be inclusive of the duty payable on such goods</p> $\text{Assessable Value} = \frac{\text{Price - cum - duty (exclusive of sales tax/local tax)} \times 100}{(100 + \text{Rate of excise duty})}$
	<p>Price charged (exclusive of sales tax/local tax) will be taken as price-cum-duty:</p> <ul style="list-style-type: none"> ♣ If the assessee has collected less duty from the buyer than what is due; or ♣ If the assessee has not collected any duty from the buyer even though the product is liable to duty; or ♣ If the assessee has paid duty on lesser value due to receipt of additional consideration.
	<ul style="list-style-type: none"> ◆ Amount of duty should be indicated prominently in all the documents/invoice, etc. ◆ Person liable to pay duty should forthwith deposit any sum collected from the buyer in name of excise duty with the Government.
Small scale industry (SSI) exemption	
What is SSI exemption?	<ul style="list-style-type: none"> ◆ Units having turnover upto ₹ 400 lakh in the previous financial year and manufacturing goods specified in the SSI exemption notification are eligible for exemption from duty up to turnover of ₹ 150 lakh in the current financial year. ◆ A SSI unit can avail CENVAT credit on inputs only after it starts paying duty. However, CENVAT credit of capital goods can be availed (but can be utilized only after the turnover crosses ₹ 150 lakh) even if the same have been received during period of exemption. ◆ SSI exemption is not available in respect of clearances bearing a brand name of another person. However, goods manufactured in rural area, packing material, account books, registers, writing pads etc. are entitled to SSI exemption even though they bear the brand name of other person.

Question 1

Examine whether central excise duty is leviable in the following situations:-

- (a) *Mohan Builders have constructed an office building for M/s XYZ & Co.*
- (b) *ABC Maintenance Services Ltd. provided maintenance services for refrigerators and air-conditioners.*

Answer

- (a) **No.** Excise duty is leviable only when manufacture results in goods that are excisable. For being called goods, items ought to be movable and marketable. Since office building is marketable but not movable, it is not 'goods' but an immovable property. Hence, excise duty is not leviable on construction of office building.
- (b) **No.** Excise duty is leviable on manufacture of excisable goods. However, activity of maintenance of refrigerators and air conditioners is not 'manufacture' as it does not result into emergence of a new article having different name, character or use. Thus, since the activity is not 'manufacture', excise duty is not leviable on the same.

Question 2

A trader of steel articles purchases steel bars of 10 meters. He cuts the bars as per requirements of customer and supplies the cut bars to them. He seeks clarification whether he will be liable to pay excise duty on the cut bars sold by him.

Answer

Supreme Court has held that 'manufacture' can be said to have taken place when after a process, a new and different article emerges having a distinctive name, character or use. However, in this case, after cutting, the product continues to be a bar. There is no change in name, character or use. Hence, the activity is not 'manufacture' and excise duty will not be payable.

Question 3

ABC Co. is buying oil in drums of 200 liters. They pack this oil in small tins of one litre each, put their label giving details of contents, volume and MRP. Advise whether ABC Co. are liable to pay excise duty on small tins sold by them.

Answer

Mere repacking from large container to small pack is not 'manufacture' of oil as oil continues to be oil – no new product comes into existence having a distinct name, character or use. Hence, the activity is not 'manufacture' and excise duty is not payable.

However, if such oil is covered under section 4A of Central Excise Act, 1944 (RSP based valuation provisions), the activity of labelling will be 'deemed manufacture' and ABC Co. will be liable to pay excise duty on such containers of one litre each.

Question 4

A purchases cloth and gives it to B, who is a tailor, to stitch a shirt as per measurements and requirements of A. B stitched the shirt and gave it to A. In the given case, who will be treated as manufacturer of the shirt for the purpose of levy of central excise duty?

Answer

A person who carries out actual manufacturing process is considered as 'manufacturer' for the purpose of levy of central excise duty even if raw material is supplied by someone else and goods are manufactured as per the specifications of such person. In other words, ownership of raw material is not relevant.

Therefore, in this case, B (tailor), being the actual manufacturer, will be treated as 'manufacturer' for purpose of levy of excise duty even though the cloth (raw material) for making shirt is provided by A and the shirt is stitched as per his specifications.

Question 5

Famous Hero Motors Ltd. purchases raw material and supplies it to JBK Engineering Company. JBK Engineering Company manufactures automobile components as per the design supplied by Famous Hero Motors. Such components bear brand name of Famous Hero Motors Ltd. namely, 'Famous Hero'. JBK Engineering Company supplies these components to Famous Hero Motors Ltd., who in turn sells them in market as spare parts of automobiles. Who is liable to pay central excise duty on such components?

Answer

Liability to pay central excise duty falls on actual manufacturer of goods. Therefore, in this case, JBK Engineering Company, being actual manufacturer, will be liable to pay excise duty. This would be so even if raw material does not belong to them and goods manufactured by them bear the brand name of Famous Hero Motors Ltd. as in case of central excise, ownership of goods is not the relevant criterion to determine duty liability.

Question 6

Distinguish between tariff rate of excise duty and effective rate of excise duty.

Answer

Tariff rate of duty is the rate which is given in Central Excise Tariff. However, Government can give partial or complete exemption from payment of excise duty. Thus, the rate at which excise duty is actually payable is termed as 'effective rate of excise duty'. For example, if rate of excise duty given in Central Excise Tariff is 12%, the same would be termed as 'tariff rate'. However, if by way of an exemption notification, excise duty payable is reduced to 6%, the effective rate of excise duty would be 6%.

Question 7

Excise duty payable on cane molasses is ₹ 1,000 per ton. Excise duty on cane sugar is 12%. A manufacturer cleared 100 tons of cane molasses from his factory. He sold the cane molasses @ ₹ 15,000 per ton. Calculate the excise duty payable.

Answer

When excise duty is payable on the basis of a specific rate, the rate at which goods are actually sold is immaterial. Therefore, since in this case, excise duty on cane molasses is payable on the basis of tonnage (specific rate), rate at which they are sold is not relevant.

Thus, excise duty payable in this case will be ₹ 1,00,000 [₹ 1,000 x 100 tons].

Question 8

GHI Co. is a manufacturer. It intends to pay ad valorem excise duty on the basis of assessable value computed under section 4 of the Central Excise Act, 1944. However, Excise Department insists that GHI Co. should pay duty under Compounded Levy Scheme as the product manufactured by it is covered under the said scheme.

You are required to examine the situation in the light of the relevant statutory provisions. Will your answer be different if the product manufactured by GHI Co. is notified under production capacity based duty scheme?

Answer

Under Compounded Levy Scheme, assessee has an **option** to pay excise duty on the basis of specified factors relevant to production of goods covered under the scheme (size of equipment employed, number and types of machines used for manufacture etc.) at specified rates. The prescribed duty has to be paid by the assessee for a specified period.

Therefore, since Compounded Levy Scheme is an **optional scheme**, GHI Co. can pay *ad valorem* duty under section 4 even if goods manufactured by it are covered under Compounded Levy Scheme.

However, duty based on production capacity is **mandatory** i.e, duty cannot be paid in any other manner in respect of the goods notified under this scheme. Therefore, if goods manufactured by GHI Co. get notified under production capacity based duty scheme, it will not be able to pay duty under section 4 and will have to compulsorily pay duty based on its production capacity.

Question 9

Decent Footwear is a leading manufacturer of shoes. Legal Metrology Act, 2009 requires declaration of retail sale price on the package of shoes and shoes are also notified under section 4A of Central Excise Act, 1944 (RSP based valuation provisions).

Following information has been furnished by Decent Footwear:

<i>Aabatement available on shoes</i>	<i>40% of retail sale price</i>
<i>MRP marked on the package</i>	<i>₹ 2,000 per pair of shoes</i>
<i>Price at which Decent Footwear sells the shoes to their wholesalers</i>	<i>₹ 1,300 per pair of shoes</i>
<i>Price at which wholesalers sell the shoes to retail shop owners</i>	<i>₹ 1,500 per pair</i>
<i>Price at which shoes are sold by retailers to final consumers</i>	<i>₹ 1,900 (₹ 100 offered as discount on printed retail sale price)</i>
<i>Excise duty</i>	<i>12%</i>
<i>Education cess</i>	<i>2%</i>
<i>Secondary and Higher Education Cess</i>	<i>1%</i>

Calculate excise duty payable on a pair of shoes.

Answer

Since Legal Metrology Act, 2009 requires declaration of retail sale price on the package of shoes and shoes are also notified under section 4A of Central Excise Act, 1944 (RSP based valuation provisions), excise duty will be payable on the basis of RSP less abatement.

Particulars	₹
MRP marked on the package of a pair of shoes	2,000
<i>Less: Abatement @ 40% of RSP [40% of ₹ 2,000]</i>	8,00
Value for purpose of excise duty	1,200
Excise duty @ 12% [12% of ₹ 1,200]	144
Education cess @ 2% [2% of ₹ 144]	2.88
Secondary and Higher Education Cess @ 1% [1% of ₹ 144]	1.44
Total excise duty payable (rounded off)	148

Question 10

Zebra Engineers are manufacturers of specialty articles. Such articles are sold through retail shops.

<i>MRP marked on the package</i>	<i>₹ 2,000 per piece</i>
<i>Price at which Zebra Engineers sells articles to their wholesalers</i>	<i>₹ 1,300 per piece</i>
<i>Price at which wholesalers sell the articles to retail shop</i>	<i>₹ 1,500 per piece</i>

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<i>owners</i>	
<i>Price at which articles are sold by retailers to final consumers</i>	<i>₹ 1,900 (₹ 100 offered as discount on printed retail sale price)</i>
<i>Excise duty</i>	<i>12%</i>
<i>Education cess</i>	<i>2%</i>
<i>Secondary and Higher Education Cess</i>	<i>1%</i>

Calculate excise duty payable on an article. Such articles are not covered under section 4A of Central Excise Act, 1944.

Answer

Since the articles are not covered under section 4A of Central Excise Act, 1944 (RSP based valuation provisions), excise duty will be payable on the basis of assessable value under section 4 of Central Excise Act (transaction value). Thus, value for purpose of excise duty will be ₹ 1,300 i.e., the price at which the articles are sold to wholesalers.

Particulars	₹
Transaction value [price at which Zebra Engineers sells articles to their wholesalers]	1,300
Excise duty @ 12% [12% of ₹ 1,300]	156
Education cess @ 2% [2% of ₹ 156]	3.12
Secondary and Higher Education Cess @ 1% [1% of ₹ 156]	1.56
Total excise duty payable (rounded off)	161

Question 11

A manufacturer of machinery sold a special machine. Following details are provided in relation to amounts charged:

	₹
<i>Price of machinery excluding taxes and duties</i>	<i>6,00,000</i>
<i>Installation charges [Machinery is fixed to earth in customer's premises]</i>	<i>21,000</i>
<i>Packing charges</i>	<i>9,000</i>
<i>Extra charges for designing the machine</i>	<i>20,000</i>
<i>Outward freight beyond place of removal</i>	<i>12,000</i>

Other information furnished is -

- (a) *Cash discount @ 2% on price of machinery was allowed as the customer paid the bill amount before dispatch.*

(b) State VAT rate – 5%

(c) Central excise duty rate 12% and education cesses as applicable.

Calculate excise duty payable on the special machine.

Answer

Computation of excise duty payable

Particulars	₹
List price of machinery	6,00,000
Add: Packing charges [Note 1(i)]	9,000
Extra design charges [Note 1(i)]	<u>20,000</u>
Total	6,29,000
Less: 2% cash discount on price of machinery [₹ 6,00,000 x 2%] [Note 1(iv)]	<u>12,000</u>
Assessable value	<u>6,17,000</u>
Excise duty @ 12.36% [inclusive of 3% education cesses]	76,261.20
Excise duty payable [rounded off]	76,261

Notes:-

1. While computing assessable value:-
 - (i) packing charges and extra designing charges have been included as such payments are 'in connection with sale'.
 - (ii) installation and erection expenses have not been included as they result in immovable property which is not goods.
 - (iii) outward freight has not been included as it is incurred for transporting the goods beyond the place of removal.
 - (iv) cash discount has been allowed as deduction as it has been passed on to the buyer.
2. State VAT does not affect excise duty payable.

Question 12

Calculate assessable value and excise duty payable on the basis of following information:

	₹
Total invoice price	40,000
State VAT	4,000
Insurance charges for dispatch of final product	200
Packing charges	1,000

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<i>Freight charged from factory to the place of customer</i>	<i>2,000</i>
<i>Excise duty rate is 12% and education cesses as applicable</i>	

Answer

Computation of excise duty payable

Particulars	₹
Total invoice price	40,000
Less: State VAT (Note 1)	4,000
Freight charges (Note 2)	2,000
Insurance charges (Note 2)	<u>200</u>
Price-cum-duty (a)	<u>33,800</u>
Less: Excise duty @ 12.36% (inclusive of 3% education cesses)	3,718.12
[₹ 33,800 x 12.36/112.36]	<u> </u>
Total excise duty including education cesses (rounded off) (b)	<u>3,718</u>
Assessable value (a) – (b)	30,082

Notes:

1. Invoice price includes State VAT. Thus for calculating assessable value, deduction has been allowed for State VAT.
2. Insurance charges for dispatch of final product and freight charged from factory to the place of customer are allowed as deduction as the same are incurred after the place of removal.
3. Since packing charges are includible in assessable value, deduction for the same has not been provided.

Question 13

A manufacturer cleared some goods by charging excise duty. The invoice provided the following details:

	₹
Price	10,000
Excise duty @ 10.30%	1,030
Total	11,030

However, he came to know later that actual rate of excise duty is 12.36%. How much differential duty is payable by him, if he is not able to recover any extra amount from the customer?

Answer

Since the manufacturer charged only ₹ 11,030 and he is not able to recover any extra amount from customer, this amount is required to be treated as price-cum-duty. Hence, differential duty payable by him will be computed as under:

Particulars	₹
Price-cum-duty	11,030
Excise duty @ 12.36% [₹ 11,030 x 12.36/112.36]	1,213.34
Excise duty (rounded off)	1,213
Differential excise duty to be paid [₹ 1,213 – ₹ 1,030 (duty already paid)]	183

Question 14

Net value of clearances (excluding taxes and duties) of Gopal Manufacturers was ₹ 345 lakh during the year 2012-13. During the year 2013-14, their net value of clearances (excluding taxes and duties) was ₹ 365 lakh. Calculate excise duty payable by Gopal Manufacturers during 2013-14, if excise duty rate is 12.36%.

Answer

Units having turnover upto ₹ 400 lakh in the previous financial year and manufacturing goods specified in the SSI exemption notification are eligible for exemption from duty up to turnover of ₹ 150 lakh in the current financial year.

Therefore, in the give case Gopal Manufacturers can avail SSI exemption of ₹ 150 lakh in 2013-14 as their turnover during 2012-13 was less than ₹ 400 lakh. It is presumed that goods manufactured by them are specified under SSI exemption notification.

Hence, they have to pay excise duty @ 12.36% on balance value i.e. on ₹ 215 lakhs (₹ 365 – ₹ 150). Thus, duty payable will be ₹ 26,57,400.

Exercise

1. *What is an excise duty? Discuss the relevant Constitutional provisions governing the imposition of such levy.*
2. *Explain different types of excise duties.*
3. *Enlist and explain various sources of central excise law.*
4. *What is the taxable event for levy of excise duty? Explain the provisions of charging section 3 of Central Excise Act, 1944?*
5. *Discuss the concept of goods and excisable goods and bring out the difference between the two.*
6. *Are non-excisable and exempted goods one and the same? Explain.*

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7. *Explain the concept of manufacture and deemed manufacture by giving two examples in each case.*
8. *Write a short note on dutiability of site-related activities and waste and scarp.*
9. *Who is a manufacturer? Discuss whether a raw material supplier or a brand name owner can be treated as a manufacturer?*
10. *Discuss the provisions governing collection of duty.*
11. *Distinguish between Section and Chapter of Central Excise Tariff.*
12. *What are the different bases of computing excise duty payable?*
13. *When will the transaction value be taken as the assessable value under section 4 of the Central Excise Act, 1944?*
14. *In what circumstances will the price charged be taken as price-cum-duty?*
15. *Write a short note on SSI exemption available under central excise.*

UNIT – 3 : CUSTOMS DUTY

KEY POINTS							
Meaning of customs duty	<p>A <u>duty or tax</u>, which is levied by the Central Government on:-</p> <ul style="list-style-type: none"> ◆ <u>import</u> of goods into, and ◆ <u>export</u> of goods from, India 						
Constitutional provisions	Power to levy customs duty is conferred by <u>Entry 83</u> of the Union List [<i>Duties of customs including export duties</i>]						
Sources of customs law	Customs Act, 1962, Customs Tariff Act, 1975, Annual Union Finance Acts, Rules, Notifications, Circulars/ Instructions, Trade Notices/Clarifications and Case Laws						
LEVY OF CUSTOMS DUTY							
Applicability of the Act	<ul style="list-style-type: none"> ◆ The Customs Act, 1962 applies to the whole of India. India includes <u>territorial waters of India</u>. ◆ Besides, the Customs Act, 1962 and Customs Tariff Act, 1975 have been further extended to:- <ul style="list-style-type: none"> (i) the <u>notified designated areas</u> in the Continental Shelf of India (CSI) and Exclusive Economic Zone of India (EEZI) and (ii) <u>whole of EEZI and CSI for the purpose of</u> processing for extraction or production of mineral oils and supply of any goods in connection thereto. <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 50%; text-align: center;">Indian territorial waters</th> <th style="width: 50%; text-align: center;">Indian customs waters</th> </tr> </thead> <tbody> <tr> <td>Indian territorial waters extend <u>upto 12 nautical miles</u> (22 km) into the sea from the appropriate base line.</td> <td>Indian customs waters extend <u>upto a total of 24 nm</u> from base line</td> </tr> <tr> <td>All the provisions of the Customs Act and rules and regulations thereunder are applicable in Indian territorial waters.</td> <td>Certain powers of the customs officers have been extended in the Indian customs waters as well (for example, power to stop and search any vessel, power to arrest a person in Indian customs waters etc.).</td> </tr> </tbody> </table>	Indian territorial waters	Indian customs waters	Indian territorial waters extend <u>upto 12 nautical miles</u> (22 km) into the sea from the appropriate base line.	Indian customs waters extend <u>upto a total of 24 nm</u> from base line	All the provisions of the Customs Act and rules and regulations thereunder are applicable in Indian territorial waters.	Certain powers of the customs officers have been extended in the Indian customs waters as well (for example, power to stop and search any vessel, power to arrest a person in Indian customs waters etc.).
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All the provisions of the Customs Act and rules and regulations thereunder are applicable in Indian territorial waters.	Certain powers of the customs officers have been extended in the Indian customs waters as well (for example, power to stop and search any vessel, power to arrest a person in Indian customs waters etc.).						
Charging section	<ul style="list-style-type: none"> ◆ Customs duties shall be levied ◆ <u>at such rates</u> as may be specified under the Customs Tariff Act, 						

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[Section 12]	<p>1975. [The two schedules of the Tariff specify the rates: First schedule specifies import duty rates and Second schedule specifies export duty rates]</p> <ul style="list-style-type: none"> ◆ <u>on goods</u> [whether belonging to Government or not] ◆ <u>imported into and exported from</u> India. <p>Note: A lower preferential rate of duty has been prescribed for the goods imported from preferential areas.</p>		
Determination of duty where goods consist of articles liable to different rates of duty	Where goods consist of a set of articles, duty shall be calculated as follows: -		
	Articles which are liable to duty with reference to	shall be chargeable to	
	quantity	that duty	
	value and liable to duty at same rate	duty at that rate	
	value and liable to duty at different rates	duty at the highest of such rates	
	Articles not liable to duty	shall be chargeable to duty at the rate at which articles liable to duty with reference to value are liable.	
Taxable event in case of import/export	Imports	In case of	taxable event is
		goods cleared for home consumption	time when the goods become part of the mass of goods within the country.
	goods cleared for warehousing	time when the goods are cleared from the warehouse.	
Goods derelict,	Exports	Export of goods is complete when the goods cross the territorial waters of India.	
	◆ Customs duty is payable on all goods, derelict, jetsam, flotsam and wreck brought or coming into India.		

wreck etc coming into India	<ul style="list-style-type: none"> ◆ If such goods are entitled to be admitted duty-free, duty would not be levied provided it is shown to the satisfaction of the proper officer that they are so entitled.
CUSTOMS DUTY NOT LEVIABLE IN CERTAIN CASES	
No duty on pilfered goods	<ul style="list-style-type: none"> ◆ If any imported goods are pilfered ◆ after the unloading thereof ◆ but before the proper officer has made an order for clearance for home consumption or deposit in a warehouse, ◆ the importer shall not be liable to pay the duty leviable on such goods.
	However, where such goods are restored to the importer after pilferage, the importer becomes liable to duty.
	Pilfer means “to steal, especially in small quantities; petty theft”. Therefore, the term does not include loss of total package.
Remission of duty on goods lost or destroyed	<ul style="list-style-type: none"> ◆ Where it is shown to the satisfaction of the Assistant Commissioner/ Deputy Commissioner of Customs that ◆ any imported goods have been lost (otherwise than as a result of pilferage) or destroyed, ◆ at any time before clearance for home consumption, ◆ the Assistant Commissioner of Customs or Deputy Commissioner of Customs shall remit the duty on such goods.
No duty in case of relinquishment of the title to the goods	<ul style="list-style-type: none"> ◆ The owner of any imported goods may, ◆ at any time before an order for clearance of goods for home consumption or an order for permitting the deposit of goods in a warehouse has been made, ◆ relinquish his title to the goods and thereupon, ◆ he shall not be liable to pay the duty thereon.
	Such relinquishment is not allowed in respect of such goods regarding which an offence appears to have been committed under this Act or any other law for the time being in force.
	“Relinquish” means to give over the possession or control of, to leave off.
Abatement of duty on damaged or	<ul style="list-style-type: none"> ◆ The importer has an option to pay the reduced duty ◆ if it is shown to the satisfaction of the Assistant Commissioner/ Deputy Commissioner of Customs that

deteriorated goods	◆ the goods are damaged/deteriorated under any of the following circumstances:	
	In case	
	any imported goods had been damaged or had deteriorated at any time before or during the unloading of the goods in India	
	any imported goods, other than warehoused goods, had been damaged on account of any accident, at any time after the unloading thereof in India but before their examination for assessment by the customs authorities	Provided such accident is not due to any wilful act, negligence or default of the importer, his employee or agent.
	any warehoused goods had been damaged on account of any accident at any time before clearance for home consumption	
$= \frac{\text{Value of damaged/deteriorated goods} *}{\text{Value of goods before damage/deterioration}} \times \text{Duty on goods before damage/deterioration}$ <p>*Valuation of the damaged or deteriorated goods: The value shall be:-</p> <p>(a) Value ascertained by the proper officer</p> <p style="text-align: center;">or</p> <p>(b) The proper officer may sell such goods by public auction/tender or if the importer agrees, in any other manner and the gross sale proceeds shall be deemed to be the value of such goods.</p>		
EXEMPTION FROM CUSTOMS DUTY		
Central Government may grant exemption from customs duty if it is satisfied that it is necessary in the public interest to do so.		
General exemption	Central Government may, by notification in the Official Gazette, exempt generally either absolutely or subject to specified conditions.	
Special exemption	Central Government may, by special order, exempt from payment of duty, any goods on which duty is leviable only under circumstances of an exceptional nature to be stated in such order.	
CLASSIFICATION OF IMPORTED GOODS		
Meaning	To determine the headings or sub-headings of the Customs Tariff Act, 1975 (CTA) under which the imported/export goods would be covered.	
Need	It determines: (a) rate of applicable duty,	

	(b) applicability of import controls or restrictions, (c) applicability of anti-dumping duty, safeguard duty etc., (d) benefits of duty exemption notifications.				
VALUATION OF IMPORTED AND EXPORT GOODS					
<div style="border: 1px solid black; padding: 5px; margin: 0 auto; width: fit-content;"> Valuation of imported/ export goods </div> <div style="display: flex; justify-content: space-around; margin-top: 10px;"> <div style="border: 1px solid black; padding: 5px; width: 45%; text-align: center;"> Where custom duty is chargeable on ad valorem basis </div> <div style="border: 1px solid black; padding: 5px; width: 45%; text-align: center;"> Where specific duty is charged </div> </div> <div style="display: flex; justify-content: space-around; margin-top: 10px;"> <div style="border: 1px solid black; padding: 5px; width: 45%; text-align: center;"> Transaction Value </div> <div style="border: 1px solid black; padding: 5px; width: 45%; text-align: center;"> Tariff Value </div> </div>					
Transaction value, in case of imported/export goods shall be <ul style="list-style-type: none"> ◆ the price actually paid or payable for the goods ◆ when sold for export to/from India ◆ for delivery at the time and place of importation/exportation ◆ where the buyer and seller of the goods are not related and ◆ price is the sole consideration for the sale subject to such other conditions as may be specified in the rules made in this behalf.	CBEC may fix tariff values for any class of imported books or export goods by notification. In such a case, duty is chargeable with reference to such tariff values.				
Date relevant for determination of rate of exchange	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 20%; text-align: center;">For imported goods</td> <td>rate of exchange, notified by CBEC, prevalent on the date of filing bill of entry</td> </tr> <tr> <td style="text-align: center;">For export goods</td> <td>rate of exchange, notified by CBEC, prevalent on the date of filing shipping bill (<i>in case of export by vessel or aircraft</i>) or bill of export (<i>in case of export by vehicle</i>)</td> </tr> </table>	For imported goods	rate of exchange, notified by CBEC, prevalent on the date of filing bill of entry	For export goods	rate of exchange, notified by CBEC, prevalent on the date of filing shipping bill (<i>in case of export by vessel or aircraft</i>) or bill of export (<i>in case of export by vehicle</i>)
For imported goods	rate of exchange, notified by CBEC, prevalent on the date of filing bill of entry				
For export goods	rate of exchange, notified by CBEC, prevalent on the date of filing shipping bill (<i>in case of export by vessel or aircraft</i>) or bill of export (<i>in case of export by vehicle</i>)				
DATE FOR DETERMINING THE RATE OF DUTY AND TARIFF VALUATION OF IMPORTED GOODS					
In case of	the rate of duty and tariff valuation shall be the rate and valuation in force on the date				
goods entered for home consumption	on which a bill of entry in respect of such goods is presented**				

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goods cleared for home consumption from the warehouse	on which a bill of entry for home consumption in respect of such goods is presented
any other goods	of payment of duty
<p>**In case the goods have been imported by a vessel or aircraft, the rate of duty and tariff valuation shall be the rate and valuation in force on:-</p> <p>(i) the date on which Bill of Entry in respect of such clearance is presented or</p> <p>(ii) the date on which Entry Inwards is granted/ arrival of aircraft takes place whichever is later.</p>	
DATE FOR DETERMINING THE RATE OF DUTY AND TARIFF VALUATION OF EXPORT GOODS	
In case of	the rate of duty and tariff valuation shall be the rate and valuation in force on the date
goods entered for export	on which the proper officer makes an order permitting clearance and loading of the goods for exportation
any other goods	of payment of duty
TYPES OF CUSTOMS DUTIES	
Basic customs duty	<ul style="list-style-type: none"> ◆ Duty levied under the charging section-section 12 of the Customs Act, 1962 ◆ on any imported/export goods ◆ at the rates specified in the First and Second Schedules of the Customs Tariff Act, 1975 ◆ on transaction value under section 14(1) /tariff value determined under section 14(2) of the Customs Act, 1962.
Additional customs duty under section 3(1) of the Customs Tariff Act, 1975 [also known as Countervailing duty (CVD)]	<ul style="list-style-type: none"> ◆ Duty imposed on any imported article ◆ equal to excise duty for the time being in force leviable on a like article if produced or manufactured in India ◆ at the rate of excise duty leviable on a like article if produced or manufactured in India** (except in case of alcoholic liquor for human consumption for which rate of additional duty is notified by the Central Government). <p><i>Note: EC and SHEC leviable on additional duty of customs are exempt.</i></p> <p><i>**If a like article is not so produced or manufactured in India, rate of duty is the rate of excise duty which would be leviable on the class/description of articles to</i></p>

	<i>which the imported article belongs, and where such duty is leviable at different rates, the highest of such rates of duty.</i>
CVD under section 3(3) of the Customs Tariff Act, 1975	<ul style="list-style-type: none"> ◆ Duty levied on any imported article ◆ equal to additional duty¹ representing such portion of the excise duty leviable on such raw materials, components and ingredients <p><i>¹as determined by rules made by the Central Government in this behalf</i></p>
Special CVD under section 3(5) of the Customs Tariff Act, 1975	<ul style="list-style-type: none"> ◆ Duty levied on any imported article ◆ to counter-balance the sales tax, VAT, local tax or any other charges for the time being in force leviable on a like article on its sale, purchase or transportation in India** ◆ at the rate as notified by the Central Government, but not exceeding 4%. <p><i>**If a like article is not so sold, purchased or transported, rate of duty is the rate at which such taxes/ charges would be leviable on the class or description of articles to which the imported article belongs, and where such taxes/ charges are leviable at different rates, the highest of such tax/ such charge.</i></p>
Education cess (EC)	<ul style="list-style-type: none"> ◆ Duty levied on imported goods ◆ at the rate of 2% on aggregate of customs duties leviable on such goods.
Secondary and Higher Education cess (SHEC)	<ul style="list-style-type: none"> ◆ Duty levied on imported goods ◆ at the rate of 1% on aggregate of customs duties leviable on such goods.
Protective duties	<ul style="list-style-type: none"> ◆ Duty imposed on imported goods ◆ for the protection of the interests of any industry established in India ◆ on the recommendation of Tariff Commission.
Safeguard duty	<ul style="list-style-type: none"> ◆ Duty levied if the Central Government is satisfied that: <ul style="list-style-type: none"> (a) any article is imported into India in increased quantities; and (b) such increased importation is causing or threatening to cause serious injury to domestic industry. ◆ Education cess and secondary and higher education cess is not payable on it. ◆ It shall be in force for a period of 4 years from the date of its imposition extendable further by 6 years. ◆ It shall not apply to articles imported by a 100% EOU undertaking or a unit in a FTZ or in a SEZ unless specifically

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	made applicable.
	In case the goods are imported in increased quantities from People's Republic of China, a specific safeguard duty is imposed
Countervailing duty on subsidized articles	<ul style="list-style-type: none"> ◆ It is imposed if:- <ul style="list-style-type: none"> (a) any country or territory, directly or indirectly, pays or bestows subsidy upon the manufacture or production or exportation of any article. Such subsidy includes subsidy on transportation of such article. (b) such articles are imported into India. (c) the importation may/may not directly be from the country of manufacture/production and (d) the article, may be in the same condition as when exported from the country of manufacture or production or may be changed in condition by manufacture, production or otherwise. ◆ It shall be in force for a period of 5 years from the date of its imposition extendable further by 5 years.
Anti-dumping duty	<ul style="list-style-type: none"> ◆ Where any article is exported by an exporter to India at less than its normal value, then, upon the importation of such article into India, the Central Government may impose an anti-dumping duty not exceeding the margin of dumping in relation to such article. Margin of dumping = Normal Value-Export Price ◆ It shall be in force for a period of 5 years from the date of its imposition extendable further by 5 years. ◆ It shall not be leviable on articles imported by a 100% EOU unless specifically made applicable

Steps for computation of basic customs duty, CVD, special CVD & education cesses:

S.No.	Particulars	₹
(1)	Assessable value for computing basic customs duty [Transaction value under section 14(1)/Tariff value under section 14(2)]	xxxxx
(2)	Add: Basic custom duty [(1) × Rate of BCD]	xxxxx
(3)	Total value for computing additional customs duty u/s 3(1) [(1)+(2)]	xxxxx
(4)	Additional custom duty u/s 3(1) [(3) × Rate of CVD]	xxxxx
(5)	Total duty amount for education cess of customs [(2)+(4)]	xxxxx
(6)	Education cess @ 2% of (5)	xx

(7)	Secondary and higher education cess @ 1% of (5)	—xx
(8)	Total duty payable before additional customs duty u/s 3(5) [(5)+(6)+(7)]	xxxx
(9)	Total value for computing additional customs duty u/s 3(5) [(1)+(8)]	xxxx
(10)	Additional customs duty u/s 3(5) [(9) × Rate of special CVD]	xxxx
(11)	Total duty payable [(8)+(10)]	xxxx

Question 1

Distinguish between Indian territorial waters and Exclusive Economic Zone of India with regard to applicability of the Customs Act, 1962.

Answer

Indian territorial waters extend upto 12 nautical miles inside the sea from normal base line. Sovereignty of India extends upto territorial waters. Hence, all provisions of the Customs Act, 1962 are applicable to area covered under territorial waters.

Area beyond 12 nautical miles and upto 200 nautical miles from normal base line is covered under Exclusive Economic Zone of India. In this area, India has exclusive economic rights. Hence, provisions of customs law do not apply in this area unless any of such provisions has been specifically so made applicable.

Question 2

Answer the following questions:-

- (i) *ABC Manufacturers Ltd. imported some goods from Japan through a vessel. After the ship entered Indian port, the goods were unloaded and were lying with the custodian. The said goods were pilfered before the proper officer made an order for clearance for home consumption. Is ABC Manufacturers Ltd. liable to pay duty on such goods? Further, what would be the customs duty implication if such goods are restored to ABC Manufactures Ltd.*
- (ii) *Amino Industries imported certain goods from Norway. The said goods were warehoused in a public warehouse for a period of 3 months after which it is cleared for home consumption on payment of applicable customs duty. While transporting the goods from customs warehouse to the factory of the importer, the said goods were damaged. Can duty paid on such goods be remitted to Amino Industries?*

Answer

- (i) No, ABC Manufacturers Ltd. is not liable to pay duty in the given case. If any goods are pilfered after the unloading thereof but before the proper officer has made an order for clearance for home consumption, the importer shall not be liable to pay duty on such goods.

However, where such goods are restored to the importer after the pilferage, the importer becomes liable to pay duty. Thus, ABC Manufacturers Ltd. will be liable to pay duty if goods are restored to it.

1.32 Indirect Taxes

- (ii) No, duty paid on the goods, in the instant case, cannot be remitted as the goods have been damaged after their clearance for home consumption from the warehouse. The duty on the imported goods can be remitted only when such goods are destroyed at any time before clearance for home consumption.

Question 3

Suhana Ltd. importes certain goods from Germany. Since the goods have been imported from outside India and are not manufactured in India, excise duty is not leviable on such goods. However, excise duty is charged indirectly by the Government on such imported goods. Do you agree?

Answer

Though excise duty cannot be charged on imported goods, an additional duty of customs also known as countervailing duty (CVD) which is equal to excise duty on similar goods manufactured in India is payable on the imported goods. CVD is payable on assessable value plus basic customs duty. Thus, indirectly, excise duty is levied on imported goods.

Question 4

An importer imports a carton of goods containing 10,000 pieces with assesable value of ₹ 1,00,000 under section 14 of the Customs Act, 1962. On said product, rate of basic customs duty is 10% and rate of excise duty is 12% ad valorem. Similar product in India is assessable under section 4A of the Central Excise Act, 1944, after allowing an abatement of 30%. MRP printed on the package at the time of import is ₹ 25 per piece. Calculate the countervailing duty (CVD) under section 3(1) of the Customs Tariff Act, 1975 payable on the imported goods.

Answer

If imported goods are similar to goods covered under section 4A of the Central Excise Act, 1944, CVD is payable on basis of MRP printed on the packing less abatement as permissible.

Particulars	Amount (₹)
Maximum retail price [10,000 pieces × 25]	2,50,000
Less: Abatement @ 30%	<u>75,000</u>
Assessable value	<u>1,75,000</u>
CVD @ 12% of ₹ 1,75,000 [Education cesses on CVD are exempted]	21,000

Question 5

Sofa Enterprises imported some goods from USA for being used in manufacture of its final product. Determine the exchange rate to be considered for computation of import duty from the following information:-

<i>Date</i>	<i>Particulars</i>	<i>Rate of exchange notified by CBEC</i>
21.10.13	Import general manifest was submitted by master of vessel	1 US Dollar = ₹ 64.20
25.10.13	Entry Inwards was granted by the customs officer	1 US Dollar = ₹ 64.30
27.10.13	Sofo Enterprises filed the Bill of Entry	1 US Dollar = ₹ 64.50
31.10.13	Goods were allowed to be cleared from the customs port	1 US Dollar = ₹ 64.60.

Answer

The relevant rate of exchange for the purpose of valuation of imported goods is the rate of exchange as in force on the date on which a bill of entry in relation to imported goods is presented, i.e. 1 US Dollar = ₹ 64.50.

Question 6

Genuine Industries exported some goods to UK in a vessel. You are required to determine the rate of exchange for the purposes of computation of export duty from the following additional information:

<i>Particulars</i>	<i>Date</i>	<i>Exchange rate notified by CBEC</i>	<i>Exchange rate notified by RBI</i>
<i>Date of presentation of shipping bill</i>	18.02.2014	₹ 89 per UK pound	₹ 90 per UK pound
<i>Date of entry outwards</i>	20.02.2014	₹ 85 per UK pound	₹ 87 per UK pound

Answer

The exchange rate in the given case will be the rate of exchange notified by CBEC on the date of presentation of shipping bill, i.e. 18.02.2014. Hence, the rate of exchange for the purposes of computation of export duty will be ₹ 89 per UK pound.

Question 7

Nanak Enterprises imported machinery from USA in an aircraft. The bill of entry was presented on 05.02.2014 and the aircraft arrived in India on 15.02.2014. The rate of import duty on the respective dates was as follows:-

<i>Particulars</i>	<i>Date</i>	<i>Rate of customs duty</i>
<i>Date of bill of entry</i>	05.02.2014	10%
<i>Date of arrival of aircraft</i>	15.02.2014	11%

Determine the rate of import duty applicable in the given case.

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Answer

In case the goods have been imported in an aircraft, the rate of duty shall be the rate in force on:-

(i) the date on which Bill of Entry in respect of such clearance is presented
or

(ii) the date on which Entry Inwards is granted/ arrival of aircraft takes place

whichever is later.

Therefore, the relevant date for determination of the rate of import duty, in the given case, is 15.02.2014.

Question 8

A German manufacturer is exporting magnets to India. He is selling the magnets in Germany @ ₹ 100 per piece, but exports same magnets to India @ ₹ 50 per piece. Due to availability of cheap imported magnets, Indian manufacturers of the magnets are suffering. What action can be taken by the Government in this regard?

Answer

Government can impose anti dumping duty on such imported magnets to protect the domestic producers. The anti-dumping duty is equal to difference between normal value (i.e. his sale price in his country) and export price (price at which he is exporting the goods).

Question 9

An importer has imported a machinery to be used for providing the service of construction of commercial buildings. The assessable value of imported machinery as approved by customs is ₹ 1,00,000. Customs duty payable is 10%. If the machinery is manufactured in India, excise duty @ 12% is leviable on such machinery. Education cess and secondary and higher education cess are as applicable. Special CVD is payable on said machinery. You are required to:-

(i) calculate the total customs duty payable.

(ii) examine whether the importer can avail any CENVAT credit? If yes, how much?

Answer

Computation of customs duty payable

Particulars	Duty %	Amount (₹)	Amount of Duty (₹)
Assessable value		1,00,000	
Basic customs duty	10	10,000.00	10,000.00
Sub-Total for calculating CVD		1,10,000.00	
CVD x excise duty rate	12	13,200.00	13,200.00
Sub-total for education cess on customs		23,200.00	

(₹ 10,000 + ₹ 13,200)			
Education cess of customs	2	464.00	464.00
Secondary and Higher Education cess of customs	1	232.00	232.00
Sub-total for Special CVD (₹ 1,00,000 + ₹ 10,000 ₹ 13,200 + ₹ 464 + ₹ 232)		1,23,896.00	
Special CVD u/s 3(5)	4	4,955.84	<u>4,955.84</u>
Total customs duty			<u>28,851.84</u>
Customs duty payable (rounded off)			28,852

Since importer is a service provider, he can avail CENVAT credit of only CVD i.e. only of ₹ 13,200 and not of special CVD.

Note: The provisions relating to CENVAT credit have been discussed under Chapter-7: CENVAT credit.

Question 10

Sumar Export House exported some goods to Switzerland. Compute the export duty payable by it from the following information available:

- (i) Assessable value ₹ 55,00,000.
- (ii) Shipping bill presented electronically on 26.02.2014.
- (iii) Proper officer passed order permitting clearance and loading of goods for export on 04.03.2014.
- (iv) Rate of export duty are as under:

	Rate of export duty
On 26.02.2014	10%
On 04.03.2014	8%

Answer

Computation of export duty

Particulars	Amount (₹)
Assessable value of the export goods	55,00,000
Export duty @ 8% [Refer Note below]	4,40,000

Note: In case of goods entered for export, the rate of duty shall be the rate in force on the date on which the proper officer makes an order permitting clearance and loading of the goods for exportation.

Exercise

1. *With reference to the Customs Act, 1962, discuss the following:-*
 - (a) *Special exemption*
 - (b) *General exemption*
2. *Distinguish between clearance of imported goods for home consumption and clearance of imported goods for warehousing.*
3. *Write short note on the following with reference to the Customs Act, 1962:-*
 - (a) *Remission of customs duty on imported goods damaged or destroyed*
 - (b) *Customs duty on pilfered goods*
4. *Distinguish between:-*
 - (a) *Jetsam and flotsam*
 - (b) *Pilferage of goods under section 13 and loss or destruction of goods under section 23(1) of the Customs Act, 1962.*
5. *Define the following terms with reference to the Customs Act, 1962:*
 - (a) *Goods*
 - (b) *Export*
 - (c) *Export goods*
 - (d) *Exporter*
6. *Briefly discuss whether the customs duty is liable to be paid on derelict, jetsam, flotsam and wreck brought or coming into India.*
7. *Enumerate the circumstances in which abatement of duty on damaged or deteriorated goods is available.*
8. *List the different types of customs duties.*
9. *How is the customs duty determined where imported goods consist of articles liable to different rates of duty?*
10. *Differentiate between protective duty and safeguard duty.*
11. *Write a brief note on education cess on customs duty.*
12. *Briefly discuss the date for determining the rate of duty and tariff valuation of export goods.*

UNIT – 4 : CENTRAL SALES TAX

For the sake of brevity, Central Sales Tax has been referred to as CST and the Central Sales Tax Act, 1956 has been referred to as CST Act.

KEY POINTS	
Meaning of inter-State sales and intra-State sales	<p>Sales made within a State are <u>intra-State sales</u> and are liable to sales tax within the State.</p> <p>Sales made from one State to another are <u>inter-State sales</u> and are liable to Central Sales Tax (CST).</p>
Constitutional provisions	<p>Central sales tax levied by drawing power from <u>Entry 92A</u> of the Union List [<i>Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-State trade or commerce</i>]</p>
Sources of central sales tax law	<p>Central Sales Tax Act, 1956, Annual Union Finance Acts, Rules, Notifications, Circulars/ Instructions, Trade Notices/Clarifications and Case Laws.</p>
Objects of the CST Act	<p>The objects of the Central Sales Tax Act include:</p> <ul style="list-style-type: none"> (i) formulation of principles for determining as to:- <ul style="list-style-type: none"> (a) when a sale or purchase of goods takes place in the course of inter-State trade or commerce, or (b) when a sale or purchase takes place outside a State, or (c) when a sale or purchase takes place in the course of import into or export from India (ii) provision for the levy, collection and distribution of taxes on sales of goods in the course of inter-State trade or commerce (iii) declaration of certain goods to be of special importance in inter-State trade or commerce (iv) State laws to be subjected to the restrictions and conditions in the matter of imposing taxes on the sale or purchase of goods declared by the Central Government to be of special importance.
Levy and collection of CST	<ul style="list-style-type: none"> ◆ CST <u>extends to whole of India</u>. ◆ It is <u>levied by the Government</u> of India. ◆ CST so levied is <u>collected by that State Government</u> from which the movement of the goods is commenced.

Charge of CST	<ul style="list-style-type: none"> ◆ Every dealer ◆ shall be liable to pay tax under CST Act ◆ <u>on sales of all goods, other than electrical energy,</u> ◆ effected by him in the course of inter-State trade or commerce ◆ during any year.
IMPORTANT TERMS	
Meaning of Goods	<ul style="list-style-type: none"> ◆ <u>include</u> all materials, articles, commodities and all other kinds of movable property, but ◆ <u>does not include</u> newspapers, actionable claims, stocks, shares and securities.
Meaning of Sale	<p><u>Conventional definition</u></p> <p>Sale <u>means</u> any transfer of property in goods by one person to another for cash or deferred payment or for any other valuable consideration but <u>does not include</u> a mortgage or hypothecation of or a charge or pledge on goods</p> <p><u>Deemed sales</u></p> <p>Sale includes:</p> <ul style="list-style-type: none"> (i) a transfer, otherwise than in pursuance of a contract, of property in any goods; (ii) transfer of property in goods involved in works contract; (iii) a delivery of goods on hire-purchase/any system of payment by instalments; (iv) a transfer of the right to use any goods; (v) a supply of goods by any unincorporated association or body of persons to a member; (vi) a supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating).
Meaning of Dealer	<ul style="list-style-type: none"> ◆ <u>means</u> any person who carries on the business of buying, selling, supplying or distributing goods, directly or indirectly, for cash, or for deferred payment, or for commission, remuneration or other valuable consideration, and ◆ <u>includes:-</u> <ul style="list-style-type: none"> ▪ a local authority, a body corporate, a company, any

	<p>cooperative society or other society, club, firm, Hindu undivided family or other association of persons which carries on such business</p> <ul style="list-style-type: none"> ▪ a factor, broker, commission agent, del credere agent, or any other mercantile agent, and ▪ an auctioneer.
	<p>A mercantile agent, agent handling goods/documents of title to goods or an agent for collection of payment, acting on behalf of a dealer residing outside the State, is also a dealer.</p>
	<p>Government is also a dealer except in case of sale of old and discarded stores or waste.</p>
Meaning of Sales tax law	<p>Sales tax law <u>means</u> any law for the time being in force in any State or part thereof, which provides for the levy of taxes on the sale or purchase of goods generally or <i>on any specified goods expressly mentioned in that behalf</i> and</p> <p><u>includes</u> Value Added Tax (VAT) law, and</p> <p>“general sales tax law” <u>means</u> the law for the time being in force in any State or part thereof which provides for the levy of tax on the sale or purchase of goods generally and <u>includes</u> VAT law.</p>
EXCEPTIONS TO LEVY OF CENTRAL SALES TAX (CST)	
No CST on penultimate sales for export	<p>A dealer shall not be liable to pay CST on the penultimate sales for export.</p>
No CST on subsequent sales	<p>Conditions to be satisfied for exemption to subsequent inter-State sale of the goods are as follows:</p> <p>(i) First sale should be an inter-State sale and <u>subsequent sale should be effected by transfer of documents of title to the goods during the movement of such goods in course of inter-State sales.</u></p> <p><i>Note: Exemption to subsequent sales is available even if the first inter-State sale is exempt from CST.</i></p> <p>(ii) Subsequent inter-State sale is exempt only if:-</p> <ul style="list-style-type: none"> (a) <u>purchaser is a registered dealer.</u> (b) <u>the goods are of description referred to in section 8(3) (subsequently discussed).</u>

	<p>(iii) The dealer effecting the subsequent sale needs to furnish following certificates/declaration:-</p> <p>(a) <u>Form E-I/Form E-II</u>: obtained from the registered dealer from whom he has purchased the goods, and</p> <p>(b) <u>Form C</u>: obtained from buying dealer if the subsequent sale is made to a registered dealer*.</p> <p>*However, it shall not be necessary to furnish Form C in respect of a subsequent sale of goods if:</p> <p>(a) the sale or purchase of such goods is, exempt from tax generally or is subject to tax lower than 2%, under the sales tax law of the appropriate State <u>and</u></p> <p>(b) the dealer effecting such subsequent sale proves to the satisfaction of the prescribed authority that such sale is of the nature referred herein.</p> <p>CST is leviable if any of the three conditions mentioned above are not fulfilled. Levy and collection of CST, in such cases, would be in the following States:-</p> <p>(a) Where such subsequent sale has been effected by a registered dealer: State in which he is registered.</p> <p>(b) Where such subsequent sale has been effected by an unregistered dealer: State from which such subsequent sale has been effected.</p>
<p>No CST on sale to foreign missions/UN etc</p>	<p>No CST is payable on inter-State sale of any goods to any official or personnel/consular/diplomatic agent of:-</p> <p>(i) any foreign diplomatic mission or consulate in India or</p> <p>(ii) the United Nations or any other similar international body.</p> <p>Conditions:</p> <p>(i) Such buyer has purchased such goods for himself or for the purposes of such mission, consulate, United Nations or other body.</p> <p>(ii) The dealer selling such goods furnishes to the prescribed authority Form J obtained from such buyer.</p>
<p>INTER-STATE SALE [SECTION 3]</p>	
<p>Where sale occasions movement of goods from one State to another</p>	<p>◆ Inter-State sale takes place if <u>sale occasions the movement of goods from one State to another.</u></p> <p>◆ Where the movement of goods commences and terminates in the same State, it shall not be deemed to be a movement of goods from one State to another.</p>

Where sale is effected by transfer of documents of title to goods during their movement from one State to another	<ul style="list-style-type: none"> ◆ Inter-State sale takes place if the sale or purchase is effected by a transfer of documents of title to the goods <i>during their movement from one State to another.</i> ◆ Where goods are delivered to a carrier or other bailee for transmission, the movement of the goods shall be deemed to commence at the time of such delivery and terminate at the time when delivery is taken from such carrier or bailee.
INTER-STATE STOCK TRANSFER/INTER-STATE CONSIGNMENT TRANSFER	
Not liable to CST	Where the goods are sent by a dealer, outside the State to his other place of business or his agent/principal in other State, such transfer is not liable to CST.
Conditions to be fulfilled	<ul style="list-style-type: none"> (i) There was no pre-existing agreement with the branch for the sale of the goods so transferred. (ii) Dealer must obtain Form H from its branch office and furnish it to the assessing authority.
SALE OUTSIDE THE STATE	
Sale outside a State	When a sale/purchase of goods is determined to take place inside a State, such sale/purchase shall be deemed to have taken place outside all other States.
Sale inside a State	<p>A sale or purchase of goods shall be deemed to take place inside a State if the goods are within the State-</p> <ul style="list-style-type: none"> (a) in the case of <u>specific or ascertained goods</u>, at the time the contract of sale is made; and (b) in the case of <u>unascertained or future goods</u>, at the time of their appropriation to the contract of sale by the seller or by the buyer, whether assent of the other party is prior or subsequent to such appropriation. <p>Where there is a single contract of sale or purchase of goods situated at more places than one, it shall be deemed that there are separate contracts in respect of the goods at each of such place.</p>
SALE IN COURSE OF IMPORT/EXPORT	
No CST	CST is not leviable on sale in course of export/import.
Sale in the course of export	<p>Following sales shall be deemed to be sale in the course of export:-</p> <ul style="list-style-type: none"> (i) Sale or purchase occasions export involving transshipment of goods from one country to the other and shall be between

	<p>two parties of two countries.</p> <p>(ii) Sale or purchase effected by transfer of documents of title to goods <u>after the goods have crossed customs frontiers of India.</u></p> <p>(iii) Penultimate sales, i.e. the sale preceding the sale occasioning the export.</p> <p>A sale is considered as penultimate sale if:</p> <p>(i) There is a pre-existing agreement or order in relation to export.</p> <p>(ii) Penultimate sale must be, after the agreement with the foreign buyer, for the purpose of complying with such agreement or order in relation to export.</p> <p>(iii) Same goods which are sold in penultimate sale must be exported, though may not be in the same form.</p> <p>Selling dealer needs to furnish Form H obtained from the exporter to whom the goods are sold.</p> <p>If any designated Indian carrier purchases Aviation Turbine Fuel for the purposes of its international flight, such purchase shall be deemed to take place in the course of the export.</p>
Sale in course of import	<p>Following sales shall be deemed to be sale in the course of import:-</p> <p>(i) Sale or purchase occasioning import of goods into India.</p> <p>(ii) Sale or purchase effected by a transfer of documents of title to goods <u>before the goods have crossed customs frontiers of India.</u></p>
Meaning of customs frontier of India	<p>Customs frontier means crossing the limits of the area of a customs station in which imported goods/export goods are ordinarily kept before clearance by customs authorities.</p>
RATES OF TAX ON SALES IN THE COURSE OF INTER-STATE TRADE OR COMMERCE	
Concessional rate of CST	<p>The concessional rate of CST is:-</p> <p>(i) 2% of the turnover of the dealer</p> <p style="text-align: center;">or</p> <p>(ii) Rate applicable to the sale or purchase of such goods inside the appropriate state under the sales tax law of that State whichever is <u>lower.</u></p>
Conditions to	<p>A dealer is liable to pay CST at the concessional rate of CST</p>

be fulfilled for concessional rate of CST	<p>provided the following conditions are satisfied:-</p> <ul style="list-style-type: none"> (i) Sale is of goods eligible for concessional rate of CST**, i.e. the goods described in section 8(3). (ii) Sale has been made to a registered dealer. (iii) Selling dealer has obtained a declaration in Form C from the purchasing dealer and furnish it to the prescribed authority. <p>** Following goods as specified in the certificate of registration of the registered purchasing dealer, are eligible for concessional rate of CST:-</p> <ul style="list-style-type: none"> (a) goods of the class/classes intended for resale by him, for use by him in manufacture or processing of goods for sale, for use in the telecommunications network, for use in mining, or for use in the generation or distribution of electricity or any other form of power. (b) containers or other materials intended for being used for the packing of goods for sale. <p>Further, containers or other materials used for the packing of any goods referred to in clause (a) or (b) above are also so eligible [Section 8(3)]</p>
Cases where concessional rate of CST is not applicable	In case any of the three conditions are not fulfilled (as specified above), the rate of CST would be the rate applicable to the sale or purchase of such goods inside the appropriate State under the sales tax law of that State.
DETERMINATION OF TURNOVER FOR CENTRAL SALES TAX	
Meaning of turnover	Turnover means the aggregate of the sale prices received and receivable by him in respect of sales of any goods in the course of inter-State trade or commerce made during any prescribed period and determined in accordance with the provisions of this Act and the rules made thereunder.
Deductions to be made from the aggregate of the sale prices while computing the turnover	<ul style="list-style-type: none"> (i) Central sales tax payable $\text{Turnover} = \text{Aggregate of sales price} \times \frac{100}{100 + \text{Rate of tax}}$ <ul style="list-style-type: none"> (ii) Sale price of all goods returned to the dealer by the purchasers of such goods within a period of 6 months from the date of delivery of the goods. <p>The period of six months for return of goods is not applicable in respect of rejected goods as it is a case of unfructified sale.</p>

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	(iii) Such other deductions as the Central Government may, having regard to the prevalent market conditions, facility of trade and interests of consumers, prescribe.
Meaning of sale price	Sale price means the amount payable to a dealer as consideration for the sale of any goods subject to following inclusions and exclusions:-
	Inclusions Any sum charged for anything done by the dealer in respect of the goods at the time of or before the delivery thereof
	Exclusions Cash discount Cost of freight/ delivery or cost of installation where such cost is separately charged by the dealer.
Other Inclusions and Deductions from sale price	
Dharmada	includible because so far as the purchaser is concerned, he has to pay the whole amount for purchasing the goods.
Weighment dues	includible if the services of weighing are in respect of the goods and incidental to their being sold.
Insurance charges	includible if incurred by the assessee prior to the delivery of the goods.
Packing charges	packing charges and cost of packing material are includible.
Indemnity/ Guarantee charges	excluded as it is recovered from the same buyers to incur loss during transit at buyers' request.
Excise duty	includible
Government subsidies	excluded
Incentive paid to supplier	includible, these are not post sales expenses.
Design Charges	includible if charged separately in respect of goods manufactured as per design and sold to buyer
Deposits for returnable containers	excluded
Free of cost material supplied by customer	excluded

Sale price in case of works contract: Sale price of goods involved in execution of works contract shall be determined in the prescribed manner (no rules so far notified) by making such deductions from the total consideration for the works contract as may be prescribed and such price shall be deemed to be the sale price.	
Collection of tax to be only by registered dealers	No person who is not a registered dealer shall collect in respect of any sale by him of goods in the course of inter-State trade or commerce any amount by way of tax under this Act.
CST payable to be rounded off	The amount of CST, interest, penalty, fine or any other sum payable, and the amount of refund due, under CST Act shall be rounded off to the nearest rupee while crediting the same to the Government.
EXEMPTION FROM CST	
Exemption by notification granted by the State Government	State Government can grant exemption if following conditions are satisfied:- (a) State Government is satisfied that such exemption is necessary in the public interest. (b) Sale is made to a registered dealer. (c) The selling dealer has furnished Form C as obtained from the registered purchasing dealer.
Exemption from CST to a sale to unit/developer in SEZ	A registered dealer in SEZ (unit in SEZ/developer of SEZ) can obtain goods from outside SEZ, for specified purposes, without payment of CST provided:- ♦ Form I has been furnished by the purchasing dealer, and ♦ goods are of such class as specified in registration certificate of the registered dealer
GOODS OF SPECIAL IMPORTANCE/DECLARED GOODS	
Declared goods/Goods of special importance	♦ “Declared goods” means goods declared to be of special importance in inter-State trade or commerce. ♦ An illustrative list of goods of special importance: (i) Cereals (ii) Coal, including coke in all its forms, but excluding charcoal (iii) Cotton, (indigenous or imported) in its unmanufactured state, whether ginned or unginned, baled, pressed or otherwise, but not including cotton waste (iv) Cotton fabrics

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	(v) Cotton yarn, but not including cotton yarn waste.
Restrictions imposed on the tax imposed on the declared goods	<ul style="list-style-type: none"> ◆ The tax payable under the sales tax law of a State in respect of any sale or purchase of such goods inside that State shall not exceed 5% of the sale or purchase price. ◆ If a tax is levied on sales or purchase of any declared goods inside a State and the same commodity is subsequently sold in the course of inter-State trade or commerce and is subjected to CST, the sales tax paid within the State realised previously in respect of the commodity is reimbursed provided:- <ul style="list-style-type: none"> (a) the tax on the inter-State sale has been actually paid, and (b) the inter-State sale of goods is in the same form.

Question 1

State distinctions and similarities between the central excise duty and central sales tax.

Answer

Central Sales Tax	Central Excise Duty
Distinctions	
Levied under Entry 92A of List I of Seventh Schedule to Constitution of India.	Levied under Entries 84 of List I of Seventh Schedule to Constitution of India.
The levy is on sale of goods.	Levy is on of manufacture or production of goods.
Revenue is collected and retained by State Government.	Revenue is collected and retained by the Central Government.
Tax is payable only when goods move from one State to another.	Duty is payable when manufactured goods are removed from the factory.

Question 2

Briefly examine the validity of the following statements with reference to the CST Act:-

- (i) *Since goods include all materials, articles and all other kinds of movable property, newspapers would also be considered as goods.*
- (ii) *'Place of business' includes place of business of the agent.*
- (iii) *Profit motive is essential to call an activity a "business".*
- (iv) *CST is leviable on transactions of leasing / hiring of assets for a defined period.*

Answer

- (i) **No, the statement is not valid.** Although as per the definition of goods, goods include all materials, articles and all other kinds of movable property, newspapers have been specifically excluded from the said definition. Hence, newspapers cannot be considered as goods.
- (ii) **Yes, the statement is valid.** The definition of place of business specifically includes the place of business of an agent where a dealer carries on business through such agent.
- (iii) **No, the statement is not valid.** Profit motive is not essential to call an activity a 'business' under the CST Act. The definition of "business" clearly specifies that for an activity to be called "business", profits motive is not necessary.
- (iv) **Yes, the statement is valid.** CST is leviable on transactions of leasing / hiring of assets for a defined period. As per the definition of sale, transaction of leasing and hiring of assets for a defined period is deemed to be a sale.

Question 3

X of Kolkata sells goods to Y of Chennai and hands over the goods to MKS Transport, Kolkata for transporting the same to Chennai. The lorry receipt is sent to Y by post. While goods are in transit, Y sells the goods to Z of Vijayawada by endorsing the lorry receipt and goods are diverted to Vijayawada. X, Y and Z are registered dealers. Is the second sale between Y and Z chargeable to tax?

Answer

The first sale by X to Y is chargeable to central sales tax. However, sale of goods by Y to Z is exempt as it is a subsequent sale by transfer of documents of title to the goods during their movement provided subsequent sale is made to a registered dealer (in the given case Z is a registered dealer), Form C is furnished by the buying dealer, Z to Y of Chennai and Y has collected Form E1 from X of Kolkata.

Question 4

Mr. 'A' of Chennai sent a consignment of goods to his branch at Bengaluru, without any prior contract of sale. When the goods were in transit, Mr. 'B' of Bengaluru bought the said goods from A's branch office. A's branch office endorsed the railway receipt in favour of Mr. 'B' who took the delivery of goods. Does this amount to sale?

Answer

Yes, in the instant case, the transaction is an inter-State sale by transfer of document of title to the goods under section 3(b) of the CST Act. If the documents of title to the goods are transferred after the goods are delivered to the carrier but before the delivery of goods is taken from it, the transaction is treated as a sale or purchase in the course of inter-State trade or commerce. Since in the given case, railway receipt is endorsed in favour of Mr. 'B' at the time when the goods were in transit and Mr. 'B' took the delivery of the goods; the transaction is an inter-State sale.

Question 5

Examine whether following amount to inter-State sales:-

- (i) *D of Delhi comes to Hyderabad, purchases certain chemicals from E and transports them in his own name to Delhi.*
- (ii) *X of Mumbai sends goods by air to his branch office at London. Subsequently, he transfers the documents of title of such goods to a buyer at Scotland after said goods have crossed the customs frontiers of India.*
- (iii) *A London based entrepreneur enters into a contract of sale of goods with Madhav of Gujarat and sends the goods to India.*

Answer

- (i) The sale is completed at Hyderabad itself. Therefore, the sale does not occasion the movement of goods from one State to another. Hence, sale of goods by E to D is not an inter-State sale.
- (ii) Since in the given case, sale is effected by transfer of documents of title to the goods after the goods have crossed the customs frontiers of India, it is not an inter-State sale, but a sale in the course of export.
- (iii) Since in this case, the sale has occasioned the import of the goods into the territory of India, it is not an inter-State sale, but a sale in the course of import.

Question 6

Examine whether CST is leviable on the following transactions:-

- (i) *Inter-State sale of the electrical energy.*
- (ii) *Samar is a dealer of textiles in Vapi. Madhav of Lucknow approached him and purchased goods worth ₹ 1,00,000. However, instead of taking the delivery of the goods in Vapi, he directed Samar to deliver said goods in his factory located at Surat.*

Answer

- (i) Although electrical energy is goods, CST is not leviable on it as the charging Section 6(1) specifically excludes it from the purview of levy of CST.
- (ii) CST is not leviable on the goods dispatched by Samar to Madhav's factory in Surat as there is no inter-State movement of goods. Goods have merely moved from one city of Gujarat to another.

Question 7

Discuss the validity of the following statements with reference to computation of turnover under CST Act:-

- (i) *Cost of freight, separately charged in the invoice, shall be deducted from sale price.*

- (ii) *Subsidy given by Government to manufacturers (selling the product at controlled price) to compensate cost of production will form part of sale price.*
- (iii) *Charity or dharmada collected by dealer will not form part of sale price.*
- (iv) *Free of cost material supplied by the customer will be added to the sale price.*

Answer

- (i) **The statement is valid.** The cost of freight is excluded from the sale price where such cost is separately charged by the dealer.
- (ii) **The statement is not valid.** Where a product is 'controlled' and has to be sold at 'controlled price', subsidies are granted by the Government to manufacturers to compensate the cost of production, which is usually higher than the 'controlled price'. Such subsidy will not form part of sale price.
- (iii) **The statement is not valid.** Charity / Dharmada collected will form part of sale price because so far as the purchaser is concerned, he has to pay the whole amount for purchasing the goods.
- (iv) **The statement is not valid.** Under CST Act, free of cost material supplied by buyer is not required to be added unlike Central Excise Law.

Question 8

Mr. Mohandas, a first stage dealer of a machine in the State of Maharashtra, furnishes the following data:

S.No.	Particulars	₹
(i)	Total inter-State sales during F.Y. 2013-14 (CST not shown separately)	93,87,000
(ii)	Above sales include:	
	Dharmada	9,00,000
	Freight	3,20,000
	(₹ 1,20,000 is not shown separately in invoices)	
	Cost of corrugated boxes specially designed for packing of the machinery	56,000
	Installation and commissioning charges shown separately	52,000
	Incentive on sales received from the manufacturer	23,000

Determine CST payable assuming that all transactions were covered by valid 'C' Forms and sales tax rate within the State is 5%.

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Answer

Computation of Mr. Mohandas's CST payable

Particulars	₹	₹
Total inter-state sales		93,87,000
Less: Freight shown separately in the invoices [Note-2]	2,00,000	
Less: Installation and commissioning charges shown separately [Note-3]	52,000	2,52,000
Turnover including CST		91,35,000
CST payable = $91,35,000 \times \frac{2}{102}$ (B) [Note-5]		1,79,118

Notes:

1. Dharmada and cost of packing material are includible while calculating turnover.
2. Freight charges of ₹ 1,20,000 are not deductible while calculating the turnover as they are not shown separately in invoices. Remaining amount of freight, shown separately in the invoices, is deductible.
3. Installation and commissioning charges are deductible while calculating the turnover since shown separately in the invoices.
4. Sale price includes incentive on sales received from the manufacturer.
5. The CST on transactions covered by valid 'C' Form is 2% or the sales tax rate within the State, whichever is lower. Since, in this case, the State sales-tax rate is higher than 2%, the rate of CST is taken as 2%.

Question 9

Solaris India Pvt. Ltd.'s total inter-State sales @ 4 % CST for the Financial Year 2013-14 is ₹ 1,50,00,000 (CST not shown separately). In this regard, following additional information is available:

- (i) Goods sold to Mr. A for ₹ 1,50,000, on 16.07.2013 were returned by him on 12.12.2013.
- (ii) A buyer, Mr. B, to whom goods worth ₹ 55,000 were dispatched on 16.04.2013, rejected such goods. The said goods were received back on 15.11.2013.
- (iii) Goods sold to Mr. C for ₹ 5,00,000, on 16.04.2013 were returned by him on 12.12.2013.

Determine the amount of taxable turnover and tax liability of Solaris India Pvt. Ltd.

Answer

Computation of taxable turnover and tax liability of Solaris India Pvt. Ltd.

Particulars	Amount (₹)
Total sales	1,50,00,000
Less: Goods returned by Mr. A (deductible as returned within 6 months)	1,50,000
Less: Goods returned by Mr. C (not deductible since returned after six months)	Nil
Less: Goods rejected by Mr. B after six months (Refer note below)	55,000
	1,47,95,000
Less : Central sales tax $= 1,47,95,000 \times \frac{4}{104}$ (Rounded off)	5,69,038
Turnover	1,42,25,962

Note: The period of six months for return of goods is not applicable in respect of rejected goods as it is a case of un-fructified sale.

Question 10

Mr. Y of Mumbai purchased declared goods (goods of special importance) from Nagpur by paying sales tax at @ 5%. Subsequently, the commodity is sold to a dealer at Chennai. The dealer Y while collecting and remitting tax on the Inter-state sale, wants refund of tax paid on sale within State (i.e. purchase from Nagpur). Is he correct?

Answer

If a tax has been levied on sale or purchase of any declared goods inside a State and the same goods are subsequently sold in the course of inter-state trade or commerce and is subjected to tax under the CST Act, sales tax paid has to be reimbursed to the dealer. However, sales tax paid within the state can be reimbursed only when the CST has been paid **subsequently** and not otherwise.

Hence, in this case, Mr. Y can claim refund of tax paid within the State after payment of central sales tax in respect of such declared goods.

Exercise

1. State the objects of the CST Act, 1956.
2. To what extent the Constitution (46th Amendment) Act, 1982 has widened the scope of making levy both in the case of Central Governments as well as State Governments.
3. Write short note on Appropriate State.

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4. *Write short note on business and place of business with reference to CST, 1956.*
5. *Write short note on:*
 - (i) *Crossing the customs frontier of India.*
 - (ii) *Prescribed period.*
6. *A branch outside the State cannot be considered as a place of business. Discuss the correctness of the said proposition.*
7. *Discuss the term 'dealer' under the CST Act, 1956.*
8. *Write short note on deemed dealer.*
9. *When can a Government be treated as a dealer?*
10. *Explain the term "declared goods". Furnish any eight items of such declared goods under the CST Act, 1956.*
11. *Explain the term "sale in course of export".*
12. *What is sale in course of import?*
13. *When does the liability to pay tax on Inter-State sales arise?*
14. *Is a subsequent inter-State sale of goods exempt from central sales tax?*

UNIT – 5 : VALUE ADDED TAX

KEY POINTS		
Value Added Tax (VAT)		<ul style="list-style-type: none"> • VAT is a tax on the value added to the commodity at each stage in production and distribution chain. • When tax is levied on tax i.e, tax leviable at each stage is chargeable on a value which includes the tax paid at earlier stage; it leads to cascading of taxes. • Under VAT, tax is not levied on tax paid at earlier stage; it is levied only on the value added as credit of tax paid at earlier stages is allowed to be set off against the tax payable at the next stage. Thus, VAT helps in eliminating cascading of taxes.
Variants of VAT	Gross Product Variant	Tax is levied on all sales and deduction for tax paid on inputs excluding capital goods is allowed.
	Income Variant	Tax is levied on all sales and deduction for tax paid on inputs and only depreciation on capital goods is allowed.
	Consumption Variant	Tax is levied on all sales and deduction for tax paid on all business inputs (including capital goods) is allowed. Consumption variant of VAT is the most widely used variant of the VAT.
Methods of computation of VAT	Addition Method	<ul style="list-style-type: none"> ❖ All factor payments (excluding value of materials) including profits aggregated to arrive at the total value addition on which tax rate is applied to calculate the tax. ❖ Mainly used with income variant of VAT.
	Invoice Method	<ul style="list-style-type: none"> ❖ Tax is imposed at each stage of sales on entire sale value and tax paid at the earlier stage (on purchases) is allowed as set-off. ❖ Also called as 'Tax Credit Method' or 'Voucher Method'. ❖ Most common and popular method for computing VAT liability. ❖ Mainly used with consumption variant of VAT.
	Subtraction	❖ Tax is charged only on value added at each stage

	Method	<p>of sale of goods i.e., difference between sales and purchases.</p> <ul style="list-style-type: none"> ❖ Applied where tax is not charged separately. ❖ Suitable for gross product variant of VAT.
Merits and Demerits of VAT	Merits	<ul style="list-style-type: none"> ➤ Reduced tax evasion ➤ Increased tax compliance ➤ Certainty ➤ Transparency ➤ Cheaper exports ➤ Better accounting systems ➤ Neutrality
	Demerits	<ul style="list-style-type: none"> ➤ Distortions in case of exemptions/ concessions ➤ Increased compliance cost ➤ Increased working capital requirements ➤ Consumption favoured over production ➤ Tax evasion through bogus invoices ➤ Regressive tax
VAT in Indian context	Central Level	<ul style="list-style-type: none"> ❖ CENVAT on manufacture of goods & services
	State Level VAT	<ul style="list-style-type: none"> ❖ State VAT on intra-State sale of goods (replacing erstwhile sales tax regime) ❖ White Paper on State-Level VAT in India provided the broad framework of State-Level VAT to be adopted in India.
	Proposed dual GST	<ul style="list-style-type: none"> ❖ GST would create a common domestic market, remove multiplicity of taxes, eliminate cascading effect of tax on tax, make prices of the Indian products competitive and, above all, benefit the end consumers. ❖ Dual model GST has been proposed in India so that both Central and State Governments can collect taxes on goods and services. ❖ GST will subsume most of the indirect taxes being levied in India including central sales tax (CST).
Constitutional provisions	<ul style="list-style-type: none"> ◆ Entry 54 of State List provides for 'Taxes on the sale or purchase of goods other than newspapers, subject to the provisions of entry 92A of Union List'. ◆ Clause (29A) of the Article 366 of the Constitution provides an inclusive definition of "tax on sale or purchase of goods" which lays down six specific instances of deemed sale i.e., cases which are not 	

	<p>sale in traditional sense but have been deemed to be sale for the purpose of leviability of CST/VAT.</p> <ul style="list-style-type: none"> ◆ Deemed sale encompass elements of both goods as well as services - goods portion is chargeable to CST/VAT and services portion to service tax. 	
	<p>Sale means-</p> <ul style="list-style-type: none"> ♣ any transfer of property in goods by one person to another for cash or deferred payment or for any other valuable consideration; and ♣ includes “deemed sales” transactions under Article 366(29A) of the Constitution of India; but ♣ does not include a mortgage or hypothecation of, or a charge or pledge on, goods. 	
	<p>Goods</p> <ul style="list-style-type: none"> ◆ Broadly the definition of goods adopted by various States is on the lines of definition of goods provided under CST Act. ◆ Goods may be tangible (like computer, pen, pencil etc.) as well as intangible (like patent, copyright). ◆ Goods include all kinds of movable property, but not newspapers, actionable claims, stocks, shares and securities. ◆ Plant and machinery erected at site, being immovable property, is not goods. ◆ Electricity is goods but lottery ticket, being actionable claim, is not goods. ◆ Software (branded as well as unbranded) is goods. 	
VAT rates	0%	❖ Natural and unprocessed products in unorganised sector - Items which are legally barred from taxation and items which have social implications
	1%	❖ Precious stones, bullion, gold and silver ornaments etc.
	5%	<ul style="list-style-type: none"> ❖ Items of basic necessities like medicines and drugs, all agricultural and industrial inputs, declared goods & capital goods. Originally White Paper had proposed 4% rate on such goods but many States have subsequently increased this rate to 5%. ❖ Rate of declared goods has also been increased to 5% by many States after amendment of CST Act w.e.f. 08.04.2011.
	12.5/13.	❖ All other goods not chargeable to any of the above

1.56 Indirect Taxes

	5%	rates. Originally White Paper had proposed 12.5% rate as the revenue neutral rate but most of the States have subsequently increased this rate to 13.5%.
Coverage of goods under VAT	❖	Generally, all the goods, including declared goods are covered under VAT (benefit of input tax credit allowed).
	❖	Liquor, lottery tickets, petrol, diesel, aviation turbine fuel and other motor spirit are not covered under VAT.
	❖	Though sale of liquor, petrol, diesel and aviation turbine fuel (ATF) is charged to tax under VAT laws in many States, taxes paid on them are not allowed as credit to the buyer. Thus, they are outside the VAT chain.
Input tax and Output tax	◆	Input tax is the tax paid or payable in the course of business on purchases of any goods (inputs, capital goods and other goods) from a registered dealer OF THE STATE.
	◆	Output tax is the tax charged or chargeable under the Act, by a registered dealer on the sale of goods in the course of business.
Input Tax Credit (ITC)		
Basic principles	◆	ITC in relation to any period means setting off the amount of input tax by a registered dealer against the amount of his output tax.
	◆	CST paid on purchases made from outside the State cannot be claimed as ITC but ITC can be used for paying CST arising on inter-State sale.
	◆	ITC can be availed by both manufacturers and traders in respect of input tax paid on purchase of inputs and capital goods within the State from a registered dealer for being sold within the State as well as in other States, irrespective of when these will be utilized/sold.
	◆	There is a negative list of capital goods (on the basis of principles already decided by the Empowered Committee) not eligible for input tax credit.
	◆	As per White Paper, input tax credit on capital goods can be adjusted over a maximum of 36 equal monthly installments.
Purchases eligible for ITC		Taxable goods should be purchased for any one of the following purposes- <ul style="list-style-type: none"> ➤ for intra-State or inter-State sale/resale; ➤ for being used in the manufacture of taxable goods or in the packing of such manufactured goods intended for intra-State or inter-State sale or exports ; ➤ for being used in the execution of a works contract;

	<ul style="list-style-type: none"> ➤ for being used as capital goods required for the purpose of manufacture or resale of taxable goods; ➤ for making zero-rated sales other than exports
Purchases not eligible for ITC	<p>ITC may not be allowed in respect of following purchases-</p> <ul style="list-style-type: none"> ➤ purchases from unregistered dealers; ➤ purchases from registered dealer who opts for composition scheme; ➤ invoice less purchases; ➤ purchase where invoice does not show amount of tax separately; ➤ purchases for being utilized in the manufacture of exempted goods or purchase of goods when sales are exempt; ➤ purchase of goods for personal use/consumption or to be provided free of charge as gifts, free samples; ➤ imports and inter-State purchases
Some special aspects	<ul style="list-style-type: none"> ◆ VAT does not require bill to bill co-relation between input and output. ◆ Proportionate ITC is available when inputs are used both for taxable and exempt output. Credit relating to exempt output has to be reversed. ◆ In case of stock transfer, input tax paid in excess of 2% is allowed as ITC. ◆ Whereas for zero rated sales ITC can be availed, it cannot be availed in respect of exempt sale. ◆ After utilizing ITC for payment of VAT and CST, excess credit, if any, can be carried forward. ◆ As per White Paper, if goods are exported, input tax paid is to be refunded within a period of 3 months from the end of the period in which export took place. ◆ As per White Paper, SEZ units and EOU are granted either exemption from payment of input tax or refund of input tax paid within three months. ◆ Special CVD paid on imported goods can be refunded if VAT is charged on further sale of such imported goods and VAT invoice mentions that buyer will not be able to avail CENVAT credit of such duty.

VAT Liability					
What is VAT liability?	<ul style="list-style-type: none"> ◆ VAT liability of the dealer is calculated by deducting input tax credit from output tax payable i.e., tax chargeable on sales during the payment period (say, a month). ◆ Net tax payable = Output tax – Input tax 				
Composition Scheme					
Scheme	<ul style="list-style-type: none"> ◆ White Paper provides a optional composition scheme for small registered dealers where tax is paid at a small percentage (composition rate) of the gross turnover. Composition rate can be reduced to as low as 0.25%. ◆ Input tax credit is not allowed under the scheme and dealer opting for the scheme is not authorized to issue VAT-able invoices. 				
Eligible and Non-eligible dealers	<p>Eligible dealer:</p> <ul style="list-style-type: none"> ❖ A registered dealer who is liable to pay VAT and whose turnover does not exceed ₹ 50 lakh in preceding financial year and whose purchases and sales are within the State, can opt for Composition Scheme. <p>Non-eligible dealer:</p> <ul style="list-style-type: none"> ❖ Dealer making inter-state purchases/sales; ❖ Dealer importing/exporting goods for sale in/outside India; ❖ Dealer stock transferring goods outside the State; ❖ Dealer desirous of issuing VAT-able invoice. 				
Exercising of option	<ul style="list-style-type: none"> ◆ On the day of exercising the option, dealer should not have any stock of goods which are brought from outside the State and not claim input tax credit on the inventory available on that day. ◆ He should also not use any goods brought from outside the State after such date. 				
Advantages and Disadvantages	<table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="text-align: left; width: 50%;">Advantages</th> <th style="text-align: left; width: 50%;">Disadvantages</th> </tr> </thead> <tbody> <tr> <td> <ul style="list-style-type: none"> ➤ Minimum records ➤ Simple tax calculation ➤ Simple return </td> <td> <ul style="list-style-type: none"> ➤ Non-availability of input tax credit ➤ VAT chain gets broken </td> </tr> </tbody> </table>	Advantages	Disadvantages	<ul style="list-style-type: none"> ➤ Minimum records ➤ Simple tax calculation ➤ Simple return 	<ul style="list-style-type: none"> ➤ Non-availability of input tax credit ➤ VAT chain gets broken
Advantages	Disadvantages				
<ul style="list-style-type: none"> ➤ Minimum records ➤ Simple tax calculation ➤ Simple return 	<ul style="list-style-type: none"> ➤ Non-availability of input tax credit ➤ VAT chain gets broken 				
VAT & Sales Tax Incentives					
	Any exemption from tax is against the principles of VAT as it breaks the VAT chain. State Governments, therefore, stopped giving incentives to new industries after January, 2000 and incentives already given to industries set up prior to January, 2000 were continued under VAT				

	<p>regime by converting them to deferral schemes so that such industries could pass on the benefit of VAT to their buyers.</p> <p>By and large sales tax incentives were given in three modes as described below:</p>
Exemption from tax	<ul style="list-style-type: none"> ❖ Neither tax charged nor tax collected by eligible industry. ❖ Input tax also not payable on purchases of raw materials. ❖ Exemption ceases either with the expiry of exemption period or the exemption amount, whichever occurs first.
Deferment of tax liability	<ul style="list-style-type: none"> ❖ Tax collected from buyers but payment thereof to the Government deferred. ❖ After expiry of prescribed period, liability to be paid in specified installments.
Remission of tax	<ul style="list-style-type: none"> ❖ Tax collected from buyers but payment thereof remitted. ❖ Input tax paid on purchases by the unit to be refunded.
VAT and Works Contract	
Basic principles	<ul style="list-style-type: none"> ◆ Works contract is a deemed sale (composite contract of goods and services) and is thus, liable to VAT. ◆ While VAT is leviable on goods involved in the execution of works contract, service tax is levied on value of services. ◆ Where labour and other service charges are quantifiable, taxable turnover would be contract price less labour and other service charges. ◆ Where labour and other service charges are not quantifiable- <ul style="list-style-type: none"> ▪ taxable turnover can be cost of goods plus cost of transfer/conversion and profit margin; or ▪ Standard rate of deduction provided in State VAT laws can be used for deducting labour and other like charges in the contract to arrive at the taxable turnover.
Tax rates	<ul style="list-style-type: none"> ◆ Schedule rate if value of each item of material transferred in the course of execution of a works contract is identifiable. Tax is charged on value of individual items of materials as provided under the schedules to the concerned State VAT legislation.

	<ul style="list-style-type: none"> ◆ Revenue neutral rate if values of individual goods are not identifiable. Contractor can pay tax at Revenue Neutral Rate (RNR - generally 12.5%/13.5%) after deducting the value attributable towards labour and other like charges.
Composition scheme	<ul style="list-style-type: none"> ◆ VAT legislations provide for an optional Composition Scheme to collect tax on works contracts in a simple manner so as to minimize the inconvenience caused to the assesseees. ◆ Tax is paid at a composite rate on the gross contract value. Tax rate is generally lower in such scheme. ◆ Input tax credit is not allowed under the scheme. However, in some States (e.g. Maharashtra) partial input tax credit is granted.
VAT and Lease Transactions	
Lease	<p>Under a lease, a party owning the asset (called the 'lessor') provides that asset for use over a certain period of time to another party (called the 'lessee') for consideration (called 'rentals'). Legal ownership of the asset remains with the lessor, but the lessee retains the possession and uses the asset over the period of the lease.</p> <ul style="list-style-type: none"> ◆ Lease is a deemed sale and is thus, liable to VAT. ◆ If complete possession and control is not handed over in respect of an asset given on rent, transaction is not a deemed sale (as it is not a transfer of right to use) but a service and is thus, liable to service tax. ◆ Sub-lease of an asset too can be taxed, unless the State Value Added Tax law has provided for the levy of tax only at one stage. ◆ Taxable event is transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration. ◆ Taxable turnover is the amount of valuable consideration paid or payable for any sale during the given period. Certain States provide deduction of interest or financial charges for determining taxable turnover. ◆ Input tax credit is allowed to lessor on purchase of the asset which is to be leased. Since these assets are generally capitalized in the books of lessor, provisions relating to input tax credit on capital goods apply in this case also. ◆ Maintenance of the leased asset involving supply of consumables by the lessor is not a works contract (as there is no transfer of property in such materials to the lessee) and is thus, not liable to

	<p>VAT. It is a service contract liable to service tax.</p> <ul style="list-style-type: none"> ▪ If parts are also supplied during maintenance, such contract becomes a works contract liable to VAT. ◆ Sale of a leased asset after the lease period is over is taxable in the same manner in which normal sale of such asset would have been taxed.
VAT and Hire Purchase	
Hire Purchase (HP)	<p>Whereas under HP, hirer acquires the goods immediately on signing the hire-purchase agreement but ownership or title of the same is transferred only when last installment is paid, under installment payment system, buyer gets ownership of the goods with the payment of first installment.</p>
	<ul style="list-style-type: none"> ◆ Since HP transactions are deemed sales, they are liable to VAT. ◆ Transactions which are purely of a financial nature between the financier and the hirer (hire-purchase finance) are not liable to VAT. ◆ Taxable event is the actual or physical delivery of goods on hire purchase or under any system of payment by installments. ◆ Some States provide for deduction of interest or finance charges included in the installment in arriving at the taxable turnover while some do not provide any such deduction. ◆ Provisions relating to input tax credit in case of a normal sale apply in case of HP also. However, some States provide for <i>pro rata</i> credit. ◆ Tax may not be payable when transaction fructifies into a concluded sale as tax has already been paid on installments. However, other view is that tax is payable again on fructified sale on depreciated value of the asset or on its market value but if no consideration is payable on fructified sale, then tax is not attracted. ◆ Goods returned are treated as normal sales return and thus refund of tax can be claimed as per the provisions of respective State VAT laws if goods are returned within the prescribed period. ◆ When transaction of hire purchase fails, vendor takes possession of the goods and normally installment received for the intervening period for forfeited.
VAT and Sale of Food Articles	
	<ul style="list-style-type: none"> ◆ Sale of food in a hotel is a deemed sale liable to VAT. Service portion involved in such a sale is declared to be a service liable to service tax.

Deficiencies in State-Level VAT	
	<ul style="list-style-type: none"> ❖ Non-uniformity in VAT rates across the country, ❖ Non-uniformity in provisions of VAT laws across the country, ❖ CST is non-Vatable, ❖ Double taxation - No clear distinction between goods and services which leads to double taxation i.e., both service tax and VAT are levied on the same transaction. ❖ Hurdles in movement of inter-state goods.

Question 1

Briefly answer the following questions:-

- (a) *Which is the most popular and common method for computing VAT liability and at what stage is the tax imposed under this method?*
- (b) *Can VAT be said to be non-beneficial as compared to single stage-last point system?*
- (c) *What are the items aggregated in the addition method to calculate the VAT payable? When is this method mainly used?*
- (d) *Does White Paper on VAT allow only a manufacturer to avail set off of input tax credit on capital goods and not a trader?*

Answer

- (a) Invoice method is the most common and popular method for computing the tax liability under the VAT system. Under this method, tax is imposed at each and every stage of sale on the entire sale value, and the tax paid at the earlier stage is allowed as set-off.
- (b) VAT system has many advantages like reduced tax evasion, transparency, certainty, reduction in cascading effect of taxes etc. which are not there in the single stage-last point system. However, since VAT is imposed or paid at various stages and not at last stage, it increases the working capital requirements and the interest burden on the same. To this extent, it may be considered to be non-beneficial as compared to the single stage-last point taxation system though to a large extent, this rigour is brought down through input tax credits on purchases.
- (c) Under addition method, all factor payments (excluding value of material) and profit are added to arrive at the value addition on which VAT rate is applied to compute the VAT payable. This method is mainly used with income variant of VAT.
- (d) No. As per the White Paper on VAT, set off of input tax credit on capital goods is available to both manufacturers and traders.

Question 2

Briefly explain whether following purchases are eligible for availing input tax credit:

- (a) *Rohan purchased goods from a registered dealer. He claims to have paid VAT on the said goods but the invoice pertaining to said purchase has been lost on account of negligence of a clerk in his office.*
- (b) *Jain & Co. purchased goods from Tide Enterprises. Tide Enterprises is an unregistered dealer.*
- (c) *Ankit purchased some capital goods. The final product manufactured by Ankit using these capital goods is exported.*
- (d) *Mohan purchased goods for being used in execution of a works contract.*
- (e) *Singla & Co. purchased goods from Malhotra Enterprises, a registered dealer. Malhotra Enterprises has opted for composition scheme under the provisions of respective State VAT Act.*
- (f) *Sahil purchased goods from Ganesh. Ganesh has not shown VAT charged on the purchase value, separately in the invoice.*

Answer

- (a) Input tax credit cannot be claimed on purchase made by Rohan as the purchase invoice is not available with him.
- (b) Purchases made by Jain & Co. from Tide Enterprises are not eligible for input tax credit as Tide Enterprises is not a registered dealer.
- (c) Capital goods used for manufacturing/packing goods to be sold in the course of export out of the territory of India are eligible for claiming input tax credit. Thus, Ankit can claim input tax credit on capital goods purchased by him.
- (d) Mohan can claim input tax credit as purchase of goods for being used in execution of a works contract are eligible for input tax credit.
- (e) Purchases made by Singla & Co. from Malhotra Enterprises are not eligible for input tax credit as purchases from registered dealer who opts for composition scheme under the provisions of respective State VAT Act are not eligible for input tax credit.
- (f) Purchases made by Sahil are not eligible for input tax credit as the invoice issued by Ganesh does not show VAT charged on the purchase value separately in the invoice.

Question 3

Mr. Goenka is a trader selling raw materials to manufacturers of finished products. He procures his stock in trade from other States as well as purchases the same from the local markets. Following transactions pertain to a sale made by Mr. Goenka to a manufacturer during financial year 2013-14:-

1.64 Indirect Taxes

S. No.	Particulars	₹
(1)	Cost of materials procured from other States excluding tax	1,00,000
(2)	Cost of local materials including VAT	2,25,000
(3)	Other expenditure including storage, transport, interest and loading and unloading and profit earned by him	87,500

Calculate the invoice value charged by Mr. Goenka to the manufacturer. Assume VAT rate to be 12.50% and central sales tax to be 2%.

Answer

Computation of invoice value

Particulars	₹
Cost of materials procured from other States	1,00,000
[Since input tax credit cannot be availed in respect of CST, it will be included in the cost of inputs]	2,000
Add: Cost of local materials	2,25,000
Less: VAT @12.5%	<u>25,000</u>
[Since, input tax credit of ₹ 25,000 would be available, it will not be included in cost of inputs]	2,00,000
Add: Other expenses and profit	<u>87,500</u>
Sales Price of goods	3,89,500
Add: VAT on the above @12.5% (rounded off)	<u>48,688</u>
Invoice value charged by Mr. Goenka to the manufacturer	4,38,188

Question 4

Mr. Rajesh, a registered dealer, sells his products to dealers in his State and in other States. Profit margin is 15% of cost of production and VAT rate is 12.5% of sales. Following further information is provided by Mr. Rajesh:

- Intra-State purchases of raw material ₹ 2,50,000/- (excluding VAT @ 4%)
- Purchases of raw materials from an unregistered dealer ₹ 80,000/- (including VAT @ 12.5%)
- High seas purchases of raw materials are ₹ 1,85,000/- (excluding custom duty @ 10%).
- Purchases of raw materials from other States (excluding CST @ 2%) ₹ 50,000/-.
- Transportation charges, wages and other manufacturing expenses excluding tax ₹ 1,45,000/-

(vi) Interest paid on bank loan ₹ 70,000/-. Loan is taken to acquire a land for building a factory.

All the afore-mentioned purchases have been sold by Mr. Rajesh. You are required to compute net tax liability and total sales value (invoice value) under value added tax.

Answer

Computation of net VAT liability and total sales value

Particulars	₹
Intra-State purchases of raw material (excluding VAT ₹ 10,000)	2,50,000
Purchases of raw materials from unregistered dealer [Refer Note 1]	80,000
High seas purchases of raw materials [Refer Note 2]	2,03,500
Purchase of raw materials from other States [Refer Note 3]	51,000
Transportation charges, wages and manufacturing expenses	<u>1,45,000</u>
Cost of production	7,29,500
Add: Profit margin 15%	<u>1,09,425</u>
	8,38,925
Add: VAT @ 12.5%	<u>1,04,866</u>
Total sales value (invoice value)	<u>9,43,791</u>

Computation of Net VAT liability

	₹	₹
VAT on above sales price @ 12.5%		1,04,866
Less: Input tax credit on intra-State purchases [Refer Note 4]		<u>10,000</u>
Net VAT payable		<u>94,866</u>

Notes:

1. Input tax credit is not available on the purchases of raw materials from unregistered dealer. Hence, VAT paid thereon is a part of cost of production.
2. Duty paid on high seas purchases i.e., imports is not a State VAT, so input tax credit is not available in respect of the same and it is a part of cost of production.
3. Input tax credit in respect of tax paid on inter-state purchases is not allowed.
4. Tax on intra-State purchases is ₹ 10,000. As credit of the same will be available, it is not included in the cost of production.
5. Interest on loan has been excluded for calculating the cost of production as the loan is availed for purposes other than working capital.

1.66 Indirect Taxes

Question 5

Following are the details of purchases, sales, etc. effected by Vasudha & Co., a registered dealer, for the year ended 31.3.2014:

Particulars	(₹)
Purchase of raw materials within State (1000 units) inclusive of VAT levy at 12.5%	2,70,000
Inter-State purchases of raw materials, inclusive of CST at 2%	2,04,000
Import of raw materials, inclusive of customs duty of ₹ 35,000	4,35,000
Capital goods purchased on 1.5.2013, inclusive of VAT levy at 10% (input credit to be spread over 2 financial years)	3,30,000
Other manufacturing expenses	1,50,000
Sale of taxable goods within State, inclusive of VAT levy at 4%	7,28,000
Sale of goods within State, exempt from levy of VAT (Goods were manufactured from the Inter-State purchase of raw materials)	1,20,000
Closing stock as on 31.3.2014 was 100 units of raw materials purchased within the State	

Input tax credit is allowed only on raw materials used in manufacture of the taxable goods. Compute net VAT liability of the dealer for the year ended 31.3.2014.

Answer

Computation of Net VAT liability of Vasudha & Co. for the year ended 31.3.2014

Particulars	(₹)
Input tax credit:	
Intra-State purchases of 1000 units raw materials [Refer Note 1]	30,000
Inter-State purchases of raw materials [Refer Note 2]	-
Import of raw materials [Refer Note 3]	
Purchase of Capital Goods [Refer Note 4]	15,000
Other manufacturing expenses [Refer Note 5]	-
Total input tax credit available (A)	<u>45,000</u>
Output VAT payable:	
Sale of taxable goods within State [(₹ 7,28,000 x 4)/104]	28,000
Sale of exempted goods within State [Refer Note 6]	-
Total VAT payable (B)	<u>28,000</u>
Net VAT liability [VAT credit to be carried forward] [(B)-(A)]	<u>(17,000)</u>

Notes:-

1. VAT paid on intra-State purchases is eligible for input tax credit $\left[\frac{2,70,000 \times 12.5}{112.5} \right]$.
2. CST paid on intra-State purchases is not eligible for input tax credit.
3. Customs duty is not eligible for input tax credit.
4. VAT paid on purchase of capital goods is eligible for input tax credit. However, the same has to be spread over a period of two years $\left[\frac{3,30,000 \times 10}{110 \times 2} \right]$.
5. No input tax credit can be availed on expenses incurred on manufacturing.
6. No VAT will be payable on sale of goods exempted from levy of VAT. Further, since these goods were manufactured from the inter-State purchases of raw materials (non-vatable inputs), input tax credit is not affected.
7. VAT system allows credit in respect of purchases made during a period to be set-off against the taxable sales during that period, irrespective of when the supplies/inputs purchased are utilized/sold. Therefore, input tax credit in respect of closing stock of raw materials need not be reduced from total input tax credit available.

Question 6

Ashok, purchased raw material 'A' for ₹ 30,00,000 plus VAT @ 4%. Out of such raw material 60% was used for manufacture of taxable goods and the remaining for manufacture of goods which are exempt from VAT.

Another raw material 'B' was purchased for ₹ 15,00,000 on which VAT was paid at 1%. Entire raw material 'B' was used for manufacture of taxable goods only.

The entire taxable goods were sold for ₹ 50,00,000 plus VAT @ 12.5%.

Compute net VAT liability of Ashok on the assumption that there was no opening or closing inventory.

Answer

Computation of Net VAT liability of Ashok

Particulars	₹	₹
Output VAT (50,00,000 × 12.5%) [A]		6,25,000
Input VAT [B]		
Raw material 'A' (30,00,000 × 60% × 4%) [Refer Note]	72,000	
Raw material 'B' (15,00,000 × 1%)	<u>15,000</u>	<u>87,000</u>
Net VAT payable by Ashok [A] – [B]		<u>5,38,000</u>

1.68 Indirect Taxes

Note : Input tax credit is allowed only in respect of the raw material used in manufacture of taxable goods and hence, the same has been restricted to the extent of 60%.

Question 7

Determine net VAT liability of X for the month of December, 2013 using invoice method of computation from the following data:

Purchase price of goods acquired from local market (including VAT)	₹ 52 lakhs
VAT rate on input	4%
Transportation, insurance, warehousing and handling cost incurred by X	₹ 20,000
Goods sold at a profit margin (% of cost of production)	14%
VAT rate on sales	12.50%

Answer

Computation of Net VAT liability

Particulars	₹
Purchase price of goods acquired from local market excluding VAT (input tax credit does not form part of cost of production)	50,00,000
₹ $\left[52,00,000 \times \frac{100}{104} \right]$	
Transportation, insurance etc.	<u>20,000</u>
Cost of production	50,20,000
Profit @ 14% on cost of production	<u>7,02,800</u>
Total Sales	<u>57,22,800</u>
Output VAT payable @ 12.5%	7,15,350
Less: Input tax credit [VAT paid on goods acquired from local market is eligible for input tax credit]	<u>2,00,000</u>
Net VAT payable	<u>5,15,350</u>

Question 8

The particulars regarding sale, purchase etc. of Shubham Udyog for the last quarter of the year 2013-14 are as under:

	Particulars	₹
1.	Purchases of raw material within the State	
	(i) taxable @ 1%	40,00,000

	(ii) taxable @ 4% (Inputs were used in the manufacture of goods meant for intra-State sale, exempted sale and inter-State sale in the ratio of 2:1:1)	60,00,000
	(iii) taxable @ 12.5%	10,00,000
2.	Sale of goods manufactured from raw material purchased @ 4% tax rate	
	(i) Sale within the State (tax rate 4%)	20,00,000
	(ii) Exempted sale within the State	10,00,000
	(iii) Sale in the course of Inter-State trade or commerce (CST rate 2%)	10,00,000
3.	Sale of raw material purchased @ 1% tax rate	44,00,000
4.	Goods manufactured from the raw material purchased @ 12.5% tax rate were given on lease. The deemed sale price of such goods is ₹ 12,00,000, taxable @ 12.5%.	

You may assume that input tax credit of tax paid on raw material used in manufacture of leased goods is available immediately. Compute the amount of net Value Added Tax (VAT) payable by M/s Shubham Udyog for the relevant quarter. There was no opening or closing inventory. All figures of purchases and sales given above are exclusive of taxes.

How can he utilize the balance of input tax credit available, if any?

Answer

Computation of Net VAT payable for the quarter ending 31st March, 2014

	Particulars	₹
(A)	Output VAT payable	
(i)	On sale of taxable finished goods within the state (₹ 20,00,000 × 4%)	80,000
(ii)	On raw material (₹ 44,00,000 × 1 %)	44,000
(iii)	On leased goods (₹ 12,00,000 × 12.5%) (Deemed sale)	<u>1,50,000</u>
	Total (A)	<u>2,74,000</u>
(B)	Input tax credit available	
(i)	On raw material purchased @ 1% (₹ 40,00,000 × 1%)	40,000
(ii)	On raw material purchased @ 4% (₹ 60,00,000 × 4%) × 3/4 (Note-1)	1,80,000
(iii)	On raw material purchased @ 12.5% (₹ 10,00,000 × 12.5%)	<u>1,25,000</u>
	Total (B)	<u>3,45,000</u>
	Net VAT payable = (A)-(B)	(71,000)
	CST payable on inter-state sale adjusted (₹ 10,00,000 × 2%)(Note-2)	<u>20,000</u>
	Excess input tax credit can be carried forward to next quarter (₹ 71,000 – ₹ 20,000)	<u>51,000</u>

1.70 Indirect Taxes

Notes :

1. If goods manufactured from raw material are exempt from tax, no input tax credit is available on such raw material. Thus, out of total sales of ₹ 40,00,000 of goods manufactured from raw material purchased @ 4%, credit will not be allowed on 1/4th of the inputs used in manufacture of exempted goods. In other words, input tax credit will be allowed in respect of 3/4th of the inputs.
2. If finished goods are sold in the course of inter-state trade and commerce, input tax credit can be set off against the output tax liability.

Question 9

From the following information provided by M/s RA Ltd., registered under VAT law of Gujarat as dealer in consumer goods, compute the amount of net VAT payable for the month of July 2013 and VAT credit to be transferred, if any:

Purchase of raw material (within the State)

Item	Amount (₹)	Rate of VAT
Goods 'X'	7,50,000	Exempt
Goods 'Y'	25,00,000	1%
Goods 'Z'	35,00,000	12.5%

Sales

Particulars of finished goods sold	State in which goods are sold	Value ₹	VAT/CST Rate %
(i) Produced from goods 'X'	Gujarat	5,00,000	12.5% VAT
	Inter-state sales to Maharashtra	6,00,000	2% CST
(ii) Produced from goods 'Y'	Gujarat	30,00,000	Exempt
(iii) Produced from goods 'Z'	Gujarat	40,00,000	4% VAT

Raw materials valued at ₹ 5 lakh of goods 'Z' have been transferred to the branch in Madhya Pradesh during the month. All figures of purchases and sales given above are exclusive of taxes.

Make assumptions where required and provide suitable explanations.

Answer

Computation of Net VAT payable by M/s. RA Ltd. for the month of July, 2013

	Particulars	₹
(A)	Output VAT payable	
	(i) On sale of finished goods produced from Goods 'X' within Gujarat (₹ 5,00,000 × 12.5%)	62,500
	(ii) On sale of finished goods produced from Goods 'Z' within Gujarat (₹ 40,00,000 × 4 %)	<u>1,60,000</u>
	Total (A)	<u>2,22,500</u>
(B)	Input tax credit available	
	(i) Goods 'X' (Exempt)	Nil
	(ii) Goods 'Y' (Note-2)	Nil
	(iii) Goods 'Z' transferred to branch (₹ 5,00,000×10.5%) (Note-3)	52,500
	(iv) Remaining Goods 'Z' after transfer to the branch [₹ (35,00,000- 5,00,000)×12.5%]	<u>3,75,000</u>
	Total (B)	<u>4,27,500</u>
	Net VAT payable = (A)-(B)	(2,05,000)
	CST payable (₹ 6,00,000 × 2% = ₹ 12,000) on inter-state sale of goods produced from Goods 'X' adjusted (Note-4)	<u>12,000</u>
	Excess input tax credit carried forward to next month	<u>1,93,000</u>

Notes:

1. It is assumed that there is no opening and closing inventory. Hence, entire purchases of the raw materials have been used to manufacture the respective finished goods.
2. Goods utilized in the manufacture of exempted goods are not eligible for input tax credit. Hence, no input tax credit is available in respect of VAT paid on purchase of Goods 'Y' as they have been used to produce goods which are exempt from VAT.
3. In case of stock transfer, input tax paid in excess of 2% can be claimed as input tax credit.
4. Input tax credit can be used to set off the central sales tax payable on the inter-state sales.

Question 10

The following particulars are provided by Mr. Purohit of Calcutta, who has purchased raw materials and other materials for manufacturing PVC Cans and PVC Pipes. The applicable State VAT rate and CST rate for raw materials and other materials is 12.5% and 2% respectively.

1.72 Indirect Taxes

S. No.	Particulars	₹
1.	Purchase of raw materials [exclusive of tax]	1,00,000
2.	Purchase of other materials [exclusive of taxes]	
	Local	20,000
	Inter-state purchases	40,000
3.	Manufacturing expenses	39,200
4.	Profit margin (on Sale Value)	20%

Mr. Purohit manufactured 75% of production as PVC cans and 25% of production as PVC pipes. While PVC cans are subject to 12.5% VAT, PVC pipes are exempt. All materials were used in production and there was no closing stock of raw materials and other materials.

What would be the invoice value of sales charged by Mr. Purohit if all the manufactured goods were sold within the State? What would be his net liability to VAT?

Answer

Computation of invoice value of sales charged by Mr. Purohit

Particulars	PVC Cans (12.5% VAT)	PVC Pipes (Exempt)
	(₹)	(₹)
	(75%)	(25%)
Raw materials	75000	25000
VAT paid on the same [₹ 1,00,000 x 12.5% = ₹ 12,500]	NIL	3125
	(Refer Note 2)	(Refer Note 3)
Other materials - Local	15000	5000
VAT paid on the same [₹ 20,000 x 12.5% = ₹ 2,500]	NIL	625
	(Refer Note 2)	(Refer Note 3)
Other materials – Inter-state purchases	30000	10000
CST paid on the same [₹ 40,000 x 2% = ₹ 800] (Refer Note 4)	600	200
Manufacturing expenses	29400	9800
Cost of goods sold	150000	53750
Add: Profit is 20% on sales (i.e., 25% of cost)	37500	13438
Sale price	187500	67188
Add: VAT payable (rounded off to nearest rupee)	23438	NIL
Invoice value	210938	67188

Computation of Net VAT liability for PVC Cans

Particulars	(₹)
Output VAT	23438
Less: Input VAT = [(12500 × 75%)+(2500×75%)] (Refer Note 5)	11250
Net VAT liability	12188

Notes:-

1. All the expenses have been apportioned in the ratio of 3:1 on *pro-rata* basis.
2. Since PVC Cans are taxable goods, VAT paid on raw materials is allowed as input tax credit and thus, the same will not form part of total cost.
3. Since PVC pipes are exempt goods, VAT paid on raw materials will not be allowed as input tax credit and thus, the same will form part of total cost.
4. Input tax credit is not available on CST. Therefore it will form part of total cost.
5. Input tax credit to the extent (75%) used in the production of taxable PVC Cans is allowed.

Question 11

Raj and Co., a manufacturer of product 'X', sold its goods to a distributor at ₹ 11,250. The distributor sold the goods to wholesaler for ₹ 13,500. The wholesaler sold the goods to a retailer for ₹ 16,875. The retailer sold the goods to consumer at ₹ 22,500. All the sales were inclusive of VAT @ 12.5%.

Compute total VAT payable under the subtraction method.

Answer

Computation of VAT payable by Raj & Co. under subtraction method

Particulars	Value added (₹)	VAT (₹)
Sale by manufacturer to distributor	11,250	$\left[11,250 \times \frac{12.5}{112.5} \right] = 1,250$
Sale by distributor to wholesaler	13,500 - 11,250 = 2,250	$\left[2,250 \times \frac{12.5}{112.5} \right] = 250$
Sale by wholesaler to retailer	16,875 - 13,500 = 3,375	$\left[3,375 \times \frac{12.5}{112.5} \right] = 375$
Sale by retailer to consumer	22,500 - 16,875 = 5,625	$\left[5,625 \times \frac{12.5}{112.5} \right] = 625$
Total VAT payable		2,500

Question 12

Sidharth Enterprises, a dealer in Gujarat, purchased raw material worth ₹ 80,00,000 (excluding VAT) and manufactured finished goods worth ₹ 1,50,00,000 from such raw material in the month of February, 2014. It received an order for the said finished goods from Mumbai in March, 2014. Hence, it transferred these finished goods to its branch in Mumbai in the same month. Compute:

- (i) Amount of input tax credit available for the month of March, 2014
- (ii) Net VAT payable for the month of March, 2014, and
- (iii) Balance input tax credit carried forward to next month, if any.

Input VAT rate is 12.5% and output VAT rate is 4%.

Answer

Computation of VAT payable and input tax credit for March, 2014

Particulars	(₹)
Output VAT payable (Note-1)	Nil
Less: Input tax credit $\left[80,00,000 \times \frac{(12.5-2)}{100} \right]$ (Note-2)	<u>8,40,000</u>
Net VAT payable	<u>Nil</u>
Balance input tax credit carried forward to next month	8,40,000

Notes:

1. Inter-State stock transfers do not involve sale and, therefore they are not subject to VAT or CST.
2. In case of stock transfer of finished goods, input tax paid (on inputs used in manufacture of such finished goods) in excess of 2% is available as input tax credit.

Question 13

Lee Traders, a registered dealer having stock of goods worth ₹ 30,000, purchased from outside the State, wishes to opt for Composition Scheme. Advise the dealer whether it is possible.

Answer

If a dealer wishes to opt for Composition Scheme, he should not have any stock of goods which are brought from outside the State on the day he exercises the option to pay tax by way of composition. Hence, it is not possible for Lee Traders to opt for Composition Scheme as it has goods worth ₹ 30,000 purchased from outside the State on the day it wishes to opt for the Composition Scheme.

Question 14

Strong Constructions undertakes works contracts and maintains sufficient records to quantify the labour and other service charges. From the details given below, calculate the taxable turnover, input tax credit and net VAT payable under the State VAT Law:

	Particulars	(₹)
(i)	Total contract price (excluding VAT)	1,80,00,000
(ii)	Materials purchased and used for the contract taxable at 12.5% VAT (inclusive of VAT)	33,75,000
(iii)	Labour charges paid for execution of the contract	40,00,000
(iv)	Other service charges paid for the execution of the contract	20,00,000
(v)	Cost of consumables used not involving transfer of property in goods	10,00,000

Strong Constructions also purchased a plant for use in the contract for ₹ 20,80,000 (inclusive of VAT). In the VAT invoice relating to the same, VAT was charged at 4% separately. Assume 100% input tax credit is available on capital goods immediately and output VAT is leviable at 12.5%. Make suitable assumptions where required and show the workings.

Answer

Under works contract, VAT is imposed on the sale price of the goods in which there is a transfer of property. Labour and other charges incurred for such execution are deductible.

Computation of the taxable turnover, input tax credit and net VAT payable

Particulars	₹	₹
Total contract price		1,80,00,000
Less : Deductions admissible		
Labour charges paid for executing the contract	40,00,000	
Service charges paid for execution of contract	20,00,000	
Cost of consumables not involving transfer of property in goods	<u>10,00,000</u>	<u>70,00,000</u>
Taxable turnover		<u>1,10,00,000</u>
Output VAT payable @ 12.5%		13,75,000
Less : <u>Input tax credit admissible</u>		
On the material purchased ₹ $\left[33,75,000 \times \frac{12.5}{112.5} \right]$	3,75,000	

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On the plant purchased ₹ $\left[20,80,000 \times \frac{4}{104} \right]$	<u>80,000</u>	
Total input tax credit		<u>4,55,000</u>
Net VAT payable		<u>9,20,000</u>

Question 15

State with reasons in brief whether the following statements are correct or incorrect with reference to the provisions of value added tax laws:

- (i) It is permitted to issue 'tax invoice' inclusive of VAT i.e., aggregate of sale price & VAT.
- (ii) VAT laws of different States require a registered dealer to compulsorily get his books of accounts audited irrespective of the quantum of his turnover.
- (iii) Taxpayer's Identification Number (TIN) is a 10 digit alpha numeral.

Answer

- (i) **Incorrect.** One of the requirements under the contents of the tax invoice is that rate and amount of tax charged in respect of taxable goods should be distinctly shown in the 'tax invoice', in order to claim input tax credit.
- (ii) **Incorrect.** Different States have prescribed different turnover limits for VAT audit and only if the turnover of the registered dealer crosses such limit, he is required to get his books of accounts audited under VAT laws.
- (iii) **Incorrect.** Taxpayer's Identification Number (TIN) is a 11 digit numeral. The first two characters represent the State Code as used by the Union Ministry of Home Affairs and the next nine characters are different in different states.

Exercise

1. Discuss the merits and demerits of VAT system.
2. Write a note on different methods of computation of VAT.
3. What are the different tax rates under VAT system?
4. Differentiate between input tax and output tax.
5. List the purchases which are not eligible for input tax credit.
6. Discuss the tax consequences of inter-state stock transfer under the VAT scheme.
7. Enumerate the eligible purchases in respect of which input tax credit can be availed.
8. State the benefits and drawbacks for a dealer who opts for Composition Scheme under VAT as per White Paper.
9. Who are not eligible for Composition Scheme under the VAT regime? Discuss briefly.

10. *Briefly explain the different modes in which VAT incentives are given.*
11. *Explain the concept of Hire-purchase transactions. Comment upon their leviability to VAT.*
12. *Write a note to explain the impact of VAT on lease transactions.*
13. *Explain briefly whether VAT is leviable on following lease transactions:-*
 - (a) *Inter-state leasing*
 - (b) *Sale of leased asset after lease period*
 - (c) *Maintenance of leased asset*
14. *State the importance of VAT invoice in administering VAT.*
15. *Briefly list out the contents of VAT invoice.*

2

Residence and Scope of Total Income

Key Points		
Section 6 [Residence in India]		
(i) <u>Individuals [Resident and ordinarily resident / Resident but not ordinarily resident / non-resident]</u>		
The residential status of an individual is determined on the basis of the period of his stay in India.		
Basic conditions:		
(i)	Must be present in India for a period of 182 days or more during the previous year	
(ii)	Must be present 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.	
However, the second condition is not applicable in the following cases:		
(1)	An Indian citizen who leaves India during the previous year for the purpose of employment outside India or as a member of the crew of an Indian ship;	
(2)	An Indian citizen or a person of Indian origin who, being outside India, comes on a visit to India during the previous year.	
Additional conditions:		
(i)	He is a resident in at least 2 out of 10 previous years preceding the relevant previous year;	
(ii)	His stay in India in the last 7 years preceding the relevant previous year is 730 days or more.	
Resident and ordinarily resident	Resident but not ordinarily resident	Non-resident
Must satisfy at least one of the basic conditions and both the additional conditions.	Must satisfy at least one of the basic conditions and one or none of the additional conditions.	Must not satisfy either of the basic conditions.

(ii) <u>HUFs [Resident and ordinarily resident / Resident but not ordinarily resident / non-resident]</u>		
(i)	A HUF would be resident in India if the control and management of its affairs is situated wholly or partly in India .	
(ii)	If the control and management of the affairs is situated wholly outside India , it would become a non-resident .	
(iii)	If the HUF is resident, then the status of the Karta would determine whether the HUF is resident and ordinarily resident or resident but not ordinarily resident	
	If the karta is resident and ordinarily resident, then the HUF would be a resident and ordinarily resident and if the karta is resident but not ordinarily resident, then the HUF would be a resident but not ordinarily resident.	
(iii) <u>Firms & AOPs [Resident / Non-resident]</u>		
(i)	A firm or AOP would be resident in India if the control and management of its affairs is situated wholly or partly in India .	
(ii)	If the control and management of the affairs is situated wholly outside India , it would become a non-resident .	
(iv) <u>Companies [Resident / Non-resident]</u>		
(i)	A company would be resident in India if the control and management of its affairs is situated wholly in India .	
(ii)	If the control and management of the affairs is situated wholly or partly outside India , the company would become a non-resident .	
<u>Section 5 [Scope of Total Income]</u>		
Resident And Ordinarily Resident	Resident But Not Ordinarily Resident	Non-Resident
Income received/ deemed to be received/ accrued or arisen/ deemed to accrue or arise in or outside India In short, the global income is taxable.	Income which is received/ deemed to be received/ accrued or arisen/ deemed to accrue or arise in India. and Income which accrues or arises outside India being derived from a business controlled from or profession set up in India.	Income received/ deemed to be received/ accrued or arisen/deemed to accrue or arise in India.

2.3 Income-tax

Question 1

Mr. Ramesh & Mr. Suresh are brothers and they earned the following incomes during the financial year 2013-14. Mr. Ramesh settled in Canada in the year 1995 and Mr. Suresh settled in Delhi. Compute the total income for the assessment year 2014-15.

Sr. No.	Particulars	Mr. Ramesh (₹)	Mr. Suresh (₹)
1.	Interest on Canada Development Bonds (only 50% of interest received in India)	35,000	40,000
2.	Dividend from British company received in London	28,000	20,000
3.	Profit from a business in Nagpur, but managed directly from London	1,00,000	1,40,000
4.	Short term capital gain on sale of shares of an Indian company received in India	60,000	90,000
5.	Income from a business in Chennai	80,000	70,000
6.	Fees for technical services rendered in India, but received in Canada	1,00,000	----
7.	Interest on savings bank deposit in UCO Bank, Delhi	7,000	12,000
8.	Agricultural income from a land situated in Andhra Pradesh	55,000	45,000
9.	Rent received in respect of house property at Bhopal	1,00,000	60,000
10.	Life insurance premium paid	---	30,000

Answer

Computation of total income of Mr. Ramesh & Mr. Suresh for the A.Y. 2014-15

S. No.	Particulars	Mr. Ramesh (Non-Resident) (₹)	Mr. Suresh (Resident) (₹)
1.	Interest on Canada Development Bond (See Note 2)	17,500	40,000
2.	Dividend from British Company received in London (See Note 3)	-	20,000
3.	Profit from a business in Nagpur but managed directly from London (See Note 2)	1,00,000	1,40,000
4.	Short term capital gain on sale of shares of an Indian company received in India (See Note 2)	60,000	90,000
5.	Income from a business in Chennai (See Note 2)	80,000	70,000
6.	Fees for technical services rendered in India, but received in Canada (See Note 2)	1,00,000	-

7.	Interest on savings bank deposit in UCO Bank, Delhi (See Note 2)	7,000	12,000
8.	Agricultural income from a land in Andhra Pradesh (See Note 4)	-	-
9.	Income from house property at Bhopal (See Note 5)	70,000	42,000
	Gross Total income	4,34,500	4,14,000
	<i>Less: Deduction under chapter VIA-</i>		
	Section 80C-Life insurance premium paid	-	30,000
	Section 80TTA (See Note 6)	7,000	10,000
	Total Income	4,27,500	3,74,000

Notes:

- Mr. Ramesh is a non-resident since he has been living in Canada since 1995. Mr. Suresh, who is settled in Delhi, is a resident.
- In case of a resident, his global income is taxable as per section 5(1). However, as per section 5(2), in case of a non-resident, only the following incomes are chargeable to tax:
 - Income received or deemed to be received in India; and
 - Income accruing or arising or deemed to accrue or arise in India.

Therefore, fees for technical services rendered in India would be taxable in the hands of Mr. Ramesh, even though he is a non-resident.

The income referred to in Sl. No. 3,4,5 and 7 are taxable in the hands of both Mr. Ramesh and Mr. Suresh since they accrue or arise in India.

Interest on Canada Development Bond would be fully taxable in the hands of Mr. Suresh, whereas only 50% which is received in India is taxable in the hands of Mr. Ramesh.

- Dividend received from British company in London by Mr. Ramesh is not taxable since it accrues and is received outside India. However, dividend received by Mr. Suresh is taxable, since he is a resident. Exemption under section 10(34) would not be available in respect of dividend received from a foreign company.
- Agricultural income from a land situated in India is exempt under section 10(1) in the case of both non-residents and residents.
- Income from house property-

	Mr. Ramesh	Mr. Suresh
	(₹)	(₹)
Rent received	1,00,000	60,000
<i>Less: Deduction under section 24 @ 30%</i>	<u>30,000</u>	<u>18,000</u>
Net income from house property	<u>70,000</u>	<u>42,000</u>

2.5 Income-tax

The net income from house property in India would be taxable in the hands of both Mr. Ramesh and Mr. Suresh, since the accrual and receipt of the same are in India.

6. In case of an individual, interest upto ₹ 10,000 from savings account with, *inter alia*, a bank is allowable as deduction under section 80TTA.

Question 2

Discuss the correctness or otherwise of the statement- "Income deemed to accrue or arise in India to a non-resident by way of interest, royalty and fees for technical services is to be taxed irrespective of territorial nexus".

Answer

This statement is correct.

As per *Explanation* to section 9, income by way of interest, royalty or fee for technical services which is deemed to accrue or arise in India by virtue of clauses (v), (vi) and (vii) of section 9(1), shall be included in the total income of the non-resident, whether or not -

- (i) non-resident has a residence or place of business or business connection in India; or
- (ii) the non-resident has rendered services in India.

In effect, the income by way of fee for technical services, interest or royalty from services utilised in India would be deemed to accrue or arise in India in case of a non-resident and be included in his total income, whether or not such services were rendered in India and irrespective of whether the non-resident has a residence or place of business or business connection in India.

Question 3

Mr. David, a Government employee serving in the Ministry of External Affairs, left India for the first time on 31.03.2013 due to his transfer to High Commission of Canada. He did not visit India any time during the previous year 2013-14. He has received the following income for the Financial Year 2013-14:

S.No.	Particulars	₹
(i)	Salary	5,00,000
(ii)	Foreign Allowance	4,00,000
(iii)	Interest on fixed deposit from bank in India	1,00,000
(iv)	Income from agriculture in Pakistan	2,00,000
(v)	Income from house property in Pakistan	2,50,000

Compute his gross total income for Assessment Year 2014-15.

Answer

As per section 6(1), Mr. David is a non-resident for the A.Y. 2014-15, since he was not present in India at any time during the previous year 2013-14.

As per section 5(2), a non-resident is chargeable to tax in India only in respect of following incomes:

- (i) Income received or deemed to be received in India; and
- (ii) Income accruing or arising or deemed to accrue or arise in India.

In view of the above provisions, income from agriculture in Pakistan and income from house property in Pakistan would not be chargeable to tax in the hands of David, assuming that the same were received in Pakistan.

Income from 'Salaries' payable by the Government to a citizen of India for services rendered outside India is deemed to accrue or arise in India as per section 9(1)(iii). Hence, such income is taxable in the hands of Mr. David, even though he is a non-resident. It has been assumed that Mr. David is a citizen of India.

However, allowances or perquisites paid or allowed as such outside India by the Government to a citizen of India for rendering service outside India is exempt under section 10(7). Hence, foreign allowance of ₹ 4,00,000 is exempt under section 10(7).

Gross Total Income of Mr. David for A.Y. 2014-15

Particulars	₹
Salaries	5,00,000
Income from other sources (Interest on fixed deposit in India)	<u>1,00,000</u>
Gross Total Income	<u>6,00,000</u>

Question 4

Brett Lee, an Australian cricket player visits India for 100 days in every financial year. This has been his practice for the past 10 financial years. Find out his residential status for the assessment year 2014-15.

Answer

Determination of Residential Status of Mr. Brett Lee for the A.Y. 2014-15:-

Period of stay during previous year 2013-14 = 100 days.

Calculation of period of stay during 4 preceding previous years (100 x 4=400 days)

2012-13	100 days
2011-12	100 days
2010-11	100 days
2009-10	<u>100 days</u>
Total	<u>400 days</u>

Mr. Brett Lee has been in India for a period more than 60 days during previous year 2013-14 and for a period of more than 365 days during the 4 immediately preceding previous years. Therefore, since he satisfies one of the basic conditions under section 6(1), he is a resident for the assessment year 2014-15.

2.7 Income-tax

Computation of period of stay during 7 preceding previous years = $100 \times 7 = 700$ days

2012-13	100 days
2011-12	100 days
2010-11	100 days
2009-10	100 days
2008-09	100 days
2007-08	100 days
2006-07	<u>100 days</u>
Total	<u>700 days</u>

Since his period of stay in India during the past 7 previous years is less than 730 days, he is a not-ordinarily resident during the assessment year 2014-15. (See Note below)

Therefore, Mr. Brett Lee is a resident but not ordinarily resident during the previous year 2013-14 relevant to the assessment year 2014-15.

Note: A not-ordinarily resident person is one who satisfies any one of the conditions specified under section 6(6), i.e.,

- (i) If such individual has been non-resident in India in any 9 out of the 10 previous years preceding the relevant previous year, or
- (ii) If such individual has during the 7 previous years preceding the relevant previous year been in India for a period of 729 days or less.

In this case, since Mr. Brett Lee satisfies condition (ii), he is a not-ordinary resident for the A.Y. 2014-15.

Question 5

Choose the correct answer with reference to the provisions of the Income-tax Act, 1961:

- (i) *Income accruing in Japan and received there is taxable in India in the case of -*
 - (a) *Resident and ordinarily resident only*
 - (b) *Both resident and ordinarily resident and resident but not ordinarily resident*
 - (c) *Both resident and non-resident*
 - (d) *Non-resident*
- (ii) *A company, other than an Indian company, would be treated as a resident in India for the previous year 2013-14 if, during that year, its control and management is situated:*
 - (a) *Wholly in India*
 - (b) *Partly in India*
 - (c) *Wholly or partly in India*
 - (d) *None of the above.*

Answer

- (i) (a) Resident and ordinarily resident only.
- (ii) (a) Wholly in India

Question 6

Miss Vivitha paid a sum of 5000 USD to Mr. Kulasekhara, a management consultant practising in Colombo, specializing in project financing. The payment was made in Colombo. Mr. Kulasekhara is a non-resident. The consultancy is related to a project in India with possible Ceylonese collaboration. Is this payment chargeable to tax in India in the hands of Mr. Kulasekhara, since the services were used in India?

Answer

A non-resident is chargeable to tax in respect of income received outside India only if such income accrues or arises or is deemed to accrue or arise to him in India.

The income deemed to accrue or arise in India under section 9 comprises, *inter alia*, income by way of fees for technical services, which includes any consideration for rendering of any managerial, technical or consultancy services. Therefore, payment to a management consultant relating to project financing is covered within the scope of "fees for technical services".

The *Explanation* below section 9(2) clarifies that income by way of, *inter alia*, fees for technical services, from services utilized in India would be deemed to accrue or arise in India in case of a non-resident and be included in his total income, whether or not such services were rendered in India or whether or not the non-resident has a residence or place of business or business connection in India.

In the instant case, since the services were utilized in India, the payment received by Mr. Kulasekhara, a non-resident, in Colombo is chargeable to tax in his hands in India, as it is deemed to accrue or arise in India.

Question 7

Mr. Ram, an Indian citizen, left India on 22.09.2013 for the first time to work as an officer of a company in Germany.

Determine the residential status of Ram for the assessment year 2014-15 and explain the conditions to be fulfilled for the same under the Income-tax Act, 1961.

Answer

Under section 6(1), an individual is said to be resident in India in any previous year if he satisfies any one of the following conditions -

- (i) He has been in India during the previous year for a total period of 182 days or more, or

2.9 Income-tax

- (ii) He has been in India during the 4 years immediately preceding the previous year for a total period of 365 days or more and has been in India for at least 60 days in the previous year.

In the case of Indian citizens leaving India for employment, the period of stay during the previous year must be 182 days instead of 60 days given in (ii) above.

During the previous year 2013-14, Mr. Ram, an Indian citizen, was in India for 175 days only (i.e 30+31+30+31+31+22 days). Thereafter, he left India for employment purposes.

Since he does not satisfy the minimum criteria of 182 days, he is a non-resident for the A.Y. 2014-15.

Question 8

From the following particulars of income furnished by Mr. Anirudh pertaining to the year ended 31.3.2014, compute the total income for the assessment year 2014-15, if he is:

- (i) Resident and ordinary resident;
(ii) Resident but not ordinarily resident;
(iii) Non-resident

	Particulars	₹
(a)	Short term capital gain on sale of shares in Indian Company received in Germany	15,000
(b)	Dividend from a Japanese Company received in Japan	10,000
(c)	Rent from property in London deposited in a bank in London, later on remitted to India through approved banking channels	75,000
(d)	Dividend from RP Ltd., an Indian Company	6,000
(e)	Agricultural income from lands in Gujarat	25,000

Answer

Computation of total income of Mr. Anirudh for the A.Y. 2014-15

Particulars	Resident & ordinarily resident	Resident but not ordinarily resident	Non-Resident
1) Short term capital gain on sale of shares of an Indian company, received in Germany	15,000	15,000	15,000
2) Dividend from a Japanese company, received in Japan	10,000	-	-
3) Rent from property in London deposited in a bank in London [See Note (i) below]	52,500	-	-

4) Dividend from RP Ltd., an Indian Company [See Note (ii) below]	-	-	-
5) Agricultural income from land in Gujarat [See Note (iii) below]	-	-	-
Total Income	77,500	15,000	15,000

Notes:

- (i) It has been assumed that the rental income is the gross annual value of the property. Therefore, deduction @30% under section 24, has been provided and the net income so computed is taken into account for determining the total income of a resident and ordinarily resident.

Rent received (assumed as gross annual value)	75,000
Less: Deduction under section 24 (30% of ₹ 75,000)	22,500
Income from house property	<u>52,500</u>

- (ii) Dividend from Indian company is exempt under section 10(34).
(iii) Agricultural income is exempt under section 10(1).

Question 9

Discuss the provisions relating to determination of residential status of Hindu undivided family, partnership firm and company.

Answer**Residential status of a HUF:**

A HUF would be resident in India if the control and management of its affairs is situated wholly or partly in India during the relevant previous year. If the control and management of its affairs is situated wholly outside India during the relevant previous year, it would be considered as a non-resident.

If the HUF is resident, then the status of its Karta determines whether it is resident and ordinarily resident or resident but not ordinarily resident.

Residential status of a firm:

A firm would be resident in India if the control and management of its affairs is situated wholly or partly in India during the relevant previous year. Where the control and management of the affairs is situated wholly outside India during the relevant previous year, the firm would be considered as a non-resident.

Residential status of a company:

A company is said to be resident in India in any previous year if :

- (a) it is an Indian company as defined under section 2(26) ,or

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(b) its control and management is situated wholly in India during that year.

Thus, every Indian company is resident in India irrespective of the fact whether the control and management of its affairs is exercised from India or outside. However, a company other than an Indian company, would become resident in India only if the entire control and management of its affairs is in India during the relevant previous year.

Question 10

Mr. Dey, a non-resident, residing in US since 1960, came back to India on 1.4.2012 for permanent settlement. What will be his residential status for assessment years 2013-14 and 2014-15?

Answer

Mr. Dey is a resident in A.Y.2013-14 and A.Y.2014-15 since he has stayed in India for a period of 365 days (more than 182 days) during the P.Y.2012-13 and P.Y.2013-14, respectively.

As per section 6(6), a person will be "Not ordinarily Resident" in India in any previous year, if such person:

- (a) has been a non-resident in 9 out of 10 previous years preceding the relevant previous year; or
- (b) has during the 7 previous years immediately preceding the relevant previous year been in India for 729 days or less.

If he does not satisfy either of these conditions, he would be a resident and ordinarily resident.

In the instant case, applying the above, the status of Mr. Dey for the previous year 2012-13 (A.Y. 2013-14) will be "Resident but not ordinarily resident".

For the previous year 2013-14 (A.Y. 2014-15) his status would continue to be Resident but not ordinarily resident since he was non-resident in 9 out of 10 previous years immediately preceding the previous year and also had stayed for less than 729 days in 7 previous years immediately preceding the previous year.

Therefore his status for

A.Y. 2013-14 – "Resident but not ordinarily resident"

A.Y. 2014-15 – "Resident but not ordinarily resident"

Question 11

State the activities and operations, income from which is not deemed to accrue or arise in India.

Answer

Explanation 1 to section 9(1)(i) lists out income which shall not be deemed to accrue or arise in India. They are given below:

(1) In the case of a business, in respect of which all the operations are not carried out in India [Explanation 1(a) to section 9(1)(i)]

In the case of a business of which all the operations are not carried out in India, the income of the business deemed to accrue or arise in India shall be only such part of income as is reasonably attributable to the operations carried out in India. Therefore, it follows that such part of income which cannot be reasonably attributed to the operations in India, is not deemed to accrue or arise in India.

(2) Purchase of goods in India for export [Explanation 1(b) to section 9(1)(i)]

In the case of a non-resident, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in India for the purpose of export.

(3) Collection of news and views in India for transmission out of India [Explanation 1(c) to section 9(1)(i)]

In the case of a non-resident, being a person engaged in the business of running a news agency or of publishing newspapers, magazines or journals, no income shall be deemed to accrue or arise in India to him through or from activities which are confined to the collection of news and views in India for transmission out of India.

(4) Shooting of cinematograph films in India [Explanation 1(d) to section 9(1)(i)]

In the case of a non-resident, no income shall be deemed to accrue or arise in India through or from operations which are confined to the shooting of any cinematograph film in India, if such non-resident is :

- (i) an individual, who is not a citizen of India or
- (ii) a firm which does not have any partner who is a citizen of India or who is resident in India ; or
- (iii) a company which does not have any shareholder who is a citizen of India or who is resident in India.

Question 12

When is an individual and HUF said to be "Resident and ordinarily Resident" under the Income-tax Act, 1961?

Answer

Individual – An individual is said to be a resident in India in any previous year if he fulfills any one of the following two basic conditions:

- (i) He is in India during the previous year for a period or periods amounting in all to 182 days or more.

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- (ii) He is in India for a period or periods amounting in all to 60 days or more during the previous year and 365 days or more during 4 years immediately preceding the relevant previous year.

Exception – If an Indian citizen leaves India for the purpose of employment or as a member of crew of an Indian ship or if an Indian citizen or person of Indian origin who is residing outside India comes to India on a visit in any previous year, he would be considered as resident in India in that year only if he has been in India in that year for 182 days or more instead of 60 days referred to in, (ii) above.

Resident and Ordinarily Resident: If an individual satisfies any one of the basic conditions and none of the following additional conditions, he will be treated as “resident and ordinarily resident”.

Additional conditions:

- (i) He has been a non-resident in India in 9 out of 10 previous years preceding the relevant previous year ; or
- (ii) He has been in India for a period of 729 days or less during 7 previous years immediately preceding the relevant previous year.

Thus in brief, an individual fulfilling any one of the basic conditions and none of the additional conditions will be “resident and ordinarily resident”.

HUF: If the control and management of the affairs of the HUF is wholly or partly situated in India and if the manager of the HUF does not satisfy either of the following two additional conditions, the HUF shall be considered as “resident and ordinarily resident” –

- (i) He has been non resident in India in 9 out of 10 previous years preceding the relevant previous year;
- (ii) He has been in India for a period of 729 days or less during the 7 previous years preceding the relevant previous year.

Question 13

In the previous year 2013-14, a sailor has remained on ship for a private company owning ocean going ships as follows:

- (1) *Outside the territorial waters of India for 182 days.*
- (2) *Inside the territorial waters of India for 183 days.*

Is he considered to be resident or not for the A.Y.2014-15 (P.Y. 2013-14)? Comment.

Answer

An individual is treated as a resident in India in any previous year if he fulfills any of the following two conditions laid down in section 6(1) -

- (a) He is in India for a period or periods amounting to 182 days or more in that year; or

- (b) In the preceding four years, he has been in India for 365 days or more, and has been in India for 60 days or more in that year.

In case an Indian citizen leaves India as a member of crew of an Indian ship, the period of stay during the previous year to be read as 182 days instead of 60 days given in (b) above.

In the given case, period of stay in India is more than 182 days. Therefore, the sailor is treated as a resident in India for the Assessment Year 2014-15.

Question 14

State with reasons, whether the following statements are true or false, with regard to the provisions of the Income-tax Act, 1961:

- (a) *Only individuals and HUFs can be resident, but not ordinarily resident in India; firms can be either a resident or non-resident.*
- (b) *Income deemed to accrue or arise in India to a non-resident by way of interest, royalty and fee for technical services is taxable in India irrespective of territorial nexus.*
- (c) *Mr. X, Karta of HUF, claims that the HUF is non-resident as the business of HUF is transacted from UK and all the policy decisions are taken there.*

Answer

- (a) **True:** A person is said to be "not-ordinarily resident" in India if he satisfies either of the conditions given in sub-section (6) of section 6. This sub-section relates to only individuals and Hindu Undivided Families. Therefore, only individuals and Hindu Undivided Families can be resident, but not ordinarily resident in India. All other classes of assesseees can be either a resident or non-resident for the purpose of income-tax. Firms and companies can, therefore, either be a resident or non-resident.
- (b) **True:** *Explanation* below section 9(2) clarifies that income by way of interest, royalty or fee for technical services which is deemed to accrue or arise in India by virtue of clauses (v), (vi) and (vii) of section 9(1), shall be included in the total income of the non-resident, whether or not :
- (i) non-resident has a residence or place of business or business connection in India; or
- (ii) the non-resident has rendered services in India
- (c) **True:** A HUF is considered to be a non-resident where the control and management of its affairs are situated wholly outside India. In the given case, since all the policy decisions of HUF are taken from UK, the HUF is a non-resident.

Question 15

Miss Charlie, an American national, got married to Mr. Radhey of India in USA on 2.03.2013 and came to India for the first time on 16.03.2013. She remained in India up till 19.9.2013 and left for USA on 20.9.2013. She returned to India again on 27.03.2014. While in India, she had purchased a show room in Mumbai on 22.04.2013, which was leased out to a company on a

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rent of ₹ 25,000 p.m. from 1.05.2013 She had taken loan from a bank for purchase of this show room on which bank had charged interest of ₹ 97,500 upto 31.03.2014. She had received the following gifts from her relatives and friends during 1.4.2013 to 30.6.2013:

- From parents of husband	₹ 51,000
- From married sister of husband	₹ 11,000
- From two very close friends of her husband, ₹ 1,51,000 and ₹ 21,000	₹ 1,72,000

Determine her residential status and compute the total income chargeable to tax along with the amount of tax payable on such income for the Asst. Year 2014-15.

Answer

Under section 6(1), an individual is said to be resident in India in any previous year, if he satisfies any one of the following conditions:

- He has been in India during the previous year for a total period of 182 days or more, or
- He has been in India during the 4 years immediately preceding the previous year for a total period of 365 days or more and has been in India for at least 60 days in the previous year.

If an individual satisfies any one of the conditions mentioned above, he is a resident. If both the above conditions are not satisfied, the individual is a non-resident.

Therefore, the residential status of Miss Charlie, an American National, for A.Y.2014-15 has to be determined on the basis of her stay in India during the previous year relevant to A.Y. 2014-15 i.e. P.Y.2013-14 and in the preceding four assessment years.

Her stay in India during the previous year 2013-14 and in the preceding four years are as under:

P.Y.2013-14

01.04.2013 to 19.09.2013	-	172 days
27.03.2014 to 31.03.2014	-	<u>5 days</u>
Total		<u>177 days</u>

Four preceding previous years

P.Y.2012-13 [1.4.2012 to 31.3.2013]	-	16 days
P.Y.2011-12 [1.4.2011 to 31.3.2012]	-	Nil
P.Y.2010-11 [1.4.2010 to 31.3.2011]	-	Nil
P.Y.2009-10 [1.4.2009 to 31.3.2010]	-	<u>Nil</u>
Total		<u>16 days</u>

The total stay of the assessee during the previous year in India was less than 182 days and during the four years preceding this year was for 16 days. Therefore, due to non-fulfillment of any of the two conditions for a resident, she would be treated as non-resident for the Assessment Year 2014-15.

Computation of total income of Miss Charlie for the A.Y. 2014-15

Particulars	₹	₹
Income from house property		
Show room located in Mumbai remained on rent from 01.05.2013 to 31.03.2014 @ ₹ 25,000/- p.m.		
Gross Annual Value [25,000 x 11] (See Note 1 below)	2,75,000	
Less: Municipal taxes	<u>Nil</u>	
Net Annual Value (NAV)	2,75,000	
Less: Deduction under section 24		
30% of NAV	82,500	
Interest on loan	<u>97,500</u>	
	<u>1,80,000</u>	95,000
Income from other sources		
Gifts received from non-relatives is chargeable to tax as per section 56(2)(vii) if the aggregate value of such gifts exceeds ₹ 50,000.		
- ₹ 50,000 received from parents of husband would be exempt, since parents of husband fall within the definition of relatives and gifts from a relative are not chargeable to tax.	Nil	
- ₹ 11,000 received from married sister of husband is exempt, since sister-in-law falls within the definition of relative and gifts from a relative are not chargeable to tax.	Nil	
- Gift received from two friends of husband ₹ 1,51,000 and ₹ 21,000 aggregating to ₹ 1,72,000 is taxable under section 56(2)(vii) since the aggregate of ₹ 1,72,000 exceeds ₹ 50,000. (See Note 2 below)	<u>1,72,000</u>	<u>1,72,000</u>
Total income		<u>2,67,000</u>

Computation of tax payable by Miss Charlie for the A.Y. 2014-15

Particulars	₹
Tax on total income of ₹ 2,67,000	6,700
Add: Education cess@2%	134
Add : Secondary and higher education cess @1%	<u>67</u>
Total tax payable	<u>6,901</u>

Notes:

1. Actual rent received has been taken as the gross annual value in the absence of other information (i.e. Municipal value, fair rental value and standard rent) in the question.
2. If the aggregate value of taxable gifts received from non-relatives exceeds ₹ 50,000 during the year, the entire amount received (i.e. the aggregate value of taxable gifts received) is taxable. Therefore, the entire amount of ₹ 1,72,000 is taxable under section 56(2)(vii).
3. Since Miss Charlie is a non-resident for the A.Y. 2014-15, rebate under section 87A would not be available to her, even though her total income is less than ₹ 5 lacs.

Question 16

Determine the taxability of income of US based company Heli Ltd., in India on entering into the following transactions during the financial year 2013-14:

- (i) ₹ 5 lacs received from an Indian domestic company for providing technical knowhow in India.
- (ii) ₹ 6 lacs from an Indian firm for conducting the feasibility study for the new project in Finland. The payment for the same was made in Finland.
- (iii) ₹ 4 lacs from a non-resident for use of patent for a business in India.
- (iv) ₹ 8 lacs from a non-resident Indian for use of know how for a business in Singapore. Such amount was received in U.S.
- (v) ₹ 10 lacs for supply of manuals and designs for the business to be established in Singapore. No payment for the same was made in India.

Answer

A non-resident is chargeable to tax in India in respect of following incomes:

- (i) Income received or deemed to be received in India; and
- (ii) Income accruing or arising or deemed to accrue or arise in India.

In view of the above provisions, taxability of income is determined in following manner:

S. No.	Particulars	₹ (in lacs)
(i)	Amount received from an Indian domestic company for providing technical knowhow in India is deemed to accrue or arise in India and is, therefore, taxable in India.	5
(ii)	Conducting the feasibility study for the new project in Finland for the Indian firm is not taxable in India as the income accrues outside India since such study is done for a business outside India.	Nil
(iii)	Income received from a non-resident for use of patent for a business in India is taxable in India as it is deemed to accrue or arise in India.	4

(iv)	Income received from a non-resident Indian for use of knowhow for a business in Singapore. It is not taxable in India since it does not accrue or arise in India nor is it deemed to accrue or arise in India,	Nil
(v)	Income received for supply of manuals and designs for the business to be established in Singapore is not taxable in India, since it does not accrue or arise in India nor is it deemed to accrue or arise in India.	Nil
Total Income		9

Question 17

State with reasons whether the following transactions attract income-tax in India in the hands of recipients:

- (i) Salary paid by Central Government to Mr. John, a citizen of India ₹ 7,00,000 for the services rendered outside India.
- (ii) Interest on moneys borrowed from outside India ₹ 5,00,000 by a non-resident for the purpose of business within India say, at Mumbai.
- (iii) Post office savings bank interest of ₹ 12,000 received by a resident assessee, Mr. Ram.
- (iv) Royalty paid by a resident to a non-resident in respect of a business carried on outside India.
- (v) Legal charges of ₹ 5,00,000 paid to a lawyer of United Kingdom who visited India to represent a case at the Delhi High Court.

Answer

	Taxable / Not Taxable	Amount liable to tax (₹)	Reason
(i)	Taxable	7,00,000	As per section 9(1)(iii), salaries payable by the Government to a citizen of India for service rendered outside India shall be deemed to accrue or arise in India. Therefore, salary paid by Central Government to Mr. John for services rendered outside India would be deemed to accrue or arise in India since he is a citizen of India.
(ii)	Taxable	5,00,000	As per section 9(1)(v)(c), interest payable by a non-resident on moneys borrowed and used for the purposes of business carried on by such person in India shall be deemed to accrue or arise in India in the hands of the recipient.
(iii)	Partly Taxable	8,500	The interest on Post Office Savings Bank Account, would be exempt under section 10(15)(i), only to the extent of ₹3,500 in case of an individual account. The

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			remaining ₹ 8,500, being less than ₹10,000, would be allowed as deduction under section 80TTA from Gross Total Income.
(iv)	Not Taxable	-	Royalty paid by a resident to a non-resident in respect of a business carried outside India would not be taxable in the hands of the non-resident provided the same is not received in India. This has been provided as an exception to deemed accrual mentioned in section 9(1)(vi)(b).
(v)	Taxable	5,00,000	Legal charges paid to the non-resident lawyer who visited India to represent a case at Delhi High Court would be taxable in India, since it accrues or arises in India.

Question 18

An individual, who is an Indian resident, is allowed to hold two different citizenships simultaneously. Is the citizenship a determining factor for residential status of an individual?

Answer

Citizenship of a country and residential status of that country are separate concepts. A person may be an Indian national /citizen, but may not be a resident in India. On the other hand, a person may be a foreign national /citizen, but may be a resident in India. The citizenship of an individual has no role in determining the residential status of an individual.

The residential status of resident, non-resident, etc. are determined on the basis of number of days an individual actually stays in India during the previous year.

The provisions of section 6 of the Income-tax Act, 1961 are the determining factor of residential status of an individual.

EXERCISES

1. If Anirudh has stayed in India in the P.Y. 2013-14 for 181 days, and he is non-resident in 9 out of 10 years immediately preceding the current previous year and he has stayed in India for 365 days in all in the 4 years immediately preceding the current previous year and 420 days in all in the 7 years immediately preceding the current previous year, his residential status for the A.Y.2014-15 would be -
 - a) Resident and ordinarily resident
 - b) Resident but not ordinarily resident
 - c) Non-resident
2. Raman was employed in Hindustan Lever Ltd. He received a salary at ₹ 40,000 p.m. from 1.4.2013 to 27.9.2013. He resigned and left for Dubai for the first time on 1.10.2013

and got salary of rupee equivalent of ₹ 80,000 p.m. from 1.10.2013 to 31.3.2014. His salary for October to December 2013 was credited in his Dubai bank account and the salary for January to March 2014 was credited in his Bombay account directly. He is liable to tax in respect of -

- a) Income received in India from Hindustan Lever Ltd;
 - b) Income received in India and in Dubai;
 - c) Income received in India from Hindustan Lever Ltd. and income directly credited in India;
3. A company, other than an Indian company, would be a resident in India for the P.Y.2013-14 if, during that year, its control and management is situated -
 - a) wholly in India
 - b) partly in India
 - c) wholly or partly in India.
 4. Income accruing in London and received there is taxable in India in the case of -
 - a) resident and ordinarily resident only
 - b) both resident and ordinarily resident and resident but not ordinarily resident
 - c) both resident and non-resident
 5. When is an individual said to be "Resident and ordinarily resident" under the Income-tax Act, 1961?
 6. Define royalty as per section 9 of the Income-tax Act, 1961?
 7. Write short notes on -
 - a) Business connection
 - b) Income deemed to accrue or arise in India.
 8. Discuss the provisions relating to determination of residential status of individuals.
 9. When are the following income deemed to accrue or arise in India?
 - a) Interest
 - b) Fees for technical services.
 10. Discuss the correctness or otherwise of the statement – "Income deemed to accrue or arise in India to a non-resident by way of interest, royalty and fees for technical services is to be taxed irrespective of territorial nexus."
 11. Explain the term "Business Connection" under section 9(1).

Answers

1. b; 2. b; 3. a; 4. a.

3

Incomes Which Do Not Form Part of Total Income

Key Points	
Section	Particulars
10(1)	<p>Agricultural income is exempt under section 10(1). However, agricultural income has to be aggregated with non-agricultural income for determining the rate at which non-agricultural income would be subject to tax, in case of individuals, HUFs, AOP & BOIs etc., where the –</p> <ul style="list-style-type: none">• agricultural income exceeds Rs.5,000 p.a. and• non-agricultural income exceeds basic exemption limit. <p>The following are the steps to be followed in computation of tax -</p> <p>Step 1: Tax on non-agricultural income plus agricultural income</p> <p>Step 2: Tax on agricultural income plus basic exemption limit</p> <p>Step 3: Tax payable by the assessee = Step 1 – Step 2</p> <p>Step 4: <i>Add Surcharges/Deduct Rebate</i> under section 87A, if applicable.</p> <p>Step 5: <i>Add Education cess@2% and SHEC@1%.</i></p>
10(2)	<p>Since the HUF is taxed in respect of its income, the share income is exempt from tax in the hands of the member under section 10(2).</p>
10(2A)	<p>The partner's share in the total income of the firm or LLP is exempt from tax.</p>
10(10BC)	<p>Compensation received by an individual or his legal heir on account of any disaster is exempt, if the same has been granted by the Central Government, State Government or a local authority</p>

10(10D)	Any sum received under a life insurance policy, including the sum allocated by way of bonus on such policy is exempt provided that –		
	In case of a policy issued between 1.4.2003 and 31.3.2012, the premium paid does not exceed 20% of the actual capital sum assured.	In case of a policy issued on or after 1.4.2012, the premium paid does not exceed 10% of the actual capital sum assured.	In case of a policy issued on or after 1.4.2013, the premium paid does not exceed 15% of the actual capital sum assured, if the insurance is on the life of a person with disability referred to in section 80U. In all other cases, the limit would be 10%.
	Any sum received under a Keyman insurance policy is, however, not exempt. Further, "keyman insurance policy" includes a policy which has been assigned to any person during its term, with or without consideration. Consequently, the sum received by the keyman on such policies would not be exempt under section 10(10D).		
10(18)	Pension received by individual who has been awarded "Param Vir Chakra" or "Maha Vir Chakra or such other gallantry award as the Central Government notifies is exempt from tax. Family pension received by any member of the family of such individual is also exempt from tax.		
10(23BBH)	Any income of the Prasar Bharati established under section 3(1) of the Prasar Bharati Act, 1990 is exempt from tax.		
10(26AAA)	Income from any source in the state of Sikkim, dividend income and interest on securities is exempt in the hands of a Sikkimese individual. This exemption is not available to a Sikkimese woman who, on or after 1 st April, 2008, marries a non-Sikkimese individual.		
10AA	<p>Tax holiday for newly established units in Special Economic Zones (SEZs), which has begun or begins to manufacture or produce articles or things or computer software or provide any service on or after 1.4.2005 in any SEZ for 15 consecutive assessment years in respect of its profits from exports.</p> <p>Amount of exemption = Profits from business of the undertaking being the unit ×</p> $\left(\frac{\text{Export turnover of the undertaking of such articles or things or computer software}}{\text{Total turnover of the business carried on by the undertaking}} \right)$		

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	100% of such profits would be exempt in the first five years, 50% in the next five years and in the last five years, 50% subject to transfer to special reserve.
11 to 13, 2(15) & 115BBC	<p>(i) Income derived from property held under trust wholly for public charitable or public religious purposes is exempt from tax under section 11 subject to fulfillment of the following conditions –</p> <ol style="list-style-type: none"> (1) the trust should be registered with the Commissioner of Income-tax under section 12AA; (2) the accounts of the trust should be audited, if the total income, before giving effect to the exemption under sections 11 and 12, exceeds the basic exemption limit; (3) atleast 85% of the income is applied for the approved purposes; and (4) the unapplied income and the money accumulated or set apart should be invested or deposited in the specified forms and modes. <p>(ii) <u>Charitable purpose [Section 2(15)]</u></p> <p>The definition of “charitable purpose” under section 2(15) includes relief of the poor, education, medical relief, preservation of environment (including watersheds, forests and wildlife) and preservation of monuments or places or objects of artistic or historic interest, and the advancement of any other object of general public utility.</p> <p>“Advancement of any other object of general public utility” shall, however, not be a charitable purpose, if it involves the carrying on of any activity in the nature of trade, commerce or business or any activity of rendering any service in relation to any trade, commerce or business, for a cess or fee or any other consideration, irrespective of the nature of use or application or retention, of the income from such activity.</p> <p>However, “advancement of any other object of general public utility” would continue to be a “charitable purpose”, if the total receipts from any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business does not exceed Rs. 25 lakh in relevant previous year.</p>

	(iii)	<p><u>Anonymous donations [Section 115BBC]</u></p> <p>Anonymous donations received by charitable trusts/institutions would be subject to tax@30% of the amount in excess of, 5% of the total donations received or Rs.1 lakh, whichever is higher, as per section 115BBC. The exemption provisions under section 11 and 12 would not apply to such anonymous donations.</p> <p>Section 115BBC does not, however, apply to a trust or institution created or established wholly for religious purposes.</p> <p>Further, anonymous donations received by partly charitable and partly religious trusts would be taxable under section 115BBC only if the same is made with a specific direction that such donation is for any university or other educational institution or any hospital or other medical institution run by such trust or institution.</p>
13A		<p>Any income from house property, income from other sources, capital gains and income by way of voluntary contributions received by the political parties from any person is exempt under section 13A, subject to satisfaction of the following conditions -</p> <p>(i) maintenance of such books and other documents as would enable the Assessing Officer to properly deduce the income of the political party;</p> <p>(ii) maintenance of record in respect of each such voluntary contribution in excess of Rs 20,000;</p> <p>(iii) audit of accounts by a chartered accountant; and</p> <p>(iv) submission of a report under section 29C(3) of the Representation of People Act, 1951 for every financial year.</p>

Question 1

State whether the following are chargeable to tax and the amount liable to tax:

- (i) Arvind received ₹ 20,000 as his share from the income of the HUF.
- (ii) Mr. Xavier, a 'Param Vir chakra' awardee, received a pension of ₹ 2,20,000 during the financial year 2013-14.
- (iii) A political party registered under section 29A of the Representation of the People Act, 1951 earned rental income of ₹ 6,00,000 by letting out premises.
- (iv) Agricultural income to a resident of India from a land situated in Malaysia.

3.5 Income-tax

(v) Allowance received by an employee working in a transport system at ₹ 10,000 per month to meet his personal expenditure while in duty. He is not receiving any daily allowance.

(vi) Amount withdrawn from Public Provident Fund as per relevant rules.

Answer

S.No.	Taxable/Not Taxable	Amount liable to tax (₹)	Reason
(i)	Not Taxable	-	Share received by member out of the income of the HUF is exempt under section 10(2).
(ii)	Not Taxable	-	Pension received by Mr. Xavier, who is a 'Param Vir Chakra' awardee, is exempt under section 10(18).
(iii)	Not Taxable	-	Any income of a political party registered under section 29A of the Representation of the People Act, 1951 which is chargeable, <i>inter alia</i> , under the head "Income from house property" is exempt under section 13A provided the political party maintains such books of account as would enable the Assessing Officer to properly deduce its income therefrom and the accounts are audited by a chartered accountant.
(iv)	Taxable	-	Agricultural income from a land in any foreign country is taxable in the case of a resident taxpayer as income under the head "Income from other sources". Exemption under section 10(1) is not available in respect of such income.
(v)	Partly taxable	36,000	Under section 10(14), any allowance granted to an employee working in a transport system to meet his personal expenditure during his duty is exempt, provided he is not in receipt of daily allowance. The exemption is 70% of such allowance (i.e., ₹ 7,000 per month, being 70% of ₹ 10,000) or ₹ 10,000 per month, whichever is less. Hence, ₹ 84,000 (i.e., ₹ 7,000 × 12) is allowable as deduction under section 10(14). Balance ₹ 36,000 (₹ 1,20,000 - ₹ 84,000) shall be taxable.
(vi)	Not taxable	-	Any amount withdrawn from public provident fund as per relevant rules is not exigible to tax. Such exemption is provided in section 10(11).

Question 2

Discuss the taxability of agricultural income under the Income-tax Act, 1961. How will income be computed where an individual derives agricultural and non-agricultural income?

Answer

Agricultural income is exempt from tax as per section 10(1). However, aggregation of agricultural and non-agricultural income is to be done to determine the rate at which the non-agricultural income shall be chargeable to tax. In case the agricultural income is not more than ₹ 5,000 or the tax-payer has non-agricultural income less than the basic exemption limit, then no such aggregation needs to be done. Further, such aggregation has to be done only if the tax-payer is an individual, HUF, AOP, BOI or an artificial judicial person, since the Finance Act prescribes slab rates of income-tax for these assesseees. In the case of other assesseees such as partnership firms, companies etc, whose income is chargeable to tax at a flat rate, aggregation of agricultural income would have no effect.

Since the second part of the question requires the manner of computation of income where an individual derives agricultural and non-agricultural income, the same can be answered on the basis of Rules 7A, 7B and 8 of the Income-tax Rules, 1962 dealing with composite income.

Rule	Particulars	Business Income	Agricultural Income
Rule 7A	Income from manufacture of rubber in India	35%	65%
Rule 7B	Income from manufacture of coffee		
	- grown and cured by the seller in India	25%	75%
	- grown, cured, roasted and grounded by the seller in India	40%	60%
Rule 8	Income from manufacture of tea in India	40%	60%

Thereafter, income-tax shall be computed by aggregating the agricultural income and the non-agricultural income in the manner described below:

- (1) Aggregate the agricultural income with non-agricultural income and determine tax payable on such amount.
- (2) Aggregate the agricultural income with the basic exemption limit of the assessee i.e. ₹ 2,00,000 / ₹ 2,50,000 / ₹ 5,00,000, as the case may be, and determine tax on such amount.
- (3) Compute the difference between the tax computed in Step (1) and Step (2), which shall be the tax payable in respect of non-agricultural income.
- (4) The tax payable so computed in step (3) shall be increased by surcharge @10%, if the total income exceeds ₹ 1 crore or reduced by rebate under section 87A if the total income does not exceed ₹ 5 lakh. Thereafter, education cess of 2% and secondary and higher education cess of 1% has to be added to compute the total tax liability.

Question 3

Whether the income derived from saplings or seedlings grown in a nursery is taxable under the Income-tax Act, 1961?

Answer

As per *Explanation 3* to section 2(1A) of the Act, income derived from saplings or seedlings grown in a nursery shall be deemed to be agricultural income and exempt from tax, whether or not the basic operations were carried out on land.

Question 4

State with reasons in brief whether the following statements are true or false with reference to the provisions of the Income-tax Act, 1961:

- (i) Exemption is available to a Sikkimese individual, only in respect of income from any source in the State of Sikkim.*
- (ii) Where the Commissioner of Income-tax is satisfied that the activities of the charitable trust, which has been accorded registration, is not genuine, he can cancel the registration by passing an order in writing.*
- (iii) In respect of voluntary contributions in excess of ₹ 20,000 received by a political party, exemption under section 13A is available where proper details about the donations are maintained; there is no need to maintain books of account.*
- (iv) Pension received by a recipient of gallantry award is exempt from income-tax.*
- (v) Mr. A, a member of a HUF, received ₹ 10,000 as his share from the income of the HUF. The same is to be included in his chargeable income.*
- (vi) Mr. Roy received a sum of ₹ 20 lakh on 31.3.2014 from Life Insurance Corporation of India in respect of a policy, where the sum assured was ₹ 15 lakh, taken on 1.10.2003 and for which a one time premium of ₹ 10 lakh was paid. Mr. Roy claims that the amount is totally exempt under section 10(10D)(c) of the Income-tax Act, 1961.*
- (vii) Voluntary contributions received by charitable trusts, universities and educational institutions are not taxable as the definition of income in section 2(24) does not cover the same.*
- (viii) Compensation on account of disaster received from a local authority by an individual or his/her legal heir is taxable.*
- (ix) Mr. P, a shareholder of a closely held company, holding 16% shares, received advances from that company which is to be deemed as dividend from an Indian Company, hence exempted under section 10(34) of the Income-tax Act, 1961.*

Answer

- (i) False** : Exemption under section 10(26AAA) is available to a Sikkimese individual not only in respect of the said income, but also in respect of income by way of dividend or interest on securities.

- (ii) **True:** As per section 12AA(3), the Commissioner has power to cancel the registration of the trust, by passing a written order, where he is satisfied, *inter alia*, that the activities of the trust are not genuine. However, the trust should be given a reasonable opportunity of being heard before such cancellation.
- (iii) **False:** The obligation under section 13A to maintain proper details of voluntary contributions in excess of ₹ 20,000 is over and above the obligation to maintain such books of account and other documents as would enable the Assessing Officer to properly deduce its income therefrom.
- (iv) **True:** Section 10(18) exempts any income by way of pension received by individual who has been awarded "Param Vir Chakra" or "Maha Vir Chakra" or "Vir Chakra" or such other gallantry award as the Central Government, may, by notification in the Official Gazette, specify in this behalf.
- (v) **False:** Section 10(2) exempts any sum received by an individual as a member of a HUF where such sum has been paid out of the income of the family. Therefore, ₹ 10,000 should not be included in Mr.A's chargeable income.
- (vi) **False:** As per section 10(10D)(c), any sum received under an insurance policy issued on or after 1.4.2003 but before 31.03.2012, in respect of which the premium payable for any year during the term of the policy exceeds 20% of actual capital sum assured, shall not be exempt from tax. Hence, the contention of Mr. Roy is not correct since the one-time premium of ₹ 10 lakh paid by him is in excess of 20% of the sum assured [i.e. it exceeds ₹ 3 lakh, being 20% of ₹ 15 lakh].
- (vii) **False:** Section 2(24) defining the term 'income' includes voluntary contributions received by any trust, university or educational institution. Hence, the statement is not correct.
- (viii) **False :** As per section 10(10BC), any amount received or receivable as compensation by an individual or his/her legal heir on account of any disaster from the Central Government, State Government or a local authority is exempt from tax. However, the exemption is not available to the extent such individual or legal heir has already been allowed a deduction under this Act on account of such loss or damage caused by such disaster.
- (ix) **False :** As per section 10(34), only income by way of dividend referred to in section 115-O shall be exempt in the hands of shareholders. Corporate dividend tax under section 115-O is not leviable on deemed dividend under section 2(22)(e) and hence, such deemed dividend is not exempt under section 10(34).

Question 5

Explain the provisions regarding exemption of compensation received on account of disaster under section 10(10BC) of the Income-tax Act, 1961.

Answer

Exemption of compensation received on account of disaster under section 10(10BC)

- (i) Section 10(10BC) exempts any amount received or receivable as compensation by an individual or his / her legal heir on account of any disaster.
- (ii) Such compensation should be granted by the Central or State Government or by a local authority.

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- (iii) Exemption would not be available in respect of the compensation for alleviating any damage or loss, which has already been allowed as deduction under the Act.
- (iv) "Disaster" means a catastrophe, mishap, calamity or grave occurrence in any area, arising from natural or man made causes, or by accident or negligence.
- (v) It should have the effect of causing substantial loss of life or human suffering, or damage to, and destruction of, property, or damage to, or degradation of, environment.
- (vi) It should be of such a nature or magnitude, which is beyond the coping capacity of the community of the affected area.

Question 6

Mr. A is a resident Indian. During the F.Y. 2013-14, interest of ₹ 1,92,000 was credited to his Non-resident (External) Account with the SBI. ₹ 20,000 being interest on fixed deposit with SBI was credited to his savings bank account during this period. He also earned ₹ 4,000 as interest on this savings account. Is Mr. A required to file return of income?

What will be your answer, if he owns one shop in Mumbai of area 130 sq.ft. ?

Answer

Computation of total income of Mr. A for A.Y. 2014-15

Particulars	₹
Income from other sources	
Interest earned from Non-resident (External) Account ₹ 1,92,000 [Exempt under section 10(4)(ii), assuming that Mr. A has been permitted by RBI to maintain the aforesaid account]	Nil
Interest on bank fixed deposit	20,000
Interest on savings bank account	4,000
Gross Total Income	24,000
<i>Less:</i> Deduction under section 80TTA – Interest on saving bank account	4,000
Total Income	20,000

An Individual is required to furnish a return of income under section 139(1) if his total income exceeds the maximum amount not chargeable to tax i.e. ₹ 2,00,000 (for A.Y. 2014-15). Hence, Mr. A is not required to file a return of income as his total income is below ₹ 2,00,000.

The aspect of Mr. A occupying / owning a shop area of 130 sq.ft in Mumbai, would not make any difference.

Question 7

Nathan Aviation Ltd. is running two industrial undertakings one in a SEZ (Unit S) and another in a normal area (Unit N). The brief summarized details for the year ended 31.3.2014 are as follows:

Particulars	₹ (in lacs)	
	S	N
Domestic turnover	10	100
Export turnover	120	Nil
Gross profit	20	10
Less: Expenses and depreciation	7	6
Profits derived from the unit	13	4

The brought forward business loss pertaining to Unit N is ₹ 2 lacs. Briefly compute the business income of the assessee.

Assume F.Y. 2013-14 falls within the first 5 year period commencing from the year of manufacture or production of articles or things or provisions of services by the Unit S.

Answer

Computation of business income of Nathan Aviation Ltd.

Particulars	₹ (in lacs)
Total profit derived from Units S & N (₹ 13 lacs + ₹ 4 lacs)	17
Less: Exemption under section 10AA [See Working Note below]	<u>12</u>
	5
Less: Brought forward business loss	<u>2</u>
	<u>3</u>

Working Note

Computation of exemption under section 10AA in respect of Unit S located in a SEZ

Particulars	₹ (in lacs)
Domestic turnover of Unit S	10
Export turnover of Unit S	<u>120</u>
Total turnover of Unit S	<u>130</u>
Profit derived from Unit S	13
Exemption under section 10AA	
Profit of Unit S x $\frac{\text{Export turnover of unit S}}{\text{Total turnover of Unit S}} = 13 \times \frac{120}{130} =$	12

Question 8

Y Co. Ltd. furnishes you the following information for the year ended 31.3.2014:

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<i>Particulars</i>	<i>₹ (in lacs)</i>
<i>Total turnover of Unit A located in Special Economic Zone</i>	100
<i>Profit of the business of Unit A</i>	30
<i>Export turnover of Unit A</i>	50
<i>Total turnover of Unit B located in Domestic Tariff Area (DTA)</i>	200
<i>Profit of the business of Unit B</i>	20

Compute deduction under section 10AA for the A.Y. 2014-15.

Answer

100% of the profit derived from export of articles or things or services is eligible for deduction under section 10AA, assuming that F.Y.2013-14 falls within the first five year period commencing from the year of manufacture or production of articles or things or provision of services by the Unit in SEZ. As per section 10AA(7), the profit derived from export of articles or things or services shall be the amount which bears to the profits of the business of the undertaking, being the Unit, the same proportion as the export turnover in respect of articles or things or services bears to the total turnover of the business carried on by the undertaking.

Deduction under section 10AA

$$\begin{aligned}
 &= \text{Profit of the business of Unit A} \times \frac{\text{Export Turnover of Unit A}}{\text{Total Turnover of Unit A}} \\
 &= ₹ 30 \text{ lakhs} \times \frac{50}{100} \\
 &= ₹ 15 \text{ lakhs}
 \end{aligned}$$

Question 9

MNO Ltd. has one undertaking at Special Economic Zone (SEZ) and another at Domestic Tariff Area (DTA). Following are the details given to you for the financial year 2013-14:

	<i>₹ in lakhs</i>	
	<i>Unit in SEZ</i>	<i>Unit in Domestic Tariff Area (DTA)</i>
<i>Total Sales</i>	200	100
<i>Export Sales</i>	150	80
<i>Net Profit</i>	40	10

Compute the quantum of eligible deduction under section 10AA for the assessment year 2014-15 in the following situations:

- (i) Both the units were set up and began manufacturing from 25-07-2006.
- (ii) Both the units were set up and began manufacturing from 10-04-2010

Answer

As per section 10AA, in computing the total income of MNO Ltd. from its unit located in a Special Economic Zone (SEZ), which begins to manufacture or produce any article or thing on or after 1.04.2005, there shall be allowed a deduction of 100% of the profit derived from export of such article or thing for the first five year period commencing from the year of manufacture or production of articles or things by the Unit in SEZ and 50% of such profits for further five years subject to fulfillment of other conditions specified in section 10AA.

(i) If Unit in SEZ were set up and began manufacturing from 25-07-2006:

Since it is the 8th year of operation of the eligible unit, it shall be eligible for deduction upto 50% of the profit of such unit assuming all the other conditions specified in section 10AA are fulfilled.

$$\begin{aligned}
 &= \text{Profits of Unit in SEZ} \quad \times \quad \frac{\text{Export turnover of Unit in SEZ}}{\text{Total turnover of Unit in SEZ}} \quad \times 50\% \\
 &= 40 \text{ lakhs} \quad \times \quad \frac{150 \text{ lakhs}}{200 \text{ lakhs}} \quad \times 50\% \quad = 15 \text{ lakhs}
 \end{aligned}$$

(ii) If Unit in SEZ were set up and began manufacturing from 10.04.2010:

Since it is 4th year of operation of the eligible unit, it shall be eligible for deduction upto 100% of profit of such unit.

$$\begin{aligned}
 &= \text{Profits of Unit in SEZ} \quad \times \quad \frac{\text{Export turnover of Unit in SEZ}}{\text{Total turnover of Unit in SEZ}} \quad \times 100\% \\
 &= 40 \text{ lakhs} \quad \times \quad \frac{150 \text{ lakhs}}{200 \text{ lakhs}} \quad \times 100\% \quad = 30 \text{ lakhs}
 \end{aligned}$$

Question 10

Will a charitable trust be forfeited of tax exemption granted to it, if it holds shares in public sector company? Will a charitable trust having business receipt and income of ₹ 20,00,000 and ₹ 2,00,000, respectively, be denied the tax exemption?

Answer

- (i) Since investment or deposit in a public sector company is one of the permitted modes of investment mentioned in section 11(5), the exemption granted to a charitable trust under section 11 will not be forfeited if it holds shares in a public sector company.
- (ii) As per section 11(4), "property held under trust" includes a business undertaking so held. If the object of the trust is relief of the poor, education, medical relief etc. (other than advancement of any other object of general public utility) and the trust has a business undertaking, then, the income from such business would also be exempt from tax provided the following conditions, as mentioned in section 11(4A) are satisfied :
 - (a) such business is incidental to the attainment of the objects of the trust; and

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- (b) separate books of accounts are maintained by such trust in respect of such business.
- (iii) Even if the main object of the charitable trust is "advancement of any other object of general public utility", tax exemption will not be denied in this case since the aggregate receipts from business has not exceeded ₹ 25 lakhs in the year.

Question 11

What are the conditions to be fulfilled by a Charitable Trust under section 12A for applicability of exemption provisions contained in sections 11 and 12?

Answer

Conditions for applicability of sections 11 and 12 [Section 12A]

The exemption provisions contained in sections 11 and 12 shall not apply in relation to the income of any trust or institution unless the following conditions are fulfilled-

- (i) An application for registration of the trust or institution in the prescribed form and in the prescribed manner should be made to the Commissioner and the trust or institution should be registered under section 12AA.
- (ii) The requirement of filing an application for registration within one year of creation of the religious or charitable trust or institution has been removed. The application can be filed at any time now.
- (iii) Accordingly, in respect of applications made on or after 1st June, 2007, the provisions of sections 11 and 12 shall apply from the assessment year relevant to the financial year in which the application is made i.e. the exemption would be available only with effect from the assessment year relevant to the previous year in which the application is filed. It would not be available in respect of any earlier assessment year.
- (iv) Where the total income of the trust or institution, without giving effect to the provisions of sections 11 and 12, exceeds the maximum amount which is not chargeable to income-tax in any previous year, the accounts of the trust or institution must be audited by a chartered accountant and the report of such audit in the prescribed form duly signed and verified by such accountant setting forth such prescribed particulars, should be furnished along with the return of income.

Question 12

Explain the meaning of expression "advancement of any other object of general public utility" in the context of "Charitable Purpose" defined under section 2(15) of the Act. Discuss its tax implication as well.

Answer

The expression "advancement of any other object of general public utility" includes any object which will be beneficial even to a segment of society and not necessarily to the whole mankind. However, the object should not be for the benefit of specified individuals.

The proviso to section 2(15) of the Act provides that "advancement of any other object of general public utility" shall not be a charitable purpose, if it involves carrying on of -

- (i) any activity in the nature of trade, commerce or business, or
- (ii) any activity of rendering of any service in relation to any trade, commerce or business, for a cess or fee or any other consideration, irrespective of the nature of use or application of the income from such activity or the retention of such income, by the concerned entity. However, "advancement of any other object of general public utility" would continue to be a "charitable purpose", if the total receipts from any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business does not exceed ₹ 25 lakh in the previous year.

Question 13

Can a political party claim exemption of its income under section 13A of the Income-tax Act, 1961?

Answer

Under section 13A, a political party registered under section 29A of the Representation of the People Act, 1951, can claim exemption under the following heads - Income from house property, capital gains and income from other sources. Income by way of voluntary contributions received by such political party is also exempt under section 13A.

These exemptions are subject to the following conditions:-

- (i) The political party must keep and maintain such books of account and other documents as would enable the Assessing Officer to properly deduce its income therefrom.
- (ii) The political party should keep and maintain a record of each such voluntary contribution in excess of ₹ 20,000 and the names and addresses of such contributors, the date of receipt and such other details as may be relevant or appropriate.
- (iii) The accounts of the political party must be audited by a chartered accountant.
- (iv) A report under section 29C(3) of the Representation of People Act, 1951 has to be submitted by the treasurer of such political party or any other person authorised by the political party in this behalf for every financial year.

EXERCISES

1. The maximum ceiling limit for exemption under section 10(10) in respect of gratuity for employees covered by the Payment of Gratuity Act, 1972 is -
 - a) 3,50,000
 - b) 10,00,000
 - c) 5,00,000

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2. The maximum ceiling limit for exemption under section 10(10C) with respect to compensation received on voluntary retirement is -
 - a) 3,00,000
 - b) 3,50,000
 - c) 5,00,000
3. The HRA paid to an employee residing in Patna is exempt up to the lower of actual HRA, excess of rent paid over 10% of salary and -
 - a) 40% of salary
 - b) 50% of salary
 - c) 60% of salary
4. Anirudh stays in New Delhi. His basic salary is ₹ 10,000 p.m., D.A. (60% of which forms part of pay) is 6,000 p.m., HRA is ₹ 5,000 p.m. and he is entitled to a commission of 1% on the turnover achieved by him. Anirudh pays a rent of ₹ 5,500 p.m. The turnover achieved by him during the current year is 12 lakhs. The amount of HRA exempt under section 10(13A) is -
 - a) ₹ 48,480
 - b) ₹ 45,600
 - c) ₹ 49,680
5. In case of a trade union registered under the Trade Unions Act, 1926 formed for regulating relations between workmen and employers or between workmen and workmen, the following incomes are exempt from tax -
 - a) Capital gains and Income from other sources.
 - b) Income from house property and capital gains.
 - c) Income from house property and income from other sources.
6. Voluntary contributions received by electoral trusts during the P.Y.2013-14 is -
 - a) Fully taxable
 - b) Fully exempt from tax
 - c) Exempt only if the trust distributes to a registered political party during the year, 95% of the aggregate donations received by it
7. The income derived from property held under trust wholly for charitable or religious purpose is exempt from tax under section 11 subject to fulfillment of certain conditions. One of the conditions is that -
 - a) At least 75% of the income is required to be applied for the approved purposes.
 - b) At least 85% of the income is required to be applied for the approved purposes.

- c) The entire income is required to be applied for the approved purposes.
8. Income by way of voluntary contributions of political parties is exempt provided -
- a) the political party keeps and maintains a record of each such voluntary contribution in excess of ₹ 10,000 and of the name and address of the person who made such contribution;
 - b) the political party keeps and maintains a record of each such voluntary contribution in excess of ₹ 20,000 and of the name and address of the person who made such contribution;
 - c) the political party keeps and maintains a record of each such voluntary contribution in excess of ₹ 30,000 and of the name and address of the person who made such contribution;
9. (a) Discuss the exemption available under the Income-tax Act in respect of specified income arising from any international sporting event in India.
- (b) What are the exemptions available under section 10 in respect of companies engaged in the business of generation or transmission or distribution of power and subsidiaries of such companies? What are the conditions to be fulfilled to avail such exemptions?
10. When can a charitable trust avail benefits under section 11 & 12 of the Income-tax Act, 1961?
11. Write short notes on:
- (i) Exemption for retrenchment compensation under section 10(10B).
 - (ii) Exceptions under section 10(10D) as regards exemption of any sum received under a life insurance policy.
 - (iii) 'Encashment of Earned Leave' and its taxability under the Act.
12. State the provisions relating to the exemption in respect of long-term capital gains on transfer of listed equity shares.

Answers

1. b; 2. c; 3. a; 4. a; 5. c; 6. c; 7. b; 8. b

4

UNIT 1 : Income From Salaries

Key Points		
Basis of Charge [Section 15]		
(i)	Salary is chargeable to tax either on 'due' basis or on 'receipt' basis, whichever is earlier.	
(ii)	However, where any salary, paid in advance, is assessed in the year of payment, it cannot be subsequently brought to tax in the year in which it becomes due.	
(iii)	If the salary paid in arrears has already been assessed on due basis, the same cannot be taxed again when it is paid.	
Taxability/Exemption of certain Allowances		
Section	Allowance	Exemption
10(13A)	House Rent Allowance	Least of the following is exempt:
		(a) HRA actually received
		(b) Rent paid <i>less</i> 10% of salary
		(c) 50% of salary, if accommodation is located in Mumbai, Kolkata, Delhi or Chennai 40% of salary, if the accommodation is located in any other city.
10(14)(ii)	Children education allowance	₹ 100 per month per child upto maximum of two children
	Transport allowance for commuting between the place of residence and the place of duty.	₹ 800 per month (₹ 1,600 per month for an employee who is blind or handicapped)
	Hostel expenditure of employee's children	₹ 300 per month per child up to a maximum of two children

Exemption of Terminal Benefits			
Section	Component of salary	Category of employee	Particulars [Taxability / Exemption under section 10]
10(10)	Gratuity	Government	Fully exempt u/s 10(10)(i)
		Non-Government	Least of the following is exempt :
			(i) ₹ 10 lacs
			(ii) Gratuity actually received
(iii) <u>In case of employees covered by the Payment of Gratuity Act, 1972</u> 15/26 x last drawn salary x number of completed years or part in excess of six months <u>In case of employees not covered by the Payment of Gratuity Act, 1972</u> 1/2 x average salary of last 10 months x number of completed years of service (fraction to be ignored).			
10(10A)	Pension		
	Uncommuted pension	Government & Non-Government	Fully taxable.
	Commuted pension	Government/ local authorities/ statutory corporation/ members of Civil services / All-India services / Defence Services.	Fully exempt under section 10(10A)(i)
		Other Employees	<u>If the employee is in receipt of gratuity</u> The amount exempt would be one-third of the amount of commuted pension which he would have received had he commuted his entire pension. <u>If the employee is not in receipt of gratuity</u> The amount exempt would be one-half of the amount of commuted pension which he would have received had he commuted his entire pension.

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10(10AA)	Leave Salary			
	Received during service	Government & Non-Government	Fully taxable	
	Received at the time of retirement, (whether on superannuation or otherwise)	Government	Fully exempt (at the time of retirement)	
		Non-Government	Least of the following is exempt :	
			(i)	₹ 3,00,000
(ii)			Leave salary actually received	
(iii)	Cash equivalent of leave standing at the credit of the employee [based on average salary of last 10 months] (maximum 30 days for every year of service)			
		(iv)	10 months salary (based on average salary of last 10 months)	
10(10B)	Retrenchment Compensation		Least of the following is exempt :	
			(i)	Compensation actually received.
			(ii)	₹ 5,00,000
			(iii)	$15/26 \times \text{Average salary of last 3 months} \times \text{Completed years of service and part thereof in excess of 6 months}$
10(10C)	Voluntary Retirement Compensation	Central and State Government, Public sector company, any other company, local authority, co-operative society, IIT etc.	Least of the following is exempt :	
			(i)	Compensation actually received
			(ii)	₹ 5,00,000
			(iii)	Last drawn salary x 3 months x completed years of service
		(iv)	Last drawn salary x remaining months of service	

Section 10(5) [Leave Travel Concession]				
Exemption is available for 2 trips in a block of 4 calendar years.				
S. No.	Journey performed by	Exemption		
1	Air	Amount not exceeding air economy fare by the shortest route.		
2	Any other mode :			
	(i) Where rail service is available	Amount not exceeding air conditioned first class rail fare by the shortest route.		
	(ii) Where rail service is not available			
	a) and public transport does not exist	Amount equivalent to air conditioned first class rail fares by the shortest route		
	b) but public transport exists.	Amount not exceeding the first class or deluxe class fare by the shortest route.		
Provident Funds - Exemption & Taxability provisions				
Particulars	Recognized PF	Unrecognized PF	Statutory PF	Public PF
Employer's Contribution	Amount in excess of 12% of salary is taxable	Not taxable yearly	Fully exempt	N.A.
Employee's Contribution	Eligible for deduction u/s 80C	Not eligible for deduction	Eligible for deduction u/s 80C	Eligible for deduction u/s 80C
Interest Credited	Amount in excess of 9.5% p.a. is taxable	Not taxable yearly	Fully exempt	Fully exempt
Amount received on retirement, etc.	Exempt from tax if employee served a continuous period of 5 years or more or retires before rendering 5 years of service because of reason beyond the control of the employee. In other case, it will be taxable.	Employer's contribution and interest thereon is taxable as salary. Employee's contribution is not taxable. Interest on employee's contribution is taxable under income from other source.	Fully exempt u/s 10(11)	Fully exempt u/s 10(11)

Valuation of Perquisites [Section 17(2) read with Rule 3]											
(A) Rent-free residential accommodation											
S. No. (A)	Category of Employee (B)	Unfurnished accommodation (C)	Furnished accommodation (D)								
1	Government employee	License fee determined as per government rules as reduced by the rent actually paid by the employee.	Value determined under column (C) <i>Add:</i> 10% p.a. of the furniture cost. However, if the furniture is hired, then hire charges payable/paid should be added to the value determined under column (C), as reduced by charges recovered from employee.								
2	Non-government employee	<p>Where accommodation is owned by employer</p> <table border="1"> <thead> <tr> <th>Location</th> <th>Perquisite value</th> </tr> </thead> <tbody> <tr> <td>In cities having a population > 25 lacs as per 2001 census.</td> <td>15% of salary</td> </tr> <tr> <td>In cities having a population > 10 lacs ≤ 25 lacs as per 2001 census.</td> <td>10% of salary</td> </tr> <tr> <td>In other areas</td> <td>7.5% of salary</td> </tr> </tbody> </table> <p>The perquisite value should be arrived at by reducing the rent, if any, actually paid by the employee, from the above value.</p>	Location	Perquisite value	In cities having a population > 25 lacs as per 2001 census.	15% of salary	In cities having a population > 10 lacs ≤ 25 lacs as per 2001 census.	10% of salary	In other areas	7.5% of salary	Value determined under column (C) <i>Add:</i> 10% p.a. of the furniture cost. However, if the furniture is hired, then hire charges payable/paid should be added to the value determined under column (C), as reduced by charges recovered from employee.
Location	Perquisite value										
In cities having a population > 25 lacs as per 2001 census.	15% of salary										
In cities having a population > 10 lacs ≤ 25 lacs as per 2001 census.	10% of salary										
In other areas	7.5% of salary										

	<p><u>Where the accommodation is taken on lease or rent by employer</u></p> <p>Lower of the following is taxable:</p> <p>(a) actual amount of lease rent paid or payable by employer or</p> <p>(b) 15% of salary</p> <p>The lower of the above should be reduced by the rent, actually paid by the employee, to arrive at the perquisite value.</p>	<p>Value determined under column (C)</p> <p><i>Add:</i> 10% p.a. of the furniture cost.</p> <p>However, if the furniture is hired, then hire charges payable/paid should be added to the value determined under column (C), as reduced by charges recovered from employee.</p>
<p>(B) Interest free or concessional loan</p> <p>In respect of any loan given by employer to employee or any member of his household (excluding for medical treatment for specified ailments or where loans amount in aggregate does not exceed ₹ 20,000), the interest at the rate charged by SBI as on the first day of the relevant previous year at maximum outstanding monthly balance (aggregate outstanding balance for each loan as on the last day of each month) as reduced by the interest, if any, actually paid by him or any member of his household.</p>		
<p>(D) Use of movable assets by employee/ any member of his household</p>		
(i)	10% p.a. of actual cost of asset owned by the employer or the amount of hire charges incurred by the employer for the asset hired would be the perquisite value.	
(ii)	There would, however, be no perquisite for use of laptops and computers.	
<p>(E) Transfer of movable assets</p> <p>Perquisite value would be the depreciated value of the asset computed by applying the rates of depreciation mentioned in the following table, as reduced by any amount paid by or recovered from the employee.</p>		
S. No.	Assets	Rate of depreciation
1	Computers and electronic items	50% of WDV for each completed year of usage
2	Motor cars	20% of WDV for each completed year of usage
3	Other assets	10% on SLM for each completed year of usage

4.7 Income-tax

(F) Motor car						
S. No.	Car owned/hired by	Expense s met by	Wholly official use	Wholly personal use	Partly personal use	
					Cc of engine	Perquisite value
1	Employer	Employer	Not a perquisite	Running and maintenance expenses, wear and tear or hire charges, driver salary less amount charged from the employee for such use.	upto 1.6 litres	₹ 1,800 p.m.
					above 1.6 litres	₹ 2,400 p.m.
					If chauffeur is also provided, ₹ 900 p.m should be added to the above value.	
2	Employee	Employer	Not a perquisite	Actual amount of expenditure incurred.	Actual amount of expenditure incurred by the employer as reduced by the perquisite value arrived at in (2) above.	
3	Employer	Employee	Not a perquisite	Wear and tear or hire charges, driver salary.	Cc of engine	Perquisite value
					upto 1.6 litres	₹ 600 p.m.
					above 1.6 litres	₹ 900 p.m.
				If chauffeur is also provided, ₹ 900 p.m should be added to the above value.		

Meaning of Salary:												
S. No.	Calculation of exemption of Allowance / Terminal benefit / Valuation of perquisite	Meaning of salary										
1	Gratuity (in case of non-Government employees covered by the Payment of Gratuity Act, 1972)	Basic salary and dearness allowance.										
2	<table border="1"> <tr> <td>a)</td> <td>Gratuity (in case of non-Government employee not covered by Payment of Gratuity Act, 1972)</td> </tr> <tr> <td>b)</td> <td>Leave Salary</td> </tr> <tr> <td>c)</td> <td>House Rent Allowance</td> </tr> <tr> <td>d)</td> <td>Recognized Provident Fund</td> </tr> <tr> <td>e)</td> <td>Voluntary Retirement Compensation</td> </tr> </table>	a)	Gratuity (in case of non-Government employee not covered by Payment of Gratuity Act, 1972)	b)	Leave Salary	c)	House Rent Allowance	d)	Recognized Provident Fund	e)	Voluntary Retirement Compensation	Basic salary and dearness allowance, if provided in terms of employment, and commission calculated as a fixed percentage of turnover.
a)	Gratuity (in case of non-Government employee not covered by Payment of Gratuity Act, 1972)											
b)	Leave Salary											
c)	House Rent Allowance											
d)	Recognized Provident Fund											
e)	Voluntary Retirement Compensation											
3	Rent free accommodation and concessional accommodation	<p>All pay, allowance, bonus or commission or any monetary payment by whatever name called but excludes-</p> <ol style="list-style-type: none"> (1) Dearness allowance not forming part of computation of superannuation or retirement benefit (2) employer's contribution to the provident fund account of the employee; (3) allowances which are exempted from the payment of tax; (4) value of the perquisites specified in section 17(2); (5) any payment or expenditure specifically excluded under the proviso to section 17(2) i.e., medical expenditure/payment of medical insurance premium specified therein. (6) lump-sum payments received at the time of termination or service or superannuation or voluntary retirement. 										

4.9 Income-tax

Deductions from gross salary [Section 16]	
(1)	Entertainment allowance (allowable only in the case of government employees) [Section 16(ii)]
	Least of the following is allowed as deduction:
(1)	₹ 5,000
(2)	1/5 th of basic salary
(3)	Actual entertainment allowance received
(2)	Profession tax [Section 16(iii)] Any sum paid by the assessee on account of tax on employment is allowable as deduction. In case profession tax is paid by employer on behalf of employee, the amount paid shall be included in gross salary as a perquisite and then deduction can be claimed.
Relief when salary is paid in arrears or in advance [Section 89]	
Step 1	Calculate tax payable of the previous year in which the arrears/advance salary is received by considering:
(a)	Total Income inclusive of additional salary
(b)	Total Income exclusive of additional salary
Step 2	Compute the difference the tax calculated in Step 1 and Step 2 i.e., (a) – (b)
Step 3	Calculate the tax payable of every previous year to which the additional salary relates:
(a)	On total income including additional salary of that particular previous year
(b)	On total income excluding additional salary.
Step 4	Calculate the difference between (a) and (b) in Step 3 for every previous year to which the additional salary relates and aggregate the same.
Step 5	Relief u/s 89(1) = Amount calculated in Step 2 – Amount calculated in Step 4

Question 1

Mr. Harish, aged 52 years, is the Production Manager of XYZ Ltd. From the following details, compute the taxable income for the assessment year 2014-15.

Basic salary	₹ 50,000 per month
Dearness allowance	40% of basic salary
Transport allowance (for commuting between place of residence and office)	₹ 3,000 per month
Motor car running and maintenance charges fully paid by employer (The motor car is owned by the company and driven by the employee. The engine cubic capacity is above 1.60 litres. The motor car is used for both official and personal purpose by the employee.)	₹ 60,000
Expenditure on accommodation in hotels while touring on official duties met by the employer	₹ 80,000
Loan from recognized provident fund (maintained by the employer)	₹ 60,000
Lunch provided by the employer during office hours.	
Cost to the employer	₹ 24,000
Computer (cost ₹ 35,000) kept by the employer in the residence of Mr. Harish from 1.06.2013	
Mr. Harish made the following payments:	
Medical insurance premium: Paid in Cash	₹ 4,800
Paid by account payee crossed cheque	₹ 15,200

Answer

Computation of taxable income of Mr. Harish for the A.Y.2014-15

Particulars	₹	₹
Basic salary (₹ 50,000 x 12)		6,00,000
Dearness allowance @ 40% of basic salary		2,40,000
Transport allowance (₹ 3,000 x 12)	36,000	
Less : Exemption under section 10(14) (₹ 800 x 12)	<u>9,600</u>	26,400
Motor car running & maintenance charges paid by employer (See Note-1)		28,800
Expenditure on accommodation in hotels while touring on official duty is not a perquisite in the hands of employee and hence not chargeable to tax		Nil
Loan from recognized provident fund – not chargeable to tax		Nil

4.11 Income-tax

Value of lunch provided during office hours	24,000	
Less: Exempt under Rule 3(7)(iii) (See Note-2)	<u>15,000</u>	9,000
Computer provided in the residence of employee by the employer – not chargeable to tax [Rule 3(7)(vii)]		<u>Nil</u>
Gross Salary		9,04,200
Less : Deduction under Chapter VI-A		
Deduction under section 80D in respect of medical insurance premium paid by cheque amounting to ₹ 15,200 but restricted to ₹15,000 (See Note-3)		<u>15,000</u>
Taxable income		<u>8,89,200</u>

Notes:

- As per Rule 3(2), if the motor car (whose engine cubic capacity is above 1.60 litres) is owned by the employer and is used for both official and personal purpose by the employee, then, the value of perquisite for use of motor car would be ₹ 2,400 per month.
Therefore value of perquisite for use of motor car would be ₹ 2,400 x 12 = ₹ 28,800
- As per Rule 3(7)(iii), lunch provided by the employer during office hours is not considered as perquisite upto ₹ 50 per meal. Since, the number of working days is not given in the question, it is assumed to be 300 days during the F.Y. 2013-14. Therefore, ₹ 15,000 (i.e. 300 x ₹ 50) would be exempt and the balance ₹ 9,000 (i.e. ₹ 24,000 - ₹ 15,000) would be taxable.
- Medical insurance premium paid in cash of ₹ 4,800 is not allowable as deduction under section 80D. Further, deduction for medical insurance premium paid through cheque is restricted to ₹ 15,000, which is the maximum deduction allowable.

Question 2

Mr. Balaji, employed as Production Manager in Beta Ltd., furnishes you the following information for the year ended 31.03.2014:

- Basic salary upto 31.10.2013 ₹ 50,000 p.m.
Basic salary from 01.11.2013 ₹ 60,000 p.m.
Note: Salary is due and paid on the last day of every month.
- Dearness allowance @ 40% of basic salary.
- Bonus equal to one month salary. Paid in October 2013 on basic salary plus dearness allowance applicable for that month.
- Contribution of employer to recognized provident fund account of the employee @ 16% of basic salary.
- Profession tax paid ₹ 3,000 of which ₹ 2,000 was paid by the employer.

(vi) Facility of laptop and computer was provided to Balaji for both official and personal use. Cost of laptop ₹ 45,000 and computer ₹ 35,000 were acquired by the company on 01.12.2013.

(vii) Motor car owned by the employer (cubic capacity of engine exceeds 1.60 litres) provided to the employee from 01.11.2013 meant for both official and personal use. Repair and running expenses of ₹ 45,000 from 01.11.2013 to 31.03.2014, were fully met by the employer. The motor car was self-driven by the employee.

(viii) Leave travel concession given to employee, his wife and three children (one daughter aged 7 and twin sons aged 3). Cost of air tickets (economy class) reimbursed by the employer ₹ 30,000 for adults and ₹ 45,000 for three children. Balaji is eligible for availing exemption this year to the extent it is permissible in law.

Compute the salary income chargeable to tax in the hands of Mr. Balaji for the assessment year 2014-15.

Answer

Computation of Taxable Salary of Mr. Balaji for A.Y. 2014-15

Particulars	₹
Basic salary [(₹ 50,000 × 7) + (₹ 60,000 × 5)]	6,50,000
Dearness Allowance (40% of basic salary)	2,60,000
Bonus (₹ 50,000 + 40% of ₹ 50,000) (See Note 1)	70,000
Employers contribution to recognised provident fund in excess of 12% of salary = 4% of ₹ 6,50,000 (See Note 4)	26,000
Professional tax paid by employer	2,000
Perquisite of Motor Car (₹ 2,400 for 5 months) (See Note 5)	<u>12,000</u>
Gross Salary	10,20,000
Less: Deduction under section 16	
Professional tax (See Note 6)	<u>3,000</u>
Taxable Salary	<u>10,17,000</u>

Notes:

1. Since bonus was paid in the month of October, the basic salary of ₹ 50,000 for the month of October is considered for its calculation.
2. As per Rule 3(7)(vii), facility of use of laptop and computer is an exempt perquisite, whether used for official or personal purpose or both.
3. Mr. Balaji can avail exemption under section 10(5) on the entire amount of ₹ 75,000 reimbursed by the employer towards Leave Travel Concession since the same was availed for himself, his wife and three children and the journey was undertaken by

economy class airfare. The restriction imposed for two children is not applicable in case of multiple births which take place after the first child.

It is assumed that the Leave Travel Concession was availed for journey within India.

4. It is assumed that dearness allowance does not form part of salary for computing retirement benefits.
5. As per the provisions of Rule 3(2), in case a motor car (engine cubic capacity exceeding 1.60 liters) owned by the employer is provided to the employee without chauffeur for personal as well as office use, the value of perquisite shall be ₹ 2,400 per month. The car was provided to the employee from 01.11.2013, therefore the perquisite value has been calculated for 5 months.
6. As per section 17(2)(iv), a "perquisite" includes any sum paid by the employer in respect of any obligation which, but for such payment, would have been payable by the assessee. Therefore, professional tax of ₹ 2,000 paid by the employer is taxable as a perquisite in the hands of Mr. Balaji. As per section 16(iii), a deduction from the salary is provided on account of tax on employment i.e. professional tax paid during the year.

Therefore, in the present case, the professional tax paid by the employer on behalf of the employee ₹ 2,000 is first included in the salary and deduction of the entire professional tax of ₹ 3,000 is provided from salary.

Question 3

From the following details, find out the salary chargeable to tax for the A.Y.2014-15 -

Mr. X is a regular employee of Rama & Co., in Gurgaon. He was appointed on 1.1.2013 in the scale of 20,000-1,000-30,000. He is paid 10% D.A. & Bonus equivalent to one month pay based on salary of March every year. He contributes 15% of his pay and D.A. towards his recognized provident fund and the company contributes the same amount.

He is provided free housing facility which has been taken on rent by the company at ₹ 10,000 per month. He is also provided with following facilities:

- (i) Facility of laptop costing ₹ 50,000.*
- (ii) Company reimbursed the medical treatment bill of his brother of ₹ 25,000, who is dependent on him.*
- (iii) The monthly salary of ₹ 1,000 of a house keeper is reimbursed by the company.*
- (iv) A gift voucher of ₹ 10,000 on the occasion of his marriage anniversary.*
- (v) Conveyance allowance of ₹ 1,000 per month is given by the company towards actual reimbursement.*
- (vi) He is provided personal accident policy for which premium of ₹ 5,000 is paid by the company.*
- (vii) He is getting telephone allowance @ ₹ 500 per month.*

(viii) Company pays medical insurance premium of his family of ₹ 10,000.

Answer

Computation of taxable salary of Mr. X for A.Y. 2014-15

Particulars	₹
Basic pay [(₹ 20,000×9) + (₹ 21,000×3)] = ₹ 1,80,000 + ₹ 63,000	2,43,000
Dearness allowance [10% of basic pay]	24,300
Bonus	21,000
Employer's contribution to Recognized Provident Fund in excess of 12% (15%-12% =3% of ₹ 2,67,300) [See Note 1 below]	8,019
Taxable allowances	
Telephone allowance	6,000
Taxable perquisites	
Rent-free accommodation [See Note 1 & 2 below]	44,145
Medical reimbursement (₹ 25,000 - ₹ 15,000) [See Note 4 below]	10,000
Reimbursement of salary of housekeeper	12,000
Gift voucher [See Note 6 below]	<u>10,000</u>
Salary income chargeable to tax	<u>3,78,464</u>

Notes:

1. It has been assumed that dearness allowance forms part of salary for retirement benefits and accordingly, the perquisite value of rent-free accommodation and employer's contribution to recognized provident fund have been worked out.
2. Where the accommodation is taken on lease or rent by the employer, the value of rent-free accommodation provided to employee would be actual amount of lease rental paid or payable by the employer or 15% of salary, whichever is lower.

For the purposes of valuation of rent free house, salary includes:

- (i) Basic salary i.e., ₹ 2,43,000
- (ii) Dearness allowance (assuming that it is included for calculating retirement benefits) i.e. ₹ 24,300
- (iii) Bonus i.e., ₹ 21,000
- (iv) Telephone allowance i.e., ₹ 6,000

Therefore, salary works out to

$$2,43,000 + 24,300 + 21,000 + 6,000 = 2,94,300.$$

4.15 Income-tax

15% of salary = $2,94,300 \times 15/100 = 44,145$

Value of rent-free house = Lower of rent paid by the employer (i.e. ₹ 1,20,000) or 15% of salary (i.e., ₹ 44,145).

Therefore, the perquisite value is ₹ 44,145.

3. Facility of use of laptop is not a taxable perquisite.
4. Clause (v) of the proviso to section 17(2) exempts any sum paid by the employer in respect of any expenditure actually incurred by the employee on his medical treatment or treatment of any member of his family to the extent of ₹ 15,000. Therefore, in this case, the balance of ₹ 10,000 (i.e., ₹ 25,000 – ₹ 15,000) is a taxable perquisite. Medical insurance premium paid by employer is exempt.
5. Conveyance allowance is exempt since it is based on actual reimbursement for official purposes.
6. The value of any gift or voucher or token in lieu of gift received by the employee or by member of his household not exceeding ₹ 5,000 in aggregate during the previous year is exempt. In this case, the gift voucher was received on the occasion of marriage anniversary and the sum exceeds the limit of ₹ 5,000.

Therefore, the entire amount of ₹ 10,000 is liable to tax as perquisite.

Note - An alternate view possible is that only the sum in excess of ₹ 5,000 is taxable in view of the language of Circular No.15/2001 dated 12.12.2001 that such gifts upto ₹ 5,000 in the aggregate per annum would be exempt, beyond which it would be taxed as a perquisite. As per this view, the value of perquisite would be ₹ 5,000.

7. Premium of ₹ 5,000 paid by the company for personal accident policy is not liable to tax.

Question 4

Shri Hari is the General Manager of ABC Ltd. From the following details, compute the taxable income for the Assessment year 2014-15:

<i>Basic salary</i>	<i>₹ 20,000 per month</i>
<i>Dearness allowance</i>	<i>30% of basic salary</i>
<i>Transport allowance (for commuting between place of residence and office)</i>	<i>₹ 2,000 per month</i>
<i>Motor car running and maintenance charges fully paid by employer</i>	<i>₹ 36,000</i>
<i>(The motor car is owned and driven by employee Hari. The engine cubic capacity is below 1.60 litres. The motor car is used for both official and personal purpose by the employee)</i>	
<i>Expenditure on accommodation in hotels while touring on official duties met by the employer.</i>	<i>₹ 30,000</i>
<i>Loan from recognised provident fund (maintained by the employer)</i>	<i>₹ 40,000</i>
<i>Lunch provided by the employer during office hours.</i>	

<i>Cost to the employer</i>	₹ 12,000
<i>Computer (cost ₹ 50,000) kept by the employer in the residence of Hari from 1.10.2013</i>	
<i>Hari made the following payments:</i>	
<i>Medical insurance premium : Paid in cash</i>	₹ 2,000
<i>Paid by cheque</i>	₹ 3,200

Answer

Computation of taxable income of Shri Hari for the A.Y. 2014-15

Particulars	₹	₹
Basic salary (₹ 20,000 x 12)		2,40,000
Dearness allowance @ 30%		72,000
Transport allowance (₹ 2,000 x 12)	24,000	
<i>Less</i> : Exemption under section 10(14) (read with Rule 2BB @ ₹ 800 p.m.)	9,600	14,400
Motor car maintenance borne by employer [₹ 36,000 - ₹ 21,600 (i.e., ₹ 1,800 × 12)]		14,400
Expenditure on accommodation while on official duty not a perquisite and hence not chargeable to tax		Nil
Loan from recognized provident fund – not chargeable to tax		Nil
Value of lunch provided during working hours (not chargeable to tax as per rule 3(7)(iii)-free food provided by the employer during working hours is not treated as perquisite provided that the value thereof does not exceed fifty rupees per meal)		Nil
Computer provided in the residence of employee by the employer – not chargeable to tax [Rule 3(7)(vii)]		Nil
Gross Salary		3,40,800
<i>Less</i> : Deduction under Chapter VI-A		
Deduction under section 80D in respect of medical insurance premium paid by cheque	3,200	
Premium paid in cash not eligible for deduction	Nil	3,200
Taxable income		3,37,600

Question 5

Mr. Vignesh, Finance Manager of KLM Ltd., Mumbai, furnishes the following particulars for the financial year 2013-14:

(i) Salary ₹ 46,000 per month

4.17 Income-tax

- (ii) Value of medical facility in a hospital maintained by the company ₹ 7,000
- (iii) Rent free accommodation owned by the company
- (iv) Housing loan of ₹ 6,00,000 given on 01.04.2013 at the interest rate of 6% p.a. (No repayment made during the year). The rate of interest charged by State Bank of India (SBI) as on 01.04.2013 in respect of housing loan is 10%.
- (v) Gifts in kind made by the company on the occasion of wedding anniversary of Mr. Vignesh ₹ 4,750.
- (vi) A wooden table and 4 chairs were provided to Mr. Vignesh at his residence (dining table). This was purchased on 1.5.2010 for ₹ 60,000 and sold to Mr. Vignesh on 1.8.2013 for ₹ 30,000.
- (vii) Personal purchases through credit card provided by the company amounting to ₹ 10,000 was paid by the company. No part of the amount was recovered from Mr. Vignesh.
- (viii) An ambassador car which was purchased by the company on 16.7.2010 for ₹ 2,50,000 was sold to the assessee on 14.7.2013 for ₹ 80,000.

Other income received by the assessee during the previous year 2013-14:

	Particulars	₹
(a)	Interest on Fixed Deposits with a company	5,000
(b)	Income from specified mutual fund	3,000
(c)	Interest on bank fixed deposits of a minor married daughter	3,000

- (ix) Contribution to LIC towards premium under section 80CCC ₹ 10,000
- (x) Deposit in PPF Account made during the year 2013-14 ₹ 1,00,000

Compute the taxable income of Mr. Vignesh and the tax thereon for the Assessment year 2014-15.

Answer

Computation of taxable income of Mr. Vignesh for the Assessment Year 2014-15

	Particulars	₹	₹
(a)	Income from salaries (See Note 1)		7,62,800
(b)	Income from other sources		
	(i) Interest on fixed deposit with a company	5,000	
	(ii) Income from specified mutual fund exempt under section 10(35)	Nil	
	(iii) Interest on Fixed Deposit received by minor daughter (₹ 3,000 - ₹ 1500)	1,500	6,500
	Gross total income		7,69,300

<i>Less:</i> Deductions under Chapter VI-A		
Section 80C – PPF	1,00,000	
Section 80CCC – LIC	<u>10,000</u>	
Overall deduction limited to ₹ 1 lakh as per section 80 CCE		<u>1,00,000</u>
Total Income		<u>6,69,300</u>
Tax on income		63,860
<i>Add:</i> Education cess @ 2%		1,277
<i>Add:</i> Secondary and Higher Education cess @ 1%		<u>639</u>
Total tax liability		<u>65,776</u>
Total tax liability (rounded off)		65,780

Note:

Computation of salary income of Mr. Vignesh for the Assessment Year 2014-15

Particulars	₹
Income under the head “salaries”	
Salary [₹ 46,000 x 12]	5,52,000
Medical facility [in the hospital maintained by the company is exempt]	–
Rent free accommodation	
15% of salary is taxable (i.e. ₹ 5,52,000 × 15% as per Rule 3(1))	82,800
Use of dining table for 4 months [₹ 60,000 x 10 /100 x 4 /12]	2,000
Valuation of perquisite of interest on loan [Rule 3(7)(i)] – 10% is taxable which is to be reduced by actual rate of interest charged i.e. [10% - 6% = 4%]	24,000
Gift given on the occasion of wedding anniversary ₹ 4,750 is exempt, since its value is less than ₹ 5,000	–
Perquisite on sale of dining tables	
Cost	60,000
<i>Less:</i> Depreciation on straight line method @ 10% for 3 years	<u>18,000</u>
W.D.V	42,000
<i>Less:</i> Amount paid by the assessee	<u>30,000</u>
Purchase through credit card – not being a privilege but covered by section 17(2)(iv)	12,000
Original cost of car	2,50,000
<i>Less:</i> Depreciation from 16.7.2010 to 15.7.2011 @ 20%	<u>50,000</u>
	2,00,000

4.19 Income-tax

Less: Depreciation from 16.7.2011 to 15.7.2012 @ 20% on WDV	<u>40,000</u>	
Value as on 14.07.2013- being the date of sale to employee	1,60,000	
Less : Amount received from the assessee on 14.07.2013	<u>80,000</u>	<u>80,000</u>
Income from Salaries		<u>7,62,800</u>

Note - Under Rule 3(7)(viii), while calculating the perquisite value of benefit to the employee arising from the transfer of any movable asset, the normal wear and tear is to be calculated in respect of each completed year during which the asset was put to use by the employer. In the given case the third year of use of ambassador car is completed on 15.7.2013 where as the car was sold to the employee on 14.7.2013. The solution worked out above provides for wear and tear for only two years.

Question 6

Mrs. Lakshmi aged about 66 years is a Finance Manager of M/s. Lakshmi & Co. Pvt. Ltd., based at Calcutta. She is in continuous service since 1975 and receives the following salary and perks from the company during the year ending 31.03.2014:

- (i) Basic Salary ($\text{₹ } 50,000 \times 12$) = ₹ 6,00,000
- (ii) D.A. ($\text{₹ } 20,000 \times 12$) = ₹ 2,40,000 (forms part of pay for retirement benefits)
- (iii) Bonus – 2 months basic pay.
- (iv) Commission – 0.1% of the turnover of the company. The turnover for the F.Y. 2013-14 was ₹ 15.00 crores.
- (v) Contribution of the employer and employee to the recognized provident fund Account ₹ 3,00,000 each.
- (vi) Interest credited to Recognized Provident Fund Account at 9.5% - ₹ 60,000.
- (vii) Rent free unfurnished accommodation provided by the company for which the company pays a rent of ₹ 70,000 per annum.
- (viii) Entertainment Allowance – ₹ 30,000.
- (ix) Hostel allowance for three children – ₹ 5,000 each.

She makes the following payments and investments :

- (i) Premium paid to insure the life of her major son – ₹ 15,000.
- (ii) Medical Insurance premium for self – ₹ 6,000 ; Spouse – ₹ 6,000.
- (iii) Donation to a public charitable institution registered under 80G ₹ 2,00,000 by way of cheque.
- (iv) LIC Pension Fund – ₹ 12,000.

Determine the tax liability for the Assessment Year 2014-15.

Answer

Computation of Total Income of Mrs. Lakshmi for A.Y. 2014-15

Particulars	₹	₹
Income from salary		
Basic salary		6,00,000
Dearness allowance		2,40,000
Bonus		1,00,000
Commission (calculated as percentage of turnover)		1,50,000
Entertainment allowance		30,000
Children's hostel allowance	15,000	
Less : Exemption (₹ 300 x 12 x 2)	<u>7,200</u>	7,800
Interest credited to recognized provident fund account (exempt)		-
Rent free unfurnished accommodation (Refer Working Note 1)		70,000
Excess contribution to PF by employer (Refer Working Note 2)		<u>1,81,200</u>
Gross salary		13,79,000
Less : Deduction under section 80C		
Life insurance premium paid for insurance of major son	15,000	
Contribution to recognized provident fund	3,00,000	
Deduction under section 80CCC in respect of LIC pension fund	<u>12,000</u>	
	3,27,000	
Deduction limited to ₹ 1,00,000 as per section 80CCE		1,00,000
Deduction under section 80D		<u>12,000</u>
Total income before deduction under section 80G		12,67,000
Deduction under section 80G :		
50% of ₹ 1,26,700 (10% total income)(Refer Working Note 3)		<u>63,350</u>
Total income		12,03,650
Tax on total income		1,91,095
Add : Education cess @ 2%		3,822
Add : Secondary and higher education cess @ 1%		<u>1,911</u>
Total tax liability		<u>1,96,828</u>
Rounded off		1,96,830

Working Notes:**1. Value of rent free unfurnished accommodation**

Particulars	₹
Basic salary	6,00,000
Dearness allowance	2,40,000
Bonus	1,00,000
Commission @ 0.1% of turnover	1,50,000
Entertainment allowance	30,000
Children's hostel allowance	<u>7,800</u>
Gross Salary	<u>11,27,800</u>
15% of salary	1,69,170
Actual rent paid by the company	70,000
The least of the above is chargeable perquisite.	

2. Employer's contribution to P.F. in excess of 12% of salary

Employer's contribution	₹ 3,00,000
Less : 12% of basic salary, dearness allowance & commission	
12% of ₹ 9,90,000	<u>₹ 1,18,800</u>
	<u>₹ 1,81,200</u>

3. As per amendment made by Finance Act, 2012, no deduction shall be allowed under section 80G in respect of any sum exceeding ₹ 10,000 unless such sum is paid by any mode other than cash. Here, since the donation of ₹ 2,00,000 is made by cheque, the same is allowed.

Question 7

Mr. M is an area manager of M/s N. Steels Co. Ltd. During the financial year 2013-14, he gets the following emoluments from his employer:

Basic Salary	
Up to 31.8.2013	₹ 20,000 p.m.
From 1.9.2013	₹ 25,000 p.m.
Transport allowance	₹ 2,000 p.m.
Contribution to recognised provident fund	15% of basic salary
Children education allowance (Total)	₹ 500 p.m. for two children
City compensatory allowance	₹ 300 p.m.
Hostel expenses allowance (Total)	₹ 380 p.m. for two children

Tiffin allowance (actual expenses ₹ 3,700)	₹ 5,000 p.a.
Tax paid on employment	₹ 2,500

Compute taxable salary of Mr. M for the Assessment year 2014-15.

Answer

Computation of taxable salary of Mr. M. for the Assessment Year 2014-15

Particulars	₹	₹
Basic Salary (₹ 20,000 x 5) +(₹ 25,000 x 7)		2,75,000
Transport allowance (₹ 2,000 x 12)	24,000	
Less: Exempt under section 10(14) (₹ 800 x 12)	<u>9,600</u>	14,400
Children education allowance (₹ 500 x 12)	6,000	
Less: Exempt under section 10(14) (₹ 100 x 2 x 12)	<u>2,400</u>	3,600
City Compensatory Allowance (₹ 300 x 12)		3,600
Hostel Expenses Allowance (₹ 380 x 12)	4,560	
Less: Exempt under section 10(14) (₹ 300 x 2 x 12 i.e. ₹ 7,200 but restricted to the actual allowance of ₹ 4,560)	<u>4,560</u>	Nil
Tiffin allowance (fully taxable)		5,000
Tax paid on employment [See Note Below]		2,500
Employer's contribution to recognized provident fund in excess of 12% of salary (i.e 3% of ₹ 2,75,000)		<u>8,250</u>
Gross Salary		3,12,350
Less: Tax on employment under section 16(iii)		<u>2,500</u>
Taxable salary		<u>3,09,850</u>

Note: Professional tax paid by employer should be included in the salary of Mr. M as a perquisite since it is discharge of monetary obligation of the employee by the employer. Thereafter, deduction of professional tax paid is allowed to the employee from his gross salary.

Question 8

Mr. X retired from the services of M/s Y Ltd. on 31.01.2014, after completing service of 30 years and one month. He had joined the company on 1.1.1984 at the age of 30 years and received the following on his retirement:

- Gratuity ₹ 6,00,000. He was covered under the Payment of Gratuity Act, 1972.
- Leave encashment of ₹ 3,30,000 for 330 days leave balance in his account. He was credited 30 days leave for each completed year of service.
- As per the scheme of the company, he was offered a car which was purchased on

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01.02.2011 by the company for ₹ 5,00,000. Company has recovered ₹ 2,00,000 from him for the car. Company depreciates the vehicles at the rate of 15% on Straight Line Method.

- (iv) An amount of ₹ 3,00,000 as commutation of pension for 2/3 of his pension commutation.
- (v) Company presented him a gift voucher worth ₹ 6,000 on his retirement.
- (vi) His colleagues also gifted him a Television (LCD) worth ₹ 50,000 from their own contribution.

Following are the other particulars:

- (i) He has drawn a basic salary of ₹ 20,000 and 50% dearness allowance per month for the period from 01.04.2013 to 31.01.2014.
- (ii) Received pension of ₹ 5,000 per month for the period 01.02.2014 to 31.03.2014 after commutation of pension.

Compute his gross total income from the above for Assessment Year 2014-15.

Answer

Computation of Gross Total Income of Mr. X for A.Y. 2014-15

Particulars	₹
Basic Salary = ₹ 20,000 x 10	2,00,000
Dearness Allowance = 50% of basic salary	1,00,000
Gift Voucher (See Note - 1)	6,000
Transfer of car (See Note - 2)	56,000
Gratuity (See Note - 3)	80,769
Leave encashment (See Note - 4)	1,30,000
Uncommuted pension (₹ 5000 x 2)	10,000
Commutated pension (See Note - 5)	1,50,000
Taxable Salary /Gross Total Income	7,32,769

Notes:

- (1) As per Rule 3(7)(iv), the value of any gift or voucher or token in lieu of gift received by the employee or by member of his household not exceeding ₹ 5,000 in aggregate during the previous year is exempt. In this case, the amount was received on his retirement and the sum exceeds the limit of ₹ 5,000.

Therefore, the entire amount of ₹ 6,000 is liable to tax as perquisite.

Note - An alternate view possible is that only the sum in excess of ₹ 5,000 is taxable in view of the language of Circular No.15/2001 dated 12.12.2001 that such gifts upto ₹ 5,000 in the aggregate per annum would be exempt, beyond which it would be taxed as a perquisite. As per this view, the value of perquisite would be ₹ 1,000 and gross taxable income would be ₹ 7,27,769.

- (2) **Perquisite value of transfer of car:** As per Rule 3(7)(viii), the value of benefit to the employee, arising from the transfer of an asset, being a motor car, by the employer is the actual cost of the motor car to the employer as reduced by 20% of such cost for each completed year during which such motor car was put to use by the employer on a written down value basis. Therefore, the value of perquisite on transfer of motor car, in this case, would be:

Particulars	₹
Purchase price (1.2.2011)	5,00,000
Less: Depreciation @ 20%	<u>1,00,000</u>
WDV on 31.1.2012	4,00,000
Less: Depreciation @ 20%	<u>80,000</u>
WDV on 31.1.2013	3,20,000
Less: Depreciation @ 20%	<u>64,000</u>
WDV on 31.1.2014	2,56,000
Less: Amount recovered	<u>2,00,000</u>
Value of perquisite	<u>56,000</u>

The rate of 15% as well as the straight line method adopted by the company for depreciation of vehicle is not relevant for calculation of perquisite value of car in the hands of Mr. X.

- (3) **Taxable gratuity**

Particulars	₹
Gratuity received	6,00,000
Less: Exempt under section 10(10) - Least of the following:	
(i) Notified limit = ₹ 10,00,000	
(ii) Actual gratuity = ₹ 6,00,000	
(iii) $15/26 \times 30,000 \times 30 =$ ₹ 5,19,231	
Taxable Gratuity	<u>5,19,231</u>
	<u>80,769</u>

- (4) **Taxable leave encashment**

Particulars	₹
Leave Salary received	3,30,000
Less: Exempt under section 10(10AA) - Least of the following:	
(i) Notified limit ₹ 3,00,000	
(ii) Actual leave salary ₹ 3,30,000	

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(iii) 10 months x ₹ 20,000 (assuming that dearness allowance does not form part of pay for retirement benefit)	₹ 2,00,000	
(iv) Cash equivalent of leave to his credit $\left(\frac{330}{30} \times 20,000\right)$	₹ 2,20,000	
		<u>2,00,000</u>
Taxable Leave encashment		<u>1,30,000</u>

Note – It has been assumed that dearness allowance does not form part of salary for retirement benefits. In case it is assumed that dearness allowance forms part of pay for retirement benefits, then, the third limit for exemption under section 10(10AA) in respect of leave encashment would be ₹ 3,00,000 (i.e. 10 x ₹ 30,000) and the fourth limit ₹ 3,30,000, in which case, the taxable leave encashment would be ₹ 30,000 (₹ 3,30,000 - ₹ 3,00,000). In such a case, the gross total income would be ₹ 6,32,769.

(5) Commuted Pension

Since Mr. X is a non-government employee in receipt of gratuity, exemption under section 10(10A) would be available to the extent of 1/3rd of the amount of the pension which he would have received had he commuted the whole of the pension.

Particulars	₹
Amount received	3,00,000
Exemption under section 10(10A) = $\frac{1}{3} \times \left[3,00,000 \times \frac{3}{2}\right]$	<u>1,50,000</u>
Taxable amount	<u>1,50,000</u>

- (6) The taxability provisions under section 56(2)(vii) are not attracted in respect of television received from colleagues, since television is not included in the definition of property therein.

Question 9

Mr. Narendra, who retired from the services of Hotel Samode Ltd., on 31.1.2014 after putting on service for 5 years, received the following amounts from the employer for the year ending on 31.3.2014:

- ◆ *Salary @ ₹ 16,000 p.m. comprising of basic salary of ₹ 10,000, Dearness allowance of ₹ 3,000, City compensatory allowance of ₹ 2,000 and Night duty allowance of ₹ 1,000.*
- ◆ *Pension @ 30% of basic salary from 1.2.2014.*
- ◆ *Leave salary of ₹ 75,000 for 225 days of leave accumulated during 5 years @ 45 days leave in each year. He has not availed any earned leave during his tenure of 5 years and utilized only his casual leave.*

- ◆ *Gratuity of ₹ 50,000.*

Compute the total income of Mr. Narendra for the assessment year 2014-15.

Answer

Computation of total income of Mr. Narendra for A.Y. 2014-15

Particulars	₹	₹
Income from Salaries		
Gross salary received during 1.4.2013 to 31.1.2014 @ ₹ 16,000 p.m. (₹ 16,000 x 10)		1,60,000
Pension for 2 months @ 30% of the basic salary of ₹ 10,000 p.m.		6,000
Leave Salary	75,000	
Less: Exempt under section 10(10AA) (Note1)	50,000	25,000
Gratuity	50,000	
Less: Exempt under section 10(10) (Note2)	25,000	25,000
Total Income		2,16,000

Notes:

1. Leave encashment is exempt to the extent of least of the following :

	Particulars	₹
(i)	Statutory limit	3,00,000
(ii)	Cash equivalent of leave for 30 days for 5 years (₹ 10,000 × 150/30)	50,000
(iii)	10 months average salary (10 x ₹ 10,000)	1,00,000
(iv)	Actual amount received	75,000

Therefore, ₹ 50,000 is exempt under section 10(10AA).

2. Assuming that the employee is not covered under the Payment of Gratuity Act, 1972, Gratuity is exempt to the extent of least of the following :

	Particulars	₹
(i)	Statutory limit	10,00,000
(ii)	Half month's salary for 5 years of service (5 x ₹ 5,000)	25,000
(iii)	Actual gratuity received	50,000

Therefore, ₹ 25,000 is exempt under section 10(10).

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3. It has been assumed that dearness allowance does not form part of salary for retirement benefits and therefore, not included in "Salary" for the purpose of computation of leave encashment and gratuity.

Question 10

Mr. Mohit is employed with XY Ltd. on a basic salary of ₹ 10,000 p.m. He is also entitled to dearness allowance @ 100% of basic salary, 50% of which is included in salary as per terms of employment. The company gives him house rent allowance of ₹ 6,000 p.m. which was increased to ₹ 7,000 p.m. with effect from 1.01.2014. He also got an increment of ₹ 1,000 p.m. in his basic salary with effect from 1.02.2014. Rent paid by him during the previous year 2013-14 is as under:

- April and May, 2013 - Nil, as he stayed with his parents
 June to October, 2013 - ₹ 6,000 p.m. for an accommodation in Ghaziabad
 November, 2013 to March, 2014 - ₹ 8,000 p.m. for an accommodation in Delhi.

Compute his gross salary for assessment year 2014-15.

Answer

Computation of gross salary of Mr. Mohit for A.Y. 2014-15

Particulars	₹
Basic salary [(₹ 10,000 × 10) + (₹ 11,000 × 2)]	1,22,000
Dearness Allowance (100% of basic salary)	1,22,000
House Rent Allowance (See Note below)	<u>21,300</u>
Gross Salary	<u>2,65,300</u>

Note: Computation of Taxable House Rent Allowance (HRA)

Particulars	April-May (₹)	June-Oct (₹)	Nov-Dec (₹)	Jan (₹)	Feb-March (₹)
Basic salary per month	10,000	10,000	10,000	10,000	11,000
Dearness allowance (included in salary as per terms of employment) (50% of basic salary)	<u>5,000</u>	<u>5,000</u>	<u>5,000</u>	<u>5,000</u>	<u>5,500</u>
Salary per month for the purpose of computation of house rent allowance	<u>15,000</u>	<u>15,000</u>	<u>15,000</u>	<u>15,000</u>	<u>16,500</u>
Relevant period (in months)	2	5	2	1	2
Salary for the relevant period (Salary per month × relevant period)	30,000	75,000	30,000	15,000	33,000

Rent paid for the relevant period	Nil	30,000 (₹6,000×5)	16,000 (₹8,000×2)	8,000 (₹8,000×1)	16,000 (₹ 8,000×2)
House rent allowance (HRA) received during the relevant period (A)	12,000 (₹6,000×2)	30,000 (₹6,000×5)	12,000 (₹6,000×2)	7,000 (₹7,000×1)	14,000 (₹7,000×2)
Least of the following is exempt [u/s 10(13A)]					
1. Actual HRA received	12,000	30,000	12,000	7,000	14,000
2. Rent paid – 10% of salary	N.A.	22,500	13,000	6,500	12,700
3. 40% of salary (Residence at Ghaziabad–June to Oct, 2013)	N.A.	30,000 (40% × ₹ 75,000)			
50% of salary (Residence at Delhi–Nov'13- March'14)			15,000 (50% × ₹30,000)	7,500 (50% × ₹15,000)	16,500 (50% × ₹33,000)
Exempt HRA (B)	Nil	22,500	12,000	6,500	12,700
Taxable HRA (Actual HRA – Exempt HRA) (A-B)	12,000	7,500	Nil	500	1,300

Taxable HRA (total) = ₹ 12,000 + ₹ 7,500 + ₹ 500 + ₹ 1,300 = ₹ 21,300

Question 11

- (i) Mr. Khanna, an employee of IOL, New Delhi, a private sector company, received the following for the financial year 2013-14:

Sl. No.	Particulars	₹
1.	Basic pay	1,20,000
2.	House rent allowance	1,00,000
3.	Special allowance	30,000

Mr. Khanna was residing at New Delhi and was paying a rent of ₹ 10,000 a month.

Compute the eligible exemption under section 10(13A) of the Income-tax Act, 1961, in respect of house rent allowance received.

- (ii) If Mr. Khanna opts for rent free accommodation whereby IOL would be paying a rent of ₹ 10,000 per month to the landlord and recovers a sum of ₹ 2,500 per month from Mr. Khanna which was in excess of his entitlement, what will be the perquisite value in respect of such rent free accommodation?

(iii) Which of the above would be beneficial to Mr. Khanna i.e., house rent allowance or rent free accommodation?

Answer

(i) The eligible exemption under section 10(13A) in respect of house rent allowance received would be least of the following:

	Particulars	₹	₹
(a)	Actual house rent allowance (HRA) received		1,00,000
(b)	Excess of rent paid over 10% of basic salary		
	Rent paid (10,000 x 12)	1,20,000	
	Less: 10% of basic pay (i.e. 10% of ₹ 1,20,000)	<u>12,000</u>	1,08,000
(c)	50% of salary (i.e. 50% of ₹ 1,20,000)		60,000

Least of the above is ₹ 60,000.

The house rent allowance received by Mr. Khanna would be exempt to the extent of ₹ 60,000 under section 10(13A). The balance of ₹ 40,000 is includible in his total income.

(ii) **Perquisite value in respect of concessional accommodation**

As per rule 3(1), where the accommodation is taken on lease or rent by the employer, the actual amount of lease rental paid or payable by the employer or 15% of salary, whichever is lower, as reduced by the rent, if any, actually paid by the employee is the value of the perquisite.

(a) Actual rent paid by the employer = ₹ 10,000 x 12 = ₹ 1,20,000

(b) 15% of salary = 15% of basic pay plus special allowance =
15% of ₹ 1,50,000 = ₹ 22,500

Lower of the above is ₹ 22,500, which should be reduced by the rent of ₹ 30,000 paid by the employee (i.e. 2,500 x 12 = ₹ 30,000). The perquisite value is, therefore, nil.

(iii) We have to see the cash flow from both the options to find out which is more beneficial.

Particulars	₹	₹
Option 1: HRA		
Cash inflows [Basic Pay + HRA + Special Allowance]		2,50,000
Less: Cash outflows:		
Rent paid	1,20,000	
Tax (See Working Note 1 below)	<u>Nil</u>	<u>1,20,000</u>
Net cash flow		<u>1,30,000</u>

Option 2: Concessional accommodation		
Cash inflows [Basic Pay + Special Allowance]		1,50,000
Less: Cash outflows:		
Rent recovery	30,000	
Tax (See Working Note 2 below)	<u>Nil</u>	<u>30,000</u>
Net cash flow		<u>1,20,000</u>

Since the net cash flow is higher in Option 1, Mr. Khanna should opt for HRA, which would be more beneficial to him.

Working Notes:

1. Computation of tax under Option 1 (HRA):

Particulars	₹
Salary:	
Basic Pay	1,20,000
HRA (taxable)	40,000
Special allowance	<u>30,000</u>
Total salary	<u>1,90,000</u>
Tax on ₹ 1,90,000 (including cess)	Nil

2. Computation of tax under Option 2 (Concessional accommodation)

Particulars	₹
Salary:	
Basic Pay	1,20,000
Special allowance	30,000
Concessional accommodation	<u>Nil</u>
Total salary	<u>1,50,000</u>
Tax on ₹ 1,50,000	Nil

Question 12

Mr. X and Mr. Y are working for M/s. Gama Ltd. As per salary fixation norms, the following perquisites were offered:

- For Mr. X, who engaged a domestic servant for ₹ 500 per month, his employer reimbursed the entire salary paid to the domestic servant i.e. ₹ 500 per month.
- For Mr. Y, he was provided with a domestic servant @ ₹ 500 per month as part of remuneration package.

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You are required to comment on the taxability of the above in the hands of Mr. X and Mr. Y, who are not specified employees.

Answer

In the case of Mr. X, it becomes an obligation which the employee would have discharged even if the employer did not reimburse the same. Hence, the perquisite will be covered under section 17(2)(iv) and will be taxable in the hands of Mr. X. This is taxable in the case of all employees.

In the case of Mr. Y, it cannot be considered as an obligation which the employee would meet. The employee might choose not to have a domestic servant. This is taxable only in the case of specified employees covered by section 17(2)(iii). Hence, there is no perquisite element in the hands of Mr. Y.

Question 13

The following benefits have been granted by Ved Software Ltd. to one of its employees Mr. Badri:

- (i) Housing loan @ 6% per annum. Amount outstanding on 1.4.2013 is ₹ 6,00,000. Mr. Badri pays ₹ 12,000 per month towards principal, on 5th of each month.*
- (ii) Air-conditioners purchased 4 years back for ₹ 2,00,000 have been given to Mr. Badri for ₹ 90,000.*

Compute the chargeable perquisite in the hands of Mr. Badri for the A.Y. 2014-15.

The lending rate of State Bank of India as on 1.4.2013 for housing loan may be taken as 10%.

Answer

Perquisite value for housing loan

The value of the benefit to the assessee resulting from the provision of interest-free or concessional loan made available to the employee or any member of his household during the relevant previous year by the employer or any person on his behalf shall be determined as the sum equal to the interest computed at the rate charged per annum by the State Bank of India (SBI) as on the 1st day of the relevant previous year in respect of loans for the same purpose advanced by it. This rate should be applied on the maximum outstanding monthly balance and the resulting amount should be reduced by the interest, if any, actually paid by him.

"Maximum outstanding monthly balance" means the aggregate outstanding balance for loan as on the last day of each month.

The perquisite value for computation is $10\% - 6\% = 4\%$

Month	Maximum outstanding balance as on last date of month (₹)	Perquisite value at 4% for the month (₹)
April, 2013	5,88,000	1,960
May, 2013	5,76,000	1,920
June, 2013	5,64,000	1,880

July, 2013	5,52,000	1,840
August, 2013	5,40,000	1,800
September, 2013	5,28,000	1,760
October, 2013	5,16,000	1,720
November, 2013	5,04,000	1,680
December, 2013	4,92,000	1,640
January, 2014	4,80,000	1,600
February, 2014	4,68,000	1,560
March, 2014	4,56,000	1,520
	Total value of this perquisite	<u>20,880</u>

Perquisite Value of Air Conditioners

Particulars	₹
Original cost	2,00,000
Depreciation on SLM basis for 4 years @10% i.e. ₹ 2,00,000 x10% x 4	80,000
Written down value	1,20,000
Amount recovered from the employee	90,000
Perquisite value	30,000

Chargeable perquisite in the hands of Mr. Badri for the assessment year 2014-15

Particulars	₹
Housing loan	20,880
Air Conditioner	30,000
Total	50,880

Question 14

Shri Bala employed in ABC Co. Ltd. as Finance Manager gives you the list of perquisites provided by the company to him for the entire financial year 2013-14:

- (i) *Medical facility given to his family in a hospital maintained by the company. The estimated value of benefit because of such facility is ₹ 40,000.*
- (ii) *Domestic servant was provided at the residence of Bala. Salary of domestic servant is ₹ 1,500 per month. The servant was engaged by him and the salary is reimbursed by the company (employer).*

In case the company has employed the domestic servant, what is the value of perquisite?

- (iii) Free education was provided to his two children Arthy and Ashok in a school maintained and owned by the company. The cost of such education for Arthy is computed at ₹ 900 per month and for Ashok at ₹ 1,200 per month. No amount was recovered by the company for such education facility from Bala.
- (iv) The employer has provided movable assets such as television, refrigerator and air-conditioner at the residence of Bala. The actual cost of such assets provided to the employee is ₹ 1,10,000.
- (v) A gift voucher worth ₹ 10,000 was given on the occasion of his marriage anniversary. It is given by the company to all employees above certain grade.
- (vi) Telephone provided at the residence of Shri Bala and the bill aggregating to ₹ 25,000 paid by the employer.

State the taxability or otherwise of the above said perquisites and compute the total value of taxable perquisites.

Answer

Taxability of perquisites provided by ABC Co. Ltd. to Shri Bala

- (i) Medical facility to employees' family in a hospital maintained by the employer is not a taxable perquisite. Regardless of the estimated value of benefit arising from such facility to the employee, it is exempt from tax. Therefore, the value of perquisite is Nil.
- (ii) Domestic servant was employed by the employee and the salary of such domestic servant was paid/reimbursed by the employer. It is taxable as perquisite for all categories of employees.

Taxable perquisite value = ₹ 1,500 × 12 = ₹ 18,000.

If the company had employed the domestic servant and the facility of such servant is given to the employee, then the perquisite is taxable only in the case of specified employees. The value of the taxable perquisite in such a case also would be ₹ 18,000.

- (iii) Where the educational institution is owned by the employer, the value of perquisite in respect of free education facility shall be determined with reference to the reasonable cost of such education in a similar institution in or near the locality. However, there would be no perquisite if the cost of such education per child does not exceed ₹ 1,000 per month.

Therefore, there would be no perquisite in respect of cost of free education provided to his child Arthy, since the cost does not exceed ₹ 1,000 per month.

However, the cost of free education provided to his child Ashok would be taxable, since the cost exceeds ₹ 1,000 per month. The taxable perquisite value would be ₹ 14,400 (₹ 1,200 × 12).

Note – An alternate view possible is that only the sum in excess of ₹ 1,000 per month is taxable. In such a case, the value of perquisite would be ₹ 2,400.

- (iv) Where the employer has provided movable assets to the employee or any member of his household, 10% per annum of the actual cost of such asset owned or the amount of hire charges incurred by the employer shall be the value of perquisite. However, this will not apply to laptops and computers. In this case, the movable assets are television, refrigerator and air conditioner and actual cost of such assets is ₹ 1,10,000.

The perquisite value would be 10% of the actual cost i.e., ₹ 11,000, being 10% of ₹ 1,10,000.

- (v) The value of any gift or voucher or token in lieu of gift received by the employee or by member of his household not exceeding ₹ 5,000 in aggregate during the previous year is exempt. In this case, the amount was received on the occasion of marriage anniversary and the sum exceeds the limit of ₹ 5,000.

Therefore, the entire amount of ₹ 10,000 is liable to tax as perquisite.

Note - An alternate view possible is that only the sum in excess of ₹ 5,000 is taxable in view of the language of Circular No.15/2001 dated 12.12.2001 that such gifts upto ₹ 5,000 in the aggregate per annum would be exempt, beyond which it would be taxed as a perquisite. As per this view, the value of perquisite would be ₹ 5,000.

Total value of taxable perquisite = ₹ 53,400 [i.e. ₹ 18,000 + 14,400 + 11,000 + 10,000].

- (v) Telephone provided at the residence of the employee and payment of bill by the employer is a tax free perquisite.

Note - In case the alternate views are taken for items (iii) & (v), the total value of taxable perquisite would be ₹ 36,400 [i.e., ₹ 18,000 + 2,400 + 11,000 + 5,000].

Question 15

AB Co. Ltd. allotted 1000 sweat equity shares to Sri Chand in June 2013. The shares were allotted at ₹ 200 per share as against the fair market value of ₹ 300 per share on the date of exercise of option by the allottee viz. Sri Chand. The fair market value was computed in accordance with the method prescribed under the Act.

- (i) *What is the perquisite value of sweat equity shares allotted to Sri Chand?*
 (ii) *In the case of subsequent sale of those shares by Sri Chand, what would be the cost of acquisition of those sweat equity shares?*

Answer

- (i) As per section 17(2)(vi), the value of sweat equity shares chargeable to tax as perquisite shall be the fair market value of such shares on the date on which the option is exercised by the assessee as reduced by the amount actually paid by, or recovered from, the

assessee in respect of such shares.

Particulars	₹
Fair market value of 1000 sweat equity shares @ ₹ 300 each	3,00,000
Less: Amount recovered from Sri Chand 1000 shares @ ₹ 200 each	2,00,000
Value of perquisite of sweat equity shares allotted to Sri Chand	1,00,000

- (ii) As per section 49(2AA), where capital gain arises from transfer of sweat equity shares, the cost of acquisition of such shares shall be the fair market value which has been taken into account for perquisite valuation under section 17(2)(vi).

Therefore, in case of subsequent sale of sweat equity shares by Sri Chand, the cost of acquisition would be ₹ 3,00,000.

Question 16

Mr. Shah an Accounts Manager has retired from JK Ltd. on 15.1.2014, after rendering services for 30 years 7 months. His salary is ₹ 25,000/- p.m. upto 30.09.2013 and ₹ 27,000/- thereafter. He also gets ₹ 2,000/- p.m. as dearness allowance (55% of it is a part of salary for computing retirement benefits). He is not covered by the Payment of Gratuity Act, 1972. He has received ₹ 8 Lacs as gratuity from the employer company. Compute the gratuity taxable in the hands of Mr. Shah.

Answer

Computation of gratuity taxable in the hands of Mr. Shah for the P.Y. 2013-14

As per section 10(10)(iii), gratuity received by an employee would be exempt upto the least of the following limits -

S.No.	Particulars	₹
(i)	Gratuity received	8,00,000
(ii)	Half-month's salary for every year of completed service (See Note below)	4,00,500
(iii)	Monetary limit	10,00,000

Therefore, ₹ 4,00,500 would be exempt under section 10(10)(iii). The balance ₹ 3,99,500 (i.e. ₹ 8,00,000 – ₹ 4,00,500) would be taxable.

Note: One of the limits for calculation of gratuity exempt under section 10(10)(iii) is one-half-month's salary for each year of completed service (fraction of a year to be ignored), {{on the basis of average salary for the ten months immediately preceding the month of retirement. In this case, the month of retirement is January, 2014. Therefore, average salary for the months of March 2013 to December 2013 has to be considered. The salary is ₹ 25,000 p.m. upto 30.9.2013 and ₹ 27,000 p.m. from 1.10.2013. Hence, average salary would be ₹ 26,700 $\{[(\text{₹ } 25,000 \times 7) + (\text{₹ } 27,000 \times 3) + (2000 \times 55\% \times 10)]/10\}$.

Further, half-month's salary should be multiplied by the number of years of completed service and any fraction of a year has to be ignored. Therefore, in this case, half-month's salary should be multiplied by 30 and the fraction of 7 months should be ignored.

Computation of average salary	₹
Basic salary March 2013 to December 2013 (25,000×7+27,000×3)	2,56,000
Dearness allowance (2,000 × 10 × 55%)	<u>11,000</u>
	<u>2,67,000</u>
Average salary = 2,67,000/10 = ₹ 26,700	
Half-month's salary for every year of completed service (fraction is to be ignored) [30 × 26,700/2]	4,00,500

Question 17

Mr. Alok, a Government employee, retired from service on 31-7-2013 after rendering service of 25 years and 7 months. He received gratuity of ₹ 7,00,000. His salary at the time of retirement was as under:

Basic salary ₹ 16,000 p.m.

Dearness Allowance ₹ 8,000 p.m. (eligible for retirement benefits)

- Compute the taxable portion of gratuity.
- If Mr. Alok is not a Government employee but covered by Payment of Gratuity Act, 1972 determine the taxable and exempt portion of gratuity.

Answer

- As per section 10(10), gratuity received by a Government employee on retirement is fully exempt from tax. Since Mr. Alok is a government employee, gratuity amounting to ₹ 7,00,000 received would be fully exempt. The taxable portion of gratuity shall be Nil.
 - If Mr. Alok is not a Government employee but covered by the Payment of Gratuity Act, 1972, then, gratuity received by him would be exempt upto least of the following :

Particulars	₹
(i) Statutory limit	10,00,000
(ii) Actual gratuity received	7,00,000
(iii) 15/26 x last drawn salary x years of service (including part of the year in excess of 6 months) 15/26 x ₹ 24,000 x 26 years	3,60,000

Therefore, ₹ 3,60,000 is exempt under section 10(10).

Therefore, taxable portion of gratuity = ₹ 7,00,000 – ₹ 3,60,000 = ₹ 3,40,000

Note: Salary, for the purpose of computation of exempt gratuity, means basic salary plus dearness allowance i.e. ₹ 24,000 (₹ 16,000 + ₹ 8,000).

Question 18

Distinguish between foregoing of salary and surrender of salary.

Answer

Foregoing of salary – Waiver by an employee of his salary is foregoing of salary. Once salary accrues, subsequent waiver does not absolve him from liability to income-tax.

Surrender of salary – If any employee surrenders his salary to the Central Government under the Voluntary Surrender of Salaries (Exemption from Taxation) Act, 1961, the surrendered salary would not be included in computing his taxable income, whether he is a private sector/public sector or Government employee.

Question 19

How is advance salary taxed in the hands of an employee? Is the tax treatment same for loan or advance against salary?

Answer

Advance Salary: Advance salary is taxable when it is received by the employee, irrespective of the fact whether it is due or not.

It may so happen that when advance salary is included and charged in a particular previous year, the rate of tax at which the employee is assessed may be higher than the normal rate of tax to which he would have been assessed. Section 89(1) provides for relief in these types of cases.

Loan or Advance against salary: Loan is different from salary. When an employee takes a loan from his employer, which is repayable in certain specified installments, the loan amount cannot be brought to tax as salary of the employee.

Similarly, advance against salary is different from advance salary. It is an advance taken by the employee from his employer. This advance is generally adjusted against his salary over a specified time period. It cannot be taxed as salary.

Question 20

Mr. Ashok, an employee of a PSU, furnishes the following particulars for the previous year ending 31.03.2014:

<i>Particulars</i>	<i>₹</i>
<i>(i) Salary income for the year</i>	<i>7,25,000</i>
<i>(ii) Salary for financial year 2009-10 received during the year</i>	<i>80,000</i>
<i>(iii) Assessed income for the financial year 2009-10</i>	<i>2,40,000</i>

You are requested by the assessee to compute relief under section 89 of the Income-tax Act, 1961 and the tax payable for assessment year 2014-15.

The rates of income tax for the assessment year 2010-11 are:

	Tax rate (%)
On first ₹ 1,60,000	Nil
On ₹ 1,60,000 – ₹ 3,00,000	10
On ₹ 3,00,000 – ₹ 5,00,000	20
Above ₹ 5,00,000	30
Education cess	3

Answer

Computation of relief under section 89 of Mr. Ashok for the A.Y. 2014-15

Particulars	₹	₹
Assessment year 2014-15		
Salary Income for the year excluding arrears		7,25,000
Add: Arrears relating to Financial Year 2009-10		<u>80,000</u>
Total Income (including arrears)		<u>8,05,000</u>
Tax on ₹ 8,05,000		
First ₹ 2,00,000 Nil	Nil	
Next ₹ 3,00,000 10%	30,000	
Balance <u>₹ 3,05,000</u> 20%	<u>61,000</u>	
	<u>₹ 8,05,000</u>	
Add: Education cess @ 2%		1,820
Secondary and higher education cess @1%		<u>910</u>
Tax on total income (including arrears) (A)		<u>93,730</u>
Total Income excluding arrears		7,25,000
Tax on ₹ 7,25,000		
First ₹ 2,00,000 Nil	Nil	
Next ₹ 3,00,000 10%	30,000	
Balance <u>₹ 2,25,000</u> 20%	<u>45,000</u>	
	<u>₹ 7,25,000</u>	
Add: Education cess @ 2%		1,500
Secondary and higher education cess @ 1%		<u>750</u>
Tax on total income (excluding arrears) (B)		<u>77,250</u>

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Difference between A & B	I		16,480
Assessment Year 2010-11			
Total Income assessed			2,40,000
Add: Arrears relating to Financial year 2009-10			<u>80,000</u>
Total income (including arrears)			<u>3,20,000</u>
Tax on ₹ 3,20,000		18,000	
Add: Education Cess @ 2%		360	
Secondary and higher education cess @1%		<u>180</u>	
Tax on total income (including arrears)	(C)	<u>18,540</u>	
Total Income excluding arrears			2,40,000
Tax on ₹ 2,40,000		8,000	
Add: Education Cess @ 2%		160	
Secondary and higher education cess @1%		<u>80</u>	
Tax on total income (excluding arrears)	(D)	<u>8,240</u>	
Difference between C & D	II		10,300
Relief under section 89	(I – II)		6,180

Note: It has been assumed that salary income of ₹ 7,25,000 for the year, as given in the question, does not include salary of ₹ 80,000 for the F. Y. 2009-10 received during the year.

EXERCISES

- Where there is a decision to increase the D.A. in March, 2014 with retrospective effect from 1.4.2013, and the increased D.A. is received in April, 2014, the increase is taxable -
 - in the previous year 2013-14
 - in the previous year 2014-15
 - in the respective years to which they relate.
- The entertainment allowance received by a Government employee is exempt up to the lower of the actual entertainment allowance received, 1/5th of basic salary and -
 - ₹ 4,000
 - ₹ 6,000
 - ₹ 5,000.
- Rajesh is provided with a rent free unfurnished accommodation, which is owned by his employer, XY Pvt. Ltd., in New Delhi. The value of perquisite in the hands of Rajesh is -

- a) 20% of salary
 - b) 15% of salary
 - c) 10% of salary
4. Anirudh is provided with furniture to the value of ₹ 70,000 along with house from February, 2013. The actual hire charges paid by his employer are ₹ 5,000 p.a.. The value of furniture to be included along with value of unfurnished house for A.Y.2014-15 is-
- a) ₹ 5,000
 - b) ₹ 7,000
 - c) ₹ 14,000
5. Employer's contribution to superannuation fund during the previous year 2013-14 is -
- a) subject to fringe benefits in the hands of the employer
 - b) fully taxable as perquisite in the hands of the employee
 - c) taxable as perquisite in the hands of the employee if it exceeds ₹ 1 lakh.
6. Write short notes on -
- a) Profits in lieu of salary
 - b) Specified employees
7. Is retrenchment compensation received by workmen taxable under the Act? If yes, to what extent is it taxable?
8. When is provision of medical facilities or assistance by an employer not treated as a perquisite in the hands of the employee? Discuss.
9. Can an assessee claim relief under section 89 in respect of VRS compensation of ₹ 6 lakh received by him from his employer, if he has claimed exemption of ₹ 5 lakh in respect of the same under section 10(10C)? Discuss.
10. Explain the term "Profit in lieu of salary".

Answers

1. a; 2. c; 3. b; 4. a; 5. c

UNIT 2 : Income From House Property

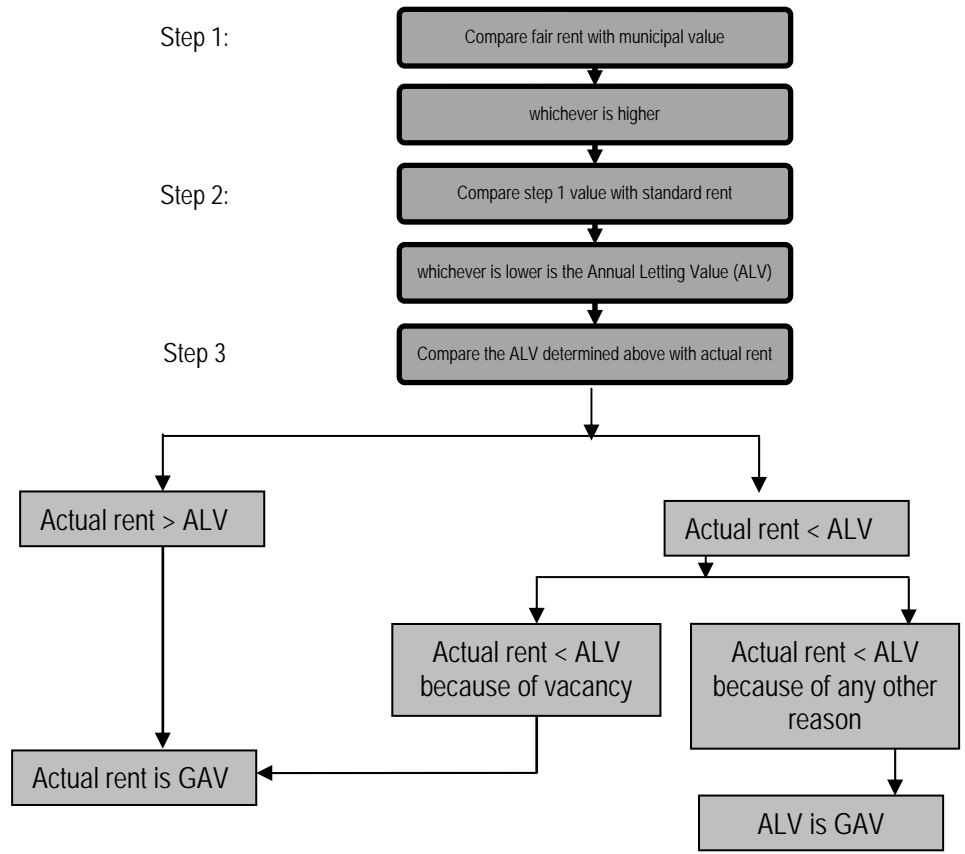
Key Points

Section 22 [Basis of Charge]

- (i) Determination of annual value of the property is the first step in computation of income under the head "Income from house property".
- (ii) The annual value of any property comprising of building or land appurtenant thereto, of which the assessee is the owner, is chargeable to tax under the head "Income from house property".
 - (i) Property should consist of any building or land appurtenant thereto
 - (a) Buildings include residential buildings as well as factory buildings, offices etc.
 - (b) Land appurtenant means land connected with the building.
 - (c) Income from letting out of vacant land is, however, taxable under the head "Income from other sources"
 - (ii) Assessee must be the owner of the property
 - (a) Owner is the person who is entitled to receive income from the property in his own right.
 - (b) The requirement of registration of the sale deed is not warranted.
 - (c) Ownership includes both free-hold and lease-hold rights.
 - (d) Ownership includes deemed ownership
 - (e) The person who owns the building need not also be the owner of the land upon which it stands.
 - (f) The assessee must be the owner of the house property during the previous year. It is not material whether he is the owner in the assessment year.
 - (iii) The property may be used for any purpose, but it should not be used by the owner for the purpose of any business or profession carried on by him, the profit of which is chargeable to tax.

- (iv) Property held as stock-in-trade etc.: Annual value of house property will be charged under the head "Income from house property" in the following cases also –
- (a) Where it is held by the assessee as stock-in-trade of a business;
 - (b) Where the assessee is engaged in the business of letting out of property on rent;
- Exceptions:**
- (1) If letting out is supplementary to the main business, the income will be assessed as business income.
 - (2) If letting out of building along with other facilities, like machinery and the two lettings are inseparable, the income will either be assessed as business income or as income from other sources, as the case may be.

Section 23(1) [Determination of Gross Annual Value(GAV) of Let-out Property]



<u>Computation of "Income from house property" in case of property let out throughout the previous year</u>	
Particulars	Amount
Gross Annual Value (GAV) [Calculated as per the chart given above]	A
Less: Municipal taxes (paid by the owner during the previous year)	B
Net Annual Value (NAV) = (A-B)	C
Less: Deductions under section 24	
(a) 30% of NAV (irrespective of the actual expenditure incurred)	D
(b) Interest on borrowed capital (actual without any ceiling limit) (See conditions given below)	E
Income from house property (C-D-E)	F
<u>Allowability of interest on borrowed capital under section 24(b)</u>	
<p>(a) Interest payable on loans borrowed can be claimed as deduction.</p> <p>(b) Interest payable on a fresh loan taken to repay the original loan is also admissible as deduction.</p> <p>(c) Interest payable on borrowed capital for the period prior to the previous year in which the property has been acquired or constructed, can be claimed as deduction over a period of 5 years in equal annual installments commencing from the year of acquisition or completion of construction.</p> <p>(d) Interest related to year of completion of construction can be fully claimed irrespective of completion date.</p>	
<u>Computation of income from self-occupied property or property unoccupied due to employment, business in another place</u>	
Particulars	Amount
Annual value under section 23(2)	Nil
Less: Deduction under section 24	
Interest on borrowed capital	
Interest on loan taken for acquisition or construction of house on or after 1.4.99 and same was completed within 3 years from the end of the financial year in which capital was borrowed, interest paid or payable subject to a maximum of ₹ 1,50,000 (including apportioned pre-construction interest).	X

	In case of loan for acquisition or construction taken prior to 1.4.99 or loan taken for repair, renovation or reconstruction at any point of time, interest paid or payable subject to a maximum of ₹ 30,000.	
Income from house property		- X
<u>Other important points</u>		
(i)	If the assessee has occupied more than one house for his own residential purposes, only one house (according to his own choice) is treated as self-occupied and all other houses will be "deemed to be let out".	
(ii)	In case of a house property which is deemed to be let-out, the annual letting value would be the gross annual value. All deductions permissible to a let-out property would be allowable in case of a "deemed to be let out" property.	
(iii)	If a portion of a property is let-out and a portion is self-occupied, then, the income will be computed separately for let out and self occupied portion.	
<u>Taxability of recovery of unrealised rent & arrears of rent received</u>		
	Unrealised rent [Section 25AA]	Arrears of rent [Section 25B]
(i)	Unrealised rent is deducted from actual rent in determination of annual value under section 23, subject to fulfillment of conditions under Rule 4. Subsequently, when the amount is realized, it gets taxed under section 25AA in the year of receipt.	If the assessee has increased the rent payable by the tenant and the same has been in dispute and later on the assessee receives the increase in rent as arrears, such arrears is assessable under section 25B.
(ii)	Unrealised rent means the rent which has been deducted from actual rent in any previous year for determining annual value.	Arrears of rent is in respect of rent not charged to income-tax for any previous year.
(iii)	Taxable in the hands of the assessee whether he is the owner of that property or not.	Taxable in the hands of the assessee whether he is the owner of that property or not.
(iv)	Taxable as income of the previous year in which he recovers the unrealized rent.	Taxable as income of the year in which he receives the arrears of rent.
(v)	No deduction shall be allowed.	30% of the amount of arrears shall be allowed as deduction.

Question 1

Mr. Vaibhav own five houses at Cochin, all of which are let out. Compute the gross annual value of each house from the information given below: (₹)

	House-I	House-II	House-III	House-IV	House-V
Municipal value	1,20,000	2,40,000	1,10,000	90,000	75,000
Fair rent	1,50,000	2,40,000	1,14,000	84,000	80,000
Standard rent	1,08,000	N.A.	1,44,000	N.A.	78,000
Actual rent received / receivable	1,80,000	2,10,000	1,20,000	1,08,000	72,000

Answer

As per section 23(1) Gross Annual Value (GAV) is the higher of Annual letting Value (ALV) and actual rent received. ALV is higher of municipal value and fair rent but restricted to standard rent.

Computation of GAV of each house owned by Mr. Vaibhav

	Particulars	House-I	House-II	House-III	House-IV	House-V
(i)	Municipal Value	1,20,000	2,40,000	1,10,000	90,000	75,000
(ii)	Fair rent	1,50,000	2,40,000	1,14,000	84,000	80,000
(iii)	Higher of (i) & (ii)	1,50,000	2,40,000	1,14,000	90,000	80,000
(iv)	Standard rent	1,08,000	N.A.	1,44,000	N.A.	78,000
(v)	ALV [Lower of (iii) & (iv)]	1,08,000	2,40,000	1,14,000	90,000	78,000
(vi)	Actual rent received/receivable	1,80,000	2,10,000	1,20,000	1,08,000	72,000
	GAV [Higher of (v) & (vi)]	1,80,000	2,40,000	1,20,000	1,08,000	78,000

Question 2

Two brothers Arun and Bimal are co-owners of a house property with equal share. The property was constructed during the financial year 1998-1999. The property consists of eight identical units and is situated at Cochin.

During the financial year 2013-14, each co-owner occupied one unit for residence and the balance of six units were let out at a rent of ₹ 12,000 per month per unit. The municipal value of the house property is ₹ 9,00,000 and the municipal taxes are 20% of municipal value, which were paid during the year. The other expenses were as follows:

	₹
(i) Repairs	40,000
(ii) Insurance premium (paid)	15,000
(iii) Interest payable on loan taken for construction of house	3,00,000

One of the let out units remained vacant for four months during the year.

Arun could not occupy his unit for six months as he was transferred to Chennai. He does not own any other house.

The other income of Mr. Arun and Mr. Bimal are ₹ 2,90,000 and ₹ 1,80,000, respectively, for the financial year 2013-14.

Compute the income under the head 'Income from House Property' and the total income of two brothers for the assessment year 2014-15.

Answer

Computation of total income for the A.Y. 2014-15

Particulars	Arun (₹)	Bimal(₹)
Income from house property		
I. Self-occupied portion (25%)		
Annual value	Nil	Nil
Less: Deduction under section 24(b)		
Interest on loan taken for construction ₹ 37,500 (being 25% of ₹ 1.5 lakh) restricted to maximum of ₹ 30,000 for each co-owner since the property was constructed before 1.04.1999	<u>30,000</u>	<u>30,000</u>
Loss from self occupied property	(30,000)	(30,000)
II. Let-out portion (75%) – See Working Note below	<u>1,25,850</u>	<u>1,25,850</u>
Income from house property	<u>95,850</u>	<u>95,850</u>
Other Income	<u>2,90,000</u>	<u>1,80,000</u>
Total Income	<u>3,85,850</u>	<u>2,75,850</u>

Working Note – Computation of income from let-out portion of house property

Particulars	₹	₹
Let-out portion (75%)		
Gross Annual Value		
(a) Municipal value (75% of ₹ 9 lakh)	6,75,000	
(b) Actual rent [(₹ 12000 x 6 x 12) – (₹ 12,000 x 1 x 4)]	8,16,000	
= ₹ 8,64,000 - ₹ 48,000		
- whichever is higher		8,16,000

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Less: Municipal taxes 75% of 1,80,000 (20% of ₹ 9 lakh)		<u>1,35,000</u>
Net Annual Value (NAV)		6,81,000
Less: Deduction under section 24		
(a) 30% of NAV	2,04,300	
(b) Interest on loan taken for the house [75% of ₹ 3 lakh]	<u>2,25,000</u>	<u>4,29,300</u>
Income from let-out portion of house property		<u>2,51,700</u>
Share of each co-owner (50%)		1,25,850

Question 3

Mr. Raman is a co-owner of a house property along with his brother holding equal share in the property.

Particulars	₹
Municipal value of the property	1,60,000
Fair rent	1,50,000
Standard rent under the Rent Control Act	1,70,000
Rent received	15,000 p.m.

The loan for the construction of this property is jointly taken and the interest charged by the bank is ₹ 25,000, out of which ₹ 21,000 has been paid. Interest on the unpaid interest is ₹ 450. To repay this loan, Raman and his brother have taken a fresh loan and interest charged on this loan is ₹ 5,000.

The municipal taxes of ₹ 5,100 have been paid by the tenant.

Compute the income from this property chargeable in the hands of Mr. Raman for the A.Y. 2014-15.

Answer

Computation of income from house property of Shri Raman for A.Y. 2014-15

Particulars	₹	₹
Gross Annual Value (See Note 1 below)		1,80,000
Less: Municipal taxes – paid by the tenant, hence not deductible		<u>Nil</u>
Net Annual Value (NAV)		1,80,000
Less: Deductions under section 24		
(i) 30% of NAV	54,000	
(ii) Interest on housing loan (See Note 2 below)		
- Interest on loan taken from bank	25,000	
- Interest on fresh loan to repay old loan for this property	<u>5,000</u>	<u>84,000</u>
Income from house property		<u>96,000</u>
50% share taxable in the hands of Shri Raman (See Note 3 below)		48,000

Notes:

1. Computation of Gross Annual Value (GAV)

GAV is the higher of Annual Letting Value (ALV) and actual rent received. ALV is the higher of municipal value and fair rent, but restricted to standard rent.

Particulars	₹	₹	₹	₹
(a) Municipal value of property	1,60,000			
(b) Fair rent	1,50,000			
(c) Higher of (a) and (b)		1,60,000		
(d) Standard rent		1,70,000		
(e) Annual Letting Value [lower of (c) and (d)]			1,60,000	
(f) Actual rent [15,000 x 12]			1,80,000	
(g) Gross Annual Value [higher of (e) and (f)]				1,80,000

- Interest on housing loan is allowable as a deduction under section 24 on accrual basis. Further, interest on fresh loan taken to repay old loan is also allowable as deduction. However, interest on unpaid interest is not allowable as deduction under section 24.
- Section 26 provides that where a house property is owned by two or more persons whose shares are definite and ascertainable, the share of each such person in the income of house property, as computed in accordance with sections 22 to 25, shall be included in his respective total income. Therefore, 50% of the total income from the house property is taxable in the hands of Mr. Raman since he is an equal owner of the property.

Question 4

Mrs. Rohini Ravi, a citizen of the U.S.A., is a resident and ordinarily resident in India during the financial year 2013-14. She owns a house property at Los Angeles, U.S.A., which is used as her residence. The annual value of the house is \$20,000. The value of one USD (\$) may be taken as ₹ 45.

She took ownership and possession of a flat in Chennai on 1.7.2013, which is used for self-occupation, while she is in India. The flat was used by her for 7 months only during the year ended 31.3.2014. The municipal valuation is ₹ 32,000 p.m. and the fair rent is ₹ 4,20,000 p.a. She paid the following to Corporation of Chennai :

Property Tax	₹ 16,200
Sewerage Tax	₹ 1,800

She had taken a loan from Standard Chartered Bank for purchasing this flat. Interest on loan was as under:

	₹
Period prior to 1.4.2013	49,200

4.49 Income-tax

1.4.2013 to 30.6.2013	50,800
1.7.2013 to 31.3.2014	1,31,300

She had a house property in Bangalore, which was sold in March, 2011. In respect of this house, she received arrears of rent of ₹ 60,000 in March, 2014. This amount has not been charged to tax earlier.

Compute the income chargeable from house property of Mrs. Rohini Ravi for the assessment year 2014-15, exercising the most beneficial option available.

Answer

Since the assessee is a resident and ordinarily resident in India, her global income would form part of her total income i.e., income earned in India as well as outside India will form part of her total income.

She possesses a self-occupied house at Los Angeles as well as at Chennai. At her option, one house shall be treated as self-occupied, whose annual value will be nil. The other self-occupied house property will be treated as "deemed let out property".

The annual value of the Los Angeles house is ₹ 9,00,000 and the Chennai flat is ₹ 3,15,000. Since the annual value of Los Angeles house is obviously more, it will be beneficial for her to opt for choosing the same as self-occupied. The Chennai house will, therefore, be treated as "deemed let out property".

As regards the Bangalore house, arrears of rent will be chargeable to tax as income from house property in the year of receipt under section 25B. It is not essential that the assessee should continue to be the owner. 30% of the arrears of rent shall be allowed as deduction.

Accordingly, the income from house property of Mrs. Rohini Ravi will be calculated as under:

	Particulars	₹	₹
1.	Self-occupied house at Los Angeles		
	Annual value	Nil	
	Less: Deduction under section 24	Nil	
	Chargeable income from this house property		Nil
2.	Deemed let out house property at Chennai		
	Annual value (Higher of municipal value and fair rent) [4,20,000 x 9/12]		3,15,000
	Less: Municipal Taxes (Property tax + Sewerage tax)		<u>18,000</u>
	Net Annual Value (NAV)		2,97,000
	Less: Deductions under section 24		
	30% of NAV	89,100	
	Interest on borrowed capital (See Note below)	<u>1,91,940</u>	<u>2,81,040</u>
			15,960
3.	Arrears in respect of Bangalore property(Section 25B)		
	Arrears of rent received	60,000	

Less: Deduction @ 30%	18,000	42,000
Income chargeable under the head "Income from house property"		57,960

Note : Interest on borrowed capital	₹
Interest for the current year (₹ 50,800 + ₹ 1,31,300)	1,82,100
Add: 1/5th of pre-construction interest (₹ 49,200 x 1/5)	9,840
Interest deduction allowable under section 24	1,91,940

Question 5

Mr. A and Mr. B constructed their houses on a piece of land purchased by them at New Delhi. The built up area of each house was 1,000 sq.ft. ground floor and an equal area in the first floor. A started construction on 1-04-2012 and completed on 1-04-2013. B started the construction on 1-04-2012 and completed the construction on 30-06-2013. A occupied the entire house on 01-04-2013. B occupied the ground floor on 01-07-2013 and let out the first floor for a rent of ₹ 15,000 per month. However, the tenant vacated the house on 31-12-2013 and B occupied the entire house during the period 01-01-2014 to 31-03-2014.

Following are the other information

- | | |
|---|------------------------------|
| (i) Fair rental value of each unit
(ground floor /first floor) | ₹ 1,00,000 per annum |
| (ii) Municipal value of each unit
(ground floor / first floor) | ₹ 72,000 per annum |
| (iii) Municipal taxes paid by | A – ₹ 8,000
B – ₹ 8,000 |
| (iv) Repair and maintenance charges paid by | A – ₹ 28,000
B – ₹ 30,000 |

A has availed a housing loan of ₹ 20 lakhs @ 12% p.a. on 01-04-2012. B has availed a housing loan of ₹ 12 lakhs @ 10% p.a. on 01-07-2012. No repayment was made by either of them till 31-03-2014. Compute income from house property for A and B for the previous year 2013-14 (A.Y. 2014-15).

Answer**Computation of income from house property of Mr. A for A.Y. 2014-15**

Particulars	₹	₹
Annual value is nil (since house is self occupied)		Nil
Less : Deduction under section 24(b)		

4.51 Income-tax

Interest paid on borrowed capital ₹ 20,00,000 @ 12%	2,40,000	
Pre-construction interest ₹ 2,40,000 / 5	<u>48,000</u>	
	2,88,000	
As per second proviso to section 24(b), interest deduction restricted to		<u>1,50,000</u>
Loss under the head "income from house property" of Mr. A		<u>(1,50,000)</u>

Computation of income from house property of Mr. B for A.Y. 2014-15

Particulars	Ground floor (Self occupied)	First floor
Gross annual value (See note below)	Nil	90,000
Less: Municipal taxes (for first floor)		<u>4,000</u>
Net annual value (A)	Nil	86,000
Less: Deduction under section 24		
(a) 30% of net annual value		25,800
(b) interest on borrowed capital		
Current year interest		
₹12,00,000 x 10% = ₹ 1,20,000	60,000	60,000
Pre-construction interest		
₹ 12,00,000 x 10% x 9/12 = ₹ 90,000		
₹ 90,000 allowed in 5 equal installments		
₹ 90000 / 5 = ₹ 18,000 per annum	<u>9,000</u>	<u>9,000</u>
Total deduction under section 24 (B)	<u>69,000</u>	<u>94,800</u>
Income from house property (A)-(B)	<u>(69,000)</u>	<u>(8,800)</u>
Loss under the head "income from house property" of Mr. B (both ground floor and first floor)	(77,800)	

Note : Computation of Gross Annual Value (GAV) of first floor of B's house

If a single unit of property (in this case the first floor of B's house) is let out for some months and self-occupied for the other months, then the annual letting value (ALV) of the property shall be taken into account for determining the annual value. The ALV shall be compared with the actual rent and whichever is higher shall be adopted as the annual value. In this case, the actual rent shall be the rent for the period for which the property was let out during the previous year.

The Annual Letting Value (ALV) is the higher of fair rent and municipal value. This should be considered for 9 months since the construction of property was completed only on 30.6.2013.

Annual letting value = ₹ 75,000 being higher of -
 Fair rent = 1,00,000 x 9 /12 = ₹ 75,000
 Municipal value = 72,000 x 9/12 = ₹ 54,000
 Actual rent = ₹ 90,000 (₹ 15,000 p.m. for 6 months from July to December, 2013)
 Gross annual value = ₹ 90,000 (being higher of ALV of ₹ 75,000 and actual rent of ₹ 90,000)

Question 6

Mr. Vikas owns a house property whose Municipal Value, Fair Rent and Standard Rent are ₹ 96,000, ₹ 1,26,000 and 1,08,000 (per annum), respectively.

During the Financial Year 2013-14, one-third of the portion of the house was let out for residential purpose at a monthly rent of ₹ 5,000. The remaining two-third portion was self-occupied by him. Municipal tax @ 11 % of municipal value was paid during the year.

The construction of the house began in June, 2006 and was completed on 31-5-2009.

Vikas took a loan of ₹ 1,00,000 on 1-7-2006 for the construction of building.

He paid interest on loan @ 12% per annum and every month such interest was paid.

Compute income from house property of Mr. Vikas for the Assessment Year 2014-15.

Answer

Computation of income from house property of Mr. Vikas for the A.Y. 2014-15

Particulars	₹	₹
Income from house property		
I. Self-occupied portion (Two third)		
Net Annual value		Nil
Less: Deduction under section 24(b)		
Interest on loan (See Note below) (₹ 18,600 x 2/3)		<u>12,400</u>
Loss from self occupied property		(12,400)
II. Let-out portion (One third)		
Gross Annual Value		
(a) Actual rent received (₹ 5,000 x 12)	₹ 60,000	
(b) ALV	₹ 36,000	
[higher of municipal valuation (i.e., ₹ 96,000) and fair rent (i.e., ₹ 1,26,000) but restricted to standard rent (i.e., ₹ 1,08,000)] = ₹ 1,08,000 x 1/3		
Higher of (a) or (b)	60,000	
Less: Municipal taxes (₹ 96,000 x 11% x 1/3)	<u>3,520</u>	
Net Annual Value		56,480

4.53 Income-tax

Less: Deductions under section 24		
(a) 30% of NAV	16,944	
(b) Interest on loan (See Note below) (₹ 18,600 x 1/3)	<u>6,200</u>	<u>33,336</u>
Income from house property		<u>20,936</u>

Note: Interest on loan taken for construction of building

Interest for the year (1.4.2013 to 31.3.2014) = 12% of ₹ 1,00,000 = ₹ 12,000

Pre-construction period interest = 12% of ₹ 1,00,000 for 33 months (from 1.07.2006 to 31.3.2009)
= ₹ 33,000

Pre-construction period interest to be allowed in 5 equal annual installments of ₹ 6,600 from the year of completion of construction i.e. from F.Y. 2009-10 till F.Y. 2013-14.

Therefore, total interest deduction under section 24 = ₹ 12,000 + ₹ 6,600 = ₹ 18,600.

Question 7

Mr. X owns one residential house in Mumbai. The house is having two identical units. First unit of the house is self occupied by Mr. X and another unit is rented for ₹ 8,000 p.m. The rented unit was vacant for 2 months during the year. The particulars of the house for the previous year 2013-14 are as under:

Standard rent	₹ 1,62,000 p.a.
Municipal valuation	₹ 1,90,000 p.a.
Fair rent	₹ 1,85,000 p. a
Municipal tax (Paid by Mr. X)	15% of municipal valuation
Light and water charges	₹ 500 p.m.
Interest on borrowed capital	₹ 1,500 p.m.
Lease money	₹ 1,200 p.a.
Insurance charges	₹ 3,000 p.a.
Repairs	₹ 12,000 p.a.

Compute income from house property of Mr. X for the A.Y. 2014-15.

Answer

Computation of Income from house property for A.Y. 2014-15

Particulars	₹	₹
(A) Rented unit (50% of total area – See Note 1 below)		
Step I - Computation of Annual letting Value		
Municipal valuation (₹ 1,90,000 x ½)	95,000	
Fair rent (₹ 1,85,000 x ½)	92,500	

Standard rent (₹ 1,62,000 x ½)	81,000	
Annual letting value is higher of municipal valuation and fair rent, but restricted to standard rent	81,000	
Step II - Actual Rent		
Rent receivable for the whole year (₹ 8,000 x 12)	96,000	
Step III – Computation of Gross Annual Value		
Actual rent received owing to vacancy (₹ 96,000 – ₹ 16,000)	80,000	
Since, owing to vacancy the actual rent received is lower than the annual letting value, the actual rent received is the Gross Annual value		
Gross annual value		80,000
Less: Municipal taxes (15% of ₹ 95,000)		<u>14,250</u>
Net Annual value		65,750
Less : Deductions under section 24 -		
(i) 30% of net annual value	19,725	
(ii) Interest on borrowed capital (₹ 750 x 12)	<u>9,000</u>	<u>28,725</u>
Taxable income from let out portion		37,025
(B) Self occupied unit (50% of total area – See Note 1 below)		
Annual value	Nil	
Less : Deduction under section 24 -		
Interest on borrowed capital (₹ 750 x 12)	<u>9,000</u>	<u>9,000</u>
Income from house property		<u>28,025</u>

Note: No deduction will be allowed separately for light and water charges, lease money paid, insurance charges and repairs.

Question 8

Mrs. Indu, a resident individual, owns a house in U.S.A. She receives rent @ \$ 2,000 per month. She paid municipal taxes of \$ 1,500 during the financial year 2013-14. She also owns a two storied house in Mumbai, ground floor is used for her residence and first floor is let out at a monthly rent of ₹ 10,000. Standard rent for each floor is ₹ 11,000 per month and fair rent is ₹ 10,000 per month. Municipal taxes paid for the house amounts to ₹ 7,500. Mrs. Indu had constructed the house by taking a loan from a nationalised bank on 20.6.2008. She repaid the loan of ₹ 54,000 including interest of ₹ 24,000. The value of one dollar is to be taken as ₹ 45.

Compute total income from house property of Mrs. Indu.

Answer

Computation of Income from House Property of Mrs. Indu for the A.Y. 2014-15

Particulars	₹	₹
House property in USA		
GAV– Rent received {treated as fair rent} (\$2,000 p.m. x ₹ 45 per USD x 12 months)	10,80,000	
Less : Municipal taxes paid (\$1,500 x ₹ 45 per USD)	67,500	
Net Annual Value (NAV)	10,12,500	
Less : Deduction under section 24		
30% of NAV	3,03,750	7,08,750
House property in Mumbai (Let- out portion - First Floor)		
Annual Letting Value (lower of standard rent and fair rent)		
Standard Rent (₹ 11,000 x 12)	₹ 1,32,000	
Fair rent (₹ 10,000 x 12)	₹ 1,20,000	1,20,000
Actual rent received (10,000 × 12)		1,20,000
Gross Annual Value (higher of ALV and actual rent)		1,20,000
Less : Municipal taxes paid (50% of ₹ 7,500)	3,750	
Net Annual Value (NAV)	1,16,250	
Less : Deduction under section 24		
30% of NAV	₹ 34,875	
Interest on housing loan (50% of ₹ 24,000)	₹ 12,000	46,875
		69,375
Income from House property in Mumbai (Self-occupied portion - Ground Floor)		
Gross annual value	Nil	
Less: Municipal taxes	Nil	
Net Annual Value (NAV)	Nil	
Less : Deduction under section 24		
30% of NAV	Nil	
Interest on housing loan (50% of ₹ 24,000)	12,000	(-) 12,000
Income from house property		7,66,125

Question 9

Explain the treatment of unrealized rent and its recovery in subsequent years under the provisions of Income-tax Act, 1961.

Answer

Unrealised rent refers to the rent payable but not paid by the tenant and which the owner is also not able to realize from the tenant. As per *Explanation* below section 23(1), the amount of rent which the owner cannot realize shall not be included in the actual rent while determining the annual value of the property, subject to fulfillment of following conditions prescribed under Rule 4 of the Income-tax Rules, 1962:

- (a) the tenancy must be bonafide;
- (b) the defaulting tenant has vacated the property or steps have been taken to compel him to vacate the property;
- (c) the defaulting tenant does not occupy any other property of the assessee; and
- (d) the assessee has taken all reasonable steps to institute legal proceedings for the recovery of unpaid rent or satisfies the Assessing Officer that the legal proceedings would be useless.

If the conditions mentioned above are satisfied, then, the actual rent should be reduced by the unrealized rent and thereafter, compared with the Annual Letting Value (being the higher of fair rent and municipal value, but restricted to standard rent) for computing the gross annual value.

As per section 25AA, the unrealised rent, when realised in any subsequent year, shall be deemed to be the income chargeable under the head 'Income from house property' in the previous year in which such rent is realised, whether or not the assessee is the owner of the property in that previous year.

Question 10

Explain briefly the applicability of section 22 for chargeability of income-tax for:

- (i) *House property situated in foreign country and*
- (ii) *House property with disputed ownership.*

Answer

Applicability of section 22 for chargeability of income-tax for –

(i) House property situated in foreign country

A resident assessee is taxable under section 22 in respect of annual value of a house property situated in foreign country. A resident but not ordinarily resident or a non resident is taxable in respect of income from such property if the income is received in India during the previous year. Once incidence of tax is attracted under section 22, the annual value will be computed as if the property is situated in India.

(ii) House property with disputed ownership

If the title of ownership of the house property is under dispute in a court of law, the decision about who is the owner lies with the Income tax Department. The assessment cannot be held up for such dispute. Generally, a person who receives the income or who enjoys the possession of the house property as owner, though his claim is under dispute, is assessable to tax under section 22.

Question 11

Ownership itself is the criteria for assessment under the head income from house property. Discuss.

Answer

Section 27 enumerates certain cases, where the legal ownership may vest with one person whereas the taxability is cast on another person who is deemed to be the owner.

In these specific cases, the charge of tax is on the deemed owner and not on the legal owner. The exceptions are given below:

- (i) In case of transfer of house property to spouse (not being a transfer in connection with an agreement to live apart) or minor child (not being a married daughter) without adequate consideration - transferor is the deemed owner.
- (ii) Holder of an impartible estate – shall be deemed to be the individual owner of all the properties comprised in the estate.
- (iii) A member of a co-operative society/company/AOP to whom a building or part thereof is allotted or leased under a house building scheme – shall be deemed to be the owner of building or part thereof.
- (iv) A person who is allowed to take or retain possession of any building or part thereof is the deemed owner of such building or part thereof if such possession is obtained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882.
- (v) A person who acquires any rights (excluding any rights by way of a lease from month to month or for a period not exceeding one year) in or with respect to any building or part thereof, by virtue of any such transaction as is referred to in section 269UA(f).

Therefore, legal ownership itself is not the criteria for assessment of income under the head "Income from house property".

Also, the provisions of section 25AA and 25B dealing with receipt of unrealised rent and arrears of rent also fall in this category. The receipt is considered as income under the head 'house property' though the recipient may not have legal ownership of the property to which the receipt relates.

Question 12

Discuss the following issues relating to Income from house property:

- (i) *Income earned by residents from house properties situated in foreign countries.*
- (ii) *Properties which are used for agricultural purposes.*

Answer

- (i) In case of resident individual, his global income is taxable in India. Therefore, income earned by residents from house properties situated in foreign countries is taxable in India.

If the income from house properties situated outside India is chargeable to tax in India the annual value of such property would be computed as if the property is situated in India. Further, municipal taxes paid under the laws of that country can also be deducted while arriving at the Annual Value of the property. The Madras High Court in *CIT v. Venugopala Reddiar [1965] 58 ITR 439* observed that while computing taxable income, no distinction should be made between a house property situated in India and a house property situated abroad.

- (ii) If the property is used for agricultural purposes, the annual value of such property would be treated as "Agricultural Income" as per section 2(1A)(c) and it is exempt under section 10(1) of the Act. However, if the house property is used for purpose other than agriculture the annual value of such property cannot be treated as agricultural income.

Question 13

- (1) *X let out his property to Y. Y sublets it. How is sub-letting receipt to be assessed in the hands of Y?*
- (2) *Y has built a house on a leasehold land. He has let out the property and claims that the income therefrom is chargeable under the head "Income from other sources". He has deducted expenses on repairs, security charges, insurance and collection charges in all amounting to 40% of receipts. Is Mr. Y's claim valid?*
- (3) *Z uses his property for his own business. Would the annual value be subject to tax under the head "Income from house property"?*

Answer

- (1) Sub-letting receipt in the hands of Y can be assessed as "Income from Other Sources" or as "Profits and gains from business or profession" depending upon the facts and circumstances of each case. It is not assessable as income from house property.
- (2) No, Mr. Y's claim is not valid. The income from letting out of house built on leasehold land is assessable as "Income from house property" since ownership of land is not a pre-requisite for assessment of income under this head. 30% of Net Annual Value is allowed as deduction under section 24.
- (3) Where the assessee uses his property for business, it is not assessable under the head "Income from house property". He is entitled to depreciation under section 32(1)(ii) on the building.

Question 14

Discuss the tax liability in respect of arrears of rent.

Answer

As per section 25B, where the assessee receives any amount by way of arrears of rent in respect of any property consisting of buildings or land appurtenant thereto of which he is the owner, the amount so received shall be chargeable to tax under the head "Income from House Property". It shall be charged to tax as the income of the previous year in which such rent is received even if the assessee is no longer the owner of such property. In computing the income chargeable to tax in respect of the arrears so received, 30% shall be allowed as a deduction, irrespective of the actual expenditure incurred.

Question 15

Mr. Kalpesh borrowed a sum of ₹ 30 lakhs from the National Housing Bank towards purchase of a residential flat. The loan amount was disbursed directly to the flat promoter by the bank. Though the construction was completed in May, 2014, repayments towards principal and interest had been made during the year ended 31.3.2014.

In the light of the above facts, state:

- (i) Whether Mr. Kalpesh can claim deduction under Section 24 in respect of interest for the assessment year 2014-15;*
- (ii) Whether deduction under Section 80C can be claimed for the above assessment year, even though the construction was completed only after the closure of the year?*

Answer

(i) Interest on borrowed capital is allowed as deduction under section 24(b)

As per section 24(b), Interest payable on loans borrowed for the purpose of acquisition, construction, repairs, renewal or reconstruction of house property can be claimed as deduction. Interest payable on borrowed capital for the period prior to the previous year in which the property has been acquired or constructed, can be claimed as deduction over a period of 5 years in equal annual installments commencing from the year of acquisition or completion of construction.

It is stated that the construction is completed only in May, 2014. Hence, deduction in respect of interest on housing loan cannot be claimed in the assessment year 2014-15.

- (ii)** Clause (xviii) of section 80C is attracted where there is any payment for the purpose of purchase or construction of a residential house property, the income from which is chargeable to tax under the head 'Income from house property'. Such payment covers repayment of any amount borrowed from the National Housing Bank.

However, deduction is *prima facie* eligible only if the income from such property is chargeable to tax under the head "Income from House Property". During the assessment year 2014-15, there is no such income chargeable under this head. Hence, deduction under section 80C cannot be claimed for A.Y. 2014-15.

EXERCISES

1. Ganesh is a member of a house building co-operative society. The society is the owner of the flats constructed by it. One of the flats is allotted to Ganesh. The income from that flat will be assessed in the hands of
 - a) Co-operative Society
 - b) Ganesh
 - c) Neither of the above.
2. Vacant site lease rent is taxable as
 - a) Income from house property
 - b) Business income
 - c) Income from other sources or business income, as the case may be
3. Treatment of unrealized rent for determining income from house property
 - a) To be deducted from annual letting value
 - b) To be deducted from actual rent
 - c) To be deducted under section 24 from annual value
4. Municipal taxes to be deducted from GAV should be
 - a) Paid by the tenant during the previous year
 - b) Paid by the owner during the previous year
 - c) Accrued during the previous year
5. Deduction under section 24(a) is
 - a) 1/3rd of NAV
 - b) repairs actually incurred by the owner
 - c) 30% of NAV
6. Interest on borrowed capital accrued up to the end of the previous year prior to the year of completion of construction is allowed
 - a) as a deduction in the year of completion of construction
 - b) in 5 equal annual installments from the year of completion of construction
 - c) In the respective year in which the interest accrues
7. The ceiling limit of deduction under section 24(b) in respect of interest on loan taken on 1.4.2011 for repairs of a self-occupied house is
 - a) ₹ 30,000 p.a.
 - b) ₹ 1,50,000 p.a.
 - c) No limit

4.61 Income-tax

8. Where an assessee has two house properties for self-occupation, the benefit of nil annual value will be available in respect of -
- Both the properties
 - The property which has been acquired/constructed first
 - Any one of the properties, at the option of the assessee
9. Leena received ₹ 30,000 as arrears of rent during the P.Y. 2013-14. The amount taxable under section 25B would be -
- 30,000
 - 21,000
 - 20,000
10. Vidya received ₹ 90,000 in May, 2013 towards recovery of unrealised rent, which was deducted from actual rent during the P.Y. 2012-13 for determining annual value. The amount taxable under section 25AA for A.Y.2014-15 would be -
- 90,000
 - 63,000
 - 60,000
11. Ganesh and Rajesh are co-owners of a self-occupied property. They own 50% share each. The interest paid by each co-owner during the previous year on loan (taken for acquisition of property during the year 2004) is ₹ 1,62,000. The amount of allowable deduction in respect of each co-owner is -
- 1,62,000
 - 75,000
 - 1,50,000
12. An assessee, who was deriving income from house property, realised a sum of ₹ 52,000 on account of display of advertisement hoardings of various concerns on the roof of the building. He claims that this amount should be considered under the head "Income from house property" and not "Income from other sources". How do you deal with the following issue under the provisions of the Income-tax Act, 1961?
13. Ram owned a house property at Chennai which was occupied by him for the purpose of his residence. He was transferred to Mumbai in June, 2013 and therefore, he let out the property w.e.f. 1.7.2013 on a monthly rent of ₹ 8,000. The corporation tax payable in respect of the property was ₹ 2,000 of which 50% was paid by him before 31.3.2014. Interest on money borrowed for the construction of the property amounted to ₹ 12,000. Compute the income from house property for the A.Y.2014-15.
14. What do you understand by "Composite Rent"? What is the tax treatment of Composite Rent under the Income-tax Act, 1961?

Answers

1. b; 2. c; 3. b; 4. b; 5. c; 6. b; 7. a; 8. c; 9. b; 10. a; 11. c, 13. ₹ 37,700

UNIT 3 : Profits and Gains of Business or Profession

Question 1

A car purchased by Dr. Soman on 10.08.2011 for ₹ 5,25,000 for personal use is brought into professional use on 1.07.2013 by him, when its market value was ₹ 2,50,000.

Compute the actual cost of the car and the amount of depreciation for the assessment year 2014-15 assuming the rate of depreciation to be 15%.

Answer

As per section 43(1), the expression "actual cost" would mean the actual cost of asset to the assessee.

The purchase price of ₹ 5,25,000 is, therefore, the actual cost of the car to Dr. Soman. Market value (i.e. ₹ 2,50,000) on the date when the asset is brought into professional use is not relevant.

Therefore, amount of depreciation on car as per section 32 for the A.Y.2014-15 would be ₹ 78,750, being ₹ 5,25,000 x 15%.

Note : Explanation 5 to section 43(1) providing for reduction of notional depreciation from the date of acquisition of asset for personal use to determine actual cost of the asset is applicable only in case of building which is initially acquired for personal use and later brought into professional use. It is not applicable in respect of other assets.

Question 2

M/s. Dollar Ltd., a manufacturing concern, furnishes the following particulars:

		₹
(i)	Opening writing down value of plant and machinery (15% block)	5,00,000
(ii)	Purchase of plant and machinery (put to use before 01.10.2013)	2,00,000
(iii)	Sale proceeds of plant and machinery which became obsolete- the plant and machinery was purchased on 01-04-2011 for ₹ 5,00,000.	5,000

Further, out of purchase of plant and machinery:

- Plant and machinery of ₹ 20,000 has been installed in office.
- Plant and machinery of ₹ 20,000 was used previously for the purpose of business by the seller.

Compute depreciation and additional depreciation as per Income-tax Act, 1961 for the Assessment Year 2014-15.

Answer

Computation of written down value of Plant and Machinery of M/s. Dollar Ltd. for the A.Y. 2014-15

Particulars	₹
Opening written down value (as on 01.04.2013)	5,00,000
Add: Purchase of plant and machinery during the previous year	<u>2,00,000</u>
	7,00,000
Less: Sale proceeds of obsolete plant and machinery sold during the year	<u>5,000</u>
Closing Written Down Value (as on 31.03.2014)	<u>6,95,000</u>

Computation of Depreciation and Additional Depreciation for A.Y. 2014-15 as per section 32 of the Income-tax Act, 1961

Particulars	₹
Normal Depreciation (₹ 6,95,000 x 15%)	1,04,250
Additional Depreciation(Refer Note 2)(₹ 2,00,000 – ₹ 20,000 - ₹ 20,000) x 20%	<u>32,000</u>
Depreciation on Plant and Machinery	<u>1,36,250</u>

Notes:-

- (1) Since the new plant and machinery was purchased and put to use before 1.10.2013, it was put to use for more than 180 days in the year. Hence, full depreciation is allowable for A.Y. 2014-15.
- (2) As per section 32(1)(ia), additional depreciation is allowable in the case of any new machinery or plant acquired and installed after 31.3.2005 by an assessee engaged, *inter alia*, in the business of manufacture or production of any article or thing, at the rate of 20% of the actual cost of such machinery or plant.

However, additional depreciation shall not be allowed in respect of, *inter alia*, –

- (i) any machinery or plant which, before its installation by the assessee, was used either within or outside India by any other person;
- (ii) any machinery or plant installed in office premises, residential accommodation or in any guest house.

In view of the above provisions, additional depreciation cannot be claimed in respect of -

- (i) Plant and machinery of ₹ 20,000 used previously for the purpose of business by the seller.
- (ii) Plant and machinery of ₹ 20,000, installed in office.

Therefore, in the given case additional depreciation has to be provided only on ₹ 1,60,000 (i.e., ₹ 2,00,000 - ₹ 40,000).

Question 3

Harish Jayaraj Pvt. Ltd. is converted into Harish Jayaraj LLP on 1.1.2014. The following particulars are available to you:

S. No.	Particulars	₹
(i)	Cost of land	5,00,000
(ii)	WDV of machinery as on 1.4.2013	3,30,000
(iii)	Patents acquired on 1.6.2013	3,00,000
(iv)	Building acquired on 12.3.2012 for which deduction was allowed under section 35AD.	7,00,000
(v)	Above building was revalued as on the date of conversion into LLP as	12,00,000
(vi)	Unabsorbed business loss as on 1.4.2013 (Related to A.Y. 2010-11)	9,00,000

Though the conversion into LLP took place on 1.1.2014, there was disruption of business and the assets were put into use by the LLP only from 1st March, 2014 onwards.

The company earned profits of ₹ 8 lacs prior to computation of depreciation.

Assuming that the necessary conditions laid down in section 47(xiiib) of the Income-tax Act, 1961 have been complied with, explain the tax treatment of the above in the hands of the LLP.

Answer

Tax treatment of depreciation and unabsorbed business loss of a private company on its conversion into a LLP

The LLP would be allowed to carry forward and set-off the business loss and unabsorbed depreciation of the predecessor company [Section 72A(6A)].

1. Depreciation

The aggregate depreciation allowable to the predecessor company and successor LLP shall not exceed, in any previous year, the depreciation calculated at the prescribed rates as if the conversion had not taken place. Such depreciation shall be apportioned between the predecessor company and the successor LLP in the ratio of the number of days for which the assets were used by them [Section 32(1)]

Therefore, depreciation has to be first calculated as if the conversion had not taken place and then apportioned between the company and the LLP in the ratio of the number of days for which the assets were used by them.

4.65 Income-tax

		₹		₹
Block I	Machinery	3,30,000	15%	49,500
Block II	Patents	3,00,000	25%	<u>75,000</u>
				<u>1,24,500</u>

Allocation of depreciation

Depreciation on machinery and patents have to be apportioned between the company and the LLP in the ratio of the number of days for which the assets were used by them. Since patents were acquired only on 1.6.2013, it could have been used by the company for 214 days only. Therefore, the depreciation on assets has to be allocated between the company and LLP as follows –

Asset	Total depreciation for the year	Company		LLP	
		No. of days of usage	Depreciation	No. of days of usage	Depreciation
Machinery	49,500	275	44,485	31	5,015
Patents	<u>75,000</u>	214	<u>65,510</u>	31	<u>9,490</u>
	<u>1,24,500</u>		<u>1,09,995</u>		<u>14,505</u>

Therefore, depreciation to be allowed in the hands of the company is ₹ 1,09,995 and depreciation to be allowed in the hands of the LLP is ₹ 14,505.

2. Unabsorbed business loss to be carried forward by the LLP:

Particulars	₹
Profits of the company before depreciation	8,00,000
Less: Current year depreciation	<u>1,09,995</u>
Business income of the company after depreciation	6,90,005
Brought forward business loss	<u>9,00,000</u>
Unabsorbed business loss as on 31.12.2013 to be carried forward by the LLP	<u>2,09,995</u>

3. Actual cost of assets to the LLP

- (1) The actual cost of the block of assets in case of the LLP shall be the WDV of the block of assets as in the case of the company on the date of conversion. The WDV as on 1.1.2014 for Machinery and Patents are ₹ 2,85,515 and ₹ 2,34,490, respectively, which would be the actual cost in the case of the LLP.

WDV of Machinery as on 1.1.2014 = ₹ 3,30,000 – ₹ 44,485 = ₹ 2,85,515

WDV of Patents as on 1.1.2014 = ₹ 3,00,000 – ₹ 65,510 = ₹ 2,34,490

- (2) Land is not a depreciable asset. The cost of acquisition of land to the LLP would be the cost for which the company acquired it, as increased by the cost of improvement.

- (3) In respect of the building, deduction had been allowed in the earlier year under section 35AD. Hence, there is no question of depreciation during the current year. The actual cost of the building to the LLP would be Nil.

Question 4

Sai Ltd. has a block of assets carrying 15% rate of depreciation, whose written down value on 01.04.2013 was ₹ 40 lacs. It purchased another asset (second-hand plant and machinery) of the same block on 01.11.2013 for ₹ 14.40 lacs and put to use on the same day. Sai Ltd. was amalgamated with Shirdi Ltd. with effect from 01.01.2014.

You are required to compute the depreciation allowable to Sai Ltd. & Shirdi Ltd. for the previous year ended on 31.03.2014 assuming that the assets were transferred to Shirdi Ltd. at ₹ 60 lacs.

Answer

Statement showing computation of depreciation allowable to Sai Ltd. & Shirdi Ltd. for P.Y. 2013-14

Particulars	₹
Written down value (WDV) as on 1.4.2013	40,00,000
Addition during the year (used for less than 180 days)	<u>14,40,000</u>
Total	<u>54,40,000</u>
Depreciation on ₹ 40,00,000 @ 15%	6,00,000
Depreciation on ₹ 14,40,000 @ 7.5%	<u>1,08,000</u>
Total depreciation for the year	<u>7,08,000</u>
Apportionment between two companies:	
(a) Amalgamating company, Sai Ltd.	
₹ 6,00,000 × 275/365	4,52,055
₹ 1,08,000 × 61/151	<u>43,629</u>
	<u>4,95,684</u>
(b) Amalgamated company, Shirdi Ltd.	
₹ 6,00,000 × 90/365	1,47,945
₹ 1,08,000 × 90/151	<u>64,371</u>
	<u>2,12,316</u>

Notes:

- (1) The aggregate deduction, in respect of depreciation allowable to the amalgamating company and amalgamated company in the case of amalgamation shall not exceed in any case, the deduction calculated at the prescribed rates as if the amalgamation had not taken place. Such deduction shall be apportioned between the amalgamating company and the amalgamated company in the ratio of the number of days for which the assets were used by them.

- (2) The price at which the assets were transferred, i.e., ₹ 60 lacs, has no implication in computing eligible depreciation.

Question 5

M/s Sidhant & Co., a sole proprietary concern is converted into a company, Sidhant Co. Ltd. with effect from November 29, 2013. The written down value of assets as on April 1, 2013 is as follows:

Items	Rate of Depreciation	WDV as on 1st April, 2013
Building	10%	₹ 3,50,000
Furniture	10%	₹ 50,000
Plant and Machinery	15%	₹ 2,00,000

Further, on October 15, 2013, M/s Sidhant & Co. purchased a plant for ₹ 1,00,000 (rate of depreciation 15%). After conversion, the company added another plant worth ₹ 50,000 (rate of depreciation 15%).

Compute the depreciation available to (i) M/s Sidhant & Co. and (ii) Sidhant Co. Ltd. for Assessment Year 2014-15.

Answer

In the case of conversion of sole proprietary concern into a company as per section 47(xiv), the depreciation should be first calculated for the whole year assuming that no succession had taken place. Thereafter, the depreciation should be apportioned between the sole proprietary concern and the company in the ratio of the number of days for which the assets were used by them. It is assumed that in this case, the conditions specified in section 47(xiv) are satisfied.

Computation of depreciation allowable to Sidhant & Co. for A.Y.2014-15

Particulars	₹	₹
Building		
WDV as on 1.4.2013	3,50,000	
Depreciation@10%		35,000
Furniture		
WDV as on 1.4.2013	50,000	
Depreciation@10%		5,000
Plant and Machinery		
WDV as on 1.4.2013	2,00,000	
Add: Additions during the year (purchased on 15.10.2013)	<u>1,00,000</u>	
	3,00,000	
Less: Depreciation for the year (15% of ₹ 2,00,000 + 50% of 15% of ₹ 1,00,000) (₹ 30,000 + ₹ 7,500)		37,500

(Depreciation on new machinery is restricted to 50% of eligible depreciation, since the asset is put to use for less than 180 days in that year)		
Total depreciation for the year		<u>77,500</u>
Proportionate depreciation allowable to Sidhant & Co. for 242 days		
On existing assets (i.e. 1.4.2013 to 28.11.2013) (i.e. $242/365 \times ₹ 70,000$)	46,411	
On new machine for 45 days i.e., $45/168 \times ₹ 7,500$	<u>2,009</u>	48,420

Computation of depreciation allowable to Sidhant Co. Ltd. for A.Y.2014-15

Particulars	₹
(i) Depreciation on the assets on conversion Proportionately for 123 days i.e. after conversion period $(123/365 \times ₹ 70,000) + (123/168 \times ₹ 7,500) = ₹ 23,589 + ₹ 5,491$	29,080
(ii) Depreciation @ 50% of normal rate of 15% on ₹ 50,000, being the value of plant purchased after conversion, which was put to use for less than 180 days	<u>3,750</u>
Depreciation allowable to Sidhant Co. Ltd.	<u>2,830</u>

Note: Since it has not been specifically mentioned that M/s Sidhant & Co. and Sidhant Co. Ltd. are manufacturing concerns or companies engaged in the business of generation or generation and distribution of power, additional depreciation is not provided for.

Question 6

What are intangible assets? Give four examples. What is the rate of depreciation on a block of intangible assets?

Answer

Intangible assets are assets which are not corporeal i.e., not capable of being touched. Such assets are represented by rights of the persons through them.

According to Explanation 3(b) to section 32(1), the following are intangible assets :

- (a) Know-how
- (b) Patents
- (c) Copyrights
- (d) Trade Marks
- (e) Licences
- (f) Franchises
- (g) any other business or commercial rights of similar nature.

They are to be depreciated at the rate of 25%.

Question 7

A car purchased by S on 10.8.2009 for ₹ 3,25,000 for personal use is brought into the business of the assessee on 01.12.2013, when its market value is ₹ 1,50,000.

Compute the actual cost of the car and the amount of depreciation for the Assessment year 2014-15 assuming the rate of depreciation to be 15%.

Answer

In this case, the car was purchased for personal use on 10.8.2009 for ₹ 3,25,000 and subsequently brought into the business of the assessee on 1.12.2013. The "actual cost" of car is ₹ 3,25,000.

Explanation 5 to section 43(1) provides for determination of "actual cost" of building used for private purposes subsequently brought into business. This Explanation does not apply to any other asset in as much as it refers only to buildings.

The admissible depreciation for A.Y.2014-15 is ₹ 48,750 (i.e.15% of ₹ 3,25,000). As the car was not acquired during the previous year 2013-14, full depreciation is available for the year even if it is put to use for less than 180 days during the previous year. The condition of restricting depreciation to 50% of the prescribed percentage would apply only where the asset was acquired by the assessee in the previous year.

Question 8

Gopichand Industries furnishes you the following information:

	(₹)
Block I WDV of Plant and machinery (consisting of 10 looms)	5,00,000
Rate of depreciation 15%	
Block II WDV of Buildings (consisting of 3 buildings)	12,50,000
Rate of depreciation 10%	
Acquired on 5-07-2013 – 5 looms for	4,00,000
Sold on 7-12-2013 – 15 looms for	10,00,000
Acquired on 10-01-2014 – 2 looms for	3,00,000

Compute depreciation claim for the Assessment year 2014-15.

Answer**Computation of depreciation for Gopichand Industries for A.Y.2014-15**

Particulars	₹	₹
Block 1 : Plant & machinery (Rate of depreciation – 15%)		
WDV as on 1 st April (10 looms)	5,00,000	
Add: Additions during the year		

- 5 looms acquired on 5 th July	4,00,000	
- 2 looms acquired on 10 th January	<u>3,00,000</u>	
	12,00,000	
<i>Less</i> : Assets sold during the year		
- 15 looms sold on 7 th December	<u>10,00,000</u>	
W.D.V. as on 31 st March (2 looms)	2,00,000	
Depreciation on ₹ 2 lakhs @ 15% (limited to 50%)		15,000
Block II: Buildings (Rate of depreciation – 10%)		
WDV as on 1 st April (3 buildings)	12,50,000	
Depreciation on ₹ 12,50,000 @ 10%		<u>1,25,000</u>
Total depreciation for the year		<u>1,40,000</u>

Notes:

1. Closing balance of Block 1 : Plant and machinery represents the looms acquired on 10th January. These looms have been put to use or less than 180 days during the previous year, and therefore, only 50% of normal depreciation is permissible.
2. No additional depreciation @ 20% of the cost of new plant and machinery is provided for assuming that all conditions contained in the section 32(1)(ia) have not been fulfilled.

Question 9

M/s. QQ & Co., a sole proprietary concern, was converted into a company on 1.9.2013. Before the conversion, the sole proprietary concern had a Block of Plant and Machinery (Rate of depreciation 15%), whose WDV as on 1.4.2013 was ₹ 3,00,000. On 1st April itself, a new plant of the same block was purchased for ₹ 1,20,000. After the conversion, the company has purchased the same type of Plant on 1.1.2014 for ₹ 1,60,000.

Compute the depreciation that would be allocated between the sole proprietary concern and the successor company.

Answer

Computation of depreciation in the case of transfer of business:

Depreciation is to be calculated as if there is no succession.	(₹)
WDV as on 1 st April	3,00,000
<i>Add</i> : Additions made before succession	<u>1,20,000</u>
	4,20,000
<i>Less</i> : Sale consideration of the asset sold	<u>Nil</u>
	4,20,000
Depreciation @ 15%	<u>63,000</u>

4.71 Income-tax

Allocation of depreciation between sole proprietary concern and the successor company:

The depreciation of ₹ 63,000 is to be allocated in the ratio of number of days the assets were used by the sole proprietary concern and the company.

Ex-sole proprietary concern

1st April to 31st August = 153 days ₹ 63,000 x 153 / 365 = ₹ 26,408

Successor company

₹ 63,000 - ₹ 26,408 = ₹ 36,592 (i.e. ₹ 63,000 x 212 / 365)

The depreciation of ₹ 12,000 [50% of 15% on ₹ 1,60,000] in respect of asset purchased by the successor company on 1st January is fully allowable in the hands of the successor company.

Note: Since it has not been specified that the company is a manufacturing company or a company engaged in the generation or generation and distribution of power, additional depreciation has not been provided for.

Question 10

Honest Industry furnishes you the following details pertaining to the financial year 2013-14:

Description	Plant & Machinery	Building	Intangible assets (patents)
Rate of depreciation	15%	10%	25%
Opening balance as on 01-04-2013	₹ 14,50,000	₹ 25,00,000	₹ 15,00,000
Acquired before 30-09-2013	₹ 12,00,000	Nil	₹ 5,00,000
Acquired after 01-12-2013	₹ 4,00,000	₹ 18,00,000	Nil
Transferred in March 2014, one of the patents held for the past 2 years	-	-	₹ 3,00,000

A machinery acquired in July 2013 original cost ₹ 1,50,000 was destroyed by fire and the assessee received compensation of ₹ 50,000 from the insurance company.

Newly acquired building given above includes value of land of ₹ 3,00,000.

Calculate the eligible depreciation claim for the assessment year 2014-15.

Note : Ignore additional/accelerated depreciation.

Answer

Computation of depreciation allowable to Honest Industry for the A.Y. 2014-15

Particulars	Plant & Machinery	Building	Intangible assets (patents)	Total (₹)
Rate of depreciation	15%	10%	25%	

Opening Balance as on 1.04.2013	14,50,000	25,00,000	15,00,000	
Add: Assets acquired during the year	<u>16,00,000</u>	<u>15,00,000</u>	<u>5,00,000</u>	
	30,50,000	40,00,000	20,00,000	
Less: Moneys payable in respect of asset sold or destroyed	<u>50,000</u>	<u>-</u>	<u>3,00,000</u>	
W.D.V as on 31.03.2014	<u>30,00,000</u>	<u>40,00,000</u>	<u>17,00,000</u>	
Asset held for less than 180 days	4,00,000	15,00,000	-	
Depreciation@50% of applicable rate	30,000	75,000	-	1,05,000
Asset held for more than 180 days	26,00,000	25,00,000	17,00,000	
Depreciation at the applicable rates	3,90,000	2,50,000	4,25,000	<u>10,65,000</u>
Total Depreciation allowable				<u>11,70,000</u>

Note - Land is not a depreciable asset. Therefore, ₹ 3 lacs, being the value of land, has been reduced from ₹ 18 lacs, being the value of building acquired during the year, for the purpose of computing depreciation.

Question 11

Mr. Praveen Kumar has furnished the following particulars relating to payments made towards scientific research for the year ended 31.3.2014:

Sl. No.	Particulars	₹ (in lacs)
(i)	Payments made to K Research Ltd.	20
(ii)	Payment made to LMN College	15
(iii)	Payment made to OPQ College	10
(iv)	Payment made to National Laboratory	8
(v)	Machinery purchased for in-house scientific research	25
(vi)	Salaries to research staff engaged in in-house scientific research	12

Note: K Research Ltd. and LMN College are approved research institutions and these payments are to be used for the purposes of scientific research.

Compute the amount of deduction available under section 35 of the Income-tax Act, 1961 while arriving at the business income of the assessee.

Answer

Computation of deduction allowable under section 35

Particulars	Amount (₹ in lacs)	Section	% of weighted deduction	Amount of deduction (₹ in lacs)
Payment for scientific research K Research Ltd. [See Note 3]	20	35(1)(ii)	175%	35.00

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LMN College	15	35(1)(ii)	175%	26.25
OPO College [See Note 1]	10	-	Nil	Nil
National Laboratory [See Note 4]	8	35(2AA)	200%	16.00
In-house research [See Note 2]				
Capital expenditure	25	35(1)(iv) r.w. 35(2)	100%	25.00
Revenue expenditure	12	35(1)(i)	100%	<u>12.00</u>
Deduction allowable under section 35				<u>114.25</u>

Notes :-

- Payment to OPO College :** Since the note in the question below item (iii) clearly mentions that only K Research Ltd. and LMN College (mentioned in item (i) and (ii), respectively) are approved research institutions, it is a logical conclusion that OPO College mentioned in item (iii) is not an approved research institution. Therefore, payment to OPO College would not qualify for deduction under section 35.
- Deduction for in-house research and development :** Only company assesseees are entitled to weighted deduction@200% under section 35(2AB) in respect of in-house research and development expenditure incurred. However, in this case, the assessee is an individual. Therefore, he would be entitled to deduction@100% of the revenue expenditure incurred under section 35(1)(i) and 100% of the capital expenditure incurred under section 35(1)(iv) read with section 35(2), assuming that such expenditure is laid out or expended on scientific research related to his business.
- Payment to K Research Ltd. (Alternative Answer) :** Any sum paid to a company registered in India which has as its main object scientific research, as is approved by the prescribed authority, qualifies for a weighted deduction of 125% under section 35(1)(iia). Therefore, it is also possible to take a view that payment of ₹ 20 lakhs to K Research Ltd. qualifies for a weighted deduction of 125% under section 35(1)(iia) since K Research Ltd. is a company. The weighted deduction under section 35(1)(iia) would be ₹ 25 lacs (i.e., 125% of ₹ 20 lacs), in which case, the total deduction under section 35 would be ₹ 104.25 lacs.
- Payment to National Laboratory:** The percentage of weighted deduction under section 35(2AA) in respect of amount paid to National Laboratory is 200%.

Question 12

Vivitha Bio-medicals Ltd. is engaged in the business of manufacture of bio-medical items. The following expenses were incurred in respect of activities connected with scientific research:

Year ended	Item	Amount (₹)
31.03.2011	Land	10,00,000
(Incurred after 1.9.2010)	Building	25,00,000
31.03.2012	Plant and machinery	5,00,000

31.03.2013	Raw materials	2,20,000
31.03.2014	Raw materials and salaries	1,80,000

The business was commenced on 01-09-2013.

In view of availability of better model of plant and machinery, the existing plant and machinery were sold for ₹ 8,00,000 on 1.03.2014.

Discuss the implications of the above for the assessment year 2014-15 along with brief computation of deduction permissible under section 35 assuming that necessary conditions have been fulfilled. You are informed that the assessee's line of business is eligible for claiming deduction under section 35 at 200% on eligible items.

Answer

- As per section 35(2AB), where a company engaged in, *inter alia*, the business of biotechnology incurs any expenditure on scientific research during the current year, it is eligible for claiming weighted deduction of a sum equal to 200% of the eligible expenditure.

Note : The benefit of weighted deduction under this section would be available for expenditure incurred upto 31st March 2017 on in-house research and development facility.

The eligible expenditure and quantum of deduction will be:

- Current year capital expenditure (except expenditure in the nature of cost of any land or building) or revenue expenditure incurred for scientific research (weighted deduction @ 200%) under section 35(2AB).
- Any expenditure incurred during earlier 3 years immediately preceding the date of commencement of business on payment of salary or purchase of materials, or capital expenditure incurred other than expenditure on acquisition of land [actual expenditure qualifies for deduction under section 35(1)].

The deduction available under section 35 for scientific research will, therefore, be:

	Particulars	₹
(a)	Land	Nil
(b)	Building	25,00,000
(c)	Revenue expenses of last 3 years	2,20,000
(d)	Capital expenditure of last 3 years: Plant and machinery	5,00,000
Expenditure allowable under section 35(1)		32,20,000
Current year revenue expenditure ₹ 1,80,000 [200% of ₹ 1,80,000 is allowable under section 35(2AB)]		3,60,000
Total deduction under section 35		35,80,000

4.75 Income-tax

2. Section 41(3) provides that where a capital asset used for scientific research is sold, without having been used for other purposes, the lower of sale proceeds or the total amount of deduction earlier allowed under section 35 will be considered as income from business of the previous year in which the sale took place.

Therefore, the income chargeable to tax under section 41(3) should be lower of the following:

- (1) Sale proceeds i.e. ₹ 8,00,000
(2) Total amount of deduction earlier allowed under section 35 i.e. ₹ 5,00,000
₹ 5,00,000 will be deemed to be the income chargeable to tax under section 41(3).

3. The difference between sale proceeds and business income under section 41(3) will be treated as short-term capital gain.

	₹
Sale proceeds of plant and machinery	8,00,000
Less: Business Income as per section 41(3)	<u>5,00,000</u>
Short-term capital gain	<u>3,00,000</u>

Question 13

Swadeshi Ltd., which follows mercantile system of accounting, obtained licence on 1.6.2012 from the Department of telecommunication for a period of 10 years. The total licence fee payable is ₹ 18,00,000. The relevant details are:

Year ended 31 st March	Licence fee payable for the year (₹)	Payments made	
		Date	Amount (₹)
2013	10,00,000	30.03.2013	3,70,000
		15.05.2013	6,30,000
2014	8,00,000	28.02.2014	5,40,000

Balance of ₹ 2,60,000 is pending as on 31.3.2014.

Compute the amount of deduction available to the assessee under section 35ABB for the assessment years 2013-14 and 2014-15. Can any deduction be claimed under section 32 also?

Answer

As per section 35ABB, any amount actually paid for obtaining licence to operate telecommunication services, shall be allowed as deduction in equal installments during the number of years for which the licence is in force. Therefore, the year of actual payment is relevant and not the previous year in which the liability for the expenditure was incurred according to the method of accounting regularly employed by the assessee.

1. ₹ 3,70,000 paid on 30.03.2013 [P.Y.2012-13]

Unexpired period of licence 10 years

Hence ₹ 37,000 [i.e. ₹ 3,70,000/10] can be claimed under section 35ABB for period of 10 years commencing from A.Y.2013-14.

2. ₹ 11,70,000 paid during year ended 31.03.2014 [P.Y.2013-14]

Unexpired period of licence 9 years

Hence, ₹ 1,30,000 [i.e. ₹ 11,70,000/9] can be claimed under section 35ABB for a period of 9 years commencing from A.Y.2014-15.

3. Amount of deduction under section 35ABB

Assessment year	Amount (₹)
2013-14	37,000
2014-15	37,000 + 1,30,000 = 1,67,000

4. Where deduction under section 35ABB is claimed and allowed, deduction under section 32(1) cannot be allowed for the same previous year or any subsequent previous year.

Question 14

Win Limited commenced the business of operating a three star hotel in Tirupati on 1-4-2013.

It furnishes you the following information:

- (i) *Cost of land (acquired in June 2011)*

₹ 60 lakhs
- (ii) *Cost of construction of hotel building*

Financial year 2011-12

Financial year 2012-13

₹ 30 lakhs

₹ 150 lakhs
- (iii) *Plant and Machineries (all new) acquired during financial year 2012-13*

[All the above expenditures were capitalized in the books of the company]

₹ 30 lakhs
- Net profit before depreciation for the financial year 2013-14*

₹ 80 lakhs

Determine the amount eligible for deduction under section 35AD of the Income-tax Act, 1961, for the assessment year 2014-15.

Answer

Under section 35AD, 100% of the capital expenditure incurred during the previous year, wholly and exclusively for the specified business, which includes the business of building and operating a hotel of two-star or above category anywhere in India which commences its operations on or after 1.4.2010, would be allowed as deduction from the business income. However, expenditure incurred on acquisition of any land, goodwill or financial instrument would not be eligible for deduction.

4.77 Income-tax

Further, the expenditure incurred, wholly and exclusively, for the purpose of specified business prior to commencement of operation would be allowed as deduction during the previous year in which the assessee commences operation of his specified business. A condition has been inserted that such amount incurred prior to commencement should be capitalized in the books of account of the assessee on the date of commencement of its operations.

Accordingly, the deduction under section 35AD for the A.Y.2014-15 in the case of Win Ltd. would be calculated as follows, assuming that the expenditures were capitalised in the books of the company on 1.4.2013, being the date of commencement of operations-

Particulars	₹ (in lakhs)
Cost of land (not eligible for deduction under section 35AD)	Nil
Cost of construction of hotel building (₹ 30 lakhs + ₹ 150 lakhs)	180
Cost of plant and machinery	<u>30</u>
Deduction under section 35AD	<u>210</u>

Note:-

- (1) For A.Y.2014-15, the loss from specified business of operating a three star hotel would be ₹ 130 lakhs (i.e. ₹ 210 lakhs – ₹ 80 lakhs). As per section 73A, any loss computed in respect of the specified business referred to in section 35AD shall be set off only against profits and gains, if any, of any other specified business. The unabsorbed loss, if any, will be carried forward for set off against profits and gains of any specified business in the following assessment year.
- (2) Since the entire cost of plant and machinery and building qualifies for deduction under section 35AD, the same does not qualify for deduction under section 32.

Question 15

MNP Ltd. commenced operations of the business of a new four-star hotel in Chennai on 1.4.2013. The company incurred capital expenditure of ₹ 40 lakh during the period January, 2013 to March, 2013 exclusively for the above business, and capitalized the same in its books of account as on 1st April, 2013. Further, during the previous year 2013-14, it incurred capital expenditure of ₹ 2.5 crore (out of which ₹ 1 crore was for acquisition of land) exclusively for the above business. Compute the income under the head "Profits and gains of business or profession" for the assessment year 2014-15, assuming that MNP Ltd. has fulfilled all the conditions specified for claim of deduction under section 35AD and has not claimed any deduction under Chapter VI-A under the heading "C. – Deductions in respect of certain incomes". The profits from the business of running this hotel (before claiming deducting under section 35AD) for the assessment year 2014-15 is ₹ 80 lakhs. Assume that the company also has another existing business of running a four-star hotel in Kanpur, which commenced operations 5 years back, the profits from which was ₹ 130 lakhs for assessment year 2014-15.

Would MNO Ltd. be entitled to deduction under section 35AD if it transfers the operation of the hotel in Chennai to PQR Ltd, while continuing to own the said hotel?

Answer

Computation of income under the head "Profit and gains of business or profession" of MNP Ltd. for A.Y. 2014-15

Particulars	₹ (in lakh)	₹ (in lakh)
Profits from the specified business of new four-star hotel in Chennai (before providing deduction under section 35AD)		80
Less: Deduction under section 35AD		
Capital expenditure incurred during the P.Y. 2013-14 (excluding the expenditure incurred on acquisition of land) = ₹ 250 lakh – ₹ 100 lakh (See Notes 1 & 2 below)	150	
Capital expenditure incurred during January 2013 to March 2013 (i.e., prior to commencement of business) and capitalized in the books of account as on 1.4.2013 (See Note 3 below)	<u>40</u>	
Total deduction under section 35AD for A.Y.2014-15		<u>190</u>
Income from the specified business of new hotel in Chennai		(110)
Profit from the existing business of running a four-star hotel in Kanpur (See Note 4 below)		<u>130</u>
Net profit from business after set-off of loss of specified business against profits of another specified business under section 73A		<u>20</u>

Notes:

- (1) According to the provisions of section 35AD, an assessee shall be allowed a deduction in respect of 100% of the capital expenditure incurred wholly and exclusively for the purpose of the specified business which, *inter alia*, includes the business in the nature of building and operating a new hotel of two-star or above category, anywhere in India. Therefore, the newly commenced four-star hotel business of MNP Ltd qualifies for deduction under section 35AD, since it has fulfilled all the conditions for claim of deduction under that section.
- (2) The expenditure on acquisition of land, however, does not qualify for deduction under section 35AD.
- (3) The capital expenditure incurred prior to commencement of specified business shall be allowed as deduction under section 35AD(1) in the year of commencement of specified business, if the same is capitalized in the books of accounts of the assessee on the date of commencement of its operations. Therefore, the expenditure of ₹ 40 lakh is allowable

as deduction in A.Y. 2014-15, since it has been capitalized in the books of accounts of MNP Ltd. as on 1.4.2013.

- (4) As per section 73A, the loss computed under section 35AD in respect of a specified business can be set off against the profit of another specified business. Building and operating a hotel of two-star and above category, anywhere in India, is a specified business, therefore, the loss from the business of new four-star hotel in Chennai can be set-off against the income of the existing four-star hotel in Kanpur.
- (5) Section 35AD(6A) provides that where the assessee, MNO Ltd., builds a hotel of two-star or above category as classified by the Central Government and subsequently, while continuing to own the hotel, transfers the operation of the said hotel to another person, the assessee shall be deemed to be carrying on the specified business of building and operating a hotel. Therefore, in this case, MNO Ltd. would be eligible to claim investment linked deduction under section 35AD even if it transfers the operation of the Chennai hotel to PQR Ltd.

Question 16

Briefly discuss about the provisions relating to deductibility of interest on capital borrowed for the purpose of business or profession.

Answer

Under section 36(1)(iii), deduction is allowed in respect of interest on capital borrowed for the purposes of business or profession while computing income under the head "Profits and gains of business or profession".

Further, *Explanation 8* to section 43(1) clarifies that interest relating to a period after the asset is first put to use cannot be capitalized. Interest in respect of capital borrowed for any period from the date of borrowing to the date on which the asset was first put to use should, however, be capitalized in the case of extension of existing business or profession.

The proviso to section 36(1)(iii) provides that no deduction shall be allowed in respect of any amount of interest paid, in respect of capital borrowed for acquisition of a new asset or for extension of existing business or profession (whether capitalized in the books of account or not) for any period beginning from the date on which the capital was borrowed for acquisition of the asset, till the date on which such asset was first put to use.

Question 17

Comment on the allowability of the following claim made by the assessee:

Mr. Achal, a hotelier, claimed expenditure on replacement of Linen and carpets in his hotel as revenue expenditure.

Answer

The expenditure on replacement of linen and carpets in a hotel are in the nature of expenses incurred for the business and are allowable as revenue expenses under section 37(1).

Question 18

What are the conditions to be satisfied for the allowability of expenditure under section 37 of the Income-tax Act, 1961?

Answer

The following conditions are to be fulfilled for the allowability of expenditure under section 37 -

- (1) The expenditure should not be of the nature described in section 30 to 36;
- (2) It should not be in the nature of personal expenditure of the assessee;
- (3) It should have been incurred by the assessee during the previous year;
- (4) The expenditure should have been laid out or expended wholly or exclusively for the purposes of the business or profession;
- (5) It should not be in the nature of a capital expenditure;
- (6) It should not have been incurred for any purpose which is an offence or which is prohibited by law.

Question 19

State with reasons, for the following sub-divisions, whether the following statements are true or false having regard to the provisions of the Income-tax Act, 1961:

- (i) *For a dealer in shares and securities, securities transaction tax paid in a recognized stock exchange is permissible business expenditure.*
- (ii) *Where a person follows mercantile system of accounting, an expenditure of ₹ 25,000 has been allowed on accrual basis and in a later year, in respect of the said expenditure, assessee makes the payment of ₹ 25,000 through a cheque crossed "& Co.", disallowance of ₹ 25,000 under section 40A(3) can be made in the year of payment.*
- (iii) *It is mandatory for an assessee to claim depreciation under section 32 of the Income-tax Act, 1961.*
- (iv) *The mediclaim premium paid to GIC by Mr. Lomesh for his employees, by a draft, on 27.12.2013 is a deductible expenditure under section 36.*
- (v) *Under section 35DDA, amortization of expenditure incurred under eligible Voluntary Retirement Scheme at the time of retirement alone, can be done.*
- (vi) *An existing assessee engaged in trading activities, can claim additional depreciation under Section 32(1)(iia) in respect of new plant acquired and installed in the trading concern, where the increase in value of such plant as compared to the approved base year is more than 10%.*

Answer

- (i) **True** : Section 36(1)(xv) allows a deduction of the amount of securities transaction tax paid by the assessee in respect of taxable securities transactions entered into in the

course of business during the previous year as deduction from the business income of a dealer in shares and securities.

- (ii) **True** : As per section 40A(3), in the case of an assessee following mercantile system of accounting, if an expenditure has been allowed as deduction in any previous year on due basis, and payment exceeding ₹ 20,000 has been made in the subsequent year otherwise than by account payee cheque or account payee bank draft, then the payment so made shall be deemed to be the income of the subsequent year in which such payment has been made.
- (iii) **True** : According to the *Explanation 5* to section 32(1), allowance of depreciation is mandatory. Therefore, depreciation has to be provided mandatorily while calculating income from business / profession whether or not the assessee has claimed the same while computing his total income.
- (iv) **True** : Section 36(1)(ib) provides deduction in respect of premium paid by an employer to keep in force an insurance on the health of his employees under a scheme framed in this behalf by GIC or any other insurer. The medical insurance premium can be paid by any mode other than cash, to be eligible for deduction under section 36(1)(ib).
- (v) **False** : Expenditure incurred in making payment to the employee in connection with his voluntary retirement either in the year of retirement or in any subsequent year, will be entitled to deduction in 5 equal annual installments beginning from the year in which each payment is made to the employee.
- (vi) **False** : Additional depreciation can be claimed only in respect of eligible plant and machinery acquired and installed by an assessee engaged in the business of manufacture or production of any article or thing or in the business of generation or generation and distribution of power. In this case, the assessee is engaged in trading activities and the new plant has been acquired and installed in a trading concern. Hence, the assessee will not be entitled to claim additional depreciation under section 32(1)(ia).

Question 20

State, with reasons, the allowability of the following expenses under the Income-tax Act, 1961 while computing income from business or profession for the Assessment Year 2014-15:

- (i) *Provision made on the basis of actuarial valuation for payment of gratuity ₹ 5,00,000. However, no payment on account of gratuity was made before due date of filing return.*
- (ii) *Purchase of oil seeds of ₹ 50,000 in cash from a farmer on a banking day.*
- (iii) *Tax on non-monetary perquisite provided to an employee ₹ 20,000.*
- (iv) *Payment of ₹ 50,000 by using credit card for fire insurance.*
- (v) *Salary payment of ₹ 2,00,000 outside India by a company without deduction of tax.*
- (vi) *Sales tax deposited in cash ₹ 50,000 with State Bank of India.*
- (vii) *Payment made in cash ₹ 30,000 to a transporter in a day for carriage of goods*

Answer

(i) Not allowable as deduction

As per section 40A(7), no deduction is allowed in computing business income in respect of any provision made by the assessee in his books of account for the payment of gratuity to his employees except in the following two cases:

- (1) where any provision is made for the purpose of payment of sum by way of contribution towards an approved gratuity fund or;
- (2) where any provision is made for the purpose of making any payment on account of gratuity that has become payable during the previous year.

Therefore, in the present case, the provision made on the basis of actuarial valuation for payment of gratuity has to be disallowed under section 40A(7), since, no payment has been actually made on account of gratuity.

Note: It is assumed that such provision is not for the purpose of contribution towards an approved gratuity fund.

(ii) Allowable as deduction

As per Rule 6DD, in case the payment is made for purchase of agricultural produce directly to the cultivator, grower or producer of such agricultural produce, no disallowance under section 40A(3) is attracted even though the cash payment for the expense exceeds ₹ 20,000.

Therefore, in the given case, disallowance under section 40A(3) is not attracted since, cash payment for purchase of oil seeds is made directly to the farmer.

(iii) Not allowable as deduction

Income-tax of ₹ 20,000 paid by the employer in respect of non-monetary perquisites provided to its employees is exempt in the hands of the employee under section 10(10CC). As per section 40(a)(v), such income-tax paid by the employer is not deductible while computing business income.

(iv) Allowable as deduction

Payment for fire insurance is allowable as deduction under section 36(1). Since payment by credit card is covered under Rule 6DD, which contains the exceptions to section 40A(3), disallowance under section 40A(3) is not attracted in this case.

(v) Not allowable as deduction

Disallowance under section 40(a)(iii) is attracted in respect of salary payment of ₹ 2,00,000 outside India by a company without deduction of tax at source.

(vi) Allowable as deduction

As per Rule 6DD, if the payment is made to the Government and, under the rules framed by it, such payment is required to be made in legal tender, no disallowance under section 40A(3) is attracted even though the cash payment for the expense exceeds ₹ 20,000.

Therefore, in the given case, no disallowance under section 40A(3) is attracted since payment of sales tax is covered by the above mentioned exception contained in Rule 6DD.

(vii) Allowable as deduction

The limit for attracting disallowance under section 40A(3) for payment otherwise than by way of account payee cheque or account payee bank draft is ₹ 35,000 in case of payment made for plying, hiring or leasing goods carriage. Therefore, in the present case, disallowance under section 40A(3) is not attracted for payment of ₹ 30,000 made in cash to a transporter for carriage of goods.

Question 21

Ramji Ltd., engaged in manufacture of medicines (pharmaceuticals), furnishes the following information for the year ended 31.03.2014:

- (i) Municipal tax relating to office building ₹ 51,000 not paid till 30.09.2014.*
- (ii) Patent acquired for ₹ 20,00,000 on 01.09.2013 and used from the same month.*
- (iii) Capital expenditure on scientific research ₹ 10,00,000 which includes cost of land ₹ 2,00,000.*
- (iv) Amount due from customer X, outstanding for more than 3 years, written off as bad debt in the books ₹ 5,00,000.*
- (v) Income-tax paid ₹ 90,000 by the company in respect of non-monetary perquisites provided to its employees.*
- (vi) Provident fund contribution of employees ₹ 5,50,000 remitted in July, 2014.*
- (vii) Expenditure towards advertisement in souvenir of a political party ₹ 1,50,000.*
- (viii) Refund of sales tax ₹ 75,000 received during the year, which was claimed as expenditure in an earlier year.*

State with reasons the taxability or deductibility of the items given above under the Income-tax Act, 1961.

Note: Computation of total income is not required.

Answer

- (i)** As per section 43B, municipal tax is not deductible for A.Y. 2014-15 since it is not paid on or before 30.09.2014, being the due date of filing the return for A.Y. 2014-15.

Note – It is assumed that the company has not undertaken any international transaction during the year, and therefore, does not have to file a transfer pricing report under section 92E. Therefore, the due date of filing of return of the company would be 30th September, 2014.

- (ii)** Patent is an intangible asset eligible for depreciation@25%, as per section 32(2)(ii). Since it has been acquired and put to use for more than 180 days during the previous year 2013-14, full depreciation of ₹ 5,00,000 (i.e. 25% of ₹ 20,00,000) is allowable as deduction.

- (iii) Weighted deduction@200% is available under section 35(2AB) in respect of expenditure incurred by a company on scientific research on in-house research and development facility as approved by the prescribed authority. However, cost of land is not eligible for deduction.

Deduction under section 35(2AB) = 200% of ₹ 8 lakhs = ₹ 16,00,000.

Note: It is presumed that the in-house research and development facility is approved by the prescribed authority and is hence, eligible for weighted deducted@200% under section 35(2AB).

- (iv) Bad debts i.e. ₹ 5,00,000 written off in the books of account as irrecoverable is deductible under section 36(1)(vii), provided the debt has been taken into account in computing the income of the company in the current previous year or any of the earlier previous years.
- (v) As per section 40(a)(v), income-tax of ₹ 90,000 paid by the company in respect of non-monetary perquisites provided to its employees, exempt in the employee's hands under section 10(10CC), is not deductible while computing business income of the employer-company.
- (vi) The employees' contribution to provident fund is taxable in the hands of the company since it is included in the definition of income under section 2(24)(x).

As per section 36(1)(va), provident fund contribution of employees is deductible only if such sum is credited to the employee's provident fund account on or before the due date under the Employees' Provident Fund and Miscellaneous Provisions Act, 1952. In this case, since it is remitted after the due date under the said Act, it is not deductible.

Note: There is an alternate view that remittance of provident fund contribution of employees is deductible even though it is remitted beyond the due date under the Employees' Provident Fund and Miscellaneous Provisions Act, 1952, in case the same is remitted before the due date of filing return of income in view of the Delhi High Court decision in *CIT vs. Aimil Ltd. (2010) 321 ITR 508*.

- (vii) Expenditure towards advertisement in souvenir of a political party is disallowed under section 37(2B) while computing business income.

However, the same is deductible under section 80GGB from gross total income provided the payment is made by any mode other than cash.

- (viii) Refund of a trading liability is taxable under section 41(1), if a deduction was allowed in respect of the same to the taxpayer in an earlier year.

Since sales tax was claimed as expenditure in an earlier year, refund of the same during the year would attract the provisions of section 41(1).

Question 22

Answer the following with reference to the provisions of the Income-tax Act, 1961:

- (a) *Bad debt claim disallowed in an earlier assessment year, recovered subsequently. Is the sum recovered, chargeable to tax?*
- (b) *Tax deducted at source on salary paid to employees not remitted till the 'due date' for filing the return prescribed in section 139. Is the expenditure to be disallowed under section 40(a)(ia)?*
- (c) *X Co. Ltd. paid ₹ 120 lakhs as compensation as per approved Voluntary Retirement Scheme (VRS) during the financial year 2013-14. How much is deductible under section 35DDA for the assessment year 2014-15?*
- (d) *Bad debt of ₹ 50,000 written off and allowed in the financial year 2011-12 recovered in the financial year 2013-14.*

Answer

- (a) Recovery of a bad debt claim disallowed in the earlier year cannot be brought to tax under section 41(4). Section 41(4) can be invoked only in a case where bad debts or part thereof has been allowed as deduction earlier under section 36(1)(vii).
- (b) The salary expenditure is allowable while computing the income of the employer even though TDS has not been deposited within the due date under section 139(1). The disallowance under section 40(a)(ia) will not apply for non-deduction of tax at source from income chargeable under the head "Salaries".
- (c) It is deductible in 5 equal annual instalments commencing from the previous year of payment. ₹ 24 lakhs, being 1/5th of ₹ 120 lakhs, is deductible under section 35DDA for the A.Y.2014-15.
- (d) As per section 41(4), any amount recovered by the assessee against bad debt earlier allowed as deduction shall be taxed as income in the year in which it is received. Therefore, in this case, ₹ 50,000 would be taxable in the F.Y.2013-14 (A.Y.2014-15).

Question 23

State with reasons, whether the following statements are true or false, with regard to the provisions of the Income-tax Act, 1961:

- (a) *Payment made in respect of a business expenditure incurred on 16th February, 2013 for ₹ 25,000 through a cheque duly crossed as "& Co." is hit by the provisions of section 40A(3).*
- (b)
 - (i) *It is a condition precedent to write off in the books of account, the amount due from debtor to claim deduction for bad debt.*
 - (ii) *Failure to deduct tax at source in accordance with the provisions of Chapter XVII-B, inter alia, from the amounts payable to a resident as rent or royalty, will result in disallowance while computing the business income where the resident payee has not paid the tax due on such income.*

- (c) *Co-operative banks are not allowed to claim provision for bad and doubtful debts in respect of advances made by rural branches of such banks.*

Answer

- (a) **True** : In order to escape the disallowance specified in section 40A(3), payment in respect of the business expenditure ought to have been made through an account payee cheque. Payment through a cheque crossed as "& Co." will attract disallowance under section 40A(3).
- (b) (i) **True** : It is mandatory to write off the amount due from a debtor as not receivable, in order to claim the same as bad debt under section 36(1)(vii).
- (ii) **True** : Section 40(a)(ia) provides that failure to deduct tax at source from rent or royalty payable to a resident, in accordance with the provisions of Chapter XVII-B, will result in disallowance of such expenditure, where the resident payee has not paid the tax due on such income.
- (c) **False** : Sub-clause (a) of section 36(1)(vii) allows the co-operative banks to claim deduction for provision for bad and doubtful debts in respect of advances made by rural branches of such banks. However, the deduction should not exceed 10% of the aggregate average advances made by the rural branches of such banks computed in the prescribed manner.

Question 24

Write short notes on:

- (i) *Restrictions on deductions allowable to the partnership firm in respect of salary and interest to its partners under section 40(b) of the Income-tax Act, 1961.*
- (ii) *Carry forward and set off of unabsorbed depreciation.*
- (iii) *Additional depreciation.*

Answer

- (i) In the case of a partnership firm, the deduction on account of interest and salary paid to its partners are as subject to the following restrictions contained in section 40(b) -
- (i) It should be authorised by and in accordance with the terms of the partnership deed.
- (ii) It should not relate to a period before the date of such deed.
- (iii) Remuneration should be paid to a working partner.
- (iv) The amounts allowable are subject to the following limits -
- (1) In the case of interest**
- Simple interest up to 12% p.a. is allowable. This restriction is not applicable if a person is a partner in his representative capacity in the firm and he receives

interest from the firm in his individual capacity. Similarly, the restriction is also not applicable if a person who is a partner in his individual capacity receives interest for and on behalf of someone else from the firm in which he is a partner.

- (2) **In the case of salary, bonus, commission or remuneration paid by a firm to its working partners** – It should not exceed the amount specified in the table below -

For all firms

- | | | |
|-----|---|---|
| (a) | On the first ₹ 3,00,000 of the book profit or in case of loss | ₹ 1,50,000 or 90% of book profit, whichever is more |
| (b) | On the balance of the book profit | @ 60% |

- (ii) Section 32(2) provides for carry forward of unabsorbed depreciation.

Where, in any previous year, the profits or gains chargeable are not sufficient to give full effect to the depreciation allowance, such unabsorbed depreciation shall be added to the depreciation allowance for the following previous year and shall be deemed to be part of that allowance.

If there is no depreciation allowance for that previous year, the unabsorbed depreciation of the earlier previous year shall become the depreciation allowance of that year. The effect of the provisions of section 32(2) is that unabsorbed depreciation brought forward shall be deemed as the current year depreciation. Consequently, such unabsorbed depreciation can be set-off not only against income under the head "Profits and gains of business or profession" but also against income under any other head. Further, the unabsorbed depreciation can be carried forward indefinitely till it is fully set off.

However, in the order of set-off losses under different heads of income, effect shall first be given to current year depreciation, then to brought forward business losses and finally to unabsorbed depreciation.

- (iii) Section 32(1)(ia) provides that in the case of any new machinery or plant (other than ships and aircraft) acquired and installed after 31.3.2005 by an assessee engaged in the business of manufacture or production of any article or thing or in the business of generation or generation and distribution of power, a further sum equal to 20% of the actual cost of such machinery or plant shall be allowable as a deduction.

The additional depreciation is available to a new machinery or plant used in the manufacture or production of any article or thing or generation or generation and distribution of power. Additional depreciation will be taken into consideration for computing the WDV of the relevant block of assets.

Additional depreciation is not available in respect of the following assets:

- (A) any machinery or plant

- (i) which has been used in India or outside India by any other person before its installation by the assessee; or
 - (ii) installed in any office premises, residential accommodation including accommodation used in the nature of guest house ; or
 - (iii) the whole of the actual cost of which is allowed as deduction (whether by way of depreciation or otherwise) in computing the income under the head "Profits and gains of business or profession" of any one previous year.
- (B) any office appliances or road transport vehicles.

Question 25

Rao & Jain, a partnership firm consisting of two partners, reports a net profit of ₹ 7,00,000 before deduction of the following items:

- (1) *Salary of ₹ 20,000 each per month payable to two working partners of the firm (as authorized by the deed of partnership).*
- (2) *Depreciation on plant and machinery under section 32 (computed) ₹ 1,50,000.*
- (3) *Interest on capital at 15% per annum (as per the deed of partnership). The amount of capital eligible for interest ₹ 5,00,000.*

Compute:

- (i) *Book-profit of the firm under section 40(b) of the Income-tax Act, 1961.*
- (ii) *Allowable working partner salary for the assessment year 2014-15 as per section 40(b).*

Answer

- (i) As per *Explanation 3* to section 40(b), "book profit" shall mean the net profit as per the profit and loss account for the relevant previous year computed in the manner laid down in Chapter IV-D as increased by the aggregate amount of the remuneration paid or payable to the partners of the firm if the same has been already deducted while computing the net profit.

In the present case, the net profit given is before deduction of depreciation on plant and machinery, interest on capital of partners and salary to the working partners. Therefore, the book profit shall be as follows:

Computation of Book Profit of the firm under section 40(b)

Particulars	₹	₹
Net Profit (before deduction of depreciation, salary and interest)		7,00,000
Less: Depreciation under section 32	1,50,000	
Interest @ 12% p.a. [being the maximum allowable as per section 40(b)] (5,00,000 × 12%)	<u>60,000</u>	<u>2,10,000</u>
Book Profit		<u>4,90,000</u>

(ii) Salary actually paid to working partners = ₹ 20,000 × 2 × 12 = ₹ 4,80,000.

As per the provisions of section 40(b)(v), the salary paid to the working partners is allowed subject to the following limits -

On the first ₹ 3,00,000 of book profit or in case of loss	₹ 1,50,000 or 90% of book profit, whichever is more
On the balance of book profit	60% of the balance book profit

Therefore, the maximum allowable working partners' salary for the A.Y. 2014-15 in this case would be:

Particulars	₹
On the first ₹ 3,00,000 of book profit [(₹ 1,50,000 or 90% of ₹ 3,00,000) whichever is more]	2,70,000
On the balance of book profit [60% of (₹ 4,90,000 - ₹ 3,00,000)]	<u>1,14,000</u>
Maximum allowable partners' salary	<u>3,84,000</u>

Hence, allowable working partners' salary for the A.Y. 2014-15 as per the provisions of section 40(b)(v) is ₹ 3,84,000.

Question 26

During the financial year 2013-14, the following payments/expenditure were made/incurred by Mr. Yuvan Raja, a resident individual (whose turnover during the year ended 31.3.2013 was ₹ 99 lacs) :

- (i) Interest of ₹ 12,000 was paid to Rehman & Co., a resident partnership firm, without deduction of tax at source;
- (ii) Interest of ₹ 4,000 was paid as interest to Mr. R.D. Burman, a non-resident, without deduction of tax at source;
- (iii) ₹ 3,00,000 was paid as salary to a resident individual without deduction of tax at source;
- (iv) Commission of ₹ 15,000 was paid to Mr. Vidyasagar on 2.7.2013. without deduction of tax at source.

Briefly discuss whether any disallowance arises under the provisions of section 40(a)(i)/40(a)(ia) of the Income-tax Act, 1961.

Answer

Disallowance under section 40(a)(i)/40(a)(ia) of the Income-tax Act, 1961 is attracted where the assessee fails to deduct tax at source as is required under the Act, or having deducted tax at source, fails to remit the same to the credit of the Central Government within the stipulated time limit.

The assessee is a resident individual, who was not subjected to tax audit during the

immediately preceding previous year i.e., P.Y.2012-13 (as his turnover was less than ₹ 100 lakh in that year) and the TDS obligations have to be considered bearing this in mind.

- (i) The obligation to deduct tax at source from interest paid to a resident arises under section 194A in the case of an individual, only where he was subject to tax audit under section 44AB in the immediately preceding previous year, i.e., P.Y.2012-13. From the data given, it is clear that he was not subject to tax audit under section 44AB in the P.Y.2012-13. Hence, disallowance under section 40(a)(ia) is not attracted in this case.
- (ii) In the case of interest paid to a non-resident, there is obligation to deduct tax at source under section 195, hence non-deduction of tax at source will attract disallowance under section 40(a)(i).
- (iii) Disallowance under section 40(a)(ia) is not attracted for failure to deduct tax at source under section 192 from salaries.
- (iv) The obligation to deduct tax at source under section 194-H from commission paid in excess of ₹ 5,000 to a resident arises in the case of an individual, only where he was subject to tax audit under section 44AB in the immediately preceding previous year. From the data given, it is clear that he was not subject to tax audit under section 44AB in the P.Y.2012-13. Hence, there is no obligation to deduct tax at source under section 194H during the P.Y. 2013-14. Therefore, disallowance under section 40(a)(ia) is not attracted in this case.

Question 27

M/s. Arora Ltd., submits the following details of expenditure pertaining to the financial year 2013-14:

- (i) *Payment of professional fees to Mr. Mani ₹ 50,000. Tax was not deducted at source.*
- (ii) *Interior works done by Mr. Hari for ₹ 2,00,000 on a contract basis. Payment made in the month of March 2014. Tax deducted in March 2014 was paid on 30.06.2014.*
- (iii) *Factory Rent paid to Mr. Rao ₹ 15,00,000. Tax deducted at source and paid on 01.10.2014.*
- (iv) *Interest paid on Fixed Deposits ₹ 2,00,000. Tax deducted on 31.12.2013 and paid on 28.09.2014.*

Examine the above with reference to allowability of the same in the assessment year 2014-15 under the Income-tax Act, 1961. Your answer must be with reference to section 40(a) read with relevant tax deduction at source provisions. Assume that the due date of filing the return of income is 30.09.2014.

Answer

Allowability of expenses of M/s. Arora Ltd. for the A.Y. 2014-15

- (i) Payment of professional fees is subject to TDS under section 194J. Since no tax is deducted at source, the expenditure of ₹ 50,000 is disallowed under section 40(a)(ia).

- (ii) Since the tax was deducted in March, 2014 and paid on or before the due date of filing the return (i.e., on or before September 30th, 2014), the expenditure on interior works will be allowed as deduction. Hence, disallowance under section 40(a)(ia) is not attracted.
- (iii) The maximum time allowable for deposit of tax deducted at source is upto the due date of filing of return i.e., 30th September, 2014. In this case, since tax deducted under section 194-I was paid after the due date of filing the return, the expenditure can be claimed only in the subsequent year i.e., P.Y. 2014-15. Hence, for the P.Y. 2013-14, the expenditure of ₹ 15,00,000 is disallowed under section 40(a)(ia).
- (iv) The tax deducted at source could be deposited on or before the due date of filing of return to avoid disallowance under section 40(a)(ia). In this case, disallowance would not be attracted since tax deducted during December 2013 was deposited before 30th September 2014 i.e. on 28.09.2014.

Question 28

Vinod is a person carrying on profession as film artist. His gross receipts from profession are as under:

	₹
<i>Financial year 2011-12</i>	<i>1,15,000</i>
<i>Financial year 2012-13</i>	<i>1,80,000</i>
<i>Financial year 2013-14</i>	<i>2,10,000</i>

What is his obligation regarding maintenance of books of accounts for each Assessment Year under section 44AA of Income-tax Act, 1961?

Answer

Section 44AA(1) requires every person carrying on any profession, notified by the Board in the Official Gazette (in addition to the professions already specified therein), to maintain such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of the Income-tax Act, 1961.

Thus, a person carrying on a notified profession shall be required to maintain specified books of accounts:

- (i) if his gross receipts in all the three years immediately preceding the relevant previous year has exceeded ₹ 1,50,000; or
- (ii) if it is a new profession which is setup in the relevant previous year, it is likely to exceed ₹ 1,50,000 in that previous year.

In the present case, Vinod is a person carrying on profession as film artist, which is a notified profession. Since his gross receipts have not exceeded ₹ 1,50,000 in financial year 2011-12, the requirement under section 44AA to compulsorily maintain the prescribed books of account is not applicable to him.

Question 29

Ramamurthy had 4 heavy goods vehicles as on 1.4.2013. He acquired 7 heavy goods vehicles on 27.6.2013. He sold 2 heavy goods vehicles on 31.5.2013.

He has brought forward business loss of ₹ 50,000 relating to assessment year 2010-11 of a discontinued business. Assuming that he opts for presumptive taxation of income as per section 44AE, compute his total income chargeable to tax for the assessment year 2014-15.

Answer

Computation of total income of Mr. Ramamurthy for A.Y.2014-15

Particulars	₹
Presumptive business income under section 44AE	
4 heavy goods vehicles for 2 months (4 x ₹ 5,000 x 2)	40,000
Balance 2 heavy goods vehicles for 10 months (2 x ₹ 5,000 x 10)	1,00,000
7 heavy goods vehicles for 10 months (7 x ₹ 5,000 x 10)	<u>3,50,000</u>
Business Income	4,90,000
Less: Brought forward business loss of discontinued business	<u>50,000</u>
Total Income	<u>4,40,000</u>

Note: The assessee is eligible for computing the income from goods carriages applying the presumptive provisions of section 44AE, since he did not own more than 10 goods carriages at any time during the previous year.

Question 30

Mr. Praveen engaged in retail trade, reports a turnover of ₹ 58,50,000 for the financial year 2013-14. His income from the said business as per books of account is computed at ₹ 2,90,000. Retail trade is the only source of income for Mr. Praveen.

- (i) *Is Mr. Praveen eligible to opt for presumptive determination of his income chargeable to tax for the assessment year 2014-15?*
- (ii) *If so, determine his income from retail trade as per the applicable presumptive provision.*
- (iii) *In case Mr. Praveen does not opt for presumptive taxation of income from retail trade, what are his obligations under the Income-tax Act, 1961?*
- (iv) *What is the due date for filing his return of income under both the options?*

Answer

- (i) Yes. Since his total turnover for the F.Y.2013-14 is below ₹ 100 lakhs, he is eligible to opt for presumptive taxation scheme under section 44AD in respect of his retail trade business.

- (ii) His income from retail trade, applying the presumptive tax provisions under section 44AD, would be ₹ 4,68,000, being 8% of ₹ 58,50,000.
- (iii) In case he does not opt for the presumptive taxation scheme under section 44AD, and claims that his income is ₹ 2,90,000 (which is lower than the presumptive business income of ₹ 4,68,000), he has to maintain books of account as required under section 44AA(2) and also get them audited and furnish a report of such audit under section 44AB, since his total income exceeds the basic exemption limit of ₹ 2,00,000.
- (iv) In case he opts for the presumptive taxation scheme under section 44AD, the due date would be 31st July, 2014.

In case he does not opt for the presumptive taxation scheme and claims that his income is ₹ 2,90,000 as per books of account, then he has to get his books of account audited under section 44AB, in which case the due date for filing of return would be 30th September, 2014.

Question 31

Mr. Sukhvinder is engaged in the business of plying goods carriages. On 1st April, 2013, he owns 10 trucks (out of which 6 are heavy goods vehicles). On 2nd May, 2013, he sold one of the heavy goods vehicles and purchased a light goods vehicle on 6th May, 2013. This new vehicle could however be put to use only on 15th June, 2013.

Compute the total income of Mr. Sukhvinder for the assessment year 2014-15, taking note of the following data :

<i>Particulars</i>	₹	₹
<i>Freight charges collected</i>		<i>8,70,000</i>
<i>Less : Operational expenses</i>	<i>6,25,000</i>	
<i>Depreciation as per section 32</i>	<i>1,85,000</i>	
<i>Other office expenses</i>	<u><i>15,000</i></u>	<u><i>8,25,000</i></u>
<i>Net Profit</i>		<u><i>45,000</i></u>
<i>Other business and non – business income</i>		<i>70,000</i>

Answer

Section 44AE would apply in the case of Mr. Sukhvinder since he is engaged in the business of plying goods carriages and owns not more than ten goods carriages at any time during the previous year.

Section 44AE provides for computation of business income of such assessee on a presumptive basis. The income shall be deemed to be ₹ 5,000 from a heavy goods vehicle and ₹ 4,500 from a vehicle other than a heavy goods vehicle - for every month or part the month during which such goods vehicle is owned by the assessee in the previous year or such higher sums as declared by the assessee in his return of income.

Mr. Sukhvinder's business income calculated applying the provisions of section 44AE is ₹ 5,75,500 (See Notes 1 & 2 below) and his total income would be ₹ 6,45,500.

However, as per section 44AE(7), Mr. Sukhvinder may claim lower profits and gains if he keeps and maintains proper books of account as per section 44AA and gets the same audited and furnishes a report of such audit as required under section 44AB. If he does so, then his income for tax purposes from goods carriages would be ₹ 45,000 instead of ₹ 5,75,500 and his total income would be ₹ 1,15,000.

Notes :

1. Computation of total income of Mr. Sukhvinder for A.Y. 2014-15

Particulars	Presumptive income	Where books are maintained
Income from business of plying goods carriages [See Note 2 Below]	5,75,500	45,000
Other business and non business income	<u>70,000</u>	<u>70,000</u>
Total Income	<u>6,45,500</u>	<u>1,15,000</u>

2. Calculation of presumptive income as per section 44AE

Type of carriage	No. of months	Rate per month	Amount
(1)	(2)	(3)	(4)
4 light goods vehicle – held throughout the year	12	4,500	2,16,000
1 heavy goods vehicle – held upto 2 nd May	2	5,000	10,000
5 heavy goods vehicle – held throughout the year	12	5,000	3,00,000
1 light goods vehicle – held from 6 th May	11	4,500	<u>49,500</u>
		Total	<u>5,75,500</u>

Question 32

X Ltd. follows mercantile system of accounting. After negotiations with the bank, interest of ₹ 4 lakhs (including interest of ₹ 1.2 lakhs pertaining to year ended 31.03.2014) has been converted into loan. Can the interest of ₹ 1.2 lakhs so capitalized be claimed as business expenditure?

Answer

Under section 43B, interest on term loans and advances to scheduled banks shall be allowed only in the year of payment of such interest irrespective of the method of accounting followed by the assessee.

Explanation 3D to section 43B provides that if any interest payable by the assessee is converted into a loan, the interest so converted and not "actually paid" shall not be deemed as actual payment, and hence would not be allowed as deduction. Therefore, the interest of ₹ 1.2 lakhs converted into loan cannot be claimed as business expenditure.

Question 33

Mr. B.A. Patel, a non-resident, operates an aircraft between London to Ahmedabad. For the Financial year ended on 31st March, 2014, he received the amounts as under:

- (i) For carrying passengers from Ahmedabad ₹ 50 lacs.
- (ii) For carrying passengers from London ₹ 75 lacs received in India.
- (iii) For carrying of goods from Ahmedabad ₹ 25 lacs.

The total expenditure incurred by Mr. B.A. Patel for the purposes of the business for the financial year 2013-14 was ₹ 1.4 crores.

Compute the income of Mr. B.A. Patel under the head "Profits and Gains from business or profession" for the financial year ended on 31st March 2014 relevant to assessment year 2014-15.

Answer

Under section 44BBA, in case of an assessee, being a non-resident, engaged in the business of operation of aircraft, a sum equal to 5% of the aggregate of the following amounts shall be deemed to be his business income:

- (a) the amount paid or payable, whether in or out of India, to the assessee on account of carriage of passengers, goods etc. from any place in India; and
- (b) the amount received or deemed to be received in India by the assessee on account of carriage of passengers, goods etc. from any place outside India.

Hence, the income of Mr. B.A. Patel chargeable to tax in India under the head "Profits and Gains of business or profession" is determined as under:

Particulars	₹
(i) For carrying passengers from Ahmedabad	50,00,000
(ii) For carrying passengers from London, amount received in India	75,00,000
(iii) For carrying goods from Ahmedabad	25,00,000
Total	1,50,00,000

Hence, income from business computed on presumptive basis as per section 44BBA is ₹ 7,50,000, being 5% of ₹ 1,50,00,000.

Note: No deduction is allowable in respect of any expenditure incurred for the purpose of the business.

Question 34

List six items of expenses which otherwise are deductible shall be disallowed, unless payments are actually made within the due date for furnishing the return of income under Section 139(1). When can the deduction be claimed, if paid after the said date?

Answer

Section 43B provides that the following expenses shall not be allowed as deduction unless the payments are actually made within the due date for furnishing the return of income under section 139(1):

- (i) Any tax, duty, cess or fees under any law in force.
- (ii) Employer's contribution to provident fund or superannuation fund or gratuity fund or any other fund for the welfare of the employees;
- (iii) Any bonus or commission for services rendered payable to employees;
- (iv) Any interest on any loan or borrowings from any public financial institution or State financial corporation or State industrial investment corporation;
- (v) Interest on loans and advances from a scheduled bank;
- (vi) Any sum paid as an employer in lieu of earned leave at the credit of his employee.

In case the payment is made after the due date of filing of return of income, deduction can be claimed only in the year of actual payment.

Question 35

Mr. Asim, a 60 year old individual, engaged in the business of roasting and grounding of coffee, derives income of ₹ 10 lacs during the financial year 2013-14. Compute the tax payable by him assuming he has not earned any other income during the financial year 2013-14. What would be your answer if Mr. Asim is also engaged in the business of growing and curing coffee?

Answer

If Mr. Asim is engaged only in the business of roasting and grounding of coffee (and not growing and curing of coffee), his entire income of ₹ 10 lakhs would be treated as business income and his tax liability would be ₹ 1,28,750 (₹ 1,25,000+₹ 2,500+₹ 1,250).

If Mr. Asim is also engaged in the business of growing and curing of coffee, in addition to roasting and grounding of coffee, the provisions of Rule 7B of the Income-tax Rules, 1962 would apply. As per Rule 7B, where income is derived from the sale of coffee grown, cured, roasted and grounded by the seller in India, 40% of such income shall be treated as business income and the balance as agricultural income.

Therefore, in such a case, the business income would be 40% of ₹ 10,00,000 = ₹ 4,00,000

Calculation of tax liability for A.Y 2014-15

Particulars	₹
Tax on ₹ 10,00,000 [being the aggregate of non-agricultural income (i.e. ₹ 4,00,000) and agricultural income (i.e. ₹ 6,00,000)]	1,25,000

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Less: Tax on ₹ 8,50,000 [being aggregate of agricultural income (i.e. ₹ 6,00,000) and basic exemption limit (i.e. ₹ 2,50,000)]	95,000
	30,000
Less: Rebate u/s 87A	2,000
	28,000
Add: Education cess @ 2%	560
Secondary and higher education cess @ 1%	280
Total tax liability	28,840

Question 36

Mr. Tenzingh is engaged in composite business of growing and curing (further processing) coffee in Coorg, Karnataka. The whole of coffee grown in his plantation is cured. Relevant information pertaining to the year ended 31.3.2014 are given below:

Particulars	₹
WDV of car as on 1.4.2013	3,00,000
WDV of machinery as on 1.4.2013 (15% rate)	15,00,000
Expenses incurred for growing coffee	3,10,000
Expenditure for curing coffee	3,00,000
Sale value of cured coffee	22,00,000

Besides being used for agricultural operations, the car is also used for personal use; disallowance for personal use may be taken at 20%. The expenses incurred for car running and maintenance are ₹ 50,000. The machines were used in coffee curing business operations.

Compute the income arising from the above activities for the assessment year 2014-15. Show the WDV of the assets as on 31.3.2014.

Answer

Where an assessee is engaged in the composite business of growing and curing of coffee, the income will be segregated between agricultural income and business income, as per Rule 7B of the Income-tax Rules, 1962.

As per the above Rule, income derived from sale of coffee grown and cured by the seller in India shall be computed as if it were income derived from business, and 25% of such income shall be deemed to be income liable to tax. The balance 75% will be treated as agricultural income.

Particulars	₹	₹	₹
Sale value of cured coffee			22,00,000
Less: Expenses for growing coffee		3,10,000	
Car expenses (80% of ₹ 50,000)		40,000	

Depreciation on car (80% of 15% of ₹ 3,00,000)		<u>36,000</u>	
Total costs of agricultural operations		3,86,000	
Expenditure for coffee curing operations	3,00,000		
Add: Depreciation on machinery (15% of 15,00,000) (See Computation below)	<u>2,25,000</u>		
Total cost of the curing operations		<u>5,25,000</u>	
Total cost of composite operations			<u>9,11,000</u>
Total profits from composite activities			<u>12,89,000</u>
Amount regarded as business income (25% of above)			3,22,250
Amount treated as agricultural income (75% of above)			9,66,750

Computation of value of depreciable assets as on 31.3.2014

Particulars	₹	₹	₹
Car Opening value as on 1.4.2013		3,00,000	
Depreciation thereon at 15%	45,000		
Less: Disallowance @20% for personal use	<u>9,000</u>		
Depreciation actually allowed		<u>36,000</u>	
Closing value as on 31.3.2014			2,64,000
Machinery Opening value as on 1.4.2013		15,00,000	
Less: Depreciation @ 15%		<u>2,25,000</u>	
Closing value as on 31.3.2014			12,75,000

Explanation 7 to section 43(6) provides that in cases of 'composite income', for the purpose of computing written down value of assets acquired before the previous year, the total amount of depreciation shall be computed as if the entire composite income of the assessee (and not just 25%) is chargeable under the head "Profits and gains of business or profession". The depreciation so computed shall be deemed to have been "actually allowed" to the assessee.

Question 37

Miss Vivitha, a resident and ordinarily resident in India, has derived the following income from various operations (relating to plantations and estates owned by her) during the year ended 31-3-2014:

S. No.	Particulars	₹
(i)	Income from sale of centrifuged latex processed from rubber plants grown in Darjeeling.	3,00,000

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(ii)	Income from sale of coffee grown and cured in Yercaud, Tamil Nadu.	1,00,000
(iii)	Income from sale of coffee grown, cured, roasted and grounded, in Colombo. Sale consideration was received at Chennai.	2,50,000
(iv)	Income from sale of tea grown and manufactured in Shimla.	4,00,000
(v)	Income from sapling and seedling grown in a nursery at Cochin. Basic operations were not carried out by her on land.	80,000

You are required to compute the business income and agricultural income of Miss Vivitha for the assessment year 2014-15.

Answer

Computation of business income and agricultural income of Ms. Vivitha for the A.Y.2014-15

Sr. No.	Source of income	Gross (₹)	Business income		Agricultural income
			%	₹	₹
(i)	Sale of centrifuged latex from rubber plants grown in India.	3,00,000	35%	1,05,000	1,95,000
(ii)	Sale of coffee grown and cured in India.	1,00,000	25%	25,000	75,000
(iii)	Sale of coffee grown, cured, roasted and grounded outside India. (See Note 1 below)	2,50,000	100%	2,50,000	-
(iv)	Sale of tea grown and manufactured in India	4,00,000	40%	1,60,000	2,40,000
(v)	Saplings and seedlings grown in nursery in India (See Note 2 below)	80,000		Nil	
				-	80,000
	Total			<u>5,40,000</u>	<u>5,90,000</u>

Notes:

- Where income is derived from sale of coffee grown, cured, roasted and grounded by the seller in India, 40% of such income is taken as business income and the balance as agricultural income. However, in this question, these operations are done in Colombo, Sri Lanka. Hence, there is no question of such apportionment and the whole income is taxable as business income. Receipt of sale proceeds in India does not make this agricultural income. In the case of an assessee, being a resident and ordinarily resident, the income arising outside India is also chargeable to tax.

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

Question 38

Mr. Tony has estates in Rubber, Tea and Coffee. He derives income from them. He has also a nursery wherein he grows and sells plants. For the previous year ending 31.3.2014, he furnishes the following particulars of his sources of income from estates and sale of plants. You are requested to compute the taxable income for the Assessment Year 2014-15:

Sl. No.	Particulars	₹
(i)	Manufacture of Rubber	5,00,000
(ii)	Manufacture of Coffee grown and cured	3,50,000
(iii)	Manufacture of Tea	7,00,000
(iv)	Sale of plants from Nursery	1,00,000

Answer

Computation of taxable income of Mr. Tony for A.Y.2014-15

	Particulars	Business Income (₹)	Agricultural Income (₹)
(a)	Income from manufacture of rubber (Rule 7A) Business income is 35% of ₹ 5,00,000 Agricultural income is 65% of ₹ 5,00,000	1,75,000	3,25,000
(b)	Income from growing and curing of coffee (Rule 7B) Business income is 25% of ₹ 3,50,000 Agricultural income is 75% of ₹ 3,50,000	87,500	2,62,500
(c)	Income from manufacture of tea (Rule 8) Business income is 40% of ₹ 7,00,000 Agricultural income is 60% of ₹ 7,00,000	2,80,000	4,20,000
(d)	Income from sale of plants in nursery is agricultural income [See Note below]	Nil	1,00,000
		5,42,500	11,07,500

Note: *Explanation 3* to Section 2(1A) provides that the income derived from saplings or seedlings grown in a nursery would be deemed to be agricultural income, whether or not the basic operations were carried out on land.

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Question 39

Mr. Gupta is having a trading business and his Trading and Profit & Loss Account for the financial year 2013-14 is as under:

Particulars	Amount (₹)	Particulars	Amount (₹)
To Opening stock	1,00,000	By Sales	70,00,000
To Purchase	49,00,000	By Closing stock	50,000
To Gross profit	<u>20,50,000</u>		
Total	<u>70,50,000</u>	Total	<u>70,50,000</u>
Salary to employees (Including Contribution to PF)	5,00,000	By Gross Profit b/d	20,50,000
Donation to Prime Minister Relief Fund	1,00,000		
Provision for bad debts	50,000		
Bonus to employees	50,000		
Interest on bank loan	50,000		
Family planning expenditure incurred on employees	20,000		
Depreciation	30,000		
Income-tax	1,00,000		
To Net profit	<u>11,50,000</u>		
Total	<u>20,50,000</u>	Total	<u>20,50,000</u>

Other information:

- (i) Depreciation allowable ₹ 40,000 as per Income-tax Rules, 1962.
- (ii) No deduction of tax at source on payment of interest on bank loan has been made.
- (iii) Payment of bonus to workers made in the month of October, 2013 on the occasion of Diwali festival.
- (iv) Out of salary, ₹ 25,000 pertains to his contributions to recognized provident fund which was deposited after the due date of filing return of income. Further, employees contribution of ₹ 25,000 was also deposited after the due date of filing return of income.

Calculate gross total income of Mr. Gupta for the Assessment Year 2014-15.

Answer

Computation of Gross Total Income of Mr. Gupta for the A.Y. 2014-15

Particulars	₹	₹
Income from Business or profession		
Net profit as per Profit and Loss Account		11,50,000
Add : Expenses not deductible		
Donation to Prime Minister Relief Fund (Refer Note 1)	1,00,000	
Provision for bad debts (Refer Note 2)	50,000	
Family planning expenditure incurred on employees (Refer Note 3)	20,000	
Depreciation as per Profit and Loss Account	30,000	
Income-tax (Refer Note 4)	1,00,000	
Employer's contribution to recognized provident fund (Note 5)	<u>25,000</u>	<u>3,25,000</u>
		14,75,000
Less : Expense allowed		
Depreciation as per Income-tax Rules, 1962		<u>40,000</u>
		14,35,000
Add : Employee's contribution included in income as per Section 2(24)(x) (Refer Note 6)		<u>25,000</u>
Business Income / Gross Total Income		<u>14,60,000</u>

Notes:-

- (1) Donation to Prime Minister Relief Fund is not allowed as deduction from the business income. It is allowed as deduction under section 80G from the gross total income.
- (2) Provisions for bad debts is allowable as deduction under section 36(1)(viii) (subject to the limits specified therein) only in case of banks, public financial institutions, State Financial Corporation and State Industrial Investment Corporation. Therefore, it is not allowable as deduction in the case of Mr. Gupta.
- (3) Expenditure on family planning is allowed as deduction under section 36(1)(ix) only to a company assessee. Therefore, such expenditure is not allowable as deduction in the hands of Mr. Gupta.
- (4) Income-tax paid is not allowed as deduction as per the provisions of section 40(a)(ii).
- (5) Since, Mr. Gupta's contribution (by the employer) to recognized provident fund is deposited after the due date of filing return of income, the same is disallowed as per provisions of section 43B.

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- (6) Employee's contribution is includible in the income of the employer by virtue of Section 2(24)(x). The deduction for the same is not provided for as it was deposited after the due date. It has been assumed that it has not been already debited in the given profit and loss account.
- (7) TDS provisions under section 194A are not attracted in respect of payment of interest on bank loan. Therefore, disallowance under section 40(a)(ia) is not attracted in this case.
- (8) Since, the payment of bonus is made in October 2013, hence, no disallowance is attracted.

Question 40

Mr. Raju, a manufacturer at Chennai, gives the following Manufacturing, Trading and Profit & Loss Account for the year ended 31.03.2014:

Manufacturing, Trading and Profit & Loss Account for the year ended 31.03.2014

Particulars	₹	Particulars	₹
To Opening Stock	71,000	By Sales	32,00,000
To Purchase of Raw Materials	16,99,000	By Closing stock	2,00,000
To Manufacturing Wages & Expenses	5,70,000		
To Gross Profit	<u>10,60,000</u>		
	<u>34,00,000</u>		<u>34,00,000</u>
To Administrative charges	3,26,000	By Gross Profit	10,60,000
To State VAT penalty	5,000	By Dividend from domestic companies	15,000
To State VAT paid	1,10,000	By Income from agriculture (net)	1,80,000
To General Expenses	54,000		
To Interest to Bank (On machinery term loan)	60,000		
To Depreciation	2,00,000		
To Net Profit	5,00,000		
	<u>12,55,000</u>		<u>12,55,000</u>

Following are the further information relating to the financial year 2013-14:

- (i) Administrative charges include ₹ 46,000 paid as commission to brother of the assessee. The commission amount at the market rate is ₹ 36,000.
- (ii) The assessee paid ₹ 33,000 in cash to a transport carrier on 29.12.2013. This amount is included in manufacturing expenses (Assume that the provisions relating to TDS are not applicable to this payment.)

- (iii) A sum of ₹ 4,000 per month was paid as salary to a staff throughout the year and this has not been recorded in the books of account.
- (iv) Bank term loan interest actually paid upto 31.03.2014 was ₹ 20,000 and the balance was paid in October 2014.
- (v) Housing loan principal repaid during the year was ₹ 50,000 and it relates to residential property occupied by him. Interest on housing loan was ₹ 23,000. Housing loan was taken from Canara Bank. These amounts were not dealt with in the profit and loss account given above.
- (vi) Depreciation allowable under the Act is to be computed on the basis of following information:

Plant & Machinery (Depreciation rate @ 15%)	₹
Opening WDV (as on 01.04.2013)	12,00,000
Additions during the year (used for more than 180 days)	2,00,000
Total additions during the year	4,00,000
<i>Note: Ignore additional depreciation under section 32(1)(ia)</i>	

Compute the total income of Mr. Raju for the assessment year 2014-15.

Note: Ignore application of section 14A for disallowance of expenditures in respect of any exempt income.

Answer

Computation of total income of Mr. Raju for the A.Y. 2014-15

Particulars	₹	₹
Profits and gains of business or profession		
Net profit as per profit and loss account		5,00,000
Add: Excess commission paid to brother disallowed under section 40A(2)	10,000	
Disallowance under section 40A(3) is not attracted since the limit for one time cash payment is ₹ 35,000 in respect of payment to transport operators. Therefore, amount of ₹ 33,000 paid in cash to a transport carrier is allowable as deduction.	Nil	
Salary paid to staff not recorded in the books (Assuming that the expenditure is in the nature of unexplained expenditure and hence, is deemed to be income as per section 69C and would be taxable @ 30% under section 115BBE – no deduction allowable in respect of such expenditure) [See Note 1 below]	48,000	

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Bank term loan interest paid after the due date of filing of return under section 139(1) – disallowed as per section 43B	40,000	
State VAT penalty paid disallowed [See Note 2 below]	5,000	
Depreciation debited to profit and loss account	<u>2,00,000</u>	<u>3,03,000</u>
		8,03,000
Less: Dividend from domestic companies [Exempt under section 10(34)]	15,000	
Income from agriculture [Exempt under section 10(1)]	1,80,000	
Depreciation under the Income-tax Act, 1961 (As per working note)	<u>2,25,000</u>	<u>4,20,000</u>
		<u>3,83,000</u>
Income from house property		
Annual value of self-occupied property	Nil	
Less: Deduction under section 24(b) – interest on housing loan	<u>23,000</u>	<u>(23,000)</u>
Gross Total Income		<u>3,60,000</u>
Less: Deduction under section 80C in respect of Principal repayment of housing loan		<u>50,000</u>
Total Income		<u><u>3,10,000</u></u>

Working Note:

Computation of depreciation under the Income-tax Act, 1961

Particulars	₹
Depreciation@15% on ₹ 14 lakh (Opening WDV of ₹ 12 lakh plus assets purchased during the year and used for more than 180 days ₹ 2 lakh)	2,10,000
Depreciation @7.5% on ₹ 2 lakh (Cost of assets used for less than 180 days)	<u>15,000</u>
	<u><u>2,25,000</u></u>

Notes (Alternate views):

1. It is also possible to take a view that the salary not recorded in the books of account was an erroneous omission and that the assessee has offered satisfactory explanation for the same. In such a case, the same should not be added back as unexplained expenditure, but would be allowable as deduction while computing profits and gains of business and profession.
2. Where the imposition of penalty is not for delay in payment of sales tax or VAT but for contravention of provisions of the Sales Tax Act (or VAT Act), the levy is not compensatory and therefore, not deductible. However, if the levy is compensatory in nature, it would be fully allowable. Where it is a composite levy, the portion which is compensatory is allowable and that portion which is penal is to be disallowed.

Since the question only mentions "State VAT penalty paid" and the reason for levy of penalty is not given, it has been assumed that the levy is not compensatory and therefore, not deductible. It is, however, possible to assume that such levy is compensatory in nature and hence, allowable as deduction. In such a case, the total income would be ₹ 3,05,000.

Question 41

Mr. Sivam, a retail trader of Cochin gives the following Trading and Profit and Loss Account for the year ended 31st March, 2014:

Trading and Profit and Loss Account for the year ended 31.03.2014

Particulars	₹	Particulars	₹
To Opening stock	90,000	By Sales	12,11,500
To Purchases	10,04,000	By Income from UTI	2,400
To Gross Profit	<u>3,06,000</u>	By Closing stock	<u>1,86,100</u>
	<u>14,00,000</u>		<u>14,00,000</u>
To Salary	60,000	By Gross profit b/d	3,06,000
To Rent and rates	36,000		
To Interest on loan	15,000		
To Depreciation	1,05,000		
To Printing & stationery	23,200		
To Postage & telegram	1,640		
To Loss on sale of shares (Short term)	8,100		
To Other general expenses	7,060		
To Net Profit	<u>50,000</u>		
	<u>3,06,000</u>		<u>3,06,000</u>

Additional Information:

- (i) *It was found that some stocks were omitted to be included in both the Opening and Closing Stock, the values of which were:*

Opening stock	₹ 9,000
Closing stock	₹ 18,000
- (ii) *Salary includes ₹ 10,000 paid to his brother, which is unreasonable to the extent of ₹ 2,000.*
- (iii) *The whole amount of printing and stationery was paid in cash by way of one time payment.*
- (iv) *The depreciation provided in the Profit and Loss Account ₹ 1,05,000 was based on the following information :*

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The written down value of plant and machinery is ₹ 4,20,000 as on 01.04.2013. A new plant falling under the same block of depreciation was bought on 1.7.2013 for ₹ 70,000. Two old plants were sold on 1.10.2013 for ₹ 50,000.

(v) Rent and rates includes sales tax liability of ₹ 3,400 paid on 7.4.2014.

(vi) Other general expenses include ₹ 2,000 paid as donation to a Public Charitable Trust.

You are required to advise Mr. Sivam whether he can offer his business income under section 44AD i.e. presumptive taxation.

Answer

Computation of business income of Mr. Sivam for the A.Y. 2014-15

Particulars	₹	₹
Net Profit as per profit and loss account		50,000
<i>Add:</i> Inadmissible expenses / losses		
Under valuation of closing stock	18,000	
Salary paid to brother – unreasonable [Section 40A(2)]	2,000	
Printing and stationery paid in cash [Section 40A(3)]	23,200	
Depreciation (considered separately)	1,05,000	
Short term capital loss on shares	8,100	
Donation to public charitable trust	<u>2,000</u>	<u>1,58,300</u>
		2,08,300
<i>Less:</i> Deductions items:		
Under valuation of opening stock	9,000	
Income from UTI [Exempt under section 10(35)]	<u>2,400</u>	<u>11,400</u>
Business income before depreciation		1,96,900
<i>Less:</i> Depreciation (See Note 1)		<u>66,000</u>
		<u>1,30,900</u>

Computation of business income as per section 44AD -

As per section 44AD, the business income would be 8% of turnover i.e., $12,11,500 \times 8/100 = ₹ 96,920$

The business income under section 44AD is ₹ 96,920.

As the business income under section 44AD is lower than the business income as per the normal provisions of the Act, it is advisable for Mr. Sivam to offer his business income under section 44AD.

Notes:

1. Calculation of depreciation

Particulars	₹
WDV of the block of plant & machinery as on 1.4.2013	4,20,000
Add: Cost of new plant & machinery	70,000
	4,90,000
Less: Sale proceeds of assets sold	50,000
WDV of the block of plant & machinery as on 31.3.2014	4,40,000
Depreciation @ 15%	66,000
No additional depreciation is allowable as the assessee is not engaged in manufacture or production of any article.	

2. Since sales-tax liability has been paid before the due date of filing return of income under section 139(1), the same is deductible.

Question 42

Following is the profit and loss account of Mr. Q for the year ended 31-03-2014:

Particulars	₹	Particulars	₹
To Repairs on Building	1,81,000	By Gross Profit	6,01,000
To Amount paid to IIT, Mumbai for an approved scientific research programme	1,00,000	By I.T. Refund	8,100
To Interest	1,10,000	By Interest on Company Deposits	6,400
To Travelling	1,30,550		
To Net Profit	93,950		
	6,15,500		6,15,500

Following additional information is furnished:

- (1) Repairs on building includes ₹ 1,00,000 being cost of laying a toilet roof.
- (2) Interest payments include ₹ 50,000 on which tax has not been deducted and penalty for contravention of Central Sales Tax Act of ₹ 24,000.

Compute the income chargeable under the head "Profits and gains of Business or Profession" of Mr. Q for the year ended 31-03-2014 ignoring depreciation.

Answer

Computation of income under the head "Profits and gains of business or profession" of Mr. Q for the A.Y. 2014-15

Particulars	₹	₹
Net profit as per profit and loss account		93,950
<i>Add:</i> Expenses not allowable		
Expenses on laying a toilet roof – Capital expenditure, hence not allowable as per section 37(1).	1,00,000	
Interest payable on which tax has not been deducted at source [disallowed under section 40(a)]	50,000	
Penalty for contravention of Central Sales Tax Act [Penalty paid for violation or infringement of any law is not allowable as deduction under section 37(1)]	24,000	
Payment to IIT, Mumbai for scientific research programme (to be treated separately)	<u>1,00,000</u>	<u>2,74,000</u>
		3,67,950
<i>Less:</i> Income not forming part of business income		
Interest from company deposits (chargeable under the head "Income from other sources") (See Note below)	6,400	
Income-tax refund (not an income chargeable to tax)	<u>8,100</u>	<u>14,500</u>
		3,53,450
<i>Less:</i> Weighted deduction@200% under section 35(2AA) for payment to IIT for an approved scientific research program.		<u>2,00,000</u>
Profit and gains of business or profession		<u>1,53,450</u>

Note – Interest on company deposits may also be treated as business income presuming that the interest has been earned by Mr. Q out of available temporary surplus funds which are not immediately required for his business purposes but nevertheless meant only for Mr. Q's business activities. In such a case, income under the head "Profit and gains of business or profession" would be ₹ 1,59,850.

Question 43

Following is the profit and loss account of Mr. A for the year ended 31.3.2014:

Particulars	₹	Particulars	₹
To Repairs on building	1,30,000	By Gross profit	6,01,000
To Advertisement	51,000	By Income Tax Refund	4,500

<i>To Amount paid to Scientific Research Association approved u/s 35</i>	<i>1,00,000</i>	<i>By Interest from company deposits</i>	<i>6,400</i>
<i>To Interest</i>	<i>1,10,000</i>	<i>By Dividends</i>	<i>3,600</i>
<i>To Traveling</i>	<i>1,30,000</i>		
<i>To Net Profit</i>	<u><i>94,500</i></u>		
	<u><i>6,15,500</i></u>		<u><i>6,15,500</i></u>

Following additional information is furnished:

- (1) Repairs on building includes ₹ 95,000 being cost of raising a compound wall for the own business premises.
- (2) Interest payments include interest of ₹ 12,000 payable outside India to a resident Indian on which tax has not been deducted and penalty of ₹ 24,000 for contravention of Central Sales Tax Act.

Compute the income chargeable under the head 'Profits and gains of business or profession' of Mr. A for the year ended 31.3.2014 ignoring depreciation.

Answer

Profits and gains of business or profession of Mr. A for the year ended 31.3.2014

Particulars	₹	₹
Net profit as per profit and loss account		94,500
<i>Add: Expenses not allowable</i>		
(i) Expenses on raising compound wall – capital expenditure, hence disallowed	95,000	
(ii) Interest payable outside India to a resident, as tax has not been deducted at source [Section 40(a)]	12,000	
(iii) Penalty for contravention of CST Act [Penalty paid for violation or infringement of any law is not allowable as deduction under section 37(1)]	24,000	
(iv) Contribution for scientific research (to be treated separately)	<u>1,00,000</u>	<u>2,31,000</u>
		3,25,500
<i>Less: Income not forming part of business income</i>		
Interest from company deposits	6,400	
Dividend	3,600	
Income Tax refund	<u>4,500</u>	<u>14,500</u>
		3,11,000
<i>Less: Deduction under section 35 for scientific research [See Note below]</i>		<u>1,75,000</u>
Profit and gains of business or profession		<u>1,36,000</u>

Note: Contribution to approved scientific research association qualifies for deduction @ 175% under section 35(1)(ii).

Question 44

Briefly explain the term "substantial interest". State three situations in which the same assumes importance.

Answer

As per *Explanation* to section 40A(2), a person shall be deemed to have a substantial interest in a business or profession, if, -

- (1) in case where the business or profession is carried on by a company, such person who, at any time during the previous year, is the beneficial owner of shares (not being shares entitled to a fixed rate of dividend, whether with or without a right to participate in profits), carrying not less than 20% of the voting power.
- (2) In any other case, such person who, at any time during the previous year, is beneficially entitled to not less than 20% of the profits of such business or profession.

Following are the situations under which the substantial interest assumes importance -

- (i) Taxability of deemed dividend under section 2(22)(e);
- (ii) Disallowance of excessive or unreasonable expenditure under section 40A(2) to an individual who has a substantial interest in the business or profession of the assessee, and
- (iii) Clubbing of salary income of spouse, under section 64(1)(ii) in respect of remuneration received by the spouse from a concern in which the individual has a substantial interest.

Question 45

Fill in the blanks:

- (i) *Where a company has incurred a capital expenditure of ₹ 1,00,000 towards promoting family planning amongst employees, ₹ will be allowed as deduction in the current year and the balance in succeeding years.*
- (ii) *A motor car is the only asset in a block. Cost ₹ 2,00,000. Rate of depreciation is 15%. 20% is disallowed for estimated personal use. WDV of the block is ₹*
- (iii) *In case of an eligible assessee, in respect of imported second hand machinery never put to use by any person in India before, additional or accelerated depreciation is allowable at the rate of on the actual cost of machinery.*
- (iv) *A private limited company incurred a capital expenditure of ₹ 5,00,000 on 1.4.2013 for acquisition of patents and copyrights, such expenditure is(eligible for deduction in 5 years/subject to depreciation under section 32).*

Answer

- (i) 20,000, four
- (ii) ₹ 1,76,000.
- (iii) Nil / 0 %.
- (iv) subject to depreciation under section 32

Question 46

Raghav Industries Ltd. furnishes you the following information for the year ended 31-03-2014:

- (i) *Scientific research expenditure related to its business ₹ 2,40,000 fully revenue in nature.*
- (ii) *Building acquired for scientific research (including cost of land ₹ 5,00,000) in June 2013 for ₹ 12,00,000.*
- (iii) *Amount paid to Indian Institute of Science, Bangalore for scientific research ₹ 50,000.*
- (iv) *Demerger expenses incurred in financial year 2012-13 ₹ 5,00,000.*
- (v) *Contribution to the account of employees as per pension scheme referred to in section 80CCD amounted to ₹ 30,00,000. Amount above 10% of the salary of employees is ₹ 7,00,000.*
- (vi) *Amount recovered from employees towards provident fund contribution ₹ 12,00,000 of which amount remitted upto the end of the year was ₹ 7,00,000 and the balance was remitted before the 'due date' for filing the return prescribed in Section 139(1).*
- (vii) *Tax on non-monetary perquisites provided to the employees, borne by the employer ₹ 4,50,000.*
- (viii) *Gain due to change in the rate of exchange of foreign currency ₹ 1,00,000 related to import of machinery. The machinery was acquired two years ago and put to regular use since then.*

Explain in brief how the above said items would be dealt with for the A. Y. 2014-15.

Note: Computation of total income not required.

Answer

- (i) The entire revenue expenditure of ₹ 2,40,000 on scientific research related to the business of the company qualifies for deduction under section 35(1)(i).

Note – *If Raghav Industries Ltd. is a company engaged in the business of biotechnology or in any business of manufacture or production of any article or thing, not being an article or thing specified in the list of the Eleventh Schedule, it would be entitled to a weighted deduction of ₹ 4,80,000 (200% of ₹ 2,40,000, being the revenue expenditure on scientific research related to its business) under section 35(2AB), if the in-house research and development facility is approved by the prescribed authority and the*

company has entered into an agreement with the prescribed authority for cooperation in such research and development facility and for audit of accounts maintained for that facility.

- (ii) As per section 35(1)(iv) read with section 35(2), if any capital expenditure (other than expenditure on acquisition of land) is incurred on scientific research related to the business carried on by the assessee, the whole of such capital expenditure is allowable as deduction in the previous year in which it is incurred. Therefore, ₹ 7,00,000 (i.e. ₹ 12,00,000 – ₹ 5,00,000, being the cost of land) is allowable as deduction for the A.Y.2014-15. It is assumed that the scientific research is related to the business of Raghav Industries Ltd.
- (iii) The amount of ₹ 50,000 paid to Indian Institute of Science, Bangalore, for scientific research qualifies for a weighted deduction@175% of the sum paid as per section 35(1)(ii). Therefore, Raghav Industries Ltd. would be entitled to a deduction of ₹ 87,500 (i.e., 175% of ₹ 50,000) for the A.Y.2014-15.
- (iv) As per section 35DD, one-fifth of the expenditure incurred on demerger would be allowable as deduction for five successive previous years beginning from previous year 2012-13. Therefore, in the previous year 2013-14, ₹ 1,00,000, being one-fifth of ₹ 5,00,000 would be allowable as deduction.
- (v) The employer's contribution to the account of an employee under a pension scheme referred to in section 80CCD, upto 10% of salary of the employee in the previous year, is allowable as deduction under section 36(1)(iva) while computing business income.
- Disallowance under section 40A(9) would be attracted only in respect of the amount in excess of 10% of salary. Accordingly, ₹ 23 lakhs would be allowed as deduction and ₹ 7 lakhs would be disallowed.
- (vi) As per section 2(24)(x), the amount of provident fund contribution recovered from employees i.e. ₹ 12 lakhs would be taxable as income of Raghav Industries Ltd. However, the company can claim deduction under section 36(1)(va) of amount credited to the account of the employee in the provident fund before the due date under the relevant Act.
- If ₹ 7 lakhs has been remitted before the said due date, the same is allowable as deduction. If it has not been so remitted, then the same is not allowable as deduction. The deduction would be restricted to the amount remitted before the due date.
- The balance ₹ 5 lakhs remitted after the due date under the said Act but before the due date of filing the return is not allowable as deduction.
- (vii) The tax of ₹ 4,50,000 borne by the employer on non-monetary perquisites provided to the employees is disallowed under section 40(a)(v).
- (viii) As per section 43A, the gain of ₹ 1,00,000, arising at the time of making payment in respect of an imported machinery, due to change in rate of exchange of foreign currency,

has to be reduced from the actual cost of machinery, and depreciation would be computed on such reduced cost.

Question 47

Explain the tax treatment of Limited Liability Partnership under the Income-tax Act, 1961.

Answer

The taxation scheme of LLPs in the Income-tax Act, 1961 is on the same lines as applicable for general partnerships, i.e. tax liability would be attracted in the hands of the LLP and tax exemption would be available to the partners. Therefore, the same tax treatment would be applicable for both general partnerships and LLPs.

The rate of income-tax applicable to LLPs is the same as the rate applicable for firms i.e. 30% of total income.

The provisions of section 40(b) requiring payment of remuneration only to working partner in accordance with the terms of the partnership deed for a period commencing on or after the date of the partnership deed, would apply to LLPs as well. Further, disallowance of interest in excess of 12% per annum and salary exceeding the prescribed percentage of book profit would also be applicable in the case of LLPs.

However, whereas a partnership firm can opt for presumptive taxation scheme under section 44AD, an LLP cannot opt for such scheme.

EXERCISES

1. An assessee uses plant and machinery for the purpose of carrying on his business. Under section 31, he shall be eligible for deduction on account of-
 - a) both capital and revenue expenditure on repairs
 - b) current repairs
 - c) current repairs plus 1/5th of capital expenditure on repairs.
2. An electricity company charging depreciation on straight line method on each asset separately, sells one of its machinery in April, 2013 at ₹ 1,20,000. The WDV of the machinery at the beginning of the year i.e. on 1st April, 2013 is ₹ 1,35,000. No new machinery was purchased during the year. The shortfall of ₹ 15,000 is treated as -
 - a) Terminal depreciation
 - b) Short-term capital loss
 - c) Normal depreciation.
3. X Ltd. acquires an asset which was previously used for scientific research for ₹ 2,75,000. The asset was brought into use for the business of X Ltd., after the research was completed. The actual cost of the asset to be included in the block of assets is -
 - a) Nil
 - b) Market value of the asset on the date of transfer to business

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- c) ₹ 2,75,000 less notional depreciation under section 32 upto the date of transfer.
4. A Ltd. has unabsorbed depreciation of ₹ 4,50,000 for the P.Y.2013-14. This can be carried forward -
- for a maximum period of 8 years and set-off against business income.
 - Indefinitely and set-off against business income.
 - Indefinitely and set-off against any head of income.
5. Deduction under section 33AB is allowed to an assessee provided the assessee deposits the profits with NABARD -
- before the end of the previous year
 - within 6 months from the end of the previous year
 - within 6 months from the end of the previous year or before the due date for filing the return of income, whichever is earlier.
6. XYZ Ltd. incurred capital expenditure of ₹ 1,50,000 on 1.4.2013 for acquisition of patents and copyrights. Such expenditure is -
- Eligible for deduction in 14 years from A.Y.2014-15
 - Eligible for deduction in 5 years from A.Y.2014-15
 - Subject to depreciation under section 32
7. Under section 44AE, presumptive taxation is applicable at a particular rate provided the assessee is the owner of a maximum of certain number of goods carriages. The rate per month or part of the month relevant for A.Y.2014-15 and the maximum number specified under the section are -
- ₹ 5,000 for a heavy goods carriage and ₹ 4,500 for other goods carriages for an assessee owning not more than 10 goods carriages at any time during the year
 - ₹ 3,500 per carriage for an assessee owning not more than 10 goods carriages at the end of the previous year
 - ₹ 5,000 for a heavy goods carriage and ₹ 4,500 for other goods carriages for an assessee owning not more than 12 goods carriages at the end of the previous year
8. In the case of a non-resident engaged in the business of operation of aircraft, the income is determined under section 44BBA at -
- 7.5% of turnover
 - 10% of turnover
 - 5% of turnover
9. The W.D.V. of a block (Plant and Machinery, rate of depreciation 15%) as on 1.4.2013 is ₹ 3,20,000. A machinery costing ₹ 50,000 was acquired on 1.9.2013 but put to use on 1.11.2013. During Jan'2014, part of this block was sold for ₹ 2,00,000. The depreciation for A.Y.2014-15 would be -
- ₹ 21,750
 - ₹ 25,500
 - ₹ 21,125

10. Employer's contribution to provident fund/superannuation fund/gratuity fund is allowed as deduction in computing income under the head "Profits and gains of business or profession", provided it has been paid -
 - a) before the end of the previous year
 - b) on or before the due date by which the employer is required to credit an employee's contribution to the employee's account in the relevant fund.
 - c) on or before the due date for filing the return of income under section 139(1).
11. Is it compulsory for an assessee to claim depreciation under section 32 of the Income-tax Act, 1961?
12. Write short notes on -
 - (i) Enhanced depreciation
 - (ii) Set-off and carry forward of unabsorbed depreciation.
13. Discuss the provisions dealing with the computation of business income on a presumptive basis in case of resident assessees.
14. Discuss the concept of "block of assets" under the Income-tax Act, 1961.
15. Which are the deductions allowable only on actual payment under section 43B?
16. Write short notes on the following -
 - (a) Compulsory maintenance of books of accounts
 - (b) Compulsory tax audit.
 - (c) Shipping business in case of non-resident.
 - (d) The circumstances where the provisions of section 40A(3), regarding cash payments in excess of ₹ 20,000, does not apply.
 - (e) Amortisation of expenditure under voluntary retirement scheme.
 - (f) Deduction to be allowed on actual payment basis.
 - (g) Special provisions under section 44DA for computing income by way of royalty, fee for technical services, etc. in case of non-residents.
17. What is the tax treatment regarding cash payments in excess of limits prescribed in section 40A(3)?
18. The written down value of plant and machinery in the books of Alpha Ltd. is ₹ 75,00,000 as on 1st April, 2013, on which date, the installed capacity of the company was 12,000 tons. Alpha Ltd. borrowed ₹ 10,00,000 @10% p.a. from ICICI Bank on 1.8.2013 for purchase of new plant and machinery for extension of its existing business, which would increase its installed capacity to 13,000 tons. The new plant and machinery was purchased on the same date but was put to use only w.e.f. 1.11.2013. Compute the depreciation admissible under section 32 for the A.Y.2014-15, assuming the applicable rate of depreciation on plant and machinery to be 15%.

Answers

1. b; 2. a; 3. a; 4. c; 5. c; 6. c; 7. a; 8. c; 9. a; 10. c 18. ₹ 13,04,375.

UNIT 4 : Capital Gains

Question 1

Dinesh received a vacant site as gift from his friend in November 2002. The site was acquired by his friend for ₹ 3,00,000 in April 1990. Dinesh constructed a residential building during the year 2004-05 in the said site for ₹ 15,00,000. He carried out some further extension of the construction in the year 2007-08 for ₹ 5,00,000.

Dinesh sold the residential building for ₹ 55,00,000 in January 2014 but the State stamp valuation authority adopted ₹ 65,00,000 as value for the purpose of stamp duty.

Compute his long term capital gain, for the assessment year 2014-15 based on the above information. The cost inflation indices are as follows:

Financial Year	Cost inflation index
1990-91	182
2002-03	447
2004-05	480
2007-08	551
2013-14	939

Answer

Computation of long term capital gain of Dinesh for the A.Y. 2014-15

Particulars	₹	₹
Full value of consideration (Note 1)		65,00,000
Less: Indexed cost of acquisition-land (₹ 3,00,000 × 939/447) (Note 2 & 3)	6,30,201	
Indexed Cost of acquisition-building (₹ 15,00,000 × 939/ 480) (Note 3)	29,34,375	
Indexed Cost of improvement-building (₹ 5,00,000 x 939/551)	<u>8,52,087</u>	<u>44,16,663</u>
Long-term capital gain		<u>20,83,337</u>

Notes:

1. As per section 50C, where the consideration received or accruing as a result of transfer of a capital asset, being land or building or both, is less than the value adopted by the Stamp Valuation Authority, such value adopted by the Stamp Valuation Authority shall be deemed to be the full value of the consideration received or accruing as a result of such transfer. Accordingly, full value of consideration will be ₹ 65 lakhs in this case.

2. Since Dinesh has acquired the asset by way of gift, therefore, as per section 49(1), cost of the asset to Dinesh shall be deemed to be cost for which the previous owner acquired the asset i.e., ₹ 3,00,000, in this case.
3. Indexation benefit is available since both land and building are long-term capital assets. However, as per the definition of indexed cost of acquisition under clause (iii) of *Explanation* below section 48, indexation benefit for land will be available only from the previous year in which Mr. Dinesh first held the land i.e., P.Y. 2002-03.

Alternative view: *In the case of CIT v. Manjula J. Shah 16 Taxmann 42 (Bom.), the Bombay High court held that indexation cost of acquisition in case of gifted asset can be computed with reference to the year in which the previous owner first held the asset.*

As per this view, the indexation cost of acquisition of land would be ₹ 15,47,802 and long term capital gain would be ₹ 11,65,736.

Question 2

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

Answer

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

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

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

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

Note: *In the question, it has been given that the borrower who is a senior citizen did not repay the loan on maturity and hence gave possession of the house to the bank to discharge the loan. It may be noted that, generally, under a Reverse Mortgage Scheme of a bank, alienation of house property for recovery of loan with accumulated interest takes place only after the death of the borrower and not during his life time unless there has been a violation of any of the terms and conditions subject to which the loan was granted. In this case, it is presumed*

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that there has been such a violation, due to which the repayment of loan has fallen due during the life time of the senior citizen.

Question 3

Anshu transfers land and building on 02-01-2014 and furnishes the following information:

Particulars	(₹)
(i) Net consideration received	18,00,000
(ii) Value adopted by Stamp Valuation Authority	20,00,000
(iii) Value ascertained by Valuation Officer on reference by the Assessing Officer	21,00,000
(iv) This land was acquired by Anshu on 1-04-1981. Fair Market Value of the land as on 01-04-181 was	1,10,000
(v) Anshu constructed a residential building on the land at a cost of ₹ 3,20,000 (construction completed on 01-12-2002 during the financial year 2002-03) Brought forward short term capital loss incurred on sale of shares during financial year 2009-10 ₹ 1,50,000,	

Anshu seeks your advice regarding the amount to be invested in NHAI bonds so as to be exempt from capital gain tax under the Income-tax Act, 1961.

Cost inflation index for FY 1981-1982 : 100

Cost inflation index for FY 2002-2003 : 447

Cost inflation index for FY 2013-2014 : 939

Answer

Computation of Capital Gains of Ms. Anshu for the A.Y. 2014-15

Particulars	₹	₹
Full value of consideration [See Notes (i) & (ii) below]		20,00,000
Less: Indexed Cost of acquisition [See Note (iii) below]		
Indexed cost of land (₹ 1,10,000 × 939/100)	10,32,900	
Indexed cost of building (₹ 3,20,000 × 939/447)	<u>6,72,215</u>	<u>17,05,115</u>
Long-term capital gain		2,94,885
Less: Brought forward short-term capital loss set off [See Note (iv) below]		<u>1,50,000</u>
Taxable capital gains (Amount to be invested in NHAI bonds to get full exemption from tax on capital gains) [See Note (v) below]		1,44,885

Notes :

- (i) As per section 50C(1), where the consideration received or accruing as a result of transfer of a capital asset, being land or building or both, is less than the value adopted by the Stamp Valuation Authority for the purpose of payment of stamp duty, such value adopted by the Stamp Valuation Authority shall be deemed to be the full value of the consideration received or accruing as a result of such transfer. Accordingly, full value of consideration would be ₹ 20 lacs in this case.
- (ii) As per section 50C(3), where the valuation is referred by the Assessing Officer to Valuation Officer and the value ascertained by such Valuation Officer exceeds the value adopted by the Stamp Valuation Authority for the purpose of payment of stamp duty, the value adopted by the Stamp Valuation Authority shall be taken as the full value of the consideration received or accruing as a result of the transfer. Since the value ascertained by the Valuation Officer (i.e. ₹ 21 lakhs), is higher than the value adopted by the Stamp Valuation Authority (i.e. ₹ 20 lakhs), the full value of consideration in this case would be ₹ 20 lakhs.
- (iii) Since the cost of land acquired by Anshu on 1.4.1981 is not given in the question, the fair market value as on 1.4.1981 is taken as the cost of acquisition. Indexation benefit is available since land and building are both long-term capital assets, as they are held by Anshu for more than 36 months.
- (iv) As per section 74, brought forward unabsorbed short term capital loss can be set off against any capital gains, short term or long term, for 8 assessment years immediately succeeding the assessment year for which the loss was first computed. Therefore, short-term capital loss on sale of shares during the F.Y.2009-10 can be set-off against the current year long-term capital gains on sale of land and building.
- (v) As per section 54EC, an assessee can avail exemption in respect of long-term capital gains, if such capital gains are invested in the bonds issued by the NHAI redeemable after 3 years. Such investment is required to be made within a period of 6 months from the date of transfer of the asset. The exemption shall be the amount of capital gains or the amount of such investment made, whichever is less. Therefore, in this case if Anshu invests the entire capital gains of ₹ 1,44,885 (rounded off to ₹ 1,45,000) in bonds of NHAI, she can get full exemption from tax on capital gains.

Question 4

Mr. Mithun purchased 100 shares of M/s Goodmoney Co. Ltd. on 01-04-2005 at rate of ₹ 1,000 per share in public issue of the company.

Company allotted bonus shares in the ratio of 1:1 on 01.12.2012. He has also received dividend of ₹ 10 per share on 01.05.2013.

He has sold all the shares on 01.10.2013 at the rate of ₹ 3,000 per share through a recognized stock exchange and paid brokerage of 1% and securities transaction tax of 0.02% to celebrate his 75th birthday. The cost inflation Index are as follows:

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<i>Financial Year</i>	<i>Cost Inflation Index</i>
2005-06	497
2013-14	939

Compute his total income and tax liability for Assessment Year 2014-15, assuming that he is having no income other than given above.

Answer

Computation of total income and tax liability of Mr. Mithun from A.Y. 2014-15

Particulars	₹
Short term capital gains on sale of bonus shares	
Gross sale consideration (100 x ₹ 3,000)	3,00,000
Less: Brokerage @ 1%	<u>3,000</u>
Net sale consideration	2,97,000
Less: Cost of acquisition of bonus shares	<u>NIL</u>
Total Income (Short term Capital Gains)	<u>2,97,000</u>
Tax Liability	
15% of (₹ 2,97,000-₹ 2,50,000)	7,050
Less: Rebate U/s 87A	<u>2,000</u>
	5,050
Add: Education cess @ 2%	101
Secondary and higher education cess @ 1%	<u>51</u>
Tax payable	<u>5,202</u>
Tax payable (Rounded Off)	5,200

Notes:

- (1) Long-term capital gains on sale of original shares through a recognized stock exchange (STT paid) is exempt under section 10(38).
- (2) Since bonus shares are held for less than 12 months before sale, the gain arising there from is a short term capital gain chargeable to tax@15% as per section 111A after adjusting the unexhausted basic exemption limit. Since Mr. Mithun is over 60 years of age, he is entitled for a higher basic exemption limit of ₹ 2,50,000 for A.Y. 2014-15.
- (3) Dividend income is exempt under section 10(34).
- (4) Brokerage paid is allowable since it is an expenditure incurred wholly and exclusively in connection with the transfer. Hence, it qualifies for deduction under section 48(i).
- (5) Cost of bonus shares will be Nil as such shares are allotted after 1.04.1981.

However, as per fifth proviso to section 48, securities transaction tax is not allowable as deduction.

Question 5

Mr. Selvan, acquired a residential house in January, 2000 for ₹ 10,00,000 and made some improvements by way of additional construction to the house, incurring expenditure of ₹ 2,00,000 in October, 2004. He sold the house property in October, 2013 for ₹ 75,00,000. The value of property was adopted as ₹ 80,00,000 by the State stamp valuation authority for registration purpose. He acquired a residential house in January, 2013 for ₹ 25,00,000. He deposited ₹ 20,00,000 in capital gains bonds issued by National Highways Authority of India (NHAI) in June, 2014.

Compute the capital gain chargeable to tax for the assessment year 2014-15.

What would be the tax consequence and in which assessment year it would be taxable, if the house property acquired in January, 2013 is sold for ₹ 40,00,000 in March, 2015?

Cost inflation index : F.Y.1999-2000 = 389

F.Y. 2004-2005 = 480

F.Y. 2013-2014 = 939

Answer

(I) Computation of Capital Gains Chargeable to tax for A.Y. 2014-15

Particulars	₹	₹
Sale consideration (i.e. Stamp Duty Value) (Note 1)		80,00,000
Less: Indexed Cost of Acquisition		
₹ 10,00,000 × 939/389	24,13,882	
Indexed Cost of Improvement		
₹ 2,00,000 × 939/480	<u>3,91,250</u>	<u>28,05,132</u>
		51,94,868
Less: Exemption under section 54 (Note 2)		<u>25,00,000</u>
Taxable Capital Gains		<u>26,94,868</u>

Notes:

- As per the provisions of section 50C, in case the stamp duty value adopted by the stamp valuation authority is higher than the actual sale consideration, the stamp duty value shall be deemed as the full value of consideration.
- Exemption under section 54 is available if a new residential house is purchased within one year before or two years after the date of transfer. Since the cost of new residential house is less than the capital gain, capital gain to the extent of cost of new asset is exempt under section 54.

3. Exemption under section 54EC is available in respect of investment in bonds of National Highways Authority of India only if the investment is made within a period of six months after the date of such transfer. In this case, since the investment is made after six months, exemption under section 54EC would not be available.
- (II) If the new asset purchased by the assessee on the basis of which exemption under section 54 is claimed, is transferred within 3 years from the date of its acquisition, then for computing the taxable short-term capital gain on such transfer, the capital gain exempted earlier shall be reduced from the cost of acquisition of such asset.

Hence, in the present case, if the house property acquired in January, 2013 is sold for ₹ 40,00,000 in March, 2015 (i.e. before the expiry of 3 years from the date of acquisition), the capital gains exempted earlier (i.e. ₹ 25,00,000) would be reduced from the cost of acquisition (i.e. ₹ 25,00,000) to arrive at the short-term capital gains for A.Y. 2015-16.

Particulars	₹	₹
Sale consideration		40,00,000
Less: Cost of acquisition	25,00,000	
Capital gains exempted earlier	<u>(25,00,000)</u>	<u>Nil</u>
Short-term capital gains		<u>40,00,000</u>

Question 6

Mr. Rakesh purchased a house property on 14th April, 1979 for ₹ 1,05,000. He entered into an agreement with Mr. Bobby for the sale of house on 15th September, 1982 and received an advance of ₹ 25,000. However, since Mr. Bobby did not remit the balance amount, Mr. Rakesh forfeited the advance.

Later on, he gifted the house property to his friend Mr. Aakash on 15th June, 1986.

Following renovations were carried out by Mr. Rakesh and Mr. Aakash to the house property:

	₹
By Mr. Rakesh during F.Y. 1979-80	10,000
By Mr. Rakesh during F.Y. 1983-84	50,000
By Mr. Aakash during F.Y. 1993-94	1,90,000

The fair market value of the property as on 1.4.1981 is ₹ 1,50,000.

Mr. Aakash entered into an agreement with Mr. Chintu for sale of the house on 1st June, 1995 and received an advance of ₹ 80,000. The said amount was forfeited by Mr. Aakash, since Mr. Chintu could not fulfil the terms of the agreement.

Finally, the house was sold by Mr. Aakash to Mr. Sanjay on 2nd January, 2014 for a consideration of ₹ 12,00,000.

Compute the capital gains chargeable to tax in the hands of Mr. Aakash for the assessment year 2014-15. Cost inflation indices are as under:

Financial Year	Cost inflation index
1981-82	100
1983-84	116
1986-87	140
1993-94	244
2013-14	939

Answer

Computation of taxable capital gains of Mr. Aakash for the A.Y. 2014-15

Particulars	₹
Sale consideration	12,00,000
Less: Indexed cost of acquisition (Note 1)	<u>4,69,500</u>
	7,30,500
Less: Indexed cost of improvement (Note 2)	<u>11,35,930</u>
Long term capital loss	<u>(4,05,430)</u>

Note 1

Indexed cost of acquisition is determined as under:

Cost to the previous owner i.e. Mr. Rakesh is ₹ 1,05,000

Fair Market Value on 1st April, 1981 is ₹ 1,50,000

Cost to the previous owner or FMV on 1st April, 1981, whichever is more, is to be taken as cost of acquisition of Mr. Aakash

₹ 1,50,000

Less: Advance money forfeited by Mr. Aakash (as per section 51)

(Note : Advance forfeited by Mr. Rakesh, the previous owner, should, however, not be deducted)

₹ 80,000

Cost of acquisition

₹ 70,000

Indexed cost of acquisition (₹ 70,000 × 939/140)

₹ 4,69,500

140 is the CII for F.Y. 1986-87, being the first year in which property is held by Mr. Aakash and 939 is the CII for F.Y. 2013-14, being the year in which the property is sold.

Alternative view: In the case of CIT v. Manjula J. Shah 16 Taxmann 42 (Bom.), the Bombay High Court held that the indexed cost of acquisition in case of gifted asset can be computed with reference to the year in which the previous owner first held the asset. As per this view, the indexation cost of acquisition of house would be ₹ 6,57,300, taking CII of 100 for the F.Y. 1980-81 since F.M.V. as on 1st April, 1981 is taken as cost of acquisition of Mr. Aakash.

Note 2

Indexed cost of Improvement is determined as under:

Expenditure incurred before 1 st April, 1981 should not be considered	NIL
Expenditure incurred on or after 1 st April, 1981	
- During 1983-84 Indexed cost of Improvement [₹ 50,000 × 939/116]	₹ 4,04,741
- During 1993-94 Indexed cost of Improvement [₹ 1,90,000 × 939/244]	<u>₹ 7,31,189</u>
Total indexed cost of improvement	<u>₹11,35,930</u>

Question 7

X Co. (P) Ltd., converted into a Limited Liability Partnership (LLP) by name All Trade LLP, with effect from 01.04.2013.

The following details are given to you:

<i>Asst. year 2006-07 : Business loss brought forward</i>	<i>₹ 2,00,000</i>
<i>Asst. year 2013-14 : Business loss brought forward</i>	<i>₹ 5,00,000</i>
<i>(These are related to erstwhile X Co. (P) Ltd.)</i>	
<i>Total income of All Trade LLP, for the financial year 2013-14 (Before set off of brought forward business losses of erstwhile company i.e. X Co. (P) Ltd.)</i>	<i>₹ 6,00,000</i>

Assume that all the conditions prescribed in section 47(xiii b) were satisfied by X Co. (P) Ltd. at the time of conversion to LLP.

- (i) Explain whether All Trade LLP can set off and carry forward the business loss of its predecessor i.e. X Co. (P) Ltd.?*
- (ii) State whether any change in partners of All Trade LLP at later date would have any tax consequence.*

Answer

- (i)** Section 72A(6A), provides that where a private company is succeeded by a LLP fulfilling the conditions laid down in the proviso to section 47(xiii b), then, notwithstanding anything contained in any other provision of the Income-tax Act, 1961, the accumulated loss and unabsorbed depreciation of the predecessor company shall be deemed to be the loss or allowance for depreciation of the successor LLP for the purpose of the previous year in which the business reorganisation was effected and other provisions of the Act relating to set-off and carry forward of losses and depreciation allowance shall apply accordingly.

Therefore, All Trade LLP can carry forward and set-off the business loss of ₹ 6 lakh of erstwhile X Co (P) Ltd. against its business income for the F.Y.2013-14. The unabsorbed business loss of ₹ 1 lakh, relating to A.Y. 2013-14, will be carried forward to the next year.

- (ii) Section 47(xiiib) requires that the shareholders of the company become partners of the LLP in the same proportion as their shareholding in the company. Further, the erstwhile shareholders of the company should continue to be entitled to receive at least 50% of the profits of the LLP for a period of 5 years from the date of conversion. If the entity fails to fulfill this condition, the benefit of set-off of business loss availed by the LLP would be deemed to be the profits and gains of the LLP chargeable to tax in the previous year in which the LLP fails to fulfill the condition.

Question 8

Ms. Chhaya transferred a vacant site to Ms. Dayama for ₹ 4,25,000. The stamp valuation authority fixed the value of vacant site for stamp duty purpose at ₹ 6,00,000. The total income of Chhaya and Dayama before considering the transfer of vacant site are ₹ 50,000 and ₹ 2,05,000, respectively. The indexed cost of acquisition for Ms. Chhaya in respect of vacant site is ₹ 4,00,000 (computed).

Determine the total income of both Ms. Chhaya and Ms. Dayama taking into account the above said transaction.

Answer

Section 56(2)(vii) would get attracted in case of transfer of immovable property for inadequate consideration, since the difference between the stamp duty value and sale consideration is more than ₹ 50,000 and therefore ₹ 1,75,000 (i.e. ₹ 6,00,000 - ₹ 4,25,000) will be taxed under the head "income from other sources" in the hands of transferee, i.e., Ms. Dayama. Further, for the transferor, Ms. Chhaya, the value adopted for stamp duty purpose will be taken as the deemed sale consideration under section 50C for computation of capital gains.

Particulars	Chhaya (Transferor) ₹	Dayama (Transferee) ₹
Capital gains		
Deemed sale consideration under section 50C	6,00,000	
Less: Indexed cost of acquisition	<u>4,00,000</u>	
	2,00,000	
Income from other sources		
Difference between stamp duty value and sale consideration of immovable property, taxable under section 56(2)(vii)		1,75,000
Other income (computed)	<u>50,000</u>	<u>2,05,000</u>
Total income	<u>2,50,000</u>	<u>3,80,000</u>

Question 9

Mr. Chandru transferred a vacant site on 28.10.2013 for ₹ 100 lakhs. The site was acquired for ₹ 9,99,300 on 30.6.2000. He invested ₹ 50 lakhs in eligible bonds issued by Rural

Electrification Corporation Ltd. (RECL) on 20.3.2014.

Again, he invested ₹ 20 lakhs in eligible bonds issued by National Highways Authority of India (NHAI) on 16.4.2014.

Compute the chargeable capital gain in the hands of Chandru for the A.Y. 2014-15.

<i>Financial year</i>	<i>Cost Inflation Index</i>
<i>2000-01</i>	<i>406</i>
<i>2013-14</i>	<i>939</i>

Answer

Computation of chargeable capital gain of Mr. Chandru for the A.Y.2014-15

Particulars	₹	₹
Sale consideration		1,00,00,000
Less: Indexed cost of acquisition (₹ 9,99,300 × 939/406)		<u>23,11,189</u>
		76,88,811
Less: Deduction under section 54EC		
20.03.2014 RECL bonds	50,00,000	
16.04.2014 NHAI bonds	<u>20,00,000</u>	<u>70,00,000</u>
Long term capital gain		<u>6,88,811</u>

Note:

- (1) Since the site was held for more than 36 months prior to the date of transfer, it is a long-term capital asset and the capital gain arising upon its transfer is long-term capital gain.
- (2) In order to claim exemption under section 54EC, Mr. Chandru has to invest in specified bonds of RECL or NHAI within a period of 6 months from the date of transfer of the asset.
- (3) However, investments made in such bonds by an assessee during any financial year cannot exceed ₹ 50 lakhs.

In this case, Mr. Chandru has invested ₹ 50 lakhs in RECL bonds in the F.Y.2013-14 and ₹ 20 lakhs in NHAI bonds in the F.Y.2014-15, both within six months from the date of transfer. He has, therefore, fulfilled both the conditions and hence, he is eligible to claim exemption of ₹ 70 lakhs under section 54EC.

Question 10

How will you calculate the period of holding in case of the following assets?

- (1) *Shares held in a company in liquidation*
- (2) *Bonus shares*
- (3) *Flat in a co-operative society*
- (4) *Transfer of a security by a depository (i.e., demat account)*

Answer

- (1) **Shares held in a company in liquidation** - The period after the date on which the company goes into liquidation shall be excluded while calculating the period of holding. Therefore, the period of holding shall commence from the date of acquisition and end with the date on which the company goes into liquidation.
- (2) **Bonus shares** - The period of holding shall be reckoned from the date of allotment of bonus shares and will end with the date of transfer.
- (3) **Flat in a co-operative society** - The period of holding shall be reckoned from the date of allotment of shares in the society and will end with the date of transfer.

Note – Any transaction whether by way of becoming a member of, or acquiring shares in, a co-operative society or by way of any agreement or any arrangement or in any other manner whatsoever which has the effect of transferring, or enabling enjoyment of, any immovable property is a transfer as per section 2(47)(vi). Hence, it is possible to take a view that any date from which such right is obtained may be taken as the date of acquisition.

- (4) **Transfer of security by a depository** - The period of holding shall be computed from the date on which the securities were credited to the demat account and will end with the date of transfer (sale). The first-in-first-out (FIFO) method will be adopted for determining the period of holding.

Question 11

Mr. A is a proprietor of Akash Enterprises having 2 units. He transferred on 1.4.2013 his Unit 1 by way of slump sale for a total consideration of ₹ 25 lacs. Unit 1 was started in the year 2002-03. The expenses incurred for this transfer were ₹ 28,000. His Balance Sheet as on 31.3.2013 is as under:

<i>Liabilities</i>	<i>Total (₹)</i>	<i>Assets</i>	<i>Unit 1 (₹)</i>	<i>Unit 2 (₹)</i>	<i>Total (₹)</i>
<i>Own Capital</i>	<i>15,00,000</i>	<i>Building</i>	<i>12,00,000</i>	<i>2,00,000</i>	<i>14,00,000</i>
<i>Revaluation Reserve (for building of unit 1)</i>	<i>3,00,000</i>	<i>Machinery</i>	<i>3,00,000</i>	<i>1,00,000</i>	<i>4,00,000</i>
<i>Bank loan (70% for unit 1)</i>	<i>2,00,000</i>	<i>Debtors</i>	<i>1,00,000</i>	<i>40,000</i>	<i>1,40,000</i>
<i>Trade creditors (25% for unit 1)</i>	<i><u>1,50,000</u></i>	<i>Other assets</i>	<i><u>1,50,000</u></i>	<i><u>60,000</u></i>	<i><u>2,10,000</u></i>
<i>Total</i>	<i><u>21,50,000</u></i>	<i>Total</i>	<i><u>17,50,000</u></i>	<i><u>4,00,000</u></i>	<i><u>21,50,000</u></i>

Other information:

- (i) *Revaluation reserve is created by revising upward the value of the building of Unit 1.*
- (ii) *No individual value of any asset is considered in the transfer deed.*

(iii) Other assets of Unit 1 include patents acquired on 1.7.2011 for ₹ 50,000 on which no depreciation has been charged.

Compute the capital gain for the assessment year 2014-15.

Answer

Computation of capital gains on slump sale of Unit 1

Particulars	₹
Sale value	25,00,000
Less: Expenses on sale	<u>28,000</u>
Net sale consideration	24,72,000
Less: Net worth (See Note 1 below)	<u>12,50,625</u>
Long term capital gain	<u>12,21,375</u>

Notes:

1. Computation of net worth of Unit 1 of Akash Enterprises

Particulars	₹	₹
Building (excluding ₹ 3 lakhs on account of revaluation)		9,00,000
Machinery		3,00,000
Debtors		1,00,000
Patents (See Note 2 below)		28,125
Other assets (₹ 1,50,000 – ₹ 50,000)		<u>1,00,000</u>
Total assets		14,28,125
Less: Creditors	37,500	
Bank Loan	<u>1,40,000</u>	<u>1,77,500</u>
Net worth		<u>12,50,625</u>

2. Written down value of patents as on 1.4.2013

Value of patents:	₹
Cost as on 1.7.2011	50,000
Less: Depreciation @ 25% for Financial Year 2011-12	<u>12,500</u>
WDV as on 1.4.2012	37,500
Less: Depreciation for Financial Year 2012-13	<u>9,375</u>
WDV as on 1.4.2013	<u>28,125</u>

For the purposes of computation of net worth, the written down value determined as per section 43(6) has to be considered in the case of depreciable assets. The problem has been solved assuming that the Balance Sheet values of ₹ 3 lakh and ₹ 9 lakh (₹ 12 lakh – ₹ 3 lakh) represent the written down value of machinery and building, respectively, of Unit 1.

3. Since the Unit is held for more than 36 months, capital gain arising would be long term capital gain. However, indexation benefit is not available in case of slump sale.

Question 12

Sachin received ₹ 15,00,000 on 23.01.2014 on transfer of his residential building in a transaction of reverse mortgage under a scheme notified by the Central Government. The building was acquired in March 1991 for ₹ 8,00,000.

Is the amount received on reverse mortgage chargeable to tax in the hands of Sachin under the head 'Capital gains'?

Cost inflation index for the F.Y. 1990-91 – 182; F.Y. 2013-14 - 939

Answer

As per section 47(xvi), any transfer of a capital asset in a transaction of Reverse Mortgage under a scheme made and notified by the Central Government will not be regarded as a transfer. Therefore, capital gains tax liability is not attracted.

Section 10(43) provides that the amount received by a senior citizen as a loan, either in lump sum or in installments, in a transaction of Reverse Mortgage would be exempt from income-tax. Therefore, the amount received by Sachin in a transaction of Reverse Mortgage of his residential building is exempt under section 10(43).

Question 13

Mukesh (aged 55 years) owned a residential house at Nagpur. It was acquired by Mukesh on 10.10.1986 for ₹ 4,00,000. It was sold for ₹ 55,00,000 on 4.11.2013. The State stamp valuation authority fixed the value of the property at ₹ 60,00,000. The assessee paid 2% of the sale consideration as brokerage for the sale of said property.

Mukesh acquired a residential house at Chennai on 10.12.2013 for ₹ 15,00,000 and deposited ₹ 10,00,000 on 10.4.2014 in the capital gain bond of Rural Electrification Corporation Ltd. (RECL). He deposited ₹ 5,00,000 on 6.07.2014 in the Capital Gain Deposit Scheme in a nationalized bank for construction of additional floor on the residential house property acquired at Chennai.

Compute the capital gain chargeable to tax in the hands of Mr. Mukesh for the assessment year 2014-15. Calculate the income-tax payable on the assumption that he has no other income chargeable to tax.

Cost inflation index : Financial year 1986-87 = 140; Financial year 2013-14 = 939

Answer

Computation of capital gains in the hands of Mukesh for the A.Y. 2014-15

Particulars	₹	₹
Deemed sale consideration (under section 50C)		60,00,000
Less: Brokerage @ 2% of ₹ 55,00,000		<u>1,10,000</u>
Net sale consideration		58,90,000

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Less: Indexed cost of acquisition ($\text{₹ } 4,00,000 \times 939/140$)		<u>26,82,857</u>
		32,07,143
Less: Exemption under sections 54 and 54EC		
Exemption under section 54 in respect of –		
(i) residential house acquired at Chennai on 10.12.2013	15,00,000	
(ii) amount deposited in Capital Gains Accounts Scheme on 06.07.2014 (before the due date of filing of return) for construction of additional floor on the residential house property acquired at Chennai		
	<u>5,00,000</u>	
	20,00,000	
Deduction under section 54EC in respect of amount deposited in RECL bonds on 10.04.2014 (within six months from the date of transfer)	<u>10,00,000</u>	<u>30,00,000</u>
Taxable long-term capital gain		<u>2,07,143</u>

Computation of tax liability of Mr. Mukesh for A.Y.2014-15

Particulars	₹
Tax on ₹ 7,143 (i.e., long term capital gain ₹ 2,07,143 less basic exemption limit of ₹ 2,00,000) @20%	1,429
Less: Rebate under section 87A	<u>1,429</u>
Total tax liability	<u>Nil</u>

Question 14

Mr. Raj Kumar sold a house to his friend Mr. Dhuruv on 1st November, 2013 for a consideration of ₹ 25,00,000. The Sub-Registrar refused to register the document for the said value, as according to him, stamp duty had to be paid on ₹ 45,00,000, which was the Government guideline value. Mr. Raj Kumar preferred an appeal to the Revenue Divisional Officer, who fixed the value of the house as ₹ 32,00,000 (₹ 22,00,000 for land and the balance for building portion). The differential stamp duty was paid, accepting the said value determined. What are the tax implications in the hands of Mr. Raj Kumar and Mr. Dhuruv for the assessment year 2014-15? Mr. Raj Kumar had purchased the land on 1st June, 2010 for ₹ 5,19,000 and completed the construction of house on 1st October, 2011 for ₹ 14,00,000.

Cost inflation indices may be taken as 711 for the financial year 2010-11, 785 for the financial year 2011-12 and 939 for the financial year 2013-14.

Answer

In the hands of the seller, Mr. Raj Kumar

As per section 50C(1), where the consideration received or accruing as a result of transfer of land or building or both, is less than the value adopted or assessed or assessable by the stamp

valuation authority, the value adopted or assessed or assessable by the stamp valuation authority shall be deemed to be the full value of consideration received or accruing as a result of transfer.

Where the assessee appeals against the stamp valuation and the value is reduced in appeal by the appellate authority (Revenue Divisional Officer, in this case), such value will be regarded as the consideration received or accruing as a result of transfer.

In the given problem, land has been held for a period exceeding 36 months and building for a period less than 36 months immediately preceding the date of transfer. So land is a long-term capital asset, while building is a short-term capital asset.

Particulars	₹
Long term capital gain on sale of land	
Consideration received or accruing as a result of transfer of land	22,00,000
Less: Indexed cost of acquisition ₹ 5,19,000 x 939/711	<u>6,85,430</u>
Long-term capital gain (A)	<u>15,14,570</u>
Short-term capital loss on sale of building	
Consideration received or accruing from transfer of building	10,00,000
Less: Cost of acquisition	<u>14,00,000</u>
Short term capital loss (B)	<u>4,00,000</u>

As per section 70, short-term capital loss can be set-off against long-term capital gains. Therefore, the net taxable long-term capital gains would be ₹ 11,14,570 (i.e., ₹ 15,14,570 – ₹ 4,00,000).

In the hands of the buyer Mr. Dhuruv

As per section 56(2)(vii), where an individual receives from a non-relative, any immovable property for a consideration which is less than the stamp value (or the value reduced by the appellate authority, as in this case) by an amount exceeding ₹ 50,000, then the difference between such value and actual consideration of such property is chargeable to tax as income from other sources. Therefore, ₹ 7,00,000 (i.e. ₹ 32,00,000 - ₹ 25,00,000) would be charged to tax as income from other sources under section 56(2)(vii).

Question 15

Compute the net taxable capital gains of Smt. Megha on the basis of the following information-

A house was purchased on 1.5.1997 for ₹ 4,50,000 and was used as a residence by the owner. The owner had contracted to sell this property in June, 2008 for ₹ 10 lacs and had received an advance of ₹ 70,000 towards sale. The intending purchaser did not proceed with the transaction and the advance was forfeited by the owner. The property was sold in April, 2013 for ₹ 15,00,000. The owner, from out of sale proceeds, invested ₹ 4 lacs in a new residential house in January, 2014.

Cost inflation index :- F.Y. 1997-98 – 331; F.Y. 2013-14 - 939

Answer

Computation of net taxable capital gains of Smt. Megha for the A.Y.2014-15

Particulars	₹
Sale consideration	15,00,000
Less: Indexed cost of acquisition (See Working note below)	<u>10,78,006</u>
Long term capital gain	4,21,994
Less: Exemption under section 54 (See Note 1 below)	<u>4,00,000</u>
Taxable long term capital gain	<u>21,994</u>

Working Note:

Indexed cost of acquisition	₹
Purchase price	4,50,000
Less: Amount forfeited (See Note 2 below)	<u>70,000</u>
Cost of acquisition	<u>3,80,000</u>

Indexed cost of acquisition ₹ 3,80,000 × 939/331 10,78,006

Notes:

- (1) Exemption under section 54 is available if a new residential house is purchased within two years from the date of transfer of existing residential house, which is a long-term capital asset. Since the cost of new residential house is less than the long-term capital gains, capital gains to the extent of cost of new house, i.e., ₹ 4 lakh, is exempt under section 54.
- (2) As per section 51, any advance received and retained by the assessee, as a result of earlier negotiations for sale of the asset, shall be deducted from the purchase price for computing the cost of acquisition of the asset.

Question 16

State, with reasons, whether the following statements are True or False.

- (i) Alienation of a residential house in a transaction of reverse mortgage under a scheme made and notified by the Central Government is treated as "transfer" for the purpose of capital gains.
- (ii) Zero coupon bonds of eligible corporation, held for more than 12 months, will be long-term capital assets.
- (iii) In the case of a dealer in shares, income by way of dividend is taxable under the head "Profits and gains of business or profession".
- (iv) Where an urban agricultural land owned by an individual, continuously used by him for agricultural purposes for a period of two years prior to the date of transfer, is compulsorily acquired under law and the compensation is fixed by the State Government, resultant capital gain is exempt.

- (v) *Zero Coupon Bond means a bond on which no payment and benefits are received or receivable before maturity or redemption.*
- (vi) *Income from growing and manufacturing tea in India is treated as agricultural income wholly.*

Answer

- (i) **False** : As per section 47(xvi), such alienation in a transaction of reverse mortgage under a scheme made and notified by the Central Government is not regarded as "transfer" for the purpose of capital gains.
- (ii) **True** : Section 2(42A) defines the term 'short-term capital asset'. Under the proviso to section 2(42A), zero coupon bond held for not more than 12 months will be treated as a short-term capital asset. Consequently, such bond held for more than 12 months will be a long-term capital asset.
- (iii) **False** : In view of the provisions of section 56(2)(i), dividend income is taxable under the head "Income from other sources" in the case of all assessees. However, the dividend referred in to in section 115-O is exempt under section 10(34).
- (iv) **False**: As per section 10(37), where an individual owns urban agricultural land which has been used for agricultural purposes for a period of two years immediately preceding the date of transfer, and the same is compulsorily acquired under any law and the compensation is determined or approved by the Central Government or the Reserve Bank of India, resultant capital gain will be exempt.
In this case, the compensation has been fixed by the State Government and hence the exemption will not be available.
- (v) **True** : As per section 2(48), 'Zero Coupon Bond' means a bond issued by any infrastructure capital company or infrastructure capital fund or a public sector company on or after 1st June 2005, in respect of which no payment and benefit is received or receivable before maturity or redemption from such issuing entity and which the Central Government may notify in this behalf.
- (vi) **False** : Only 60% of the income derived from the sale of tea grown and manufactured by the seller in India is treated as agricultural income and the balance 40% of the income shall be non-agricultural income chargeable to tax [Rule 8 of Income-tax Rules, 1962].

Question 17

Singhania & Co. own six machines, put in use for business in March, 2013. The depreciation on these machines is charged @ 15%. The written down value of these machines as on 1st April, 2013 was ₹ 8,50,000. Three of the old machines were sold on 10th June, 2013 for ₹ 11,00,000.

A new plant was bought for ₹ 8,50,000 on 30th November, 2013.

You are required to:

- (i) *determine the claim of depreciation for Assessment Year 2014-15.*
- (ii) *compute the capital gains liable to tax for Assessment Year 2014-15.*

(iii) If Singhanian & Co. had sold the three machines in June, 2013 for ₹ 21,00,000, will there be any difference in your above workings? Explain.

Answer

(i) Computation of depreciation for A.Y.2014-15

Particulars	₹
W.D.V. of the block as on 1.4.2013	8,50,000
Add: Purchase of new plant during the year	<u>8,50,000</u>
	17,00,000
Less: Sale consideration of old machinery during the year	<u>11,00,000</u>
W.D.V of the block as on 31.03.2014	<u>6,00,000</u>

Since the value of the block as on 31.3.2014 comprises of a new asset which has been put to use for less than 180 days, depreciation is restricted to 50% of the prescribed percentage of 15% i.e. depreciation is restricted to 7½%. Therefore, the depreciation allowable for the year is ₹ 45,000, being 7½% of ₹ 6,00,000.

Note: It is assumed that the firm is not eligible for additional depreciation under section 32(1)(ia).

(ii) The provisions under section 50 for computation of capital gains in the case of depreciable assets can be invoked only under the following circumstances:

- When one or some of the assets in the block are sold for consideration more than the value of the block.
- When all the assets are transferred for a consideration more than the value of the block.
- When all the assets are transferred for a consideration less than the value of the block.

Since in the first two cases, the sale consideration is more than the written down value of the block, the computation would result in short term capital gains.

In the third case, since the written down value exceeds the sale consideration, the resultant figure would be a short term capital loss.

In the given case, capital gains will not arise as the block of asset continues to exist, and some of the assets are sold for a price which is lesser than the written down value of the block.

(iii) If the three machines are sold in June, 2013 for ₹ 21,00,000, then short term capital gains would arise, since the sale consideration is more than the aggregate of the written down value of the block at the beginning of the year and the additions made during the year.

Particulars	₹	₹
Sale consideration		21,00,000
Less:		

W.D.V. of the machines as on 1.4.2013	8,50,000	
Purchase of new plant during the year	<u>8,50,000</u>	<u>17,00,000</u>
Short term capital gains		<u>4,00,000</u>

Question 18

Paulomi has transferred 1,000 shares of Hetal Ltd., (which she acquired at a cost of ₹ 10,000 in the financial year 2002-03) to Dhaval, her brother, at a consideration of ₹ 3,12,934 on 15.5.2013 privately.

During the financial year 2013-14, she has paid through e-banking ₹ 15,000 towards medical premium, ₹ 50,000 towards life insurance premium and ₹ 25,000 towards PPF.

Assuming she has no other source of income, compute her total income and tax payable for the Assessment Year 2014-15.

Cost Inflation Index:

F.Y.2002- 03 - 447

F.Y.2013- 14 - 939

Answer**Computation of total income and tax liability of Paulomi for Assessment year 2014-15**

Particulars	₹
Sale consideration	3,12,934
Less: Indexed cost of acquisition ₹ 10,000 × 939/447	<u>21,007</u>
Long term capital gain	<u>2,91,927</u>
Total income	2,91,930
Tax liability	
Income-tax @ 20% on ₹ 91,930 (₹ 2,91,930 – ₹ 2,00,000)	18,386
Less: Rebate under section 87A	<u>2,000</u>
	16,386
Add: Education cess and secondary and higher education cess @ 3%	<u>492</u>
Total tax payable	<u>16,878</u>

Notes :

- As per section 112, deductions under Chapter VI-A are not allowable against long term capital gain. Therefore, Paulomi is not entitled to deduction under section 80C in respect of payment of life insurance premium and contribution to PPF. She is also not entitled to deduction under section 80D in respect of medical insurance premium paid by her.
- Since Paulomi has not transferred her shares through the Stock Exchange and, therefore, has not paid securities transaction tax, she is not entitled to claim exemption under section 10(38) in respect of long term capital gain.

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3. She is, however, entitled to reduce the long-term capital gain by the unexhausted basic exemption limit and pay tax on the balance @20% as per section 112. In this case, since she has no other source of income, the entire basic exemption limit of ₹ 2,00,000 to the extent of long-term capital gain can be reduced from the long-term capital gain.

Question 19

Aarav converts his plot of land purchased in July, 2002 for ₹ 80,000 into stock-in-trade on 31st March, 2013. The fair market value as on 31.3.2013 was ₹ 1,90,000. The stock-in-trade was sold for ₹ 2,25,000 in the month of January, 2014.

Find out the taxable income, if any, and if so under which 'head of income' and for which Assessment Year?

Cost Inflation Index: F.Y. 2002-03: 447; F.Y. 2012-13: 852; F.Y. 2013-14: 939.

Answer

Conversion of a capital asset into stock-in-trade is a transfer within the meaning of section 2(47) in the previous year in which the asset is so converted. However, the capital gains will be charged to tax only in the year in which the stock-in-trade is sold.

The cost inflation index of the financial year in which the conversion took place should be considered for computing indexed cost of acquisition. Further, the fair market value on the date of conversion would be deemed to be the full value of consideration for transfer of the asset as per section 45(2). The sale price less the fair market value on the date of conversion would be treated as the business income of the year in which the stock-in-trade is sold.

Therefore, in this problem, both capital gains and business income would be charged to tax in the A.Y. 2014-15.

Particulars	₹
Capital Gains	
Sale consideration (Fair market value on the date of conversion)	1,90,000
Less: Indexed cost of acquisition (₹ 80,000 × 852/447)	<u>1,52,483</u>
Long-term capital gain	<u>37,517</u>
Profits & Gains of Business or Profession	
Sale price of stock-in-trade	2,25,000
Less: Fair market value on the date of conversion	<u>1,90,000</u>
	<u>35,000</u>
Computation of taxable income of Mr. Aarav for A.Y.2014-15	
Particulars	₹
Profits and gains from business or profession	35,000
Long term capital gains	<u>37,517</u>
	<u>72,517</u>

Question 20

Discuss the tax implications arising consequent to conversion of a capital asset into stock-in-trade of business and its subsequent sale.

Answer

The conversion of a capital asset into stock-in-trade is treated as a transfer under section 2(47). It would be treated as a transfer in the year in which the capital asset is converted into stock-in-trade. However, as per section 45(2), the profits or gains arising from the transfer by way of conversion of capital assets into stock-in-trade will be chargeable to tax only in the year in which the stock-in-trade is sold. For the purpose of computing capital gains in such cases, the fair market value of the capital asset on the date on which it was converted into stock-in-trade shall be deemed to be the full value of consideration received or accruing as a result of the transfer of the capital asset. Indexation benefit is available upto the year of conversion of capital asset in stock-in-trade.

On subsequent sale of such stock-in-trade, business profits would arise. The business income chargeable to tax would be the difference between the price at which the stock-in-trade is sold and the fair market value on the date of conversion of the capital asset into stock-in-trade.

Question 21

What is the cost of acquisition of self-generated assets, for the purpose of computation of capital gains?

Answer

1. **Cost of acquisition of a capital asset, being goodwill of a business or a trade mark or brand name associated with a business or a right to manufacture, produce or process any article or thing, or right to carry on any business, tenancy rights, stage carriage permits and loom hours [Section 55(2)(a)]**
 - (i) If the above capital assets have been purchased by the assessee, the cost of acquisition is the amount of the purchase price. For example, if Mr. A purchases a stage carriage permit from Mr. B for ₹ 2 lacs, that will be the cost of acquisition for Mr. A.
 - (ii) If the above capital assets are self-generated, the cost of acquisition shall be taken as nil.
 - (iii) In case the capital asset is acquired by any mode given under clauses (i) to (iv) of section 49(1), the cost of acquisition will be the cost to the previous owner if the previous owner paid for it. However, if it was self-generated by the previous owner, the cost of acquisition will be taken as nil.
2. **Cost of acquisition of other self-generated assets not covered under section 55(2)(a):**

In respect of self-generated goodwill of a profession and other self-generated assets not specifically covered under section 55(2)(a), the decision of the Supreme Court in *CIT v. B.C.*

Srinivasa Setty [1981] 128 ITR 294 will apply. In that case, the Supreme Court held that if the cost of acquisition of a self-generated asset is incapable of determination, then transfer of such asset is not taxable and consequently the gains thereon cannot be brought to charge.

Question 22

Mr. Malik owns a factory building on which he had been claiming depreciation for the past few years. It is the only asset in the block. The factory building and land appurtenant thereto were sold during the year. The following details are available:

Particulars	₹
Building completed in September, 2008 for	10,00,000
Land appurtenant thereto purchased in April, 2002 for	12,00,000
Advance received from a prospective buyer for land in May, 2003, forfeited in favour of assessee, as negotiations failed	50,000
WDV of the building block as on 1.4.2013	8,74,800
Sale value of factory building in November, 2013	8,00,000
Sale value of appurtenant land in November, 2013	40,00,000

The assessee is ready to invest in long-term specified assets under section 54EC, within specified time.

Compute the amount of taxable capital gain for the assessment year 2014-15 and the amount to be invested under section 54EC for availing the maximum exemption.

Cost inflation indices are as under :

Financial Year	Cost inflation index
2002-03	447
2003-04	463
2013-14	939

Answer**Computation of taxable capital gain of Mr. Malik for A.Y.2014-15**

Particulars	₹	₹
Factory building		
Sale price of building	8,00,000	
Less: WDV as on 1.4.2013	<u>8,74,800</u>	
Short-term capital loss on sale of building		(-) 74,800
Land appurtenant to the above building		
Sale value of land	40,00,000	
Less: Indexed cost of acquisition (₹ 11,50,000 × 939/447)	<u>24,15,772</u>	
Long-term capital gains on sale of land		<u>15,84,228</u>
Chargeable long term capital gain		<u>15,09,428</u>

Investment under section 54EC

In this case, both land and building have been held for more than 36 months and hence, are long-term capital assets. Exemption under section 54EC is available if the capital gains arising from transfer of a long-term capital asset are invested in long-term specified assets like bonds of National Highways Authority of India and Rural Electrification Corporation Ltd., within 6 months from the date of transfer. As per section 54EC, the amount to be invested for availing the maximum exemption is the net amount of capital gain arising from transfer of long-term capital asset, which is ₹ 15,09,428 (rounded off to ₹ 15,10,000) in this case.

Notes :

1. Where advance money has been received by the assessee, and retained by him, as a result of failure of the negotiations, section 51 will apply. The advance retained by the assessee will go to reduce the cost of acquisition. Indexation is to be done on the cost of acquisition so arrived at after reducing the advance money forfeited i.e. ₹ 12,00,000 – ₹ 50,000 = ₹ 11,50,000.
2. Factory building on which depreciation has been claimed, is a depreciable asset. Profit / loss arising on sale is deemed to be short-term capital gain/loss as per section 50, and no indexation benefit is available.
3. Land is not a depreciable asset, hence section 50 will not apply. Being a long-term capital asset (held for more than 36 months), indexation benefit is available.
4. As per section 74, short term capital loss can be set-off against any income under the head "Capital gains", long-term or short-term. Therefore, in this case, short-term capital loss of ₹ 74,800 can be set-off against long-term capital gain of ₹ 15,84,228.

Question 23

Mr. A is an individual carrying on business. His stock and machinery were damaged and destroyed in a fire accident.

The value of stock lost (total damaged) was ₹ 6,50,000. Certain portion of the machinery could be salvaged. The opening WDV of the block as on 1-4-2013 was ₹ 10,80,000.

During the process of safeguarding machinery and in the fire fighting operations, Mr. A lost his gold chain and a diamond ring, which he had purchased in April, 2003 for ₹ 1,20,000. The market value of these two items as on the date of fire accident was ₹ 1,80,000.

Mr. A received the following amounts from the insurance company:

<i>(i) Towards loss of stock</i>	<i>₹ 4,80,000</i>
<i>(ii) Towards damage of machinery</i>	<i>₹ 6,00,000</i>
<i>(iii) Towards gold chain and diamond ring</i>	<i>₹ 1,80,000</i>

You are requested to briefly comment on the tax treatment of the above three items under the provisions of the Income-tax Act, 1961.

Answer

- (i) **Compensation towards loss of stock:** Any compensation received from the insurance company towards loss/damage to stock in trade is to be construed as a trading receipt. Hence, ₹ 4,80,000 received as insurance claim for loss of stock has to be assessed under the head "Profit and gains of business or profession".

Note - The assessee can claim the value of stock destroyed by fire as revenue loss, eligible for deduction while computing income under the head "Profits and gains of business or profession".

- (ii) **Compensation towards damage to machinery:** The question does not mention whether the salvaged machinery is taken over by the Insurance company or whether there was any replacement of machinery during the year. Assuming that the salvaged machinery is taken over by the Insurance company, and there was no fresh addition of machinery during the year, the block of machinery will cease to exist. Therefore, ₹ 4,80,000 being the excess of written down value (i.e ₹ 10,80,000) over the insurance compensation (i.e. ₹ 6,00,000) will be assessable as a short-term capital loss.

Note – If new machinery is purchased in the next year, it will constitute the new block of machinery, on which depreciation can be claimed for that year.

- (iii) **Compensation towards loss of gold chain and diamond ring:** Gold chain and diamond ring are capital assets as envisaged by section 2(14). They are not "personal effects", which alone are to be excluded. As per section 45(1A), if any profit or gain arises in a previous year owing to receipt of insurance claim, the same shall be chargeable to tax as capital gains. The capital gains has to be computed by reducing the indexed cost of acquisition of jewellery from the insurance compensation of ₹ 1,80,000.

Question 24

Mr. A who transfers land and building on 2.01.2014, furnishes the following information:

- (i) *Net consideration received ₹ 12 lakhs.*
- (ii) *Value adopted by stamp valuation authority, which was not contested by Mr. A ₹ 19.5 lakhs.*
- (iii) *Value ascertained by Valuation Officer on reference by the Assessing Officer ₹ 20 lakhs.*
- (iv) *This land was distributed to Mr. A on the partial partition of his HUF on 1.4.1981. Fair market value of the land as on 1.4.81 was ₹ 1,10,000.*
- (v) *A residential building was constructed on the above land by Mr. A at a cost of ₹ 3,20,000 (construction completed on 1.12.2003) during the financial year 2003-04.*

(vi) Brought forward unabsorbed short-term capital loss (incurred on sale of shares during the financial year 2010-11) ₹ 2,05,000.

Mr. A seeks your advice as to the amount to be invested in NHAI/RECL bonds so as to be exempt from clutches of capital gain tax. Cost inflation indices for the financial years 1981-82, 2003-04 & 2013-14 are 100, 463 and 939 respectively.

Answer

Computation of Capital Gains of Mr. A for the Assessment Year 2014-15

Particulars	₹	₹
Full value of consideration (deemed) (See Note-1&2) (Indexation benefit is available since land and buildings are long-term capital assets)		19,50,000
Less: Indexed cost of land (₹ 1,10,000 × 939/100)	10,32,900	
Indexed cost of building (₹ 3,20,000 × 939/ 463)	<u>6,48,985</u>	<u>16,81,885</u>
Long-term capital gain		2,68,115
Less: Brought forward short-term capital loss set off(See Note-4)		<u>2,05,000</u>
Amount to be invested in NHAI / RECL bonds		<u>63,115</u>

Notes :

- (1) Where the consideration received or accruing as a result of transfer of a capital asset, being land or building or both, is less than the value adopted or assessed by any authority of a State Government (Stamp Valuation Authority) for the purpose of payment of stamp duty in respect of such asset and the same is not contested by the assessee, such value adopted or assessed shall be deemed to be the full value of the consideration received or accruing as a result of such transfer [Section 50C(1)]. Accordingly, the full value of consideration will be ₹ 19.5 lakhs in this case.
- (2) It is further provided in section 50C(3) that where the valuation is referred by the Assessing Officer to Valuation Officer and the value ascertained by such Valuation Officer exceeds the value adopted or assessed by the Stamp Valuation Authority, the value adopted or assessed by the Stamp Valuation Authority shall be taken as the full value of the consideration received or accruing as a result of the transfer. Since the value ascertained by the valuation officer (i.e. ₹ 20 lakhs) is higher than the value adopted by the stamp valuation authority (i.e. ₹ 19.5 lakhs), the full value of consideration in this case is ₹ 19.5 lakhs.
- (3) Cost of land which is acquired on partition of HUF is the cost to the previous owner. Since date and cost of acquisition to the previous owner are not given, fair market value as on 1.4.1981 is taken as the cost and indexed.

- (4) Brought forward unabsorbed short term capital loss can be set off against any capital gains, short term or long term, for 8 assessment years immediately succeeding the assessment year for which the loss was first computed.
- (5) As per section 54EC, an assessee can avail exemption in respect of long-term capital gains, if such capital gains are invested in the bonds issued by the NHAI / RECL redeemable after 3 years. Such investment is required to be made within a period of 6 months from the date of transfer of the asset. The exemption shall be the amount of capital gain or the amount of such investment made, whichever is less.

Question 25

X is in possession of agricultural land situated within urban limits, which is used for agricultural purposes during the preceding 3 years by his father. On 4.4.2013, this land is compulsorily acquired by the Central Government of India on a compensation fixed and paid by it for ₹ 10 lakhs. Advise X as to the tax consequences, assuming that the entire amount is invested in purchase of shares.

Answer

Section 10(37) exempts the capital gains arising to an individual or a Hindu Undivided Family from transfer of agricultural land by way of compulsory acquisition, or a transfer, the consideration for which is determined or approved by the RBI or the Central Government.

Such exemption is available where the compensation or the enhanced compensation or consideration, as the case may be, is received on or after 1st April, 2004 and the land has been used for agricultural purposes during the preceding two years by such individual or a parent of his or by such Hindu undivided family.

Since all the above conditions are fulfilled in this case, X is entitled to exemption under section 10(37) of the entire capital gains arising on sale of agricultural land.

Question 26

Mr. Paari, a resident individual acquired a plot of land at a cost of ₹ 75,000 in June, 1999. He constructed a house for his residence on that land at a cost of ₹ 1,25,000 in the financial year 2001-02.

He transferred the house for ₹ 15,00,000 in May, 2013 and acquired another residential house in June, 2013 for ₹ 8,00,000.

He furnishes other particulars as under

<i>Insurance agency commission earned</i>	<i>45,000</i>
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(Net of TDS of ₹ 5,000)

<i>Investment in NSC VIII issue</i>	<i>20,000</i>
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(i.e. on 20-3-2014)

Cost inflation index details are given below:

<i>Financial Year</i>	<i>Cost Inflation Index</i>
1999 – 2000	389
2001 – 2002	426
2013 – 2014	939

Compute the total income of Mr. Paari for the assessment year 2014-15.

Answer

Computation of total income of Mr. Paari for the A.Y. 2014-15

Particulars	₹	₹
Capital Gains		
Sale consideration		15,00,000
Less: Indexed cost of land (₹ 75,000 x 939/389)	1,81,041	
Indexed cost of building (₹ 1,25,000 x 939/426)	<u>2,75,528</u>	<u>4,56,569</u>
		10,43,431
Less: Exemption under section 54 (See Note 2 below)		<u>8,00,000</u>
Long-term capital gain		2,43,431
Profit and gains from business or profession/Income from other sources		
Insurance agency commission earned (Gross) (₹ 45,000 + ₹ 5,000)		<u>50,000</u>
Gross Total Income		2,93,431
Less: Deduction under Chapter VI-A Section 80C - Investment in NSC VIII		<u>20,000</u>
Total Income		<u>2,73,431</u>

Notes:

- (1) Since the building and the land are held for more than 36 months, the same are long-term capital assets and the capital gain arising on sale of such assets is a long-term capital gain.
- (2) As per the provisions of section 54, the capital gain arising on transfer of a long-term residential property shall not be chargeable to tax to the extent such capital gain is invested in the purchase of a residential house property one year before or two years after the date of transfer of original asset or constructed a residential house property

within three years after such date. Since Mr. Parri has purchased another residential house in June, 2013 for ₹ 8,00,000, the capital gain arising on transfer of residential house property in May, 2013 is exempt under section 54 to that extent.

Question 27

Mr. Y submits the following information pertaining to the year ended 31st March, 2014:

- (i) On 30.11.2013, when he attained the age of 60, his friends in India gave a flat at Surat as a gift, each contributing a sum of ₹ 20,000 in cash. The cost of the flat purchased using the various gifts was ₹ 3.40 lacs.
- (ii) His close friend abroad sent him a cash gift of ₹ 75,000 through his relative for the above occasion.
- (iii) Mr. Y sold the above flat on 30.1.2014 for ₹ 3.6 lacs. The Registrar's valuation for stamp duty purposes was ₹ 3.7 lacs. Neither Mr. Y nor the buyer, questioned the value fixed by the Registrar.
- (iv) He had purchased some equity shares in X Pvt. Ltd., on 5.2.2007 for ₹ 3.5 lacs. These shares were sold on 15.3.2014 for ₹ 2.8 lacs.

You are requested to calculate the total income of Mr. Y for the assessment year 2014-15.

[Cost Inflation Index for F.Y. 2006-07: 519, 2013-14: 939]

Answer**Computation of total income of Mr.Y for A.Y. 2014-15**

Particulars	₹	₹	₹
Capital Gains			
Short term capital gains (on sale of flat)			
(i) Sale consideration	3,60,000		
(ii) Stamp duty valuation	<u>3,70,000</u>		
Consideration for the purpose of capital gains as per section 50C (stamp duty value, since it is higher than sale consideration)		3,70,000	
<i>Less: Cost of acquisition [As per section 49(4), cost to be taken into consideration for 56(2)(vii) will be the cost of acquisition]</i>		<u>3,40,000</u>	30,000
Long term capital loss on sale of equity shares of X Pvt. Ltd			
Sale consideration		2,80,000	
<i>Less: Indexed cost of acquisition (₹ 3,50,000 × 939/519)</i>		<u>6,33,237</u>	

Long term capital loss to be carried forward (See Note 1 below)	3,53,237	
Income from other sources:		
Gift from friends by way of immovable property on 30.11.2013 [See Note 3 below].		3,40,000
Gift received from a close friend (unrelated person) [See Note 2 below]		<u>75,000</u>
Total income		<u>4,45,000</u>

Notes:

1. In the given problem, shares have been held for more than 12 months and hence, constitute a long term capital asset. The loss arising from sale of such shares is, therefore, a long-term capital loss. As per section 70(3), long term capital loss can be set-off only against long-term capital gains. Therefore, long-term capital loss cannot be set-off against short-term capital gains. However, such long-term capital loss can be carried forward to the next year for set-off against long-term capital gains arising in that year.
2. Any sum received from an unrelated person will be deemed as income and taxed as income from other sources if the aggregate sum received exceeds ₹ 50,000 in a year [Section 56(2)(vii)].
3. Receipt of immovable property without consideration would attract the provisions of section 56(2)(vii).

Question 28

Bala sold his vacant site on 21.09.2013 for ₹ 7,00,000. It was acquired by him on 01.10.1995 for ₹ 1,50,000.

The State stamp valuation authority fixed the value of the site at the time of transfer @ ₹ 13,00,000.

Compute capital gains in the hands of Bala and give your reasons for computation.

Cost inflation index : F.Y.1995-96: 281 and F.Y. 2013-14 : 939.

Answer**Computation of capital gains of Bala for the A.Y.2014-15**

Particulars	₹
Deemed sale consideration as per section 50C	13,00,000
Less : Indexed cost of acquisition (₹ 1,50,000 × 939 /281)	<u>5,01,246</u>
Taxable long term capital gain	<u>7,98,754</u>

Note: According to section 50C(1), where the consideration received or accruing as a result of the transfer of land or building or both is less than the value adopted or assessed or

assessable by the State Stamp Valuation Authority for the purpose of payment of stamp duty in respect of such transfer, then the value so adopted or assessed or assessable by the State Stamp Valuation Authority shall be deemed to be the full value of the consideration received or accruing as a result of the transfer.

In this case, since the consideration of ₹ 7,00,000 received on transfer of land is less than the value of ₹ 13,00,000 fixed by the State Stamp Valuation Authority, the value adopted by the State Stamp Valuation Authority is deemed to be the full value of consideration and capital gains is calculated accordingly.

Question 29

Mr. 'X' furnishes the following data for the previous year ending 31.3.2014:

- (a) Unlisted Equity Shares of AB Ltd., 10,000 in number were sold on 31.5.2013, at ₹ 500 for each share.
- (b) The above shares of 10,000 were acquired by 'X' in the following manner:
 - (i) Received as gift from his father on 1.6.1980 (5,000 shares) the fair market value on 1.4.1981 ₹ 50 per share.
 - (ii) Bonus shares received from AB Ltd. on 21.7.1985 (2,000 shares).
 - (iii) Purchased on 1.2.1994 at the price of ₹ 125 per share (3,000 shares).
- (c) Purchased one residential house at ₹ 25 lakhs, on 1.5.2014 from the sale proceeds of shares.
- (d) 'X' is already owning a residential house, even before the purchase of above house.

You are required to compute the taxable capital gain. He has no other source of income chargeable to tax.

(Cost Inflation Index – Financial year 1993-94: 244; Financial year 2013-14: 939)

Answer

Computation of taxable capital gain of Mr. 'X' for A.Y. 2014-15

Particulars	₹	₹
Sale consideration received on sale of 10,000 shares @ ₹ 500 each		50,00,000
Less: Indexed cost of acquisition		
(a) 5,000 shares received as gift from father on 1.6.1980 Indexed cost 5,000 x ₹ 50 x 939/100	23,47,500	
(b) 2,000 bonus shares received from AB Ltd Bonus shares are acquired on 21.7.1985 i.e after 01.04.1981. Hence, the cost is Nil.	Nil	
(c) 3000 shares purchased on 1.2.1994 @ ₹ 125 per share. The indexed cost is 3000 x 125 x 939/244	14,43,135	37,90,635
Long term capital gain		12,09,365

Less : Exemption under section 54F (See Note below) ₹ 12,09,365 x ₹ 25,00,000 / ₹ 50,00,000		<u>6,04,683</u>
Taxable long term capital gain		<u>6,04,682</u>

Note:

Exemption under section 54F can be availed by the assessee subject to fulfillment of the following conditions:

- The assessee should not own more than one residential house on the date of transfer of the long-term capital asset;
- The assessee should purchase a residential house within a period of 1 year before or 2 years after the date of transfer or construct a residential house within a period of 3 years from the date of transfer of the long-term capital asset.

In this case, the assessee has fulfilled the two conditions mentioned above. Therefore, he is entitled to exemption under section 54F.

Question 30

Ms. Vimla sold a residential building at Jodhpur for ₹ 15,00,000 on 01-07-2013.

The building was acquired for ₹ 1,50,000 on 01-06-1997.

She paid brokerage @ 2% at the time of sale of the building. She invested ₹ 7 lakhs in purchase of a residential building in December 2013 and deposited ₹ 2 lakhs in NHAI Capital Gains Bond in March, 2014. Compute her taxable capital gain.

Cost inflation index of F.Y. 1997-98: 331; F.Y. 2013-14: 939

Answer**Computation of taxable capital gain of Ms. Vimla for A.Y.2014-15**

Particulars	₹	₹
Sale price of residential building	15,00,000	
Less : Brokerage @ 2%	<u>30,000</u>	
Net consideration		14,70,000
Less : Indexed cost of acquisition ₹ 1,50,000 x 939/331		<u>4,25,529</u>
		10,44,471
Less: Deduction under section 54 for purchase of new residential house in December 2013		<u>7,00,000</u>
Taxable long term capital gain		<u>3,44,471</u>

Note : One of the conditions for claiming deduction under section 54EC for the investment in RECL/NHAI Capital Gains bonds is that the deposit should be made within 6 months from the date of transfer. In this case, the transfer took place on 1.7.2013 and the 6 months period within which the deposit should be made for the purpose of section 54EC would expire by

1.1.2014. The investment in REC/NHAI Capital Gains bonds was made only in March 2014. Therefore, the assessee is not eligible for section 54EC deduction.

Question 31

Mrs. Malini Hari shifted her industrial undertaking located in corporation limits of Faridabad, to a Special Economic Zone (SEZ) on 1.12.2013.

The following particulars are available:

Particulars		₹
(a)	Land: Purchased on 20.01.2003	4,26,000
	Sold for	22,00,000
(b)	Building [Construction completed on 14.03.2005]	
	WDV of building as on 01.04.2013	8,20,000
	Sold for	11,39,000
(c)	WDV of cars as on 01.04.2013	7,40,000
	Sold for	6,00,000
(d)	Expenses on shifting the undertaking	1,15,000
(e)	Assets acquired for the undertaking in the SEZ (on or before 25.06.2014):	
	(i) Land	3,00,000
	(ii) Building	5,00,000
	(iii) Computers	1,00,000
	(iv) Car	4,20,000
	(v) Machinery (Second hand)	2,00,000
	(vi) Furniture	50,000

There is no intention of investing in any other asset in this undertaking.

Compute the exemption available under section 54GA for the assessment year 2014-15.

Cost inflation indices for F.Y.2002-03 – 447; F.Y.2013-14: 939.

Answer

Where an assessee shifts an existing undertaking from an urban area to a SEZ and incurs expenses for shifting and acquires new assets for the undertaking in the SEZ, exemption under section 54GA would be available in such a case.

The capital gain, short-term or long-term, arising from transfer of land, building, plant and machinery in the existing undertaking would be exempt under section 54GA if the assessee, within a period of one year before or three years after the date on which the transfer took place,

- (i) acquires plant and machinery for use in the undertaking in the SEZ;
- (ii) acquires land or building or constructs building for the business of the undertaking in the SEZ;

(iii) incurs expenses on shifting of the undertaking.

Computation of capital gain :

(a) *Land:*

Sale price	22,00,000
Less: Indexed cost of acquisition $4,26,000 \times 939/447$	<u>8,94,886</u>
Long-term capital gain	<u>13,05,114</u>

(b) *Building:*

Sale value	11,39,000
Less: Opening WDV	<u>8,20,000</u>
Short-term capital gain under section 50	<u>3,19,000</u>

(c) *Plant:*

Car

Sale value	6,00,000
Less: Opening WDV	<u>7,40,000</u>
Short term capital loss under section 50	<u>(-),1,40,000</u>

Net short term capital gain (₹ 3,19,000 – ₹ 1,40,000) 1,79,000

Total capital gain (LTCG+STCG) i.e. ₹ 13,05,114 + ₹ 1,79,000 = ₹ 14,84,114

Exemption under section 54GA is available in respect of the following assets acquired and expenses incurred:

Particulars	₹
Land	3,00,000
Building	5,00,000
Plant:	
Computers	1,00,000
Car	4,20,000
Machinery	2,00,000
Expenses of shifting	<u>1,15,000</u>
Total Exemption	<u>16,35,000</u>

Note:

- The total exemption available under section 54GA is the lower of capital gains of ₹ 14,84,114 or the amount of investment which is ₹ 16,35,000. Hence, the amount of exemption available under section 54GA is ₹ 14,84,114. The taxable capital gains would be Nil.

2. Furniture purchased is not eligible for exemption under section 54GA.
3. There is no restriction regarding purchase of second hand machinery.
4. Computers and car would constitute Plant.

Question 32

Mr. Thomas inherited a house in Jaipur under will of his father in May, 2003. The house was purchased by his father in January, 1980 for ₹ 2,50,000. He invested an amount of ₹ 7,00,000 in construction of one more floor in this house in June, 2005. The house was sold by him in November, 2013 for ₹ 37,50,000. The valuation adopted by the registration authorities for charge of stamp duty was ₹ 47,25,000 which was not contested by the buyer, but as per assessee's request, the Assessing Officer made a reference to Valuation officer. The value determined by the Valuation officer was ₹ 47,50,000. Brokerage @ 1% of sale consideration was paid by Mr. Thomas to Mr. Sunil. The fair market value of house as on 01.04.1981 was ₹ 2,70,000.

You are required to compute the amount of capital gain chargeable to tax for A.Y. 2014-15 with the help of given information and by taking CII for the F.Y. 2003-04 : 463, F.Y. 2005-06 as 497 and for F.Y. 2013-14 as 939.

Answer**Computation of Long term Capital Gain for A.Y. 2014-15**

Particulars	₹	₹
Sale consideration as per section 50C (Note-1)		47,25,000
Less: Expenses incurred on transfer being brokerage @ 1% of sale consideration of ₹ 37.50 lacs		<u>37,500</u>
		46,87,500
Less: Indexed cost of acquisition (Note-2) (₹ 2,70,000 × 939/463)	5,47,581	
Indexed cost of improvement (₹ 7,00,000 × 939/497)	<u>13,22,535</u>	<u>18,70,116</u>
Long term capital gain		<u>28,17,384</u>

Notes:

1. As per section 50C, where the consideration received or accruing as a result of transfer of a capital asset, being land or building or both, is less than the valuation by the stamp valuation authority, such value adopted or assessed by the stamp valuation authority shall be deemed to be the full value of consideration. Where a reference is made to the valuation officer, and the value ascertained by the valuation officer exceeds the value adopted by the stamp valuation authority, the value adopted by the stamp valuation authority shall be taken as the full value of consideration.

Sale consideration	₹ 37,50,000
Valuation made by registration authority for stamp duty	₹ 47,25,000
Valuation made by the valuation officer on a reference	₹ 47,50,000

Applying the provisions of section 50C to the present case, ₹ 47,25,000, being, the value adopted by the registration authority for stamp duty, shall be taken as the sale consideration for the purpose of charge of capital gain.

- The house was inherited by Mr. Thomas under the will of his father and therefore, the cost incurred by the previous owner shall be taken as the cost. Fair market value as on 01.04.81, accordingly, shall be adopted as the cost of acquisition of the house property. However, indexation benefit will be given from the year in which Mr. Thomas first held the asset i.e. P.Y.2003-04.

Alternative view: In the case of *CIT v. Manjula J. Shah 16 Taxmann 42 (Bom.)*, the Bombay High Court held that the indexed cost of acquisition in case of gifted asset can be computed with reference to the year in which the previous owner first held the asset.

As per this view, the indexation cost of acquisition of house would be ₹ 25,35,300 and long term capital gain would be ₹ 8,29,665.

Question 33

Ms. Vasudha contends that sale of a work of art held by her is not exigible to capital gains tax. Is she correct?

Answer

As per section 2(14)(ii), the term "personal effects" excludes any work of art. As a result, any work of art will be considered as a capital asset and sale of the same will attract capital gains tax. Thus, the contention of Ms. Vasudha is not correct.

Question 34

Ms. Vasumathi purchased 10,000 equity shares of ABC Co. Pvt. Ltd. on 28.2.2005 for ₹ 1,20,000. The company was wound up on 31.7.2013. The following is the summarized financial position of the company as on 31.7.2013:

Liabilities	₹	Assets	₹
60,000 Equity shares	6,00,000	Agricultural lands	42,00,000
General reserve	40,00,000	Cash at bank	6,50,000
Provision for taxation	<u>2,50,000</u>		<u> </u>
	<u>48,50,000</u>		<u>48,50,000</u>

The tax liability was ascertained at ₹ 3,00,000. The remaining assets were distributed to the shareholders in the proportion of their shareholding. The market value of 6 acres of agricultural land (in an urban area) as on 31.7.2013 is ₹ 10,00,000 per acre.

The agricultural land received above was sold by Ms. Vasumathi on 28.2.2014 for ₹ 15,00,000.

Discuss the tax consequences in the hands of the company and Ms. Vasumathi.

The cost inflation indices are: F.Y.2004-05: 480; F.Y.2013-14 : 939

Answer**In the hands of the company**

As per section 46(1), distribution of capital assets amongst the shareholders on liquidation of the company is not regarded as "transfer" in the hands of the company. Consequently, there will be no capital gains in the hands of the company.

In the hands of Ms. Vasumathi (shareholder)

Section 46(2) provides that such capital gains would be chargeable in the hands of the shareholder.

Particulars	₹
Ms. Vasumathi holds 1/6 th of the shareholding of the company	
Market value of agricultural land received (1 acre @ ₹ 10 Lakhs)	10,00,000
Cash at bank [1/6 th of (₹ 6,50,000 – ₹ 3,00,000)]	<u>58,333</u>
	10,58,333
Less: Deemed dividend under section 2(22)(c) - 1/6 th of (₹ 40,00,000- ₹ 50,000)	<u>6,58,333</u>
Consideration for computing Capital Gain	4,00,000
Less: Indexed cost of acquisition of Shares (₹ 1,20,000 x 939/ 480)	<u>2,34,750</u>
Long term capital gains	<u>1,65,250</u>

Notes:

- Where the capital asset became the property of the assessee on the distribution of the capital assets of a company on its liquidation and the assessee has been assessed to capital gains in respect of that asset under section 46, the cost of acquisition means the fair market value of the asset on the date of distribution. Hence, the short-term capital gains in the hands of Ms. Vasumathi (shareholder) at the time of sale of urban agricultural land should be computed as follows:

Particulars	₹
Sale consideration	15,00,000
Less: Fair market value of the agricultural land on the date of distribution	<u>10,00,000</u>
Short term capital gain	<u>5,00,000</u>

- Dividend under section 2(22)(c) amounting to ₹ 6,58,333 will be exempt under section 10(34).
- The tax liability ascertained at ₹ 3,00,000 has to be reduced from bank balance while computing full value of consideration under section 46(2). ₹ 50,000, being the difference between ₹ 3,00,000 and ₹ 2,50,000, has to be reduced from General Reserve for calculating deemed dividend under section 2(22)(c).

Question 35

State with reasons whether the following statements are true or false having regard to the provisions of the Income-tax Act, 1961:

- (a) *Capital gain of ₹ 75 lakh arising from transfer of long term capital assets on 1.5.2013 will be exempt from tax if such capital gain is invested in the bonds redeemable after three years, issued by NHAI under section 54EC.*
- (b) *As per section 49(2A), read with section 47(xa) of the Income-tax Act, 1961, no capital gains would arise on conversion of foreign currency exchangeable bonds into shares or debentures, for facilitating the issue of FCEBs by companies.*

Answer

- (a) **False** : The exemption under section 54EC has been restricted, by limiting the maximum investment in long term specified assets (i.e. bonds of NHAI or RECL, redeemable after 3 years) to ₹ 50 lakh during any financial year. Therefore, in this case, the exemption under section 54EC can be availed only to the extent of ₹ 50 lakh, provided the investment is made before 1.11.2013 (i.e., within six months from the date of transfer).
- (b) **True** : As per section 47(xa), any transfer by way of conversion of bonds referred to in section 115AC into shares and debentures of any company is not regarded as transfer. Therefore, there will be no capital gains on conversion of foreign currency exchangeable bonds into shares or debentures.

Question 36

Mrs. X, an individual resident woman, wanted to know whether income-tax is attracted on sale of gold and jewellery gifted to her by her parents on the occasion of her marriage in the year 1979 which was purchased at a total cost of ₹ 2,00,000?

Answer

The definition of capital asset under section 2(14) includes jewellery. Therefore, capital gains is attracted on sale of jewellery, since jewellery is excluded from personal effects. The cost to the previous owner or the fair market value as on 1.4.1981, whichever is more beneficial to the assessee, would be treated as the cost of acquisition. Accordingly, in this case, long term capital gain @ 20% will be attracted in the year in which the gold and jewellery is sold by Mrs.X.

Question 37

Mr. Kumar is the owner of a residential house which was purchased in September, 1993 for ₹ 5,00,000. He sold the said house on 5th August, 2013 for ₹ 24,00,000. Valuation as per stamp valuation authority of the said residential house was ₹ 35,00,000. He invested ₹ 5,00,000 in NHAI Bonds on 12th January, 2014. He purchased a residential house on 5th July, 2014 for ₹ 10,00,000. He gives other particulars as follows:

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Interest on Bank Fixed Deposit ₹ 32,000

Investment in public provident fund ₹ 50,000

You are requested to calculate the taxable income for the assessment year 2014-15 and the tax liability, if any.

Cost inflation index for F.Y. 1993-94 and 2013-14 are 244 and 939, respectively.

Answer

Computation of total income and tax liability of Mr. Kumar for the A.Y.2014-15

Particulars	₹	₹
Capital Gains:		
Sale price of the residential house	24,00,000	
Valuation as per Stamp Valuation authority (Value to be taken is the higher of actual sale price or valuation adopted for stamp duty purpose as per section 50C)	35,00,000	
Therefore, Consideration for the purpose of Capital Gains	35,00,000	
Less: Indexed Cost of Acquisition = ₹ 5,00,000 x 939/244	<u>19,24,180</u>	
	15,75,820	
Less: Exemption under section 54 ₹ 10,00,000	₹ 10,00,000	
Exemption under section 54EC ₹ 5,00,000	<u>₹ 5,00,000</u>	
Long-term Capital Gain		75,820
Income from other sources:		
Interest on bank deposits		<u>32,000</u>
Gross Total Income		1,07,820
Less: Deduction under Chapter VI-A		
Section 80C – Investment in PPF (restricted to ₹ 32,000)		<u>32,000</u>
Total Income		<u>75,820</u>
Tax liability		NIL

Notes:

1. The basic exemption limit can be adjusted against long term capital gains, since the entire income comprises of only long term capital gains and is below the basic exemption limit, the tax liability shall be NIL.
2. Deduction under section 80C should be restricted to gross total income excluding long term capital gain.

Question 38

Mr. Abhik's father, who is a senior citizen, had pledged his residential house to a bank under a

notified reverse mortgage scheme. He was getting loan from bank in monthly installments. Mr. Abhik's father did not repay the loan on maturity and gave possession of the house to the bank to discharge his loan. How will the treatment of long-term capital gain be made on such reverse mortgage transaction?

Answer

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

Accordingly, the transaction made by Mr. Abhik's father will not be regarded as a transfer. Therefore, no capital gain will be charged on such transaction.

Further, section 10(43) provides that the amount received by the senior citizen as a loan, either in lump sum or in installment, in a transaction of reverse mortgage would be exempt from income-tax.

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

Question 39

Mr. Pranav, aged 55 years, resident individual had purchased a plot of land at a cost of ₹ 75,000 in June, 1999. He constructed a house for his residence on that land at a cost of ₹ 1,25,000 in August, 2001. He sold that house in May, 2013 at ₹ 15,00,000 and purchased another residential house in June, 2013 for ₹ 8,00,000. He furnishes other income and investment as follows :

Particulars	₹
Interest on fixed deposit with a bank (Net of TDS ₹ 5,000)	45,000
Investment in PPF	20,000

Cost inflation index for financial year 1999-2000, 2001-02 and 2013-14 are 389, 426 and 939 respectively.

You are required to compute taxable income and tax payable by Mr. Pranav for the assessment year 2014-15.

Answer

Computation of taxable income and tax payable by Mr. Pranav for the A.Y. 2014-15

	Particulars	₹	₹
1.	Income from Capital Gains		
	Full value of consideration		15,00,000
	Less : Indexed cost of acquisition of land (₹ 75,000 × 939/389)		<u>1,81,041</u>

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			13,18,959
	Less : Indexed cost of construction of house ($\text{₹ } 1,25,000 \times 939/426$)		<u>2,75,528</u>
			10,43,431
	Less : Deduction under section 54		
	Cost of new residential house		<u>8,00,000</u>
	Long term capital gains		2,43,431
2.	Income from other sources		
	Interest on Bank deposit (Net)	45,000	
	Add : Tax deducted at source	<u>5,000</u>	<u>50,000</u>
	Gross total income		2,93,431
	Less: Deduction under section 80C :		
	Investment in PPF		<u>20,000</u>
	Taxable income		<u>2,73,431</u>
	Components of Total income		
	Special income		
	Long-term Capital gains	2,43,431	
	Normal Income ($\text{₹ } 50,000 - \text{₹ } 20,000$)	<u>30,000</u>	
		<u>2,73,431</u>	
	Tax on normal income of $\text{₹ } 30,000$		Nil
	Tax on LTCG		
	[LTCG (Maximum amount not chargeable to tax - Normal Income) @ 20%] under section 112 = $\{\text{₹ } 2,43,431 - (\text{₹ } 2,00,000 - \text{₹ } 30,000)\} \times 20\%$		14,686
	Less: Rebate under section 87A		<u>2,000</u>
			12,686
	Add : Education cess @ 2%		254
	Secondary and higher education cess @ 1%		<u>127</u>
	Tax payable		13,067
	Less: Tax deducted at source		<u>5,000</u>
			<u>8,067</u>
	Tax payable (rounded off)		8,070

Question 40

Mr. C inherited from his father 8 plots of land in 1980. His father had purchased the plots in 1960 for ₹ 5 lakhs. The fair market value of the plots as on 1-4-1981 was ₹ 8 lakhs. (₹ 1 lakh for each plot)

On 1st June 2001, C started a business of dealer in plots and converted the 8 plots as stock-in-trade of his business. He recorded the plots in his books at ₹ 45 lakhs being the fair market value on that date. In June 2005, C sold the 8 plots for ₹ 50 lakhs.

In the same year, he acquired a residential house property for ₹ 35 lakhs. He invested an amount of ₹ 5 lakhs in construction of one more floor in his house in June 2006. The house was sold by him in June 2013 for ₹ 63,50,000.

The valuation adopted by the registration authorities for charge of stamp duty was ₹ 85,50,000. As per the assessee's request, the Assessing Officer made a reference to a Valuation Officer. The value determined by the Valuation Officer was ₹ 87,20,000. Brokerage of 1 % of sale consideration was paid by C.

The relevant Cost Inflation Indices are :

F.Y.	1981-82	100
F.Y.	2001-02	426
F.Y.	2005-06	497
F.Y.	2006-07	519
F.Y.	2013-14	939

Give the tax computation for the Assessment Year 2014-15.

Answer

Computation of total income and tax liability of Mr. C for A.Y. 2014-15

Particulars	₹	₹
Capital Gains on sale of residential house property		
Value declared by Mr. C ₹ 63,50,000		
Value adopted by Stamp Valuation Authority ₹ 85,50,000		
Valuation as per Valuation Officer ₹ 87,20,000		
Gross Sale consideration (See Note 1)		85,50,000
Less: Brokerage@1% of sale consideration		63,500
Net Sale consideration		84,86,500
Less: Indexed cost of acquisition (₹ 35,00,000 × 939/497)	66,12,676	
Indexed cost of improvement (₹ 5,00,000 × 939/519)	<u>9,04,624</u>	75,17,300
Long-term capital gains (Total Income)		9,69,200
Tax on total income (See Note 2)		
Long-term capital gain taxable@20% (₹ 9,69,200 – ₹ 2,00,000)		1,53,840
Add: Education cess @ 2%		3,077
Secondary and higher education cess @ 1%		<u>1,538</u>
Total tax liability		<u>1,58,455</u>

Notes:

1. As per section 50C, in case the value of sale consideration declared by the assessee is less than the value adopted by the Stamp Valuation Authority for the purpose of charging stamp duty, then, the value adopted by the Stamp Valuation Authority shall be taken to be the full value of consideration. In case the valuation is referred to the Valuation Officer and the value determined is more than the value adopted by the Stamp Valuation Authority, the value determined by the Valuation Officer shall be ignored. Therefore, in the present case, the sale consideration would be the stamp valuation of ₹ 85,50,000, since the same is more than the sale value declared by Mr. C and less than the value determined by the Valuation Officer.
2. As per section 112, the unexhausted basic exemption limit can be exhausted against the long-term capital gains. Since Mr. C does not have any other income in the current year, the whole of the basic exemption limit of ₹ 2,00,000 is exhausted against the long-term capital gains of ₹ 9,69,200 and the balance long-term capital gains shall be taxable@20%. It is assumed that Mr. C is a resident individual below the age of 60 years.

EXERCISES

1. Distribution of assets at the time of liquidation of a company -
 - (a) is not a transfer in the hands of the company or the shareholders
 - (b) is not a transfer in the hands of the company but capital gains is chargeable to tax on such distribution in the hands of the shareholders
 - (c) is not a transfer in the hands of the shareholders but capital gains is chargeable to tax on such distribution in the hands of the company.
2. For an assessee, who is a salaried employee who invests in shares, what is the benefit available in respect of securities transaction tax paid by him on sale of 100 listed shares of X Ltd. which has been held by him for 14 months before sale?
 - (a) Rebate under section 88E is allowable in respect of securities transaction tax paid
 - (b) Securities transaction tax paid is treated as expenses of transfer and deducted from sale consideration.
 - (c) Long term capital gains is completely exempt under section 10(38)
3. Under section 50C, the guideline value for stamp duty is taken as the full value of consideration only if -
 - (a) the asset transferred is building and the actual consideration is less than the guideline value
 - (b) the asset transferred is either land or building or both and the actual consideration is less than the guideline value

- (c) the asset transferred is building, irrespective of the actual consideration.
- 4. When there is a reduction of capital by a company and amounts are distributed to shareholders,
 - (a) the entire distribution is subject to capital gains tax.
 - (b) the entire distribution is subject to tax under the head "Income from other sources".
 - (c) The distribution attributable to accumulated profits is chargeable as deemed dividend and distribution attributable to capital is subject to capital gains tax.
- 5. Where there is a transfer of a capital asset by a partner to the firm by way of capital contribution or otherwise, the consideration would be taken as -
 - (a) The market value of the capital asset on the date of transfer
 - (b) The cost less notional depreciation of the capital asset
 - (c) The value of the asset recorded in the books of the firm.
- 6. Under section 54EC, capital gains are exempted if invested in the bonds issued by NHAI & RECL -
 - (a) within a period of 6 months from the date of transfer of the asset
 - (b) within a period of 6 months from the end of the previous year
 - (c) within a period of 6 months from the end of the previous year or the due date for filing the return of income under section 139(1), whichever is earlier
- 7. If an assessee receives advance money in any earlier occasion of transfer, which is forfeited, since the transfer eventually did not materialize, then such forfeited amount would be -
 - (a) taxable in the year of receipt
 - (b) deducted from the cost of acquisition of the asset or fair market value or written down value, as the case may be
 - (c) exempt from taxation
- 8. Any payment made by a company on purchase of its own listed shares from a shareholder in accordance with the provisions of section 77A of the Companies Act, 1956 -
 - (a) shall be regarded as dividend
 - (b) shall not be regarded as dividend but capital gains tax liability is attracted in the hands of the shareholder
 - (c) shall neither be regarded as dividend nor will it attract capital gains tax in the hands of the shareholder.
- 9. Discuss the conditions to be satisfied for claiming exemption of tax in respect of -
 - (a) Capital gains on compulsory acquisition of agricultural land situated within specified urban limits

- (b) Capital gains on sale of listed equity shares/units of an equity oriented fund.
10. Write short notes on -
- (i) Capital gains in the case of slump sale under section 50B
 - (ii) Reference to Valuation Officer under section 55A
11. What is the tax treatment, under the Income-tax Act, 1961, of capital gains arising on transfer of assets in case of shifting of industrial undertaking from an urban area to any special economic zone? Discuss.
12. List ten transactions which are not regarded as transfer for the purpose of capital gains. Discuss the provisions relating to the same.
13. Explain the computation of capital gain in case of depreciable asset under section 50.
14. What are the transactions not regarded as transfer as per section 47 of the Income-tax Act, 1961?

Answers

1. b; 2. c; 3. b; 4. c; 5. c; 6. a; 7. b; 8. b

UNIT 5 : Income From Other Sources

Key Points

Where any income, profits or gains includible in the total income of an assessee, cannot be included under any of the other heads, it would be chargeable under the head 'Income from other sources'. Hence, this head is the residuary head of income [Section 56(1)]

Specific Incomes Chargeable under this head [Section 56(2)]

- (1) Dividend Income
- (2) Casual income (winnings from lotteries, cross word puzzles, races including horse races, card games and other games, gambling, betting etc.). Such winnings are chargeable to tax at a flat rate of 30% under section 115BB and no expenditure or deduction under Chapter VIA can be allowed from such income. No loss can be set-off against such income and even the unexhausted basic exemption limit cannot be exhausted against such income.
- (3) Sum of money or property received by an Individual or a Hindu undivided family [Section 56(2)(vii)]

	Nature of asset	Particulars	Taxable value
1	Money	Without consideration	The whole amount, if the same exceeds ₹ 50,000.
2	Movable property	Without consideration	The aggregate fair market value of the property, if it exceeds ₹ 50,000.
3	Movable property	Inadequate consideration	The difference between the aggregate fair market value and the consideration, if such difference exceeds ₹ 50,000.
4	Immovable property	Without consideration	The stamp value of the property, if it exceeds ₹ 50,000.
5	Immovable property	Inadequate consideration	The difference between the stamp duty value and the consideration, if such difference exceeds ₹ 50,000.

Receipts exempted from the applicability of section 56(2)(vii)

Any sum of money or value of property received -

- (a) from any relative; or
- (b) on the occasion of the marriage of the individual; or
- (c) under a will or by way of inheritance; or
- (d) in contemplation of death of the payer or donor, as the case may be; or
- (e) from any local authority as defined in the *Explanation* to section 10(20); or
- (f) from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in section 10(23C); or
- (g) from any trust or institution registered under section 12AA

Meaning of "relative" for the purpose of section 56(2)(vii)

- (a) in case of an individual –
 - (i) spouse of the individual;
 - (ii) brother or sister of the individual;
 - (iii) brother or sister of the spouse of the individual;
 - (iv) brother or sister of either of the parents of the individual;
 - (v) any lineal ascendant or descendant of the individual;
 - (vi) any lineal ascendant or descendant of the spouse of the individual;
 - (vii) spouse of any of the persons referred to above.
- (b) In case of Hindu Undivided Family, any member thereof.

(4) Other receipts chargeable under this head

Section	Provision
56(2)(vii)	<ul style="list-style-type: none"> (i) Transfer of shares of a company without consideration or for inadequate consideration would attract the provisions of section 56(2), if the recipient is a firm or a company. (ii) If such shares are received without consideration, the aggregate fair market value on the date of transfer would be taxed as the income of the recipient firm or company, if it exceeds ₹ 50,000. (iii) If such shares are received for inadequate consideration, the difference between the aggregate fair market value and the consideration would be taxed as the income of the recipient firm or company, if such difference exceeds ₹ 50,000. (iv) However, the provisions of section 56(2)(vii) would not apply in the case of transfer of shares -

56(2)(viib)	(1) of a company in which the public are substantially interested; or (2) to a company in which the public are substantially interested. Consideration received in excess of FMV of shares issued by a closely held company to any person, being a resident, to be treated as income of such company, where shares are issued at a premium
56(2)(viii)	Interest received on compensation/enhanced compensation deemed to be income in the year of receipt and taxable under the head "Income from Other Sources".

Deductions allowable [Section 57]

S. No.	Particulars	Deduction
1.	In case of dividends (other than dividends u/s 115-O) or interest on securities	Any reasonable sum paid by way of commission or remuneration to a banker or any other person.
2.	Family Pension	Sum equal to - 33 ¹ / ₃ % of such income or - ₹ 15,000, whichever is less
3.	Interest on compensation/enhanced compensation received	50% of such interest income

Deductions not allowable [Section 58]

S. No.	Deductions not allowable
1.	Any personal expense of the assessee
2.	Any interest chargeable to tax under the Act which is payable outside India on which tax has not been paid or deducted at source.
3.	Any payment taxable in India as salaries, if it is payable outside India unless tax has been paid thereon or deducted at source.
4.	Any payment to a relative or associate concern otherwise than by account payee cheque or draft, if the aggregate of such payments exceed ₹ 20,000 during a day
5.	Income-tax and wealth-tax paid.
6.	Any expenditure or allowance in connection with income by way of earnings from lotteries, cross word puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature

Question 1

State whether the following are chargeable to tax and the amount liable to tax :

- (i) A sum of ₹ 1,20,000 was received as gift from non-relatives by Raj on the occasion of the marriage of his son Pravin.
- (ii) Interest on enhanced compensation of ₹ 50,000 was received as per court decree in December 2013 by Mr. Yogesh. Out of the said amount, a sum of ₹ 35,000, relates to preceding financial years.

Answer

S.No.	Taxable/Not Taxable	Amount liable to tax (₹)	Reason
(i)	Taxable	1,20,000	The exemption from applicability of section 56(2)(vii) would be available if, <i>inter alia</i> , gift is received from a relative or gift is received on the occasion of marriage of the individual himself. In this case, since gift is received by Mr. Raj from a non-relative on the occasion of marriage of his son, it would be taxable in his hands under section 56(2)(vii).
(ii)	Taxable	25,000	As per section 56(2)(viii), interest on enhanced compensation is taxable in the year in which it is received. Deduction of 50% in respect of the said income is allowed under section 57(iv). Therefore, ₹ 25,000 (i.e., ₹ 50,000 – ₹ 25,000) is taxable in the hands of Mr. Yogesh in the F.Y.2013-14.

Question 2

On 10.10.2013, Mr. Govind (a bank employee) received ₹ 5,00,000 towards interest on enhanced compensation from State Government in respect of compulsory acquisition of his land effected during the financial year 2008-09.

Out of this interest, ₹ 1,50,000 relates to the financial year 2010-11; ₹ 1,65,000 to the financial year 2011-12; and ₹ 1,85,000 to the financial year 2012-13. He incurred ₹ 50,000 by way of legal expenses to receive the interest on such enhanced compensation.

How much of interest on enhanced compensation would be chargeable to tax for the assessment year 2014-15?

Answer

Section 145A provides that interest received by the assessee on enhanced compensation shall be deemed to be the income of the assessee of the year in which it is received, irrespective of the method of accounting followed by the assessee and irrespective of the financial year to which it relates.

Section 56(2)(viii) states that such income shall be taxable as 'Income from other sources'.

50% of such income shall be allowed as deduction by virtue of section 57(iv) and no other deduction shall be permissible from such Income.

Therefore, legal expenses incurred to receive the interest on enhanced compensation would not be allowed as deduction from such income.

Computation of interest on enhanced compensation taxable as "Income from other sources" for the A.Y 2014-15:

Particulars	₹
Interest on enhanced compensation taxable under section 56(2)(viii)	5,00,000
Less: Deduction under section 57(iv) (50% x ₹ 5,00,000)	<u>2,50,000</u>
Taxable interest on enhanced compensation	<u>2,50,000</u>

Question 3

The following details have been furnished by Mrs. Hemali pertaining to the year ended 31.3.2014 :

- (i) *Cash gift of ₹ 51,000 received from her friend on the occasion of her "Shastiaptha Poorthi", a wedding function celebrated on her husband completing 60 years of age. This was also her 25th wedding anniversary.*
- (ii) *On the above occasion, a diamond necklace worth ₹ 2 lacs was presented by her sister living in Dubai.*
- (iii) *When she celebrated her daughter's wedding on 21.2.2014, her friend assigned in Mrs. Hemali's favour, a fixed deposit held by the said friend in a scheduled bank; the value of the fixed deposit and the accrued interest on the said date was ₹ 51,000.*

Compute the income, if any, assessable as income from other sources.

Answer

- (i) Any sum of money received by an individual on the occasion of the marriage of the individual is exempt. This provision is, however, not applicable to a cash gift received during a wedding function celebrated on completion of 60 years of age.

The gift of ₹ 51,000 received from a non-relative is, therefore, chargeable to tax under section 56(2)(vii) in the hands of Mrs. Hemali.

- (ii) The provisions of section 56(2)(vii) are not attracted in respect of any sum of money or property received from a relative. Thus, the gift of diamond necklace received from her sister is not taxable under section 56(2)(vii), even though jewellery falls within the definition of "property".
- (iii) To be exempt from applicability of section 56(2)(vii), the property should be received on the occasion of the marriage of the individual, not that of the individual's son or daughter. Therefore, this exemption provision is not attracted in this case.

Any sum of money received without consideration by an individual is chargeable to tax under section 56(2)(vii), if the aggregate value exceeds ₹ 50,000 in a year. "Sum of money" has, however, not been defined under section 56(2)(vii).

Therefore, there are two possible views in respect of the value of fixed deposit assigned in favour of Mrs. Hemali –

- (1) The first view is that fixed deposit does not fall within the meaning of "sum of money" and therefore, the provisions of section 56(2)(vii) are not attracted. It may be noted that fixed deposit is also not included in the definition of "property".
- (2) However, another possible view is that fixed deposit assigned in favour of Mrs. Hemali falls within the meaning of "sum of money" received.

Income assessable as "Income from other sources"

If the first view is taken, the total amount chargeable to tax as "Income from other sources" would be ₹ 51,000, being cash gift received from a friend on her Shastiaptha Poorthi.

As per the second view, the provisions of section 56(2)(vii) would also be attracted in respect of the fixed deposit assigned and the "Income from other sources" of Mrs. Hemali would be ₹ 1,02,000 (₹ 51,000 + ₹ 51,000).

Question 4

Decide the following transactions in the context of Income-tax Act, 1961:

- (i) *Mr. B transferred 500 shares of Reliance Industries Ltd. to M/s. B Co. (P) Ltd. on 10.10.2013 for ₹ 3,00,000 when the market price was ₹ 5,00,000. The indexed cost of acquisition of shares for Mr. B was computed at ₹ 4,45,000. The transfer was not subjected to securities transaction tax.*

Determine the income chargeable to tax in the hands of Mr. B and M/s. B Co. (P) Ltd. because of the above said transaction.

- (ii) *Mr. Chezian is employed in a company with taxable salary income of ₹ 5,00,000. He received a cash gift of ₹ 1,00,000 from Atma Charitable Trust (registered under section 12AA) in December 2013 for meeting his medical expenses.*

Is the cash gift so received from the trust chargeable to tax in the hands of Mr. Chezian?

Answer

- (i) Transfer of shares without consideration or for inadequate consideration would attract the provisions of section 56(2)(vii), if the recipient is a firm or a company. The purpose of this provision is to prevent the practice of transferring unlisted shares at prices much below the fair market value.

The provisions of section 56(2)(vii) would, however, not be attracted in the case of, *inter alia*, transfer of shares of a company in which public are substantially interested. In this case, the shares of Reliance Industries Ltd. are transferred. Since Reliance Industries Ltd. is a company in which public are substantially interested, the provisions of section 56(2)(vii) would not be attracted in the hands of M/s. B Co. (P) Ltd.

The indexed cost of acquisition (₹ 4,45,000) less the actual sale consideration (₹ 3,00,000) would result in a long term capital loss of ₹ 1,45,000 in the hands of Mr. B, which is eligible for set off against any other long term capital gain.

- (ii) The provisions of section 56(2)(vii) would not apply to any sum of money or any property received from any trust or institution registered under section 12AA. Therefore, the cash gift of ₹ 1 lakh received from Atma Charitable Trust, being a trust registered under section 12AA, for meeting medical expenses would not be chargeable to tax under section 56(2)(vii) in the hands of Mr. Chezian.

Question 5

Check the taxability of the following gifts received by Mrs. Rashmi during the previous year 2013-14 and compute the taxable income from gifts for Assessment Year 2014-15:

- (i) On the occasion of her marriage on 14.8.2013, she has received ₹ 90,000 as gift out of which ₹ 70,000 are from relatives and balance from friends.
- (ii) On 12.9.2013, she has received gift of ₹ 18,000 from cousin of her mother.
- (iii) A cell phone worth ₹ 21,000 is gifted by her friend on 15.8.2013.
- (iv) She gets a cash gift of ₹ 25,000 from the elder brother of her husband's grandfather on 25.10.2013.
- (v) She has received a cash gift of ₹ 12,000 from her friend on 14.4.2013.

Answer**Computation of taxable income of Mrs. Rashmi from gifts for A.Y.2014-15**

Sl. No.	Particulars	Taxable amount (₹)	Reason for taxability or otherwise of each gift
1.	Relatives and friends	Nil	Gifts received on the occasion of marriage are not taxable.
2.	Cousin of Mrs. Rashmi's mother	18,000	Cousin of Mrs. Rashmi's mother is not a relative. Hence, the cash gift is taxable.

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3.	Friend	Nil	Cell phone is not included in the definition of property as per <i>Explanation</i> to section 56(2)(vii). Hence, it is not taxable.
4.	Elder brother of husband's grandfather	25,000	Brother of husband's grandfather is not a relative. Hence, the cash gift is taxable.
5.	Friend	<u>12,000</u>	Cash gift from friend is taxable.
Aggregate value of gifts		<u>55,000</u>	

Since the sum of money received by Mrs. Rashmi without consideration during the previous year 2013-14 exceeds ₹ 50,000, the whole of the amount is chargeable to tax under section 56(2)(vii) of the Income-tax Act, 1961.

Question 6

Smt. Laxmi reports the following transactions to you:

- (i) *Received cash gifts on the occasion of her marriage on 18-7-2013 of ₹ 1,20,000. It includes gift of ₹ 20,000 received from non-relatives.*
- (ii) *On 1-8-2013, being her birthday, she received a gift by means of cheque from her mother's maternal uncle, the amount being ₹ 40,000.*
- (iii) *On 1-12-2013 she acquired a vacant site from her friend for ₹ 1,05,000. The State stamp valuation authority fixed the value of site at ₹ 1,80,000 for stamp duty purpose.*
- (iv) *She bought 100 equity shares of a listed company from another friend for ₹ 60,000. The value of share in the stock exchange on the date of purchase was ₹ 1,15,000.*

Determine the amounts chargeable to tax in the hands of Smt. Laxmi for the A.Y. 2014-15.

Your answer should be supported by reasons.

Answer

Computation of amount chargeable to tax in hands of Smt. Laxmi for A.Y. 2014-15

	Particulars	₹
(i)	Cash gift of ₹ 1,20,000 received on the occasion of her marriage is not taxable since gifts received by an individual on the occasion of marriage is excluded under section 56(2)(vii), even if the same are from non-relatives.	Nil
(ii)	Even though mother's maternal uncle does not fall within the definition of "relative" under section 56(2)(vii), gift of ₹ 40,000 received from him by cheque is not chargeable to tax since the aggregate sum of money received by Smt. Laxmi without consideration from non-relatives (other than on the occasion of marriage) during the previous year 2013-14 does not exceed ₹ 50,000.	Nil

(iii)	Purchase of land for inadequate consideration on 1.12.2013 would attract the provisions of section 56(2)(vii). Where any immovable property is received for a consideration which is less than the stamp duty value of the property by an amount exceeding ₹ 50,000, the difference between the stamp duty value and consideration is chargeable to tax in the hands of Individual. Therefore, in the given case ₹ 75,000 is taxable in the hands of Smt. Laxmi.	75,000
(iv)	Since shares are included in the definition of "property" and difference between the purchase value and fair market value of shares is ₹ 55,000 (₹ 1,15,000 - ₹ 60,000) i.e. it exceeds ₹ 50,000, the difference would be taxable under section 56(2)(vii).	55,000
Amount chargeable to tax		1,30,000

Question 7

State with proper reasons whether the following statement is True/False with regard to provisions of Income-tax Act, 1961:

"A" receives ₹ 2 lakh from his friends on the occasion of his marriage on 22.04.2013 and ₹ 1 lakh from the brother of his father-in-law on 31.12.2013. A's income includible under "other sources" for the previous year 2013-14 would be ₹ 3 lakh.

Answer

False : As per section 56(2)(vii), where any sum of money is received without consideration by an individual or a Hindu undivided family from any person or persons and the aggregate value of all such sums received during the previous year exceeds ₹ 50,000, the whole of the aggregate value of such sum shall be included in the total income of such individual or Hindu Undivided Family under the head "Income from other sources".

However, in order to avoid hardship in genuine cases, certain sums of money received have been exempted, which includes, *inter-alia*, any sum received on the occasion of the marriage of the individual and any sum received from any relative. As such, ₹ 2 lakh received from friends on the occasion of marriage is exempt.

However, brother of father-in-law is not included in the definition of relative. Hence, ₹ 1 lakh is taxable under the head "Income from other sources".

The statement that ₹ 3 lakh is includible in A's income is, therefore, false.

Question 8

From the following particulars of Pankaj for the previous year ended 31st March, 2014, compute the income chargeable under the head "Income from other sources":

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Sl. No.	Particulars	₹
(i)	Directors fee from a company	10,000
(ii)	Interest on bank deposits	3,000
(iii)	Income from undisclosed source	12,000
(iv)	Winnings from lotteries (Net)	35,000
(v)	Royalty on a book written by him	9,000
(vi)	Lectures in seminars	5,000
(vii)	Interest on loan given to a relative	7,000
(viii)	Interest on debentures of a company (listed in a recognised stock exchange) net of taxes	3,600
(ix)	Interest on Post Office Savings Bank Account	500
(x)	Interest on Government Securities	2,200
(xi)	Interest on Monthly Income Scheme of Post Office	33,000

He paid ₹ 1,000 for typing the manuscript of book written by him.

Answer

Computation of income of Pankaj chargeable under the head "Income from other sources" for the A.Y. 2014-15

Particulars	₹	₹
1. Directors' fees		10,000
2. Interest on bank deposit		3,000
3. Income from undisclosed source (taxable @ 30% u/s 115BBE)		12,000
4. Royalty on books written (See Note below)	9,000	
Less: expenses	<u>1,000</u>	8,000
5. Lectures in seminars		5,000
6. Interest on loan given to a relative		7,000
7. Interest on listed debentures		
Net Received	3,600	
Add: T.D.S. @ 10%		
$\frac{3600 \times 10}{100 - 10}$	<u>400</u>	4,000
8. Interest on Post Office Savings Bank [exempt under section 10(15)]		-

9. Interest on Government securities		2,200
10. Interest on Post Office Monthly Income Scheme		33,000
11. Winnings from lotteries (taxable @ 30% u/s 115BB)		
Net	35,000	
Add: T.D.S. @ 30% $\left(\frac{35,000 \times 30}{100 - 30}\right)$	<u>15,000</u>	
		<u>50,000</u>
Income from Other Sources		<u>1,34,200</u>

Note : Royalty income would be chargeable to tax under the head "Income from Other Sources", only if it is not chargeable to tax under the head "Profits and gains of business or profession". This problem has been solved assuming that the same is not taxable under the head "Profits and gains of business or profession" and hence, is chargeable to tax under the head "Income from other sources".

Question 9

Rahul holding 28% of equity shares in a company, took a loan of ₹ 5,00,000 from the same company. On the date of granting the loan, the company had accumulated profit of ₹ 4,00,000. The company is engaged in some manufacturing activity.

- (i) Is the amount of loan taxable as deemed dividend in the hands of Rahul, if the company is a company in which the public are substantially interested?
- (ii) What would be your answer, if the lending company is a private limited company (i.e. a company in which the public are not substantially interested)?

Answer

Any payment by a company, other than a company in which the public are substantially interested, of any sum by way of advance or loan to an equity shareholder, being a person who is the beneficial owner of shares holding not less than 10% of the voting power, is deemed as dividend under section 2(22)(e), to the extent the company possesses accumulated profits.

- (i) The provisions of section 2(22)(e), however, will not apply where the loan is given by a company in which public are substantially interested. In such a case, the loan would not be taxable as deemed dividend in the hands of Rahul.
- (ii) However, if the loan is taken from a private company (i.e. a company in which the public are not substantially interested), which is a manufacturing company and not a company where lending of money is a substantial part of the business of the company, then, the provisions of section 2(22)(e) would be attracted, since Rahul holds more than 10% of the equity shares in the company.

The amount chargeable as deemed dividend cannot, however, exceed the accumulated profits held by the company on the date of giving the loan. Therefore, the amount taxable as deemed

dividend in the hands of Rahul would be limited to the accumulated profit i.e., ₹ 4,00,000 and not the amount of loan which is ₹ 5,00,000.

Question 10

When would the dividend income be taxed in the hands of a shareholder?

Answer

The provisions relating to the year of taxability of dividend are contained in section 8 of the Income-tax Act, 1961.

- (a) Any dividend declared by a company or distributed or paid by it within the meaning of section 2(22) shall be deemed to be the income of the previous year in which it is so declared, distributed or paid, as the case may be.
- (b) Any interim dividend shall be deemed to be the income of the previous year in which the amount of such dividend is unconditionally made available by the company to the member who is entitled to it.

Students may note that any dividend which is liable for dividend distribution tax covered by section 115-O (being a dividend declared by a domestic company) is exempt under section 10(34) and hence would not be chargeable to tax. However, dividend referred to in Section 2(22)(e) is not subject to dividend distribution tax in the hands of the domestic company under section 115-O, but would be chargeable to tax in the hands of the shareholder.

Question 11

How is "dividend stripping" enforced by section 94(7) of the Income-tax Act, 1961?

Answer

According to section 94(7), where :

- (a) any person buys or acquires any securities or units within a period of three months prior to the record date ; and
- (b) such person sells or transfers such securities within a period of three months after such record date or transfers such units within a period of nine months after such record date ; and
- (c) the dividend or income on such securities or units received or receivable by such person is exempt from tax,

then, the loss, if any, arising to him on account of such purchase and sale of securities or units, to the extent such loss does not exceed the amount of dividend or income received or receivable on such securities or units, has to be ignored for the purposes of computing his income chargeable to tax.

EXERCISES

1. Income from letting of machinery, plant and furniture is -
 - a) always chargeable to tax under the head "Profits and gains of business and profession"
 - b) always chargeable to tax under the head "Income from other sources"
 - c) chargeable under the head "Income from other sources" only if not chargeable under the head "Profits and gains of business and profession".
2. In respect of winnings from lottery, crossword puzzle or race including horse race or card game etc.
 - a) no deduction under Chapter VI-A is allowed and basic exemption limit cannot be exhausted.
 - b) no deduction under Chapter VI-A but unexhausted basic exemption can be exhausted.
 - c) Both deduction under Chapter VI-A and basic exemption are allowed.
3. The deduction allowable in respect of family pension taxable under "Income from other sources" is
 - a) 33-1/3% of the pension
 - b) 30% of the pension or ₹ 15,000, whichever is less
 - c) 33-1/3% of the pension or ₹ 15,000, whichever is less
4. Deemed dividend under section 2(22)(e) is chargeable to tax -
 - a) On the basis of method of accounting regularly employed by the assessee
 - b) On the basis of mercantile system of accounting only
 - c) On payment basis as prescribed under section 8 of the Income-tax Act, 1961.
5. Ganesh received ₹ 60,000 from his friend on the occasion of his birthday.
 - a) The entire amount of ₹ 60,000 is taxable.
 - b) ₹ 25,000 is taxable.
 - c) The entire amount is exempt.
6. Write short notes on -
 - a) Bond washing transactions
 - b) Dividend stripping
7. State the incomes which are chargeable only under the head "Income from other sources".
8. Which are incomes chargeable under the head "Income from other sources" only if they are not chargeable under the head "Profits and gains of business or profession"?

9. What are the deductions allowable from the following income -
- a) Dividend
 - b) Income from letting on hire machinery, plant or furniture.
10. What are the inadmissible deductions while computing income under the head "Income from other sources".
11. Karan's bank account shows the following deposits during the financial year 2013-14. Compute his total income for the A.Y. 2014-15, assuming that his income from house property (computed) is ₹ 62,000.
- | | |
|--|------------|
| (i) Gift from his sister in Amsterdam | ₹ 2,30,000 |
| (ii) Gift from his friend on his birthday | ₹ 10,000 |
| (iii) Dividend from shares of various Indian companies | ₹ 12,600 |
| (iv) Gift from his mother's friend on his engagement | ₹ 25,000 |
| (v) Gift from his fiancée | ₹ 75,000 |
| (vi) Interest on bank deposits (Fixed Deposit) | ₹ 25,000 |
12. What are the deductions allowable under section 57 of the Income-tax Act, 1961 in respect of "Income from other sources"?

Answers

1. c; 2. a; 3. c; 4. c; 5. a; 11. ₹ 1,97,000

5

Income of Other Persons Included in Assessee's Total Income

Key Points		
Section	Income to be clubbed	Provision
60	Income transferred without transfer of asset	When a person transfers the income accruing to an asset without the transfer of the asset itself, such income is to be included in the total income of the transferor, whether the transfer is revocable or irrevocable.
61	Income arising from revocable transfer of assets	Such income is to be included in the hands of the transferor. A transfer is deemed to be revocable if it – (i) contains any provision for re-transfer of the whole or any part of the income or assets to the transferor; or (ii) gives right to re-assume power over the whole or any part of the income or the asset.
64(1)(ii)	Income arising to spouse by way of remuneration from a concern in which the individual has substantial interest	Such income arising to spouse is to be included in the total income of the individual. However, if remuneration received is attributable to the application of technical or professional knowledge and experience of spouse, then, such income is not to be clubbed.
64(1)(iv)	Income arising to spouse from assets transferred without adequate consideration	Income arising from an asset (other than house property) transferred otherwise than for adequate consideration or in connection with an agreement to live apart, from one spouse to another shall be included in the total income of the transferor.

5.2 Income-tax

		However, this provision will not apply in the case of transfer of house property, since the transferor-spouse would be the deemed owner as per section 27.
64(1)(vi)	Income arising to son's wife from an asset transferred without adequate consideration	Income arising from an asset transferred otherwise than for adequate consideration, by an individual to his or her son's wife shall be included in the total income of the transferor.
64(1)(vii)/ 64(1)(viii)	Income arising from transfer of assets for the benefit of spouse or son's wife	All income arising to any person or association of persons from assets transferred without adequate consideration is includible in the income of the transferor, to the extent such income is used by the transferee for the immediate or deferred benefit of the transferor's spouse or son's wife.
64(1A)	Income of minor child	<p>All income arising or accruing to a minor child (including a minor married daughter) shall be included in the total income of his or her parent.</p> <p>The income of the minor child shall be included with the income of that parent, whose total income, before including minor's income, is higher.</p> <p>The parent, in whose total income, the income of the minor child or children are included, shall be entitled to exemption of such income subject to a maximum of ₹ 1,500 per child.</p> <p>The following income of a minor child shall, however, not be clubbed in the hands of his or her parent -</p> <p>(a) Income from manual work done by him or activity involving application of minor's skill, talent or specialized knowledge and experience; and</p> <p>(b) Income of a minor child suffering from any disability specified in section 80U.</p>
<p><i>Note: As per Explanation 2 to section 64 'income' includes 'loss'. Therefore, clubbing provisions would be attracted in all the above cases, even if there is a loss and not income.</i></p>		

Question 1

Mr. Sharma has four children consisting 2 daughters and 2 sons. The annual income of 2 daughters were ₹ 9,000 and ₹ 4,500 and of sons were ₹ 6,200 and ₹ 4,300, respectively. The daughter who has income of ₹ 4,500 was suffering from a disability specified under section 80U.

Compute the amount of income earned by minor children to be clubbed in hands of Mr. Sharma.

Answer

As per section 64(1A), in computing the total income of an individual, all such income accruing or arising to a minor child shall be included. However, income of a minor child suffering from disability specified under section 80U would not be included in the income of the parent but would be taxable in the hands of the minor child. Therefore, in this case, the income of daughter suffering from disability specified under section 80U should not be clubbed with the income of Mr. Sharma.

Under section 10(32), income of each minor child includible in the hands of the parent under section 64(1A) would be exempt to the extent of the actual income or ₹ 1,500, whichever is lower. The remaining income would be included in the hands of the parent.

Computation of income earned by minor children to be clubbed with the income of Mr. Sharma:

	Particulars	₹
(i)	Income of one daughter	9,000
	Less: Income exempt under section 10(32)	<u>1,500</u>
	Total (A)	<u>7,500</u>
(ii)	Income of two sons (₹ 6,200 + ₹ 4,300)	10,500
	Less: Income exempt under section 10(32) (₹ 1,500 + ₹ 1,500)	<u>3,000</u>
	Total (B)	<u>7,500</u>
	Total Income to be clubbed as per section 64(1A) (A+B)	15,000

Note: It has been assumed that:

- (1) All the four children are minor children;
- (2) The income does not accrue or arise to the minor children on account of any manual work done by them or activity involving application of their skill, talent or specialized knowledge and experience;
- (3) The income of Mr. Sharma, before including the minor children's income, is greater than the income of Mrs. Sharma, due to which the income of the minor children would be included in his hands; and
- (4) This is the first year in which clubbing provisions are attracted.

Question 2

During the previous year 2013-14, the following transactions occurred in respect of Mr. A.

- Mr. A had a fixed deposit of ₹ 5,00,000 in Bank of India. He instructed the bank to credit the interest on the deposit @ 9% from 1-4-2013 to 31-3-2014 to the savings bank account of Mr. B, son of his brother, to help him in his education.
- Mr. A holds 75% share in a partnership firm. Mrs. A received a commission of ₹ 25,000 from the firm for promoting the sales of the firm. Mrs. A possesses no technical or professional qualification.
- Mr. A gifted a flat to Mrs. A on April 1, 2013. During the previous year, the flat generated a net income of ₹ 52,000 to Mrs. A.
- Mr. A gifted ₹ 2,00,000 to his minor son who invested the same in a business and he derived income of ₹ 20,000 from the investment.
- Mr. A's minor son derived an income of ₹ 20,000 through a business activity involving application of his skill and talent.

During the year, Mr. A got a monthly pension of ₹ 10,000. He had no other income. Mrs. A received salary of ₹ 20,000 per month from a part time job.

Discuss the tax implications of each transaction and compute the total income of Mr. A, Mrs. A and their minor child.

Answer

Computation of total income of Mr. A, Mrs. A and their minor son for the A.Y. 2014-15

Particulars	Mr. A (₹)	Mrs. A (₹)	Minor Son (₹)
Salary income (of Mrs. A)	-	2,40,000	-
Pension income (of Mr. A) (₹ 10,000×12)	1,20,000		
Income from House Property [See Note (3) below]	52,000	-	-
Income from other sources			
Interest on Mr. A's fixed deposit with Bank of India (₹ 5,00,000×9%) [See Note (1) below]	45,000	-	-
Commission received by Mrs. A from a partnership firm, in which Mr. A has substantial interest [See Note (2) below]	<u>25,000</u>	-	-
Income before including income of minor son under section 64(1A)	2,42,000	2,40,000	-
Income of the minor son from the investment made in the business out of the amount gifted by Mr. A [See Note (4) below]	18,500	-	-

Income of the minor son through a business activity involving application of his skill and talent <i>[See Note (5) below]</i>		-	-	20,000
Total Income		2,60,500	2,40,000	20,000

Notes:

(1) As per section 60, in case there is a transfer of income without transfer of asset from which such income is derived, such income shall be treated as income of the transferor. Therefore, the fixed deposit interest of ₹ 45,000 transferred by Mr. A to Mr. B shall be included in the total income of Mr. A.

(2) As per section 64(1)(ii), in case the spouse of the individual receives any amount by way of income from any concern in which the individual has substantial interest (i.e. holding shares carrying at least 20% voting power or entitled to at least 20% of the profits of the concern), then, such income shall be included in the total income of the individual. The only exception is in a case where the spouse possesses any technical or professional qualifications and the income earned is solely attributable to the application of her technical or professional knowledge and experience, in which case, the clubbing provisions would not apply.

In this case, the commission income of ₹ 25,000 received by Mrs. A from the partnership firm has to be included in the total income of Mr. A, as Mrs. A does not possess any technical or professional qualification for earning such commission and Mr. A has substantial interest in the partnership firm as he holds 75% share in the firm.

(3) According to section 27(i), an individual who transfers any house property to his or her spouse otherwise than for adequate consideration or in connection with an agreement to live apart, shall be deemed to be the owner of the house property so transferred. Hence, Mr. A shall be deemed to be the owner of the flat gifted to Mrs. A and hence, the income arising from the same shall be computed in the hands of Mr. A.

Note:

(i) *It has been assumed that the net income from the flat i.e., ₹ 52,000 given in the question is the net income computed under the head "Income from house property".*

Note: *Alternatively, the net income from the flat i.e., ₹ 52,000 given in the question may be taken as the net income before providing for deduction @ 30% under section 24(a) and accordingly, the solution can be worked out on this basis.*

(ii) *The provisions of section 56(2)(vii) would not be attracted in the hands of Mrs. A, since she has received immovable property without consideration from a relative i.e., her husband.*

(4) As per section 64(1A), the income of the minor child is to be included in the total income of the parent whose total income (excluding the income of minor child to be so clubbed) is greater. Further, as per section 10(32), income of a minor child which is includible in the income of the parent shall be exempt to the extent of ₹ 1,500 per child.

Therefore, the income of ₹ 20,000 received by minor son from the investment made out

of the sum gifted by Mr. A shall, after providing for exemption of ₹ 1,500 under section 10(32), be included in the income of Mr. A, since Mr. A's income of ₹ 2,42,000 (before including the income of the minor child) is greater than Mrs. A's income of ₹ 2,40,000. Therefore, ₹ 18,500 (i.e., ₹ 20,000 – ₹ 1,500) shall be included in Mr. A's income. It is assumed that this is the first year in which clubbing provisions are attracted.

Note – The provisions of section 56(2)(vii) would not be attracted in the hands of the minor son, since he has received a sum of money exceeding ₹ 50,000 without consideration from a relative i.e., his father.

- (5) In case the income earned by the minor child is on account of any activity involving application of any skill or talent, then, such income of the minor child shall not be included in the income of the parent, but shall be taxable in the hands of the minor child.

Therefore, the income of ₹ 20,000 derived by Mr. A's minor son through a business activity involving application of his skill and talent shall not be clubbed in the hands of the parent. Such income shall be taxable in the hands of the minor son.

Question 3

Mr. Vaibhav started a proprietary business on 01.04.2012 with a capital of ₹ 5,00,000. He incurred a loss of ₹ 2,00,000 during the year 2012-13. To overcome the financial position, his wife Mrs. Vaishaly, a software Engineer, gave a gift of ₹ 5,00,000 on 01.04.2013, which was immediately invested in the business by Mr. Vaibhav. He earned a profit of ₹ 4,00,000 during the year 2013-14. Compute the amount to be clubbed in the hands of Mrs. Vaishaly for the Assessment Year 2014-15. If Mrs. Vaishaly gave the said amount as loan, what would be the amount to be clubbed?

Answer

Section 64(1)(iv) of the Income-tax Act, 1961 provides for the clubbing of income in the hands of the individual, if the income earned is from the assets (other than house property) transferred directly or indirectly to the spouse of the individual, otherwise than for adequate consideration or in connection with an agreement to live apart.

In this case, Mr. Vaibhav received a gift of ₹ 5,00,000 on 1.4.2013 from his wife Mrs. Vaishaly, which he invested in his business immediately. The income to be clubbed in the hands of Mrs. Vaishaly for the A.Y. 2014-15 is computed as under:

Particulars	Mr. Vaibhav's capital contribution (₹)	Capital contribution out of gift from Mrs. Vaishaly (₹)	Total (₹)
Capital as on 1.4.2013	3,00,000 (5,00,000 - 2,00,000)	5,00,000	8,00,000
Profit for P.Y.2013-14 to be	1,50,000	2,50,000	4,00,000

apportioned on the basis of capital employed on the first day of the previous year i.e. as on 1.4.2013 (3:5)	$\left(4,00,000 \times \frac{3}{8}\right)$	$\left(4,00,000 \times \frac{5}{8}\right)$	
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Therefore, the income to be clubbed in the hands of Mrs. Vaishaly for the A.Y.2014-15 is ₹ 2,50,000.

In case Mrs. Vaishaly gave the said amount of ₹ 5,00,000 as a *bona fide* loan, then, clubbing provisions would not be attracted.

Question 4

State True or False, with reasons:

Mr. Y, who is a physically handicapped minor (suffering from a disability of the nature specified in section 80U), earns bank interest of ₹ 50,000 and ₹ 60,000 from marking bags manually by himself. The total income of Mr. Y shall be computed in his hands separately.

Answer

True. The clubbing provisions of section 64(1A) are not applicable in a case where the minor child is suffering from any disability of the nature specified in section 80U. The income of such minor child will not be clubbed in the hands of either of the parents. Consequently, the total income of Mr. Y will be assessed in his hands.

Question 5

On 21-3-2013, Mr. Janak gifted to his wife Mrs. Thilagam 200 listed shares, which had been bought by him on 19-4-2012 at ₹ 2,000 per share. On 1-6-2013, bonus shares were allotted in the ratio of 1:1. All these shares were sold by Mrs. Thilagam as under:

Date of sale	Manner of sale	No. of shares	Net sales value (₹)
21.5.2013	Sold in recognized stock exchange, STT paid	100	2,20,000
21.7.2013	Private sale to an outsider	All bonus shares	1,25,000
28.2.2014	Private sale to her friend Mrs. Hema (Market value on this date was ₹ 2,10,000)	100	1,75,000

Briefly state the income-tax consequences in respect of the sale of the shares by Mrs. Thilagam, showing clearly the person in whose hands the same is chargeable, the quantum and the head of income in respect of the above transactions. Detailed computation of total income is NOT required.

Net sales value represents the amount credited after all taxes, levies, brokerage, etc., and the same may be adopted for computing the capital gains.

Cost inflation index for the FY 2013-14 is 939 and for the FY 2012-13 is 852.

Answer

Where an asset has been transferred by an individual to his spouse otherwise than for adequate consideration, the income arising from the sale of the said asset by the spouse will be clubbed in the hands of the individual.

Where there is any accretion to the asset transferred, income arising to the transferee from such accretion will not be clubbed. Hence, the profit from sale of bonus shares allotted to Mrs. Thilagam will be chargeable to tax in the hands of Mrs. Thilagam.

Therefore, the capital gains arising from the sale of the original shares has to be included in the hands of Mr. Janak, and the capital gains arising from the sale of bonus shares would be taxable in the hands of Mrs. Thilagam.

Where an asset received by way of gift has been sold, the period of holding of the previous owner should be considered for determining whether the capital gain is long term or short term. The cost to the previous owner has to be taken as the cost of acquisition.

**Income/loss to be clubbed in the hands of Mr. Janak
Long-term capital gains/loss**

	Particulars	₹
(i)	100 shares sold on 21.5.2013 in a recognized stock exchange, STT paid. Long-term capital gains on sale of such shares is exempt under section 10(38)	Nil
(ii)	Shares sold to a friend on 28.2.2014	
	Sale consideration	1,75,000
	Less: Indexed cost of acquisition of 100 shares (₹ 2,000 x 100 x 939/852)	<u>2,20,423</u>
	Long term capital loss to be included in the hands of Mr. Janak	<u>45,423</u>

**Income taxable in the hands of Mrs. Thilagam
Short-term capital gains (on sale of 100 bonus shares)**

Particulars	₹
Sale consideration	1,25,000
Less: Cost of acquisition of bonus shares	<u>Nil</u>
Short-term capital gains	<u>1,25,000</u>

Taxability in the hands of Mrs. Hema under the head "Income from other sources"

Mrs. Hema has received shares from her friend, Mrs. Thilagam, for inadequate consideration. Even though shares fall within the definition of "property" under section 56(2)(vii), the provisions of section 56(2)(vii) would not be attracted in the hands of Mrs. Hema, since the

difference between the fair market value of shares and actual sale consideration does not exceed ₹ 50,000.

Question 6

Mrs. Kasturi transferred her immovable property to ABC Co. Ltd. subject to a condition that out of the rental income, a sum of ₹ 36,000 per annum shall be utilized for the benefit of her son's wife.

Mrs. Kasturi claims that the amount of ₹ 36,000 (utilized by her son's wife) should not be included in her total income as she no longer owned the property.

State with reasons whether the contention of Mrs. Kasturi is valid in law.

Answer

The clubbing provisions under section 64(1)(viii) are attracted in case of transfer of any asset, directly or indirectly, otherwise than for adequate consideration, to any person to the extent to which the income from such asset is for the immediate or deferred benefit of son's wife. Such income shall be included in computing the total income of the transferor-individual.

Therefore, income of ₹ 36,000 meant for the benefit of daughter-in-law is chargeable to tax in the hands of transferor i.e., Mrs. Kasturi in this case.

The contention of Mrs. Kasturi is, hence, not valid in law.

Note - In order to attract the clubbing provisions under section 64(1)(viii), the transfer should be otherwise than for adequate consideration. In this case, it is presumed that the transfer is otherwise than for adequate consideration and therefore, the clubbing provisions are attracted.

If it is presumed that the transfer was for adequate consideration, the provisions of section 64(1)(viii) would not be attracted.

Question 7

Discuss the tax implications of income arising from revocable transfer of assets. When will the clubbing provisions not apply at present, even where there is revocable transfer of assets?

Answer

Income arising from revocable transfer of assets [Sections 61 & 63]

- (i) All income arising to any person by virtue of a revocable transfer of assets is to be included in the total income of the transferor.
- (ii) A transfer is deemed to be revocable if:
 - (a) it contains any provision for the re-transfer, directly or indirectly, of the whole or any part of the income or assets to the transferor, or
 - (b) it gives, in any way, the transferor, a right to re-assume power, directly or indirectly, over the whole or any part of the income or the assets.

Transfer not revocable during the life time of the beneficiary or the transferee [Section 62]

If there is a transfer of asset which is not revocable during the life time of the beneficiary or transferee, the income from the transferred asset is not includible in the total income of the transferor provided the transferor derives no direct or indirect benefit from such income.

If the transferor receives direct or indirect benefit from such income, such income is to be included in his total income even though the transfer may not be revocable during the life time of the beneficiary or transferee.

Question 8

Explain the provisions of the Income-tax Act, 1961, with regard to clubbing of income of spouse under section 64.

Answer

As per section 64(1)(ii), any income arising directly or indirectly to the spouse of an individual by way of salary, commission, fees or any other form of remuneration, whether in cash or in kind, from a concern in which such individual has a substantial interest, would be clubbed. However, such rule does not apply where the spouse possesses technical or professional qualification and the income of the spouse is solely attributable to the application of his or her technical or professional knowledge and experience.

Where both husband and wife have substantial interest in a concern and both are in receipt of salary etc. from the said concern, such income will be clubbed with the income of the spouse whose total income, excluding such income, is greater.

An individual shall be deemed to have substantial interest in a concern under the following circumstances:

- (a) If the concern is a company, equity shares carrying not less than 20% of the voting power are, at any time during the previous year, owned beneficially by such person or partly by such person and partly by one or more of his relatives.
- (b) In any other case, if such person is entitled, or such person and one or more of his relatives are entitled in the aggregate, at any time during the previous year, to not less than 20% of the profits of such concern.

As per section 64(1)(iv), where there is a transfer of an asset other than house property, directly or indirectly from one spouse to another, otherwise than for adequate consideration or in connection with an agreement to live apart, any income that arises either directly or indirectly to the transferee from the transfer of the asset shall be included in the total income of the transferor.

However, any income from the accretion of transferred asset is not liable to be clubbed. It may be noted that natural love and affection will not constitute adequate consideration for the purpose of section 64(1).

Question 9

Compute the gross total income of Mr. & Mrs. A from the following information:

	<i>Particulars</i>	₹
(a)	Salary income (computed) of Mrs.A	2,30,000
(b)	Income from profession of Mr.A	3,90,000
(c)	Income of minor son B from company deposit	15,000
(d)	Income of minor daughter C from special talent	32,000
(e)	Interest from bank received by C on deposit made out of her special talent	3,000
(f)	Gift received by C on 30.09.2013 from friend of Mrs. A	2,500

Brief working is sufficient. Detailed computation under various heads of income is NOT required.

Answer

As per the provisions of section 64(1A) of the Income-tax Act, 1961, all the income of a minor child has to be clubbed in the hands of that parent whose total income (excluding the income of the minor) is greater. The income of Mr. A is ₹ 3,90,000 and income of Mrs. A is ₹ 2,30,000. Since the income of Mr. A is greater than that of Mrs. A, the income of the minor children have to be clubbed in the hands of Mr. A. It is assumed that this is the first year when clubbing provisions are attracted.

Income derived by a minor child from any activity involving application of his/her skill, talent, specialised knowledge and experience is not to be clubbed. Hence, the income of minor child C from exercise of special talent will not be clubbed.

However, interest from bank deposit has to be clubbed even when deposit is made out of income arising from application of special talent.

The Gross total income of Mrs. A is ₹ 2,30,000. The total income of Mr. A giving effect to the provisions of section 64(1A) is as follows:

Computation of gross total income of Mr. A for the A.Y. 2014-15

Particulars	₹	₹
Income from profession		3,90,000
Income of minor son B from company deposit	15,000	
Less: Exemption under section 10(32)	<u>1,500</u>	13,500
Income of minor daughter C		
From special talent – not to be clubbed	-	
Interest from bank	3,000	
Gift of ₹ 2,500 received from a non-relative is not taxable under section		

5.12 Income-tax

56(2)(vii) being less than the aggregate limit of ₹ 50,000	Nil	
	3,000	
Less : Exemption under section 10(32)	<u>1,500</u>	<u>1,500</u>
Gross Total Income		<u>4,05,000</u>

Question 10

A proprietary business was started by Smt. Rani in the year 2011. As on 1.4.2012 her capital in business was ₹ 3,00,000.

Her husband gifted ₹ 2,00,000 on 10.4.2012, which amount Smt. Rani invested in her business on the same date. Smt. Rani earned profits from her proprietary business for the Financial year 2012-2013, ₹ 1,50,000 and Financial year 2013-14 ₹ 3,90,000. Compute the income, to be clubbed in the hands of Rani's husband for the Assessment year 2014-15 with reasons.

Answer

Section 64(1) of the Income-tax Act, 1961 provides for the clubbing of income in the hands of the individual, if the income earned is from the assets transferred directly or indirectly to the spouse of the individual, otherwise than for adequate consideration. In this case Smt. Rani received a gift of ₹ 2,00,000 from her husband which she invested in her business. The income to be clubbed in the hands of Smt. Rani's husband for A.Y.2014-15 is computed as under:

Particulars	Smt. Rani's Capital Contribution	Capital Contribution Out of gift from husband	Total
	₹	₹	₹
Capital as at 1.4.2012	3,00,000	--	3,00,000
Investment on 10.04.2012 out of gift received from her husband		2,00,000	2,00,000
	3,00,000	2,00,000	5,00,000
Profit for F.Y. 2012-13 to be apportioned on the basis of capital employed on the first day of the previous year i.e. on 1.4.2012	1,50,000		1,50,000
Capital employed as at 1.4.2013	4,50,000	2,00,000	6,50,000
Profit for F.Y.2013-14 to be apportioned on the basis of capital employed as at 1.4.2013 (i.e. 45 : 20)	2,70,000	1,20,000	3,90,000

Therefore, the income to be clubbed in the hands of Smt. Rani's husband for A.Y.2014-15 is ₹ 1,20,000.

Question 11

Write short notes on "Clubbing of income of minor children in the hands of parent".

Answer

Income earned by a minor child would be clubbed in the hands of the parent. If both parents are having income, then income of minor child would be clubbed in the hands of that parent whose income is higher before clubbing the income of minor child.

Under the following situations the income of the minor child would not be clubbed in the hands of parent :-

- (a) Income earned by minor child through manual work done by him.
- (b) Income from activity involving application of his skill, talent or specialised knowledge and experience.

If the relationship of husband and wife does not subsist between the parents, the income of the minor child would be clubbed in the hands of the parent who maintains the child during the previous year. The parent is entitled to claim an exemption under section 10(32) upto ₹ 1,500 per minor child if the income of the minor child is included in his total income.

Where any such income is once included in the total income of either parent, any such income arising in any succeeding previous year shall not be included in the total income of the other parent, unless the Assessing Officer is satisfied after giving that parent an opportunity of being heard, that it is necessary to do so.

Question 12

Mr. Vatsan has transferred, through a duly registered document, the income arising from a godown to his son, without transferring the godown. In whose hands will the rental income from godown be charged?

Answer

Section 60 expressly states that where there is transfer of income from an asset without transfer of the asset itself, such income shall be included in the total income of the transferor. Hence, the rental income derived from the godown shall be clubbed in the hands of Mr. Vatsan.

Question 13

Mr. Dhaval and his wife Mrs. Hetal furnish the following information:

Sl. No.	Particulars	₹
(i)	Salary income (computed) of Mrs. Hetal	4,60,000
(ii)	Income of minor son 'B' who suffers from disability specified in Section 80U	1,08,000
(iii)	Income of minor daughter 'C' from singing	86,000

5.14 Income-tax

(iv)	Income from profession of Mr. Dhaval	7,50,000
(v)	Cash gift received by 'C' on 2.10.2013 from friend of Mrs. Hetal on winning of singing competition	48,000
(vi)	Income of minor married daughter 'A' from company deposit	30,000

Compute the total income of Mr. Dhaval and Mrs. Hetal for the Assessment Year 2014-15.

Answer

Computation of Total Income of Mr. Dhaval and Mrs. Hetal for the A.Y. 2014-15

Particulars		Mr. Dhaval (₹)	Mrs. Hetal (₹)
Salaries			4,60,000
Profits and gains of business or profession		7,50,000	
Income from other sources:			
Income by way of interest from company deposit earned by minor daughter A [See Note (d)]	30,000		
Less: Exemption under section 10(32)	<u>1,500</u>	28,500	
Total Income		7,78,500	4,60,000

Notes:

- The income of a minor child suffering from any disability of the nature specified in section 80U shall not be included in the hands of the parents. Hence, ₹ 1,08,000, being the income of minor son 'B' who suffers from disability specified under section 80U, shall not be included in the hands of either of his parents.
- The income derived by the minor from manual work or from any activity involving exercise of his skill, talent or specialised knowledge or experience will not be included in the income of his parent. Hence, in the given case, ₹ 86,000 being the income of the minor daughter 'C' shall not be clubbed in the hands of the parents.
- Under section 56(2)(vii), cash gifts received from any person/persons exceeding ₹ 50,000 during the year in aggregate is taxable. Since the cash gift in this case does not exceed ₹ 50,000, the same is not taxable.
- The clubbing provisions are attracted even in respect of income of minor married daughter. The income of the minor will be included in the income of that parent whose total income is greater. Hence, income of minor married daughter 'A' from company deposit shall be clubbed in the hands of the Mr. Dhaval and exemption under section 10(32) of ₹ 1,500 per child shall be allowed in respect of such income.

Question 14

Mr. Dhaval has an income from salary of ₹ 3,50,000 and his minor children's income are as under:

<i>Particulars</i>	<i>₹</i>
<i>Minor daughter has earned the following income:</i>	
<i>From a TV show</i>	<i>50,000</i>
<i>From interest on FD with a bank (deposited by Mr. Dhaval from his income)</i>	<i>5,000</i>
<i>Minor son has earned the following income:</i>	
<i>From the sale of a own painting</i>	<i>10,000</i>
<i>From interest on FD with a bank (deposited by Mr. Dhaval from his income)</i>	<i>1,000</i>

Compute the gross total income of Mr. Dhaval.

Answer

Computation of Gross Total Income of Mr. Dhaval

Particulars	₹	₹
Income from Salary		3,50,000
Income from other sources:		
Minor Daughter's income		
Income from T.V. show (See Note below)		Nil
Interest income from FD with a Bank	5,000	
<i>Less : Exempt under section 10(32)</i>	<u>1,500</u>	3,500
Minor son's income		
Income from sale of self made painting (See Note below)		Nil
Interest income from FD with a Bank	1,000	
<i>Less : Exempt under section 10(32)</i>	<u>1,000</u>	<u>Nil</u>
Gross Total Income		<u>3,53,500</u>

Note: The income derived by the minor from manual work or from any activity involving exercise of his skill, talent or specialised knowledge or experience will not be included in the income of his parent. Hence, in the given case ₹ 50,000 being the income of the minor daughter from TV show and ₹ 10,000 being the income of minor son from sale of own painting, shall not be clubbed in the hands of Mr. Dhaval.

Question 15

Mr. B is the Karta of a HUF, whose members derive income as given below:

	<i>Particulars</i>	<i>₹</i>
(i)	<i>Income from B's profession</i>	<i>45,000</i>
(ii)	<i>Mrs. B's salary as fashion designer</i>	<i>76,000</i>
(iii)	<i>Minor son D (interest on fixed deposits with a bank which were gifted to</i>	<i>10,000</i>

5.16 Income-tax

	<i>him by his uncle)</i>	
(iv)	<i>Minor daughter P's earnings from sports</i>	<i>95,000</i>
(v)	<i>D's winnings from lottery (gross)</i>	<i>1,95,000</i>

Discuss the tax implications in the hands of Mr. and Mrs. B.

Answer

Clubbing of income and other tax implications

As per the provisions of section 64(1A), in case the marriage of the parents subsist, the income of a minor child shall be clubbed in the hands of the parent whose total income, excluding the income of the minor child to be clubbed, is greater. In this problem, it has been assumed that the marriage of Mr. B and Mrs. B subsists.

Further, in case the income arises to the minor child on account of any manual work done by the child or as a result of any activity involving application of skill, talent, specialized knowledge or experience of the child, then, the same shall not be clubbed in the hands of the parent.

Tax implications

- (i) Income of ₹ 45,000 from Mr. B's profession shall be taxable in the hands of Mr. B under the head "Profits and gains of business or profession".
- (ii) Salary of ₹ 76,000 received by Mrs. B as a fashion designer shall be taxable as "Salaries" in the hands of Mrs. B.
- (iii) Income from fixed deposit of ₹ 10,000 arising to the minor son D, shall be clubbed in the hands of the mother, Mrs. B as "Income from other sources", since her income is greater than income of Mr. B before including the income of the minor child.

As per section 10(32), income of a minor child which is includible in the income of the parent shall be exempt to the extent of ₹ 1,500 per child. The balance income would be clubbed in the hands of the parent as "Income from other sources".

- (iv) Income of ₹ 95,000 arising to the minor daughter P from sports shall not be included in the hands of the parent, since such income has arisen to the minor daughter on account of an activity involving application of her skill.
- (v) Income of ₹ 1,95,000 arising to minor son D from lottery shall be included in the hands of Mrs. B as "Income from other sources", since her income is greater than the income of Mr. B before including the income of minor child.

Note – Mrs. B can reduce the tax deducted at source from such lottery income while computing her net tax liability.

EXERCISES

1. Income of a minor child suffering from any disability of the nature specified in section 80U is -
 - a) to be assessed in the hands of the minor child
 - b) to be clubbed with the income of that parent whose total income, before including minor's income, is higher
 - c) completely exempt from tax
2. Income arising to a minor married daughter is -
 - a) to be assessed in the hands of the minor married daughter
 - b) to be clubbed with the income of that parent whose total income, before including minor's income, is higher
 - c) completely exempt from tax
3. Where a member of a HUF has converted or transferred his self-acquired property for inadequate consideration into joint family property, income arising therefrom is taxable -
 - a) as the income of the transferor-member
 - b) in the hands of the HUF
 - c) in the hands of the karta of the HUF
4. If such converted property is subsequently partitioned among the members of the family, the income derived from such converted property as is received by the spouse of the transferor will be taxable -
 - a) as the income of the transferor-member
 - b) as the income of the spouse of the transferor
 - c) as the income of the HUF.
5. Exemption of a certain amount (not exceeding the income clubbed) is available under section 10(32), where a minor's income is clubbed with the income of the parent. The maximum exemption available is -
 - a) upto ₹ 1,200 in respect of each minor child
 - b) upto ₹ 1,500 in respect of each minor child
 - c) upto ₹ 2,000 in respect of each minor child
6. Income arising to a minor married daughter is -
 - a) to be assessed in the hands of the minor married daughter
 - b) to be clubbed with the income of that parent whose total income, before including minor's income, is higher
 - c) to be clubbed with the income of her husband.

5.18 Income-tax

7. Mr. A gifts cash of ₹ 1,00,000 to his brother's wife Mrs. B. Mr. B gifts cash of ₹ 1,00,000 to Mrs. A. From the cash gifted to her, Mrs. B invests in a fixed deposit, income therefrom is ₹ 10,000. Aforesaid ₹ 10,000 will be included in the total income of
- a) Mr. A
 - b) Mr. B
 - c) Mrs. B
8. Write short notes on the following in the context of clubbing of income -
- a) Substantial interest
 - b) Transfer and revocable transfer.
9. Under what circumstances can an income arising to the spouse of an individual be included in the income of the individual? Discuss.
10. State when the income arising to the son's wife can be included in the hands of the individual.
11. When can income arising to a minor child be clubbed in the hands of the father or mother? Discuss.
12. Discuss the tax consequences arising on conversion of self-acquired property into joint family property.

Answers

1. a; 2. b; 3. a; 4. a; 5. b; 6. b; 7. b.

6

Set Off and Carry Forward of Losses

Key Points			
Inter-source and Inter-head Set-off [Sections 70 & 71]			
Section	Provision	Exceptions	
70	<u>Inter-source set-off under the same head of income</u> Any loss in respect of one source shall be set-off against income from any other source under the same head of income.	(i)	Loss from speculative business
		(ii)	Loss from specified business under section 35AD
		(iii)	Long term capital loss and
		(iv)	Loss from the activity of owning and maintaining race horses
71	<u>Inter head adjustment</u> Loss under one head of income can be set-off against income assessable under any other head of income.	(i)	Loss under the head "Profits and gains of business or profession" cannot be set off against income under the head "Salaries"
		(ii)	Loss under the head "Capital gains" cannot be set-off against income under any other head.
		(iii)	Speculation loss and loss from the activity of owning and maintaining race horses cannot be set-off against income under any other head.

6.2 Income-tax

<u>Carry forward and Set-off of brought forward losses</u>			
Section	Nature of loss to be carried forward	Income against which the brought forward loss can be set-off	Maximum permissible period [from the end of the relevant assessment year] for carry forward of losses
71B	Unabsorbed loss from house property	Income from house property	8 assessment years
72	Unabsorbed business loss	Profits and gains from business or profession	8 assessment years
73	Loss from speculation business	Income from speculation business	4 assessment years
73A	Loss from specified business under section 35AD	Profit from any specified business	Indefinite period
74	Long-term capital loss	Long-term capital gains	8 assessment years
	Short-term capital loss	Short-term/Long-term capital gains	8 assessment years
74A	Loss from the activity of owning and maintaining race horses	Income from the activity of owning and maintaining race horses.	4 assessment years
<u>Order of set-off of losses</u>			
1.	Current year depreciation / Current year capital expenditure on scientific research and current year expenditure on family planning, to the extent allowed.		
2.	Brought forward loss from business/profession [Section 72(1)]		
3.	Unabsorbed depreciation [Section 32(2)]		
4.	Unabsorbed capital expenditure on scientific research [Section 35(4)].		
5.	Unabsorbed expenditure on family planning [Section 36(1)(ix)]		

Question 1

Mr. Batra furnishes the following details for year ended 31.03.2014:

Particulars	₹
Short term capital gain	1,40,000
Loss from speculative business	60,000
Long term capital gain on sale of land	30,000
Long term capital loss on sale of shares (securities transaction tax not paid)	1,00,000
Income from business of textile (after allowing current year depreciation)	50,000
Income from activity of owning and maintaining race horses	15,000
Income from salary	1,00,000
Loss from house property	40,000

Following are the brought forward losses:

- (i) Losses from activity of owning and maintaining race horses-pertaining to A.Y. 2011-12 ₹ 25,000.
- (ii) Brought forward loss from business of textile ₹ 60,000 - Loss pertains to A.Y. 2006-07.

Compute gross total income of Mr. Batra for the Assessment Year 2014-15. Also state the eligible carry forward losses for the Assessment Year 2014-15.

Answer

Computation of Gross Total Income of Mr. Batra for the A.Y. 2014-15

Particulars	₹	₹
Salaries	1,00,000	
Less: Current year loss from house property	<u>(40,000)</u>	60,000
Profit and gains of business or profession		
Income from textile business	50,000	
Less: Loss from textile business brought forward from A.Y. 2006-07	<u>60,000</u>	
Balance business loss of A.Y. 2006-07 [See Note-1]	<u>(10,000)</u>	NIL
Income from the activity of owning and maintaining race horses	15,000	
Less: Loss from activity of owning and maintaining race horses brought forward from A.Y. 2011-12	<u>25,000</u>	
Loss to be carried forward to A.Y. 2015-16 [See Note-2]	<u>(10,000)</u>	NIL
Capital Gain		
Short term capital gain		1,40,000
Long term capital gain on sale of land	30,000	

6.4 Income-tax

Less: Long term capital loss on sale of shares	1,00,000	
Loss to be carried forward to A.Y. 2015-16 [See Note-3]	(70,000)	NIL
Gross Total Income		<u>2,00,000</u>

Losses to be carried forward to A.Y. 2015-16

Particulars	₹
Current year loss from speculative business [See Note-4]	60,000
Current year long term capital loss on sale of shares	70,000
Loss from activity of owning and maintaining of race horse pertaining to A.Y.2011-12	10,000

Notes:-

- (1) As per section 72(3), business loss can be carried forward for a maximum of eight assessment years immediately succeeding the assessment year for which the loss was first computed. Since the eight year period for carry forward of business loss of A.Y. 2006-07 expired with the A.Y. 2014-15, the balance unabsorbed business loss of ₹ 10,000 cannot be carried forward to A.Y. 2015-16.
- (2) As per section 74A(3), the loss incurred on maintenance of race horses cannot be set-off against income from any source other than the activity of owning and maintaining race horses. Such loss can be carried forward for a maximum period of 4 assessment years.
- (3) Long term capital gains on sale of shares on which securities transaction tax is not paid is not exempt under section 10(38). Therefore, long-term capital loss on sale of such shares can be set-off against long-term capital gain on sale of land. The balance loss of ₹ 70,000 cannot be set-off against short term capital gain or against any other head of income. The same has to be carried forward for set-off against long-term capital gain of the subsequent assessment year. Such long-term capital loss can be carried forward for a maximum of eight assessment years.
- (4) Loss from speculation business cannot be set-off against any income other than profit and gains of another speculation business. Such loss can, however, be carried forward for a maximum of four years as per section 73(4) to be set-off against income from speculation business.

Question 2

The following are the details relating to Mr. Srivatsan, a resident Indian, aged 57, relating to the year ended 31.3.2014:

Particulars	₹
Income from salaries	2,20,000
Loss from house property	1,90,000
Loss from cloth business	2,40,000
Income from speculation business	30,000

Loss from specified business covered by section 35AD	20,000
Long-term capital gains from sale of urban land	2,50,000
Long-term capital loss from sale of listed shares in recognized stock exchange (STT paid)	1,10,000
Loss from card games	32,000
Income from betting (Gross)	45,000
Life Insurance Premium paid	1,20,000

Compute the total income and show the items eligible for carry forward.

Answer

Computation of total income of Mr. Srivatsan for the A.Y.2014-15

Particulars	₹	₹
Salaries		
Income from salaries	2,20,000	
Less: Loss from house property	<u>1,90,000</u>	30,000
Profits and gains of business or profession		
Income from speculation business	30,000	
Less: Loss from cloth business set off	<u>30,000</u>	Nil
Capital gains		
Long-term capital gains from sale of urban land	2,50,000	
Less: Loss from cloth business set off	<u>2,10,000</u>	40,000
Income from other sources		
Income from betting		<u>45,000</u>
Gross total income		1,15,000
Less: Deduction under section 80C (life insurance premium paid)		<u>30,000</u>
Total income		<u>85,000</u>

Losses to be carried forward:

Particulars	₹
(1) Loss from cloth business (₹ 2,40,000 - ₹ 30,000 - ₹ 2,10,000)	Nil
(2) Loss from specified business covered by section 35AD	20,000

Notes:

- (i) Long-term capital gains from sale of listed shares in a recognized stock exchange is exempt under section 10(38). Loss from an exempt source cannot be set off against profits from a taxable source. Therefore, long-term capital loss on sale of listed shares cannot be set-off against long-term capital gains from sale of urban land.

6.6 Income-tax

- (ii) Loss from specified business covered by section 35AD can be set-off only against profits and gains of any other specified business. Therefore, such loss cannot be set off against any other income. The unabsorbed loss has to be carried forward for set-off against profits and gains of any specified business in the following year.
- (iii) Business loss cannot be set off against salary income. However, the balance business loss of ₹ 2,10,000 (₹ 2,40,000 – ₹ 30,000 set-off against income from speculation business) can be set-off against long-term capital gains of ₹ 2,50,000 from sale of urban land. Consequently, the taxable long-term capital gains would be ₹ 40,000.
- (iv) Loss from card games can neither be set off against any other income, nor can it be carried forward.
- (v) For providing deduction under Chapter VI-A, gross total income has to be reduced by the amount of long-term capital gains and casual income. Therefore, the deduction under section 80C in respect of life insurance premium paid has to be restricted to ₹ 30,000 [i.e., Gross Total Income of ₹ 1,15,000 – ₹ 40,000 (LTCG) – ₹ 45,000 (Casual income)].
- (vi) Income from betting is chargeable at a flat rate of 30% under section 115BB and no expenditure or allowance can be allowed as deduction from such income, nor can any loss be set-off against such income.

Question 3

Mr. Soohan submits the following details of his income for the assessment year 2014-15:

Particulars	₹
Income from salary	3,00,000.00
Loss from let out house property	40,000.00
Income from sugar business	50,000.00
Loss from iron ore business b/f (discontinued in 2007-08)	1,20,000.00
Short term capital loss	60,000.00
Long term capital gain	40,000.00
Dividend	5,000.00
Income received from lottery winning (Gross)	50,000.00
Winnings from card games	6,000.00
Agricultural income	20,000.00
Long term capital gain from shares (STT paid)	10,000.00
Short term capital loss under section 111A	10,000.00
Bank interest	5,000.00

Calculate gross total income and losses to be carried forward.

Answer

Computation of gross total income of Mr. Soohan for the A.Y.2014-15

Particulars	₹	₹
Salaries		
Income from salary	3,00,000	
Less: Loss from house property set-off against salary income as per section 71	<u>(40,000)</u>	2,60,000
Profits and gains of business or profession		
Income from sugar business	50,000	
Less: Brought forward loss from iron-ore business set-off as per section 72(1)	<u>(50,000)</u>	Nil
Balance business loss of ₹ 70,000 of P.Y.2007-08 carried forward to A.Y.2015-16		
Capital gains		
Long term capital gain	40,000	
Less: Short term capital loss set-off	<u>(40,000)</u>	Nil
Balance short-term capital loss of ₹ 20,000 to be carried forward		
Short-term capital loss of ₹ 10,000 under section 111A also to be carried forward		
Income from other sources		
Winnings from lottery	50,000	
Winnings from card games	6,000	
Bank interest	<u>5,000</u>	<u>61,000</u>
Gross Total Income		<u>3,21,000</u>
Losses to be carried forward to A.Y.2015-16		
Loss of iron-ore business	70,000	
Short term capital loss (₹ 20,000 + ₹ 10,000)	30,000	

Notes:

- The following income are exempt under section 10 –
 - Dividend income [Exempt under section 10(34)], assuming that dividend is received from a domestic company.
 - Agricultural income [Exempt under section 10(1)].
 - Long-term capital gains on which STT is paid [Exempt under section 10(38)].
- It is presumed that loss from iron-ore business relates to P.Y.2007-08, the year in which the business was discontinued.

Question 4

Mr. Rajat submits the following information for the financial year ending 31st March, 2014. He desires that you should:

- (a) Compute the total income and
(b) Ascertain the amount of losses that can be carried forward.

	Particulars	₹
(i)	He has two houses :	
(a)	House No. I – Income after all statutory deductions	72,000
(b)	House No. II – Current year loss	(30,000)
(ii)	He has three proprietary businesses :	
(a)	Textile Business :	
(i)	Discontinued from 31 st October, 2013 – Current year loss	40,000
(ii)	Brought forward business loss of A.Y.2010-11	95,000
(b)	Chemical Business :	
(i)	Discontinued from 1 st March, 2012 – hence no profit/loss	Nil
(ii)	Bad debts allowed in earlier years recovered during this year	35,000
(iii)	Brought forward business loss of A.Y. 2012-13	50,000
(c)	Leather Business : Profit for the current year	1,00,000
(d)	Share of profit in a firm in which he is partner since 2003	16,550
(iii)	(a) Short-term capital gain	60,000
(b)	Long-term capital loss	35,000
(iv)	Contribution to LIC towards premium	10,000

Answer

Computation of total income of Mr. Rajat for the A.Y. 2014-15

Particulars	₹	₹
1. Income from house property		
House No.1	72,000	
House No.2	(-) <u>30,000</u>	42,000
2. Profits and gains of business or profession		
Profit from leather business	1,00,000	
Bad debts recovered taxable under section 41(4)	<u>35,000</u>	
	1,35,000	
Less: Current year loss of textile business	(-) <u>40,000</u>	
	95,000	

Less: Brought forward business loss of textile business for A.Y.2010-11 set off against the business income of current year	<u>95,000</u>	Nil
3. Capital Gains		
Short-term capital gain		<u>60,000</u>
Gross Total Income		1,02,000
Less: Deduction under Chapter VI-A		
Under section 80C – LIC premium paid		<u>10,000</u>
Total Income		<u>92,000</u>

Statement of losses to be carried forward to A.Y. 2015-16

Particulars	₹
Business loss of A.Y. 2012-13 to be carried forward under section 72	50,000
Long term capital loss of A.Y. 2014-15 to be carried forward under section 74	35,000

Notes:

- (1) Share of profit from firm of ₹ 16,550 is exempt under section 10(2A).
- (2) Long-term capital loss cannot be set-off against short-term capital gains. Therefore, it has to be carried forward to the next year to be set-off against long-term capital gains of that year.

Question 5

Explain the provisions of carry forward and set off of business losses under section 72 of the Income-tax Act, 1961.

Answer

- (i) Section 72 applies where the net result of the computation under the head "Profits and gains of business and profession" for any assessment year is a loss to the assessee and such loss cannot be wholly set off against income under any head of income in accordance with the provisions of section 71. Such unabsorbed business loss can be carried forward to the subsequent assessment year for set off against the business income of that year and so on.
- (ii) However, such loss should not be in the nature of speculation business loss
- (iii) Business loss carried forward can be set off only against the income under the head "Profits and gains of business or profession", though not necessarily against the income from same business in which the loss was incurred.
- (iv) Business loss can be carried forward and set off even if the business in respect of which it was incurred and computed has been discontinued.
- (v) Business loss cannot be carried forward for more than 8 assessment years immediately succeeding the assessment year for which the loss was first computed.

- (vi) Under section 72(2), business loss brought forward should be adjusted first and thereafter unabsorbed depreciation, unabsorbed scientific research expenditure etc. should be adjusted.

Question 6

Write short notes on:

- (a) *Loss can be carried forward only by the person who has incurred the loss.*
(b) *Carry forward and set off of losses by closely held companies.*

Answer

- (a) As per section 78(2), where any person carrying on business or profession has been succeeded in such capacity by another person otherwise than by inheritance, then the successor cannot have the loss of the predecessor being carried forward and set off against his income. However, there are certain exceptions, which are briefed hereunder:
- (i) Carry forward and set off of accumulated business loss of the amalgamating company against the income of the amalgamated company, if the amalgamation is within the meaning of section 72A.
 - (ii) Carry forward and set off of accumulated business loss of the demerged company in the hands of the resulting company, in a scheme of demerger, subject to fulfillment of certain conditions which the Central Government may for this purpose notify, to ensure that the demerger is for genuine business purposes;
 - (iii) In the case of reorganization of business, where a firm is succeeded by a company as per the provisions of section 47(xiii), or a sole proprietary concern is succeeded by a company as per the provisions of section 47(xiv), the accumulated loss of the firm or sole proprietor shall be deemed to be the loss of the successor company for the previous year in which the business reorganization was effected and the carry forward provisions shall be applicable to the successor company;
 - (iv) Where a business carried on by one person is acquired by another person through inheritance, then the successor can carry-forward and set-off the loss of the predecessor against his income.
 - (v) Carry forward and set off of business loss and unabsorbed depreciation of a predecessor company against the income of successor Limited Liability partnership if the conditions specified in section 47(xiiib) are fulfilled.
- (b) According to section 79, in the case of a company in which public are not substantially interested, the unabsorbed business loss relating to any assessment year can be carried forward and set-off against the income in a subsequent assessment year subject to the fulfillment of the following condition:-

As on the last day of the previous year in which the loss is sought to be carried forward and set off, the shares of the company carrying not less than 51% of the voting power

continue to be held by the persons who held 51% of the total voting power on the last day of the previous year in which the loss was incurred. For example, if 60% of shareholders of the company as on 31st March, 2010 continue to hold shares without interruption up to end of the previous year 2013-14 i.e. as on 31.03.2014, then, the loss of A.Y. 2010-11 (previous year 2009-10) is eligible for set off against the income of the A.Y.2014-15.

This restriction is not applicable if the change in the said voting power takes place due to the death of a shareholder or transfer of shares by way of gift by a shareholder to his relative. Further, the restriction placed under section 79 is not applicable where there is a change in the shareholding of an Indian company which is a subsidiary of a foreign company as a result of amalgamation or demerger of a foreign company, provided 51% of the shareholders of the amalgamating or demerged foreign company continue to be shareholders of the amalgamated or the resulting foreign company.

Question 7

Mr. A furnishes you the following information for the year ended 31.03.2014:

	(₹)
(i) Income from plying of vehicles (computed as per books) (He owned 5 heavy goods vehicle throughout the year)	2,10,400
(ii) Income from retail trade of garments (Computed as per books) (Sales turnover ₹ 21,70,000)	75,000
(iii) He has brought forward depreciation relating to A.Y. 2013-14	1,00,000
(iv) He deposited ₹ 70,000 into his PPF account on 6.1.2014 and ₹ 30,000 in 5 year bank fixed deposit	

Compute taxable income of Mr. A and his tax liability for the assessment year 2014-15 with reasons for your computation.

Answer

Computation of total income of Mr. A for the A.Y. 2014-15

Particulars	₹
Income from retail trade – as per books (See Note 1 below)	75,000
Income from plying of vehicles – as per books (See Note 2 below)	<u>2,10,400</u>
	2,85,400
Less : Set off of brought forward depreciation relating to A.Y. 2013-14	<u>1,00,000</u>
Gross total income	1,85,400
Less: Deduction under section 80C – Contribution to PPF and bank FD	<u>1,00,000</u>
Taxable income	<u>85,400</u>
Tax liability	Nil

Note :

1. **Income from retail trade:** Presumptive business income under section 44AD is ₹ 1,73,600 i.e. 8% of turnover of ₹ 21,70,000. However, the income computed as per books is ₹ 75,000 which is to be further reduced by the amount of unabsorbed depreciation. Since the income computed as per books is lower than the income deemed under section 44AD, the assessee can adopt the income as per books.

The requirement to maintain books of accounts under section 44AA and to get them audited under section 44AB in case the assessee claims the profit and gains of business to be lower than the presumptive income determined under section 44AD, would arise only if the total income exceeds the basic exemption limit. In this case, since the total income does not exceed the basic exemption limit, this mandatory requirement does not arise.

The total unabsorbed depreciation is ₹ 1,00,000. Out of this, ₹ 75,000 can be set-off against income from retail trade. The balance of ₹ 25,000 remains to be set-off from income from plying of vehicles.

2. **Income from plying of vehicles:** Income calculated under section 44AE(1) would be ₹ 5,000 x 12 x 5 which is equal to ₹ 3,00,000. However, the income from plying of vehicles as per books is ₹ 2,10,400 less ₹ 25,000, being the balance unabsorbed depreciation remaining to be set-off under section 32(2). Therefore, the income from plying of vehicles as per books is ₹ 1,85,400, which is lower than the presumptive income of ₹ 3,00,000 calculated as per section 44AE(1). Hence, the assessee can adopt the income as per books i.e. ₹ 1,85,400, provided he maintains books of account as per section 44AA and gets his accounts audited and furnishes an audit report as required under section 44AB.

It is to be further noted that in both the above cases, had presumptive income provisions been opted, all deductions under sections 30 to 38, including depreciation would have been deemed to have been given full effect to and no further deduction under those sections would be allowable.

If the assessee opted for income to be assessed on presumptive basis, his total income would be as under:

Particulars	₹
Income from retail trade under section 44AD [₹ 21,70,000 @ 8%]	1,73,600
Income from plying of vehicles under section 44AE [₹ 5,000 x 12 x 5]	<u>3,00,000</u>
	4,73,600
<i>Less:</i> Set off of brought forward depreciation – not possible and it is deemed that it has been allowed and set off	<u>Nil</u>
Gross total income	4,73,600
<i>Less:</i> Deduction under section 80C - Contribution to PPF and bank FD	<u>1,00,000</u>
Taxable income	<u>3,73,600</u>

Tax thereon	17,360
Less: Rebate under section 87A	<u>2,000</u>
	15,360
Add : Education cess @ 2% and Secondary and higher education cess @ 1%	461
Total tax liability	<u>15,821</u>

Note: If the assessee has not maintained books of account as required under section 44AA for the business of plying of vehicles, then, he has to offer income only on presumptive basis given above.

Question 8

Compute the tax liability of Mr. Madhavan for the Assessment Year 2014-15 from the following particulars:

Sl. No.	Particulars	₹
(i)	Net house property income as computed under the head "Income from house property"	2,70,000
(ii)	Income from business before adjusting the following:	90,000
	(a) Brought forward business loss	70,000
	(b) Current year depreciation	30,000
	(c) Brought forward unabsorbed depreciation	1,40,000
(iii)	Short term capital gain – jewellery	1,60,000
(iv)	Long term capital loss –listed equity shares (STT paid)	40,000
(v)	Long term capital gains – Debentures	2,00,000
(vi)	Dividend on shares held as stock in trade	10,000
(vii)	Dividend from a company carrying on agricultural operation	12,000
(viii)	Income from growing and manufacturing coffee (cured and roasted)	1,00,000

During the previous year 2013-14, the assessee has purchased NSC VIII issue for ₹ 1,00,000.

Answer

Computation of taxable income of Mr. Madhavan for the A.Y 2014-15

	Particulars	₹	₹
I.	Net income from house property		2,70,000
II.	Income from business		
	Income from business	90,000	
	Income from coffee (cured and roasted) @ 40%	<u>40,000</u>	
		1,30,000	
	Less :Current year depreciation [Section 32(1)]	<u>30,000</u>	
		1,00,000	
	Less: Brought forward business loss	<u>70,000</u>	30,000

6.14 Income-tax

III.	Capital gains		
	Long term capital gain – debentures	2,00,000	
	Short term capital gain – Jewellery	<u>1,60,000</u>	3,60,000
IV.	Income from other sources		
	Dividend on shares (including shares in company carrying on agricultural operations)– exempt under section 10(34)		<u>Nil</u>
			6,60,000
	<i>Less:</i> Brought forward unabsorbed depreciation (set-off against long-term capital gains)		<u>1,40,000</u>
	Gross total income		5,20,000
	<i>Less:</i> Chapter VIA deduction		
	Section 80C : NSC VIII issue purchase		<u>1,00,000</u>
	Total income		<u>4,20,000</u>

Computation of tax liability after applying the aggregation of agricultural income with non-agricultural income

Particulars	₹	₹
Agricultural income + non agricultural income = Total income = ₹ 60,000 + ₹ 4,20,000		4,80,000
Tax on LTCG of ₹ 60,000 @ 20%	12,000	
Tax on the remainder at slab rate	<u>22,000</u>	34,000
<i>Less:</i> Tax on ₹ 2,60,000 being basic exemption limit ₹ 2,00,000 plus ₹ 60,000 agricultural income		<u>6,000</u>
Tax liability		28,000
<i>Less:</i> Rebate under section 87A		<u>2,000</u>
		26,000
<i>Add:</i> Education cess and Secondary and higher education cess @ 3%		<u>780</u>
Total tax liability		<u>26,780</u>

Notes: (1) Loss from an exempt source cannot be set-off against gains from a taxable source. Therefore, long-term capital loss on sale of listed equity shares cannot be set-off against long-term capital gains on sale of debentures.

(2) Brought forward unabsorbed depreciation can be adjusted against any head of income. However, it is most beneficial to set-off unabsorbed depreciation against long-term capital gains, since it is taxable at a higher rate of 20% (the other income of the assessee falling in the 10% slab rate).

Question 9

Simran, engaged in various types of activities, gives the following particulars of her income for the year ended 31.3.2014:

	Particulars	₹
(a)	Profit of business of consumer and house-hold products	50,000
(b)	Loss of business of readymade garments	10,000
(c)	Brought forward loss of catering business which was closed in Asst. Year 2013-14	15,000
(d)	Short-term loss on sale of securities and shares	15,000
(e)	Profit of speculative transactions entered into during the year	12,500
(f)	Loss of speculative transactions of Asst. Year 2009-10 not set off till Asst. Year 2013-14	15,000

Compute the total income of Simran for the A.Y. 2014-15.

Answer

Computation of total income of Simran for the A.Y. 2014-15

Particulars	₹	₹
Profit of business of consumer and house-hold products	50,000	
Less: Loss of business of readymade garments for the year adjusted under section 70(1)	<u>10,000</u>	
	40,000	
Less: Brought forward loss of catering business closed in A.Y. 2013-14 set off against business income for the current year as per section 72(1)	<u>15,000</u>	25,000
Profit of speculative transaction		<u>12,500</u>
Total Income		<u>37,500</u>

Notes :

- Loss of speculative transaction of A.Y. 2009-10 is not allowed to be set off against the profit of speculative transaction of the A.Y.2014-15, since, as per the provisions of section 73(4), such loss can be carried forward for set-off for a maximum period of 4 years only i.e. up to A.Y.2013-14.
- Short term capital loss of ₹ 15,000 on sale of securities and shares has to be carried forward as per section 74 since there is no income under the head Capital Gains for the A.Y.2014-15. The loss is to be carried forward for set off in future years against income chargeable under the head Capital Gains. Such loss can be carried forward for a maximum period of 8 assessment years.

Question 10

M/s. Vivitha & Co., a partnership firm, with four partners A, B, C and D having equal shares, furnishes the following details, summarized from the valid returns of income filed by it:

Assessment year	Item eligible for carry forward and set off
2012-13	Unabsorbed business loss ₹ 1,20,000
2013-14	Unabsorbed business loss ₹ 1,90,000
2013-14	Unabsorbed depreciation ₹ 1,20,000
2013-14	Unabsorbed long-term capital losses: -from shares ₹ 1,10,000; -from building ₹ 1,90,000

C who was a partner during the last three years, retired from the firm with effect from 1.4.2013.

The summarized results of the firm for the assessment year 2014-15 are as under:

Particulars	₹
Income from house property	70,000
Income from business:	
Speculation	2,20,000
Non-speculation	(-) 50,000
Capital gains	
Short-term (from sale of shares)	40,000
Long-term (from sale of building)	2,10,000
Income from other sources	60,000

Briefly discuss how the items brought forward from earlier years can be set off in the hands of the firm for the assessment year 2014-15, in the manner most beneficial to the assessee. Also show the items to be carried forward.

Answer

According to section 78(1), where there is a change in the constitution of the firm, the loss relating to outgoing partner (whether by way of retirement or death) has to be excluded for the purposes of carry forward. However, this provision does not apply in the case of unabsorbed depreciation.

Accordingly, M/s. Vivitha & Co. is entitled to carry forward the losses to the extent given below:

Item	Loss (₹)	Relatable to C (₹)	Balance eligible for carry forward (₹)
Business loss of A.Y.2012-13	1,20,000	30,000	90,000
Business loss of A.Y.2013-14	1,90,000	47,500	1,42,500
Long term capital loss of A.Y.2013-14	3,00,000	75,000	2,25,000

Set off of items in the hands of M/s. Vivitha & Co. for the A.Y. 2014-15

	Particulars	₹	₹
1.	Income from house property		
	Current year income	70,000	
	Less: Brought forward unabsorbed depreciation (See Note 1)	<u>70,000</u>	NIL
2.	Profits and gains of business or profession		
	Current year speculative business profits	2,20,000	
	Less: Current year Non-speculation loss set off (See Note 2)	<u>50,000</u>	
		1,70,000	
	Less: Brought forward business losses of earlier year (2012-13 ₹ 90,000 and 2013-14 ₹ 80,000) (See Note 3)	<u>1,70,000</u>	NIL
3.	Capital gain		
	Short term (from sale of shares)		40,000
	Long-term (from sale of building)	2,10,000	
	Less: Brought forward long term capital loss of A.Y.2013-14 (See Note 4)	<u>2,10,000</u>	NIL
4.	Income from other sources		
	Current year income (before set off)	60,000	
	Less: Brought forward depreciation (See Note 1)	<u>50,000</u>	<u>10,000</u>
	Total Income		<u>50,000</u>
	Losses to be carried forward to A.Y. 2015-16		
	Business loss (₹ 1,42,500 - ₹ 80,000)		62,500
	Long term capital loss (₹ 2,25,000 – ₹ 2,10,000)		15,000
	Both these losses relate to A.Y. 2013-14		

Notes:

- (1) Unabsorbed depreciation can be set off against income from any head. Hence, it will be advantageous to set off unabsorbed depreciation against income from house property and income from other sources.
- (2) In the current year, non-speculation business loss can be set off against speculation business income.
- (3) Brought forward non-speculation business loss can also be set off against speculation business income of current year.
- (4) According to section 74, brought forward long-term capital losses shall be set off only against long-term capital gains of current year.
- (5) The set-off and carry forward of losses should be most beneficial to the assessee. If the students set off brought forward depreciation against current year's business income first, then the quantum of brought forward business loss which can set off against current year's business income will be lower. This will not be beneficial to the assessee.

Question 11

Mr. P, a resident individual, furnishes the following particulars of his income and other details for the previous year 2013-14:

Sl. No.	Particulars	₹
(i)	Income from salary	18,000
(ii)	Net annual value of house property	70,000
(iii)	Income from business	80,000
(iv)	Income from speculative business	12,000
(v)	Long term capital gain on sale of land	15,800
(vi)	Loss on maintenance of race horse	9,000
(vii)	Loss on gambling	8,000

Depreciation allowable under the Income-tax Act, 1961, comes to ₹ 8,000, for which no treatment is given above.

The other details of unabsorbed depreciation and brought forward losses (pertaining to A.Y. 2013-14) are:

Sl. No.	Particulars	₹
(i)	Unabsorbed depreciation	9,000
(ii)	Loss from speculative business	16,000
(iii)	Short term capital loss	7,800

Compute the gross total income of Mr. P for the Assessment year 2014-15, and the amount of loss that can or cannot be carried forward.

Answer

Computation of Gross Total Income of Mr. P for the A.Y. 2014-15

Particulars		₹	₹
(i)	Income from salary		18,000
(ii)	Income from House Property		
	Net Annual Value	70,000	
	Less : Deduction under section 24 (30% of ₹ 70,000)	<u>21,000</u>	49,000
(iii)	Income from business and profession		
(a)	Income from business	80,000	
	Less : Current year depreciation	<u>8,000</u>	
		72,000	
	Less : Unabsorbed depreciation	<u>9,000</u>	63,000

(b) Income from speculative business	12,000	
Less: Brought forward loss from speculative business (Balance loss of ₹ 4,000 (i.e. ₹ 16,000 – ₹ 12,000) can be carried forward to the next year)	<u>12,000</u>	Nil
(iv) Income from capital gain		
Long term capital gain on sale of land	15,800	
Less: Brought forward short term capital loss	<u>7,800</u>	<u>8,000</u>
Gross total income		<u>1,38,000</u>

Amount of loss to be carried forward to the next year

Particulars	₹
Loss from speculative business (to be carried forward as per section 73)	4,000
Loss on maintenance of race horses (to be carried forward as per section 74A)	9,000

Notes :

- (i) Loss on gambling can neither be set-off nor be carried forward.
- (ii) As per section 74A(3), the loss incurred on maintenance of race horses cannot be set-off against income from any other source other than the activity of owning and maintaining race horses. Such loss can be carried forward for a maximum period of 4 assessment years.
- (iii) Speculative business loss can set off only against income from speculative business of the current year and the balance loss can be carried forward to A.Y. 2015-16. It may be noted that speculative business loss can be carried forward for a maximum of four years as per section 73(4).

Question 12

Ms. Geeta, a resident individual, provides the following details of her income / losses for the year ended 31.3.2014:

- (i) Salary received as a partner from a partnership firm ₹ 7,50,000. The same was allowed to the firm.
- (ii) Loss on sale of shares listed in BSE ₹ 3,00,000. Shares were held for 15 months and STT paid on sale.
- (iii) Long-term capital gain on sale of land ₹ 5,00,000.
- (iv) ₹ 51,000 received in cash from friends in party.
- (v) ₹ 55,000, received towards dividend on listed equity shares of domestic companies.
- (vi) Brought forward business loss of assessment year 2013-14 ₹ 12,50,000.

The return for assessment year 2013-14 was filed in time.

6.20 Income-tax

Compute gross total income of Ms. Geeta for the Assessment Year 2014 -15 and ascertain the amount of loss that can be carried forward.

Answer

Computation of Gross Total Income of Ms. Geeta for the Assessment Year 2014-15

Particulars	₹
Profits and gains of business and profession	
Salary received as a partner from a partnership firm is taxable under the head "Profits and gains of business and profession"	7,50,000
Less: Brought forward business loss of Assessment Year 2013-14 to be set-off against business income	<u>7,50,000</u>
	Nil
Capital Gains	
Long term capital gain on sale of land (See Note 2)	5,00,000
Income from other sources	
Cash gift received from friends - since the value of cash gift exceeds ₹ 50,000, the entire sum is taxable	51,000
Dividend received from a domestic company is exempt under section 10(34)	<u>Nil</u>
Gross Total Income	<u>5,51,000</u>

Notes :

- Balance brought forward business loss of assessment year 2013-14 of ₹ 5,00,000 has to be carried forward to the next year.
- Long-term capital loss on sale of shares cannot be set-off against long-term capital gain on sale of land since loss from an exempt source cannot be set-off against profit from a taxable source. Since long-term capital gain on sale of listed shares on which STT is paid is exempt under section 10(38), loss on sale of listed shares is a loss from an exempt source. So, it cannot be set-off against long-term capital gain on sale of land, which is a profit from a taxable source.

EXERCISES

- In a case where the business is succeeded by inheritance, and the legal heirs constitute themselves as a partnership firm, then -
 - the partnership firm can carry forward and set-off the loss of the predecessor.
 - the partnership firm cannot carry forward and set-off the loss of the predecessor.
 - the loss of the predecessor can be carried forward and set-off only by the individual partners in proportion to the share of profits of the firm.

2. According to section 80, no loss which has not been determined in pursuance of a return filed in accordance with the provisions of section 139(3), shall be carried forward. The exceptions to this are -
 - a) Only loss under the head "Capital Gains" under section 74.
 - b) Loss under the head "Capital Gains" and unabsorbed depreciation carried forward under section 32(2)
 - c) Loss from house property and unabsorbed depreciation carried forward under section 32(2).
3. Section 70 enables set off of losses under one source of income against income from any other source under the same head. The exceptions to this section are -
 - a) Loss under the head "Capital Gains", Loss from speculative business and loss from the activity of owning and maintaining race horses
 - b) Long-term capital loss, Loss from speculative business and loss from the activity of owning and maintaining race horses
 - c) Short-term capital loss and loss from speculative business
4. The maximum period for which speculation loss can be carried forward is -
 - a) 4 years
 - b) 8 years
 - c) indefinitely
5. Mr. A incurred short-term capital loss of ₹ 10,000 on sale of shares through the National Stock Exchange. Such loss can be set-off -
 - a) only against short-term capital gains
 - b) against both short-term capital gains and long-term capital gains
 - c) against any head of income.
6. Write short notes on -
 - a) Inter-head adjustment
 - b) Inter-source adjustment.
7. Discuss the correctness of the following statements -
 - (i) Long term capital loss can be set-off against short-term capital gains arising in that year.
 - (ii) Business loss can be set-off against salary income arising in that year.
8. Discuss briefly on -
 - a) Carry forward and set-off of losses by closely held companies
 - b) Set-off and carry forward of speculation business loss.

Answers

1. a; 2. c; 3. b; 4. a; 5. b.

Deductions from Gross Total Income

Key Points			
Deductions in respect of payments			
Section	Eligible Assessee	Eligible Payments	Permissible Deduction
80C	Individual or HUF	Contribution to PPF, Payment of LIC premium, etc. Sums paid or deposited in the previous year <ul style="list-style-type: none"> - Life insurance premium paid - Contribution to PPF, SPF, RPF and superannuation fund - Repayment of housing loan - Payment of tuition fees of children etc. 	
80CCC	Individual	Contribution to certain pension funds Any amount paid or deposited to keep in force a contract for any annuity plan of LIC of India or any other insurer for receiving pension from the fund.	Maximum permissible deduction under section 80C, 80CCC & 80CCD(1) is ₹ 1,00,000.
80CCD	Individuals employed by the Central Government or any other employer as well as self-employed individuals.	Contribution to Pension Scheme of Central Government An individual employed by the Central Government or any other employer on or after 1.1.2004 or any other assessee, being an individual, who has paid or deposited any amount in his account under a notified pension scheme.	In case of a salaried individual, deduction of own contribution under section 80CCD(1) is restricted to 10% of his salary. In any other case, deduction under section 80CCD(1) is restricted to 10% of gross total income.

			The entire employer's contribution would be included in the salary of the employee. However, deduction of employer's contribution under section 80CCD(2) would be restricted to 10% of salary, which is in addition to the limit of ₹ 1 lakh.
80CCG	Resident Individual, being a new retail investor	<p>Investment made under notified equity savings scheme</p> <p>Payment made for acquisition of listed equity shares or listed units of equity oriented fund by new retail investor in accordance with the scheme notified by the Central Government.</p> <p>For availing this deduction, gross total income of the individual \leq ₹ 12 lacs.</p> <p>Minimum lock in period is three years from acquisition date.</p>	<p>50% of the amount invested in such listed equity shares or listed units</p> <p>(or)</p> <p>₹ 25,000,</p> <p>whichever is lower.</p> <p>The deduction is available for three consecutive assessment years beginning with the assessment year in which equity shares or units were first acquired.</p>
80DD	Resident Individual or HUF	<p>Maintenance including medical treatment of a dependent disabled</p> <p>Any amount incurred for the medical treatment, training and rehabilitation of a dependent disabled</p> <p>and / or</p> <p>Any amount paid or deposited under the scheme framed in this behalf by the LIC or any other insurer or Administrator or Specified Company.</p>	<p>Flat deduction of ₹ 50,000.</p> <p>In case of severe disability (i.e. person with 80% or more disability) the flat deduction shall be ₹ 1,00,000.</p>

7.3 Income-tax

80D	Individual and HUF	<p>Medical Insurance Premium</p> <p>(1) Any premium paid, otherwise than by way of cash, to keep in force an insurance on the health of –</p> <table border="1" data-bbox="603 573 970 763"> <tr> <td data-bbox="603 573 767 685">in case of an individual</td> <td data-bbox="767 573 970 685">self, spouse and dependent children</td> </tr> <tr> <td data-bbox="603 685 767 763">in case of HUF</td> <td data-bbox="767 685 970 763">family member</td> </tr> </table> <p>(2) Contribution to CGHS of such other scheme as notified by Central Government.</p> <p>(3) Payment, including cash payment, for preventive health check up of himself, spouse, dependent children.</p>	in case of an individual	self, spouse and dependent children	in case of HUF	family member	<p>Maximum ₹15,000 (₹ 20,000, in case the individual or his or her spouse is a senior citizen)</p> <div data-bbox="1077 689 1324 1008" style="border: 1px solid black; padding: 5px; margin: 10px auto; width: fit-content;"> <p>Maximum ₹ 5,000, in aggregate (subject to the overall individual limits of ₹ 15,000/ ₹ 20,000, as the case may be)</p> </div>
in case of an individual	self, spouse and dependent children						
in case of HUF	family member						
		<p>(4) Any premium paid, otherwise than by way of cash, to keep in force an insurance on the health of parents, whether or not dependent on the individual.</p> <p>(5) Payment, including cash payment, for preventive health check up of parents.</p>	<p>Maximum ₹15,000 (₹ 20,000, in case either or both of the parents are senior citizen)</p>				
80DDB	Resident Individual or HUF	<p>Deduction for medical treatment of specified diseases or ailments</p> <p>Amount paid for specified diseases or ailment</p> <table border="1" data-bbox="571 1489 970 1769"> <tr> <td data-bbox="571 1489 735 1657">In case the assessee is an individual</td> <td data-bbox="735 1489 970 1657">For himself or his dependent spouse, children, parents, brothers or sisters</td> </tr> <tr> <td data-bbox="571 1657 735 1769">In case the assessee is a HUF</td> <td data-bbox="735 1657 970 1769">For any member of his family</td> </tr> </table>	In case the assessee is an individual	For himself or his dependent spouse, children, parents, brothers or sisters	In case the assessee is a HUF	For any member of his family	<p>Actual sum paid or ₹ 40,000 (₹ 60,000, if the payment is for medical treatment of a senior citizen), whichever is less,</p> <p>minus</p> <p>the amount reimbursed from the insurance company or the employer.</p>
In case the assessee is an individual	For himself or his dependent spouse, children, parents, brothers or sisters						
In case the assessee is a HUF	For any member of his family						

80E	Individual	<p>Interest on loan taken for higher education</p> <p>Interest on loan should be taken from any financial institution or approved charitable institution.</p> <p>Such loan is taken for pursuing his higher education or higher education of his or her relative i.e., spouse or children of the individual.</p>	<p>The deduction is available for interest payment in the initial assessment year (year of commencement of interest payment) and seven assessment years immediately succeeding the initial assessment year or until the interest is paid in full by the assessee, whichever is earlier.</p>								
80EE	Individual	<p>Interest on loan for acquisition of residential house property for self-occupation</p> <p>Conditions :</p> <table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 5%; text-align: center;">1.</td> <td>Loan sanctioned by financial institution between 1.4.2013 – 31.3.2014.</td> </tr> <tr> <td style="text-align: center;">2.</td> <td>Loan sanctioned ≤ ₹ 25 lakh</td> </tr> <tr> <td style="text-align: center;">3.</td> <td>Value of house property ≤ ₹ 40 lakh</td> </tr> <tr> <td style="text-align: center;">4.</td> <td>Assessee does not own any house property on the date of sanction of loan.</td> </tr> </table>	1.	Loan sanctioned by financial institution between 1.4.2013 – 31.3.2014.	2.	Loan sanctioned ≤ ₹ 25 lakh	3.	Value of house property ≤ ₹ 40 lakh	4.	Assessee does not own any house property on the date of sanction of loan.	<p>Interest payable on loan taken, subject to a maximum of ₹ 1 lakh (for A.Y.2014-15). [The amount of shortfall (i.e. the amount, if any, by which the deduction under this section for A.Y.2014-15 falls short of ₹ 1 lakh) would be allowed in A.Y.2015-16]</p>
1.	Loan sanctioned by financial institution between 1.4.2013 – 31.3.2014.										
2.	Loan sanctioned ≤ ₹ 25 lakh										
3.	Value of house property ≤ ₹ 40 lakh										
4.	Assessee does not own any house property on the date of sanction of loan.										
80G	All assesseees	<p>Donations to certain funds, charitable institutions etc.</p> <p>Prime Minister's National Relief Fund, Prime Minister's Drought Relief Fund, National Children's Fund, Rajiv Gandhi Foundation, Government or any approved local authority, institution for promotion of family planning</p>	<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td colspan="2" style="text-align: center;">There are four categories of deductions –</td> </tr> <tr> <td style="width: 5%; text-align: center;">(1)</td> <td>100% deduction of amount donated, without any qualifying limit</td> </tr> </table>	There are four categories of deductions –		(1)	100% deduction of amount donated, without any qualifying limit				
There are four categories of deductions –											
(1)	100% deduction of amount donated, without any qualifying limit										

		<p>Certain funds/institutions etc.</p> <p>Qualifying amount is calculated as follows:</p> <p>Step 1: Compute adjusted total income, i.e., the gross total income as reduced by the following:</p> <table border="1"> <tr> <td>1.</td> <td>Deductions under Chapter VI-A, except under section 80G</td> </tr> <tr> <td>2.</td> <td>Short term capital gains taxable under section 111A</td> </tr> <tr> <td>3.</td> <td>Long term capital gains taxable under section 112</td> </tr> </table> <p>Step 2: Calculate 10% of adjusted total income.</p> <p>Step 3: Calculate the actual donation, which is subject to qualifying limit</p> <p>Step 4: Lower of Step 2 or Step 3 is the maximum permissible deduction.</p> <p>Step 5: The said deduction is given first for donations qualifying for 100% deduction and thereafter, the balance for donations qualifying for 50% deduction.</p>	1.	Deductions under Chapter VI-A, except under section 80G	2.	Short term capital gains taxable under section 111A	3.	Long term capital gains taxable under section 112	<table border="1"> <tr> <td>(2)</td> <td>50% deduction of amount donated, without any qualifying limit</td> </tr> <tr> <td>(3)</td> <td>100% deduction of amount donated, subject to qualifying limit</td> </tr> <tr> <td>(4)</td> <td>50% deduction of amount donated, subject to qualifying limit.</td> </tr> </table> <p>No deduction shall be allowed for donation in excess of ₹ 10,000, if paid in cash.</p>	(2)	50% deduction of amount donated, without any qualifying limit	(3)	100% deduction of amount donated, subject to qualifying limit	(4)	50% deduction of amount donated, subject to qualifying limit.
1.	Deductions under Chapter VI-A, except under section 80G														
2.	Short term capital gains taxable under section 111A														
3.	Long term capital gains taxable under section 112														
(2)	50% deduction of amount donated, without any qualifying limit														
(3)	100% deduction of amount donated, subject to qualifying limit														
(4)	50% deduction of amount donated, subject to qualifying limit.														
80GGB	Indian company	<p>Contributions to political parties</p> <p>Any sum contributed by it to a political party or an electoral trust.</p>	Actual contribution (otherwise than by way of cash)												
80GGC	Any person, other than local authority and an artificial juridical person funded by the Government.	<p>Contributions to political parties</p> <p>Amount contributed to a political party or an electoral trust.</p>	Actual contribution (otherwise than by way of cash)												

<u>Deductions in respect of Certain Incomes</u>			
Section	Eligible Assessee	Eligible Income	Permissible Deduction
80QQB	Resident individual	<p>Royalty income, etc., of authors of certain books other than text books</p> <p>Lump sum consideration for assignment or grant of any of his interests in the copyright of any book, being a work of literary, artistic or scientific nature or of royalty or copyright fees</p> <p>Royalty or copyright fee received otherwise than by way of lump sum</p>	<p>Amount received or receivable or ₹ 3,00,000, whichever is less.</p> <p>Maximum 15% of value of books sold</p>
80RRB	Resident individual, being patentee ^a	<p>Royalty on patents</p> <p>Any income by way of royalty on patents</p>	Whole of such income or ₹ 3,00,000, whichever is less.
80TTA	Individual or a HUF	<p>Interest on deposits in savings account</p> <p>Any income by way of interest on deposits in a savings account with a bank, a co-operative society or a post office (not being time deposits, which are repayable on expiry of fixed periods)</p>	Actual interest subject to a maximum of ₹ 10,000.
<u>Other Deductions</u>			
Section	Eligible Assessee	Condition for deduction	Permissible Deduction
80U	Resident Individual	<p>Deduction in case of a person with disability</p> <p>Any person, who is certified by the medical authority to be a person with disability.</p>	<p>₹ 50,000, in case of a person with disability.</p> <p>₹ 1,00,000, in case of a person with severe disability (80% or more disability).</p>

Question 1

Explain how contributions to political parties are deductible in the hands of corporate and non-corporate assessee under the income-tax law.

Answer

Section 80GGB provides for deduction of any sum contributed in the previous year by an Indian company to a political party.

Section 80GGC provides for deduction of any sum contributed by any other person to a political party. However, this deduction will not be available in respect of sum contributed by a local authority and every artificial juridical person, wholly or partly funded by the Government.

It may be noted that cash donations to political parties would not qualify for deduction under section 80GGB and section 80GGC.

Deduction under sections 80GGB and 80GGC would be available in respect of contributions made to a political party registered under section 29A of the Representation of the People Act, 1951.

Note: For the purpose of section 80GGB, the word "contribute" shall have the same meaning assigned to it under section 293A of the Companies Act, 1956, which provides that –

- (a) a donation or subscription or payment given by a company to a person for carrying on any activity which is likely to effect public support for a political party shall also be deemed to be contribution for a political purpose;
- (b) the expenditure incurred, directly or indirectly, by a company on advertisement in any publication (being a publication in the nature of a souvenir, brochure, tract, pamphlet or the like) by or on behalf of a political party or for its advantage shall also be deemed to be a contribution to such political party or a contribution for a political purpose to the person publishing it.

However, it may be noted that as per section 37(2B), no allowance shall be allowed in respect of expenses incurred by him on advertisement in any souvenir, brochure, tract or the like published by any political party. It is only after computation of gross total income, contribution to a registered political party is allowed as deduction under section 80GGB to a company.

Question 2

The gross total income of Mr. Nepal for the Assessment Year 2014-15, was ₹ 12,00,000. He has made the following investment/payments during the year 2013-14-

	<i>Particulars</i>	<i>₹</i>
1.	<i>L.I.C. premium paid (Policy value ₹ 1,00,000) (taken on 1.04.2006)</i>	<i>25,000</i>
2.	<i>Contribution to Public Provident Fund (PPF)</i>	<i>25,000</i>
3.	<i>Repayment of housing loan to Indian Bank</i>	<i>50,000</i>
4.	<i>Payment made to L.I.C. pension fund</i>	<i>20,000</i>

5.	Medical insurance premium for self, wife and dependent children.	18,000
6.	Mediclaime premium for parents (aged over 80 years)	30,000

Compute eligible deduction under Chapter VI-A for the Assessment Year 2014-15.

Answer

Computation of eligible deduction under Chapter - VI A of Mr. Nepal for A.Y. 2014-15

Particulars	₹	₹
Deduction under Section 80C		
LIC premium paid ₹ 25,000 [Limited to 20% of policy value, since policy has been taken before 1.04.2012 (20% x ₹ 1,00,000)]	20,000	
Contribution to P.P.F.	25,000	
Repayment of housing loan to Indian Bank	<u>50,000</u>	
	95,000	
Deduction under Section 80CCC		
Payment to LIC Pension Fund	<u>20,000</u>	
	1,15,000	
Eligible deduction limited to ₹ 1,00,000 as per section 80CCE		1,00,000
Deduction under Section 80D		
Payment of medical insurance premium ₹ 18,000 for self, wife and dependent children. Deduction limited to ₹ 15,000.	15,000	
Medical insurance premium paid for parents ₹ 30,000 (limited to ₹ 20,000, being the limit applicable for senior citizens)	<u>20,000</u>	<u>35,000</u>
Eligible deduction under Chapter VI A		<u>1,35,000</u>

Question 3

Fill in the blanks having regard to the provisions of the Income-tax Act, 1961:

- For new two, three and four star hotels started in the specified districts on or after 1.4.2008, tax holiday of years is available under section 80-ID.
- Mr. Z has paid a sum of ₹ 65,000 on 30.11.2013 as tuition fees to a university in Australia. The amount deductible under section 80C for A.Y. 2014-15 is ₹
- Where an individual has repaid in the second year, ₹ 20,000 towards principal and ₹ 60,000 towards interest on eligible education loan from an approved bank, the deduction available under section 80E is ₹

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- (iv) Deduction under Section 80GGC in respect of contribution to approved political parties given by a local authority partly funded by the Government is.....
- (v) The maximum qualifying limit for deduction under section 80C, 80CCC and 80CCD(1) is ₹

Answer

- (i) Five
- (ii) Nil.
- (iii) ₹ 60,000
- (iv) Nil / not allowed.
- (v) ₹ 1,00,000

Question 4

Mr. Chaturvedi having gross total income of ₹ 6,35,000 for the financial year 2013-14 furnishes you the following information:

- (i) Deposited ₹ 50,000 in tax saver deposit in the name of major son in a nationalized bank.
- (ii) Paid ₹ 25,000 towards premium on life insurance policy of his married daughter (Sum Assured ₹ 2,50,000).
- (iii) Contributed ₹ 10,000 to Prime Minister's National Relief Fund.
- (iv) Donated ₹ 20,000 to a Government recognized institution for scientific research by a cheque.

Note: Assume that the gross total income of Mr. Chaturvedi comprises of only income under the head 'Salaries' and 'Income from house property'.

Compute the total income of Mr. Chaturvedi for the assessment year 2014-15.

Answer

Computation of total income of Mr. Chaturvedi for the A.Y.2014-15

Particulars	₹	₹
Gross total income		6,35,000
Less: Deductions under Chapter VI-A		
(i) Deposit of ₹ 50,000 in tax saver deposit in the name of major son in a nationalized bank – Fixed deposit in the name of son does not qualify for deduction under section 80C	-	
(ii) Premium on life insurance policy of his married daughter - Eligible for deduction under section 80C	25,000	
(iii) Contribution of ₹ 10,000 to PM's National Relief Fund, eligible for 100% deduction under section 80G	10,000	

(iv) Payment of ₹ 20,000 to a Government recognized institution for scientific research - Eligible for deduction under section 80GGA since the payment is made by way of cheque	<u>20,000</u>	<u>55,000</u>
Total Income		<u>5,80,000</u>

Question 5

State with proper reasons whether the following statements are True/False with regard to the provisions of the Income-tax Act, 1961:

- (i) During the financial year 2013-14, Mr. Amit paid interest on loan availed by him for his son's higher education. His son is already employed in a firm. Mr. Amit will get the deduction under section 80E.
- (ii) Subscription to notified bonds of NABARD would qualify for deduction under section 80C.
- (iii) In order to be eligible to claim deduction under section 80C, investment/contribution/subscription etc. in eligible or approved modes, should be made from out of income chargeable to tax.
- (iv) Where an individual repays a sum of ₹ 30,000 towards principal and ₹ 14,000 as interest in respect of loan taken from a bank for pursuing eligible higher studies, the deduction allowable under section 80E is ₹ 44,000.

Answer

- (i) **True** : The deduction under section 80E available to an individual in respect of interest on loan taken for his higher education or for the higher education of his relative. For this purpose, relative means, *inter alia*, spouse and children of the individual. Therefore, Mr. Amit will get the deduction under section 80E. It is immaterial that his son is already employed in a firm. This would not affect Mr. Amit's eligibility for deduction under section 80E.
- (ii) **True** : Under section 80C(2) subscription to such bonds issued by NABARD (as the Central Government may notify in the Official Gazette) would qualify for deduction under section 80C.
- (iii) **False** : There is no stipulation under section 80C that the investment, subscription, etc. should be made from out of income chargeable to tax.
- (iv) **False** : Deduction under section 80E is in respect of interest paid on education loan. Hence, the deduction will be limited to ₹ 14,000.

Question 6

Discuss the allowability of the following:

- (i) Rajan has to pay to a hospital for treatment ₹ 42,000 and spent nothing for life insurance or for maintenance of handicapped dependent.

7.11 Income-tax

- (ii) Raja, a resident Indian, has spent nothing for treatment in the previous year and deposited ₹ 25,000 with LIC for maintenance of handicapped dependant.
- (iii) Rajan has incurred ₹ 20,000 for treatment and ₹ 25,000 was deposited with LIC for maintenance of handicapped dependant.
- (iv) Payment of ₹ 50,000 by cheque to an electoral trust by an Indian company.

Answer

- (i) The deduction of ₹ 50,000 under section 80DD is allowed in full, irrespective of whether the expenditure was actually incurred or paid by the assessee. If the expenditure is incurred in respect of a dependant with severe disability, the deduction allowable is ₹ 1,00,000.
- (ii) The assessee Rajan has deposited ₹ 25,000 for maintenance of handicapped dependent. The assessee is, however, eligible to claim ₹ 50,000 since the deduction of ₹ 50,000 is allowed in full, irrespective of the amount deposited with LIC. In the case of dependant with severe disability, the deduction allowable is ₹ 1,00,000.
- (iii) Section 80DD allows a deduction of ₹ 50,000 irrespective of the actual amount spent on maintenance of handicapped dependent and/or actual amount deposited with LIC. Therefore, the deduction will be ₹ 50,000 even though the total amount incurred/deposited is ₹ 45,000. If the dependant is a person with severe disability the quantum of deduction is ₹ 1,00,000.
- (iv) Amount paid by an Indian Company to an electoral trust is eligible for deduction under section 80GGB from gross total income, since such payment is made otherwise than by way of cash.

Question 7

For the Assessment year 2014-15, the Gross Total Income of Mr. Chaturvedi, a resident in India, was ₹ 2,68,240 which includes long-term capital gain of ₹ 45,000 and Short-term capital gain of ₹ 8,000. The Gross Total Income also includes interest income of ₹ 12,000 from savings bank deposits with banks. Mr. Chaturvedi has invested in PPF ₹ 60,000 and also paid a medical insurance premium ₹ 11,000. Mr. Chaturvedi also contributed ₹ 15,000 to Public Charitable Trust eligible for deduction under section 80G by way of an account payee cheque. Compute the total income and tax thereon of Mr. Chaturvedi, who is 70 years old as on 31.3.2014.

Answer

Computation of total income and tax payable by Mr. Chaturvedi

Particulars	₹	₹
Gross total income including long term capital gain		2,68,240
Less : Long term capital gain		<u>45,000</u>
		2,23,240

<i>Less</i> : Deductions under Chapter VI-A:		
Under section 80C in respect of PPF deposit	60,000	
Under section 80D (it is assumed that premium is paid by otherwise than by cash and since the amount paid is less than ₹ 20,000, it is fully deductible)	11,000	
Under section 80G (See Notes 1 & 2 below)	7,112	
Under section 80TTA (See Note 3 below)	<u>10,000</u>	<u>88,112</u>
Total income (excluding long term capital gains)		<u>1,35,128</u>
Total income (including long term capital gains)		1,80,128
Total income (rounded off)		1,80,130
Tax on total income (including long-term capital gains of ₹ 45,000) (See Note 4)		Nil

Notes :**1. Computation of deduction under section 80G:**

Particulars	₹
Gross total income (excluding long term capital gains)	2,23,240
<i>Less</i> : Deduction under section 80C, 80D & 80TTA	81,000
	<u>1,42,240</u>
10% of the above	14,224
Contribution made	15,000
Lower of the two eligible for deduction under section 80G	14,224
Deduction under section 80G – 50% of ₹ 14,224	7,112

- Deduction under section 80G is allowed only if amount is paid by any mode other than cash, in case of amount exceeding ₹ 10,000. Therefore the contribution made to public charitable trust is eligible for deduction since it is made by way of an account payee cheque.
- Deduction of upto ₹ 10,000 under section 80TTA is allowed, *inter alia*, to an individual assessee if gross total income includes interest income from deposits in a saving account with bank.
- As per section 112, the unexhausted basic exemption limit can be exhausted against long-term capital gains. Therefore, since the total income of ₹ 1,80,130 (inclusive of long-term capital gains of ₹ 45,000) is less than the basic exemption limit of ₹ 2,50,000, there would be no tax liability.

Question 8

Mr. Rajmohan whose gross total income was ₹ 6,40,000 for the financial year 2013-14 furnishes you the following information:

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- (i) Stamp duty paid on acquisition of residential house (self-occupied) ₹ 50,000.
(ii) Five year time deposit in an account under Post Office Time Deposit Rules, 1981 ₹ 20,000.
(iii) Donation to a recognized charitable trust ₹ 25,000 which is eligible for deduction under section 80G at the applicable rate.
(iv) Interest on loan taken for higher education of spouse paid during the year ₹ 10,000.

Compute the total income of Mr. Rajmohan for the Assessment year 2014-15.

Answer

Computation of total income of Mr. Rajmohan for the A.Y.2014-15

Particulars	₹	₹
Gross Total Income		6,40,000
Less: Deduction under Chapter VI-A		
<u>Under section 80C</u>		
Stamp duty paid on acquisition of residential house	50,000	
Five year time deposit with Post Office	20,000	
	70,000	
<u>Under section 80E</u>		
Interest on loan taken for higher education of spouse, being a relative.	10,000	
<u>Under section 80G (See Note below)</u>		
Donation to recognized charitable trust (50% of ₹ 25,000)	12,500	92,500
Total Income		5,47,500

Note: In case of deduction under section 80G in respect of donation to a charitable trust, the net qualifying amount has to be restricted to 10% of adjusted total income, i.e., gross total income less deductions under Chapter VI-A except 80G. The adjusted total income is, therefore, ₹ 5,60,000 (i.e. 6,40,000 – ₹ 80,000), 10% of which is ₹ 56,000, which is higher than the actual donation of ₹ 25,000. Therefore, the deduction under section 80G would be ₹ 12,500, being 50% of the actual donation of ₹ 25,000.

Question 9

State with reasons, whether the following statements are true or false, with regard to the provisions of the Income-tax Act, 1961:

- (a) For grant of deduction under section 80-IB, filing of audit report in prescribed form is must for a corporate assessee; filing of return within the due date laid down in section 139(1) is not required.

(b) *Filing of belated return under section 139(4) of the Income-tax Act, 1961 will debar an assessee from claiming deduction under sections 80-ID or 80-IE.*

Answer

- (a) **False** : Section 80AC stipulates compulsory filing of return of income on or before the due date specified under section 139(1), as a pre-condition for availing the benefit of deduction, *inter alia*, under section 80-IB.
- (b) **True** : As per section 80AC, the assessee has to furnish his return of income on or before the due date specified under section 139(1), to be eligible to claim deduction under, *inter alia*, section 80-ID or 80-IE.

Question 10

Can a Primary Co-operative Agricultural and Rural Development Bank claim deduction under section 80P in respect of income derived from the business of banking?

Answer

Sub-section (4) to section 80P provides that the provisions of section 80P shall not apply to any co-operative bank, other than, *inter alia*, a primary co-operative agricultural and rural development bank (PCARB). Thus, a PCARB is entitled to claim deduction under section 80P in respect of income derived from the business of banking.

Question 11

Deduction under section 80CCD is available only to individuals employed by the Central Government. Discuss the correctness of this statement.

Answer

The deduction under section 80CCD is available to the individuals employed by the Central Government or any other employer. The deduction is also available to self-employed individuals. Therefore, the statement is incorrect.

Question 12

Mr. Abhik, an individual, made payment of health insurance premium to GIC in an approved scheme. Premium paid on his health is ₹ 10,000 and his spouse's health is ₹ 15,000 during the year 2013-14. He also paid health insurance premium of ₹ 25,000 on his father's health who is a senior citizen and not dependent on him. The payments have not been made by cash. Compute the amount of deduction under section 80D available to Mr. Abhik from his gross total income for the assessment year 2014-15.

Answer

Mr. Abhik will be eligible to claim deduction under section 80D on payment of health insurance premium to GIC in a medical insurance scheme approved by the Central Government. The premium is paid otherwise than by way of cash and hence qualifies for deduction under section 80D. Therefore, the amount of deduction under section 80D would be –

7.15 Income-tax

Particulars	₹
On health insurance premium paid on the health of himself and his spouse (₹ 10,000 + ₹ 15,000 = ₹ 25,000, but restricted to ₹ 15,000)	15,000
On health insurance premium paid on the health of his father, ₹ 25,000 but restricted to ₹ 20,000 in the case of a parent, who is a senior citizen (whether dependent or not)	<u>20,000</u>
Total deduction under section 80D	<u>35,000</u>

EXERCISES

- Mr. Srivastav, aged 72 years, paid medical insurance premium of ₹ 22,000 by cheque and ₹ 1,000 by cash during May, 2013 under a Medical Insurance Scheme of the General Insurance Corporation. The above sum was paid for insurance of his own health. He would be entitled to a deduction under section 80D of a sum of -
 - ₹ 22,000
 - ₹ 20,000
 - ₹ 15,000
- Mr. Ramesh pays a rent of ₹ 5,000 per month. His total income is ₹ 2,40,000 (i.e. Gross Total Income as reduced by deductions under Chapter VI-A except section 80GG). He is also in receipt of HRA. He would be eligible for a deduction under section 80GG of an amount of -
 - ₹ 24,000
 - ₹ 36,000
 - Nil
- The deduction allowable under section 80LA in respect of eligible income of Offshore Banking Units and International Financial Services Centre is -
 - 50% of such income for 5 consecutive assessment years
 - 100% of such income for 10 consecutive assessment years
 - 100% of such income for 5 consecutive assessment years and 50% of such income for 5 consecutive assessment years thereafter
- The deduction under section 80QQB in respect of royalty income of authors of certain books is subject to a maximum limit of -
 - ₹ 1,00,000
 - ₹ 3,00,000
 - ₹ 5,00,000
- Under section 80GGB, deduction is allowable in respect of contribution to political parties by -
 - any person other than local authority and every artificial juridical person wholly or partly

- funded by the Government
- b) Local authority and every artificial juridical person wholly or partly funded by the Government
 - c) An Indian company
6. ₹ 1 lakh is the maximum qualifying limit for deduction under -
- a) Section 80C alone.
 - b) Sections 80C and 80CCC
 - c) Sections 80C, 80CCC and 80CCD(1)
7. Write short notes on -
- (i) Deduction in respect of royalty income on patents
 - (ii) Deduction in respect of royalty income of authors of certain books.
 - (iii) Deduction in respect of royalty income on patents.
 - (iv) Deduction from Gross Total Income under section 80GG.
8. What is the deduction available from the gross total income of a company in respect of any contribution given to a political party?
9. Who are the assessee eligible to claim deduction under section 80LA? What is the quantum of deduction available under this section? What are the conditions to be fulfilled for claiming such deduction?
10. Write briefly about the provisions regarding deductions from gross total income in respect of medical treatment of dependent disabled under section 80DD of the Income-tax Act, 1961 and in respect of medical treatment of assessee himself/dependent under section 80DDB of the Income-tax Act, 1961.

Answers

1. b; 2. c; 3. c; 4. b; 5. c; 6. c

8

Computation of Total Income and Tax Payable

Steps in computation of total income & tax liability

Income-tax is a tax levied on the total income of the previous year of every person. The levy of income-tax is, therefore, on the total income of the assessee. The total income has to be computed as per the provisions of the Income-tax Act, 1961 in the following manner -

(1)	Ascertain residential status	<ul style="list-style-type: none">• In case of an individual, the number of days of his stay in India during the relevant previous year and/or the earlier previous years would determine his residential status.• An individual/HUF can be either a -<ul style="list-style-type: none">▪ Resident and ordinarily resident▪ Resident but not ordinarily resident▪ Non-resident• Persons, other than an individual and HUF, can be either resident or non-resident. An Indian company is resident in India. The determining factor for every other assessee is the place where the control and management of its affairs are situated during that year i.e., whether in India or outside India.• The residential status of a person determines the scope of his taxable income. For example, income which accrues outside India and is received outside India is taxable in the hands of a resident and ordinarily resident but is not taxable in the case of a non-resident.
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(2)	<p>Exclude income which do not form part of total income</p>	<ul style="list-style-type: none"> • Exclude income which do not form part of total income, like, agricultural income, dividend income from domestic companies, etc. These income are wholly exempt from tax • Certain income are excluded from total income subject to limits, like house rent allowance, leave encashment etc. In such cases, the exempt portion has to be excluded and the remaining amount has to be included under the respective head of income. • Section 10 of the Income-tax Act, 1961 provides for the exclusions from total income.
(3)	<p>Identify & Group income under the respective head</p>	<ul style="list-style-type: none"> • There are five heads of income, namely, - <ul style="list-style-type: none"> ▪ Salaries, ▪ Income from house property, ▪ Profits and gains of business or profession ▪ Capital Gains ▪ Income from other sources • The income of a person should be identified and grouped under the respective head of income. • Each head of income has a charging section (for example, section 15 for salaries, section 22 for income from house property). • Deeming provisions are also contained under certain heads, by which specific items are sought to be taxed under those heads. For example, if bad debts allowed as deduction in an earlier year is recovered in a subsequent year, then the amount recovered would be deemed as business income of the person in the year of recovery. • The charging section and the deeming provisions would help you to determine the scope of income chargeable under a particular head.
(4)	<p>Compute the income under each head</p>	<ul style="list-style-type: none"> • Assess the income under each head by - <ul style="list-style-type: none"> ▪ applying the charging and deeming provisions, ▪ excluding the specific exemptions provided for in section 10 relating to that head, subject to the limits specified therein, ▪ allowing the permissible deductions under that head, and ▪ disallowing the non-permissible deductions. • For example, while computing net consideration for capital gains, brokerage is a permissible deduction from gross sale consideration but securities transaction tax paid is not permissible.

(5)	Apply clubbing provisions	<ul style="list-style-type: none"> • An individual in a higher tax bracket may have a tendency to divert his income to another person who is not subject to tax or who is in a lower tax bracket. For example, an individual may make a fixed deposit in the name of his minor son, so that income from such deposit would accrue to his son, who does not have any other income. • In order to prevent evasion of income-tax by such means, there are specific provisions under the Income-tax Act, 1961 to include the income of one person in the hands of another person, in certain cases. • For example, income of a minor child (say, interest income) is includible in the hands of the parent whose total income is higher before including minor's income. Such interest income will be included in the hands of the parent under the head "Income from other sources" after providing for deduction of up to ₹ 1,500 under section 10(32). • However, if a minor child earns income on account of his or her special skills or talent, like music or dance, then such income is not includible in the hands of the parent.
(6)	Give effect to the provisions for set-off and carry forward and set-off of losses	<ul style="list-style-type: none"> • Inter-source set-off of losses <ul style="list-style-type: none"> ▪ A person may have income from one source and loss from another source under the same head of income. For instance, a person may have profit from wholesale trade of merchandise and loss from the business of plying vehicles. The loss of one business can be set-off against the profits of another business to arrive at the net income under the head "Profits and gains of business or profession". ▪ Set-off of loss from one source against income from another source within the same head of income is permissible, subject to certain exceptions, like long-term capital loss cannot be set-off against short-term capital gains though short-term capital loss can be set-off against long-term capital gains. • Inter-head set-off of losses <ul style="list-style-type: none"> ▪ Likewise, set-off of loss from one head (say, loss from house property) against income from another head (say, Salaries) is also permissible, subject to certain exceptions, like business loss cannot be set-off against salary income.

		<ul style="list-style-type: none"> • Carry forward and set-off of losses <ul style="list-style-type: none"> ▪ Unabsorbed losses of the current year can be carried forward to the next year for set-off only against the respective head of income. ▪ Here again, if there are any restrictions relating to inter-source set-off, the same will apply, like long-term capital loss which is carried forward can be set-off only against long-term capital gains and not short-term capital gains of a later year. ▪ The maximum number of years up to which any particular loss can be carried forward is also provided under the Act. For example, business loss can be carried forward for a maximum of 8 assessment years to be set-off against business income. 								
(7)	Determine the gross total income (GTI)	<ul style="list-style-type: none"> • The income computed under each head, after giving effect to the clubbing provisions and provisions for set-off and carry forward and set-off of losses, have to be aggregated to arrive at the gross total income. • The process of computing GTI is depicted hereunder - <table border="1" style="margin-left: 20px; width: 80%; border-collapse: collapse;"> <tr> <td style="padding: 2px;">Add income computed under each head</td> <td style="padding: 2px;">→ Apply clubbing provisions</td> <td style="padding: 2px;">→ Apply the provisions for set-off and carry forward of losses</td> </tr> </table> 	Add income computed under each head	→ Apply clubbing provisions	→ Apply the provisions for set-off and carry forward of losses					
Add income computed under each head	→ Apply clubbing provisions	→ Apply the provisions for set-off and carry forward of losses								
(8)	Allow deductions permissible from gross total income	<p>Certain deductions are allowable from gross total income to arrive at the total income. These deductions contained in Chapter VI-A can be classified as –</p> <ul style="list-style-type: none"> • Deduction in respect of certain payments, for example, <table border="1" style="margin-left: 20px; width: 80%; border-collapse: collapse;"> <thead> <tr> <th style="text-align: left; padding: 2px;">Section</th> <th style="text-align: left; padding: 2px;">Nature of Payment/Deposit</th> </tr> </thead> <tbody> <tr> <td style="padding: 2px;">80C</td> <td style="padding: 2px;">Payment of life insurance premium, tuition fees of children, deposit in public provident fund, repayment of housing loan etc.</td> </tr> <tr> <td style="padding: 2px;">80D</td> <td style="padding: 2px;">Medical insurance premium paid by an individual/HUF for the specified persons/contribution to CGHS etc.</td> </tr> <tr> <td style="padding: 2px;">80E</td> <td style="padding: 2px;">Payment of interest on educational loan taken for self or relative</td> </tr> </tbody> </table> 	Section	Nature of Payment/Deposit	80C	Payment of life insurance premium, tuition fees of children, deposit in public provident fund, repayment of housing loan etc.	80D	Medical insurance premium paid by an individual/HUF for the specified persons/contribution to CGHS etc.	80E	Payment of interest on educational loan taken for self or relative
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(9)	Find out the total income	<ul style="list-style-type: none"> • The gross total income as reduced by the above deductions under Chapter VI-A is the total income. <table border="1" data-bbox="576 958 1177 1003"> <tr> <td>Total income = GTI – Deductions under Chapter VI-A</td> </tr> </table> <ul style="list-style-type: none"> • Tax is calculated on the total income of the assessee. 	Total income = GTI – Deductions under Chapter VI-A							
Total income = GTI – Deductions under Chapter VI-A										
(10)	Calculate the tax liability (apply the rates of tax on the total income)	<ul style="list-style-type: none"> • The rates of tax are specified in the Finance Act. <ul style="list-style-type: none"> ▪ For individuals and HUF, there is a basic exemption limit and slab rate of tax. ▪ Companies and firms are subject to a flat rate of tax, without any basic exemption limit. ▪ The rates of tax have to be applied on the total income to compute the tax liability. • Rates of tax in respect of certain income are provided under the Income-tax Act, 1961 itself. <p>For instance, casual income, like lottery income, is chargeable to tax at a flat rate of 30% as per section 115BB and long-term capital gains is chargeable to tax at a flat rate of 20% as per section 112. These are also to be considered while calculating the tax liability.</p> • Rebate of upto ₹ 2,000 from income-tax is available under section 87A, for resident individuals having total income upto ₹ 5 lakh. • Surcharge@10% is attracted, if total income exceeds ₹ 1 crore • Education cess (EC) @2% of tax liability and Secondary and higher education cess (SHEC)@1% have to be added to arrive at the total tax liability. 								

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Total Tax Liability	=	Tax on total income at applicable rates	+	Surcharge, if total income > ₹ 1 crore	+	EC @2%	+	SHEC @1%												
			-	Rebate u/s 87A, if total income ≤ ₹ 5 lakh																
(11)	Reduce tax deducted at source (TDS) and advance tax to arrive at the net tax liability	<ul style="list-style-type: none"> Tax is deductible at source at the time of payment of salary, rent, interest, fees for professional services, royalty etc. The payer has to deduct tax at source at the rates specified in the respective section, say, tax is deductible@10% in respect of royalty and fees for professional services. Such tax deducted at source has to be reduced by the payee to determine his net tax liability. The Income-tax Act, 1961 also requires payment of advance tax in instalments during the previous year itself on the basis of estimated income, if the tax payable, after reducing TDS, is ₹ 10,000 or more. Companies are required to pay advance tax in four instalments, on or before 15th June, 15th September, 15th December and 15th March of the financial year. Other assesseees are required to pay advance tax in three instalments, on or before 15th September, 15th December and 15th March of the financial year. The advance tax so paid should also be deducted to arrive at the net tax liability. <table style="width: 100%; border: 1px solid black; margin-top: 10px;"> <tr> <td style="width: 15%;">Net Tax Liability</td> <td style="width: 10%; text-align: center;">=</td> <td style="width: 30%;">Total tax liability</td> <td style="width: 5%; text-align: center;">-</td> <td style="width: 10%;">TDS</td> <td style="width: 5%; text-align: center;">-</td> <td style="width: 25%;">Advance tax paid</td> </tr> </table>	Net Tax Liability	=	Total tax liability	-	TDS	-	Advance tax paid											
Net Tax Liability	=	Total tax liability	-	TDS	-	Advance tax paid														
(12)	Return of Income	<ul style="list-style-type: none"> Return of income is the form in which an assessee has to fill the particulars relating to his total income and tax liability. The net tax liability arrived at after deducting TDS and advance tax, has to be paid on or before the due date of filing of return of income by way of self-assessment tax. An individual/HUF is required to file a return of income, if his/its total income, before giving effect to Chapter VIA deductions, exceed the basic exemption limit. A firm or company has to file its return of income, irrespective of whether it earns a profit or incurs loss. 																		

8.7 Income-tax

Question 1

Ms. Vaishali, employed in a private sector company, furnishes following information for the year ended 31.03.2014.

Particulars	₹
Income from salary (computed)	3,45,000
Bank interest (Fixed Deposit)	15,000
Tax on non-monetary perquisite paid by employer	20,000
Amount contributed by her during the year are given below:	
Contribution to recognized provident fund	60,000
Health insurance premium-on self (paid by crossed cheque)	7,000
Medical expenditure for dependent sister with disability	20,000

Compute the total income of Ms. Vaishali for the assessment year 2014-15.

Answer

Computation of total income of Ms. Vaishali for the A.Y. 2014-15

Particulars	₹	₹
Income from salary (computed)		3,45,000
Income from other sources		
Bank Interest (Fixed Deposit)		<u>15,000</u>
Gross Total Income		3,60,000
Less: Deductions under Chapter VI-A		
Section 80C		
Contribution to recognized provident fund	60,000	
Section 80D		
Medical insurance premium (Note -2)	7,000	
Section 80DD		
Medical expenditure for dependent sister with disability (flat deduction irrespective of expenditure incurred)	<u>50,000</u>	<u>1,17,000</u>
Total income		<u>2,43,000</u>

Note:

1. Tax on non-monetary perquisite paid by employer is exempt in the hands of employee under section 10(10CC).
2. Medical insurance premium paid by cheque for self is allowed as deduction under section 80D.

Question 2

Dr. Gurumoorthy, a resident individual at Madurai, aged 50 years is running a clinic. His Income and Expenditure Account for the year ending March 31st 2014 is as under :

<i>Expenditure</i>	<i>₹</i>	<i>Income</i>	<i>₹</i>
<i>To Medicine consumed</i>	<i>8,40,000</i>	<i>By Consultation and Medical charges</i>	<i>21,00,000</i>
<i>To Staff salary</i>	<i>4,25,000</i>	<i>By Income-tax refund (principal ₹ 15,000, interest ₹ 1,500)</i>	<i>16,500</i>
<i>To clinic consumables</i>	<i>1,55,000</i>	<i>By Dividend from Indian companies</i>	<i>27,000</i>
<i>To Rent paid</i>	<i>1,20,000</i>	<i>By Winning from lottery</i>	<i>35,000</i>
<i>To Administrative expenses</i>	<i>3,00,000</i>	<i>Net of TDS</i>	<i>54,000</i>
<i>To Donation to IIT Delhi for Research approved under section 35(2AA)</i>	<i>1,00,000</i>	<i>By Rent</i>	<i>54,000</i>
<i>To Net Profit</i>	<i>2,92,500</i>		
	<u><i>22,32,500</i></u>		<u><i>22,32,500</i></u>

- (i) *Rent paid includes ₹ 36,000 paid by cheque towards rent for his residence.*
- (ii) *Clinic equipments are :*
 - 01.04.2013 Opening WDV ₹ 4,50,000*
 - 07.02.2014 Acquired (cost) ₹ 1,00,000*
- (iii) *Rent received relates to property let out at Madurai. Gross Annual Value ₹ 54,000. The municipal tax of ₹ 9,000, paid in January 2014 has been included in "administrative expenses".*
- (iv) *Dr. Gurumoorthy availed a loan of ₹ 5,50,000 from a bank for higher education of his daughter. He repaid principal of ₹ 50,000, and interest thereon ₹ 65,000 during the year 2013-14.*
- (v) *He paid ₹ 60,000 as tuition fee to the university for full time education of his son.*

From the above, compute the total income of Dr. Gurumoorthy for the A.Y.2014-15.

Answer

Computation of total income of Dr. Gurumoorthy for the A.Y. 2014-15

	Particulars	₹	₹	₹
I	Income from profession			
	Net profit as per Income and Expenditure account		2,92,500	
	Less: Items of income to be treated separately			
	(i) Income tax refund (including interest)	16,500		

8.9 Income-tax

	(ii) Dividend from Indian companies	27,000		
	(iii) Winning from lottery (net of TDS)	35,000		
	(iv) Rent received	<u>54,000</u>	<u>1,32,500</u>	
			1,60,000	
	Add: Expenditure debited but not allowable			
	(i) Rent for his residence	36,000		
	(ii) Municipal tax paid relating to residential house at Madurai included in administrative expenses	<u>9,000</u>	<u>45,000</u>	
			2,05,000	
	Less: Expenditure allowable but not debited			
	Depreciation on Clinic equipments u/s 32			
	- on ₹ 4,50,000 @ 15%	67,500		
	- on ₹ 1,00,000 @ 7.5% (i.e.50% of 15%)	<u>7,500</u>		
	Additional deduction of 100% in respect of amount paid to IIT [since weighted deduction of 200% is available in respect of such payment under section 35(2AA)]	75,000		
		<u>1,00,000</u>	<u>1,75,000</u>	30,000
II	Income from house property			
	Gross Annual Value (GAV)		54,000	
	Less : Municipal taxes paid		<u>9,000</u>	
	Net Annual Value (NAV)		45,000	
	Less : Deduction under section 24 @ 30%		<u>13,500</u>	31,500
III	Income from other sources			
	Interest on Income-tax refund		1,500	
	Dividend from Indian companies	27,000		
	Less: Exempt under section 10(34)	<u>27,000</u>	Nil	
	Winnings from lottery (See Note 1)		<u>50,000</u>	<u>51,500</u>
	Gross Total Income			1,13,000
	Less: Deductions under Chapter VI A:			
	- Under section 80C			
	Tuition fee paid to university for full time education of his son		60,000	
	- Under section 80E			
	Interest on loan taken for higher education of daughter		<u>65,000</u>	
			1,25,000	
	but restricted to (See Note 2)			<u>63,000</u>
	Total income			<u>50,000</u>

Notes:

1. Winnings from lottery should be grossed up for the chargeability under the head "Income from other sources". The applicable rate of TDS is 30%. Gross income from lottery, would, therefore, be ₹ 35,000/70% = ₹ 50,000
2. Deduction under Chapter VI-A cannot exceed Gross Total Income. Further, no deduction is allowable from income by way of winning from lottery. Therefore, the maximum deduction allowable would be ₹ 63,000.

	₹
Gross Total Income	1,13,000
Less: Winnings from lottery	<u>50,000</u>
Maximum deduction under Chapter VI-A	<u>63,000</u>

The total income of ₹ 50,000 would, therefore, represent winnings from lottery taxable at a flat rate of 30%, without any basic exemption limit.

3. Dr. Gurumoorthy is staying in a rented premises in Madurai itself. Hence, he would not be eligible for deduction under section 80GG, since he owns a house in Madurai which he has let out.

Question 3

Ms. Purvi, aged 55 years, is a Chartered Accountant in practice. She maintains her accounts on cash basis. Her Income and Expenditure account for the year ended March 31, 2014 reads as follows:

<i>Expenditure</i>	<i>(₹)</i>	<i>Income</i>	<i>(₹)</i>	<i>(₹)</i>
<i>Salary to staff</i>	<i>5,50,000</i>	<i>Fees earned:</i>		
<i>Stipend to articled assistants</i>	<i>37,000</i>	<i>Audit</i>	<i>7,88,000</i>	
<i>Incentive to articled assistants</i>	<i>3,000</i>	<i>Taxation services</i>	<i>5,40,300</i>	
<i>Office rent</i>	<i>24,000</i>	<i>Consultancy</i>	<u><i>2,70,000</i></u>	<i>15,98,300</i>
<i>Printing and stationery</i>	<i>22,000</i>	<i>Dividend on shares of Indian companies (Gross)</i>		<i>10,524</i>
<i>Meeting, seminar and Conference</i>	<i>31,600</i>	<i>Income from UTI</i>		<i>7,600</i>
<i>Purchase of car</i>	<i>80,000</i>	<i>Honorarium received from various institutions for valuation of answer papers</i>		<i>15,800</i>
<i>Repair, maintenance and petrol of car</i>	<i>4,000</i>	<i>Rent received from residential flat let out</i>		<i>85,600</i>
<i>Travelling expenses</i>	<i>35,000</i>			

8.11 Income-tax

Municipal tax paid in respect of house property	3,000			
Net Profit	9,28,224			
	17,17,824			17,17,824

Other Information:

- Allowable rate of depreciation on motor car is 15%.
- Value of benefits received from clients during the course of profession is ₹ 10,500.
- Incentives to articled assistants represent amount paid to two articled assistants for passing IPCC Examination at first attempt.
- Repairs and maintenance of car include ₹ 2,000 for the period from 1-10-2013 to 30-09-2014.
- Salary include ₹ 30,000 to a computer specialist in cash for assisting Ms. Purvi in one professional assignment.
- The total travelling expenses incurred on foreign tour was ₹ 32,000 which was within the RBI norms.
- Medical Insurance Premium on the health of dependent brother and major son dependent on her amounts to ₹ 5,000 and ₹ 10,000, respectively, paid in cash.
- She invested an amount of ₹ 10,000 in National Saving Certificate.

Compute the total income and tax payable of Ms. Purvi for the assessment year 2014-2015.

Answer

Computation of total income and tax liability of Ms. Purvi for the A.Y. 2014-15

Particulars	₹	₹
Income from house property (See Working Note 1)		57,820
Profit and gains of business or profession (See Working Note 2)		9,20,200
Income from other sources (See Working Note 3)		<u>15,800</u>
Gross Total Income		9,93,820
Less: Deductions under Chapter VI-A (See Working Note 4)		<u>10,000</u>
Total Income		<u>9,83,820</u>
Tax on total income		
Upto ₹ 2,00,000	Nil	
₹ 2,00,001 – ₹ 5,00,000 @10%	30,000	
₹ 5,00,001 - ₹ 9,83,820 @20%	<u>96,764</u>	1,26,764
Add: Education cess @ 2%		2,535
Secondary and higher education cess @ 1%		<u>1,268</u>
Total tax liability		<u>1,30,567</u>

Working Notes :

(1) Income from House Property

Particulars	₹	₹
Gross annual value under section 23(1)	85,600	
<i>Less:</i> Municipal taxes paid	<u>3,000</u>	
Net Annual Value (NAV)	82,600	
<i>Less:</i> Deduction under section 24 @ 30% of NAV	<u>24,780</u>	57,820

Note - Rent received has been taken as the Gross Annual Value in the absence of other information relating to Municipal Value, Fair Rent and Standard Rent.

(2) Income under the head "Profits & Gains of Business or Profession"

Particulars	₹	₹
Net profit as per Income and Expenditure account		9,28,224
<i>Add:</i> Expenses debited but not allowable		
(i) Salary paid to computer specialist in cash disallowed under section 40A(3), since such cash payment exceeds ₹ 20,000	30,000	
(ii) Amount paid for purchase of car is not allowable under section 37(1) since it is a capital expenditure	80,000	
(ii) Municipal Taxes paid in respect of residential flat let out	<u>3,000</u>	<u>1,13,000</u>
		10,41,224
<i>Add:</i> Value of benefit received from clients during the course of profession [taxable as business income under section 28(iv)]		<u>10,500</u>
		10,51,724
<i>Less:</i> Income credited but not taxable under this head:		
(i) Dividend on shares of Indian companies	10,524	
(ii) Income from UTI	7,600	
(iii) Honorarium for valuation of answer papers	15,800	
(iv) Rent received from letting out of residential flat	<u>85,600</u>	<u>1,19,524</u>
		9,32,200
<i>Less:</i> Depreciation on motor car @15% (See Note (i) below)		<u>12,000</u>
		<u>9,20,200</u>

Notes :

- (i) It has been assumed that the motor car was put to use for more than 180 days during the previous year and hence, full depreciation @ 15% has been provided for under section 32(1)(ii).

Note : Alternatively, the question can be solved by assuming that motor car has been put to use for less than 180 days and accordingly, only 50% of depreciation would be allowable as per the second proviso below section 32(1)(ii).

8.13 Income-tax

- (ii) Incentive to articled assistants for passing IPCC examination in their first attempt is deductible under section 37(1).
- (iii) Repairs and maintenance paid in advance for the period 1.4.2014 to 30.9.2014 i.e. for 6 months amounting to ₹ 1,000 is allowable since Ms. Purvi is following the cash system of accounting.
- (iv) ₹ 32,000 expended on foreign tour is allowable as deduction assuming that it was incurred in connection with her professional work. Since it has already been debited to income and expenditure account, no further adjustment is required.

(3) Income from other sources

Particulars	₹	₹
Dividend on shares of Indian companies	10,524	
Less: Exempt under section 10(34)	<u>10,524</u>	Nil
Income from UTI	7,600	
Less: Exempt under section 10(35)	<u>7,600</u>	Nil
Honorarium for valuation of answer papers		<u>15,800</u>
		<u>15,800</u>

(4) Deduction under Chapter VI-A :

Particulars	₹
Deduction under section 80C (Investment in NSC)	10,000
Deduction under section 80D (See Notes (i) & (ii) below)	<u>Nil</u>
Total deduction under Chapter VI-A	<u>10,000</u>

Notes:

- (i) Premium paid to insure the health of brother is not eligible for deduction under section 80D, even though he is a dependent, since brother is not included in the definition of "family" under section 80D.
- (ii) Premium paid to insure the health of major son is not eligible for deduction, even though he is a dependent, since payment is made in cash.

Question 4

Calculate the income-tax liability for the assessment year 2014-15 in the following cases:

	Mr. A (age 45)	Mrs. B (age 62)	Mr. C (age 81)	Mr. D (age 82)
Status	Resident	Non-resident	Resident	Non-resident
Total income other than long-term capital gain	2,40,000	2,30,000	5,90,000	4,80,000

Long-term capital gain	15,000 from sale of vacant site	10,000 from sale of listed shares (STT* paid)	60,000 from sale of agricultural land in rural area	Nil
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Answer

Computation of income-tax liability for the A.Y.2014-15

Particulars	Mr. A (age 45)	Mrs. B (age 62)	Mr. C (age 81)	Mr. D (age 82)
Residential Status	Resident	Non-resident	Resident	Non-resident
Applicable basic exemption limit	₹ 2,00,000	₹ 2,00,000	₹ 5,00,000	₹ 2,00,000
Asset sold	Vacant site	Listed shares (STT paid)	Rural agricultural land	-
Long-term capital gain (on sale of above asset)	₹ 15,000 [Taxable@20% u/s 112]	₹ 10,000 [exempt u/s 10(38)]	₹ 60,000 (Exempt – not a capital asset)	-
Other income	₹ 2,40,000	₹ 2,30,000	₹ 5,90,000	₹ 4,80,000
Tax liability				
On LTCG	₹ 3,000	-	-	-
On Other income (after adjusting Basic Exemption limit)	₹ 4,000	₹ 3,000	₹ 18,000	₹ 28,000
	₹ 7,000	₹ 3,000	₹ 18,000	₹ 28,000
Less: Rebate u/s 87A	₹ 2,000			
	₹ 5,000			
Add: Education cess @2% & SHEC @1%	150	90	540	840
Total tax liability	₹ 5,150	₹ 3,090	₹ 18,540	₹ 28,840

Notes:

1. Since Mrs. B and Mr. D are non-residents, they cannot avail the higher basic exemption limit of ₹ 2,50,000 and ₹ 5,00,000 for persons over the age of 60 years and 80 years, respectively.
2. Since Mr. A is a resident whose total income does not exceed ₹ 5 lakhs, he is eligible for rebate of ₹ 2,000 under section 87A.

Question 5

Mr. Y carries on his own business. An analysis of his trading and profit & loss for the year ended 31-3-2014 revealed the following information :

- (1) The net profit was ₹ 11,20,000.
- (2) The following incomes were credited in the profit and loss account :
 - (a) Dividend from UTI ₹ 22,000.
 - (b) Interest on debentures ₹ 17,500.
 - (c) Winnings from races ₹ 15,000.
- (3) It was found that some stocks were omitted to be included in both the opening and closing stocks, the value of which were:

Opening stock ₹ 8,000.
Closing stock ₹ 12,000.
- (4) ₹ 1,00,000 was debited in the profit and loss account, being contribution to a University approved and notified under section 35(1)(ii).
- (5) Salary includes ₹ 20,000 paid to his brother which is unreasonable to the extent of ₹ 2,500.
- (6) Advertisement expenses include 15 gift packets of dry fruits costing ₹ 1,000 per packet presented to important customers.
- (7) Total expenses on car was ₹ 78,000. The car was used both for business and personal purposes. $\frac{3}{4}$ th is for business purposes.
- (8) Miscellaneous expenses included ₹ 30,000 paid to A & CO., a goods transport operator in cash on 31-1-2014 for distribution of the company's product to the warehouses.
- (9) Depreciation debited in the books was ₹ 55,000. Depreciation allowed as per Income-tax Rules, 1962 was ₹ 50,000.
- (10) Drawings ₹ 10,000.
- (11) Investment in NSC ₹ 15,000.

Compute the total income of Mr. Y for the assessment year 2014-15.

Answer

Computation of total income of Mr. Y for the A.Y. 2014-15

Particulars	₹
Profits and gains of business or profession (See Working Note 1 below)	10,46,500
Income from other sources (See Working Note 2 below)	<u>32,500</u>
Gross Total Income	10,79,000

<i>Less:</i> Deduction under section 80C (Investment in NSC)	15,000
Total Income	10,64,000

Working Notes :

1. Computation of profits and gains of business or profession

Particulars	₹	₹
Net profit as per profit and loss account		11,20,000
Add: Expenses debited to profit and loss account but not allowable as deduction		
Salary paid to brother disallowed to the extent considered unreasonable [Section 40A(2)]	2,500	
Motor car expenses attributable to personal use not allowable (₹ 78,000 × ¼)	19,500	
Depreciation debited in the books of account	55,000	
Drawings (not allowable since it is personal in nature) [See Note (iii)]	10,000	
Investment in NSC [See Note (iii)]	15,000	1,02,000
		12,22,000
<i>Add:</i> Under statement of closing stock		12,000
		12,34,000
<i>Less:</i> Under statement of opening stock		8,000
		12,26,000
<i>Less:</i> Contribution to a University approved and notified under section 35(1)(ii) is eligible for weighted deduction@175%. Since only the actual contribution (100%) has been debited to profit and loss account, the additional 75% has to be deducted.		75,000
		11,51,000
<i>Less:</i> Incomes credited to profit and loss account but not taxable as business income		
Income from UTI [Exempt under section 10(35)]	22,000	
Interest on debentures (taxable under the head "Income from other sources")	17,500	
Winnings from races (taxable under the head "Income from other sources")	15,000	54,500
		10,96,500
<i>Less:</i> Depreciation allowable under the Income-tax Rules, 1962		50,000
		10,46,500

Notes :

- (i) Advertisement expenses of revenue nature, namely, gift of dry fruits to important customers, is incurred wholly and exclusively for business purposes. Hence, the same is allowable as deduction under section 37.
- (ii) Disallowance under section 40A(3) is not attracted in respect of cash payment of ₹ 30,000 to A & Co., a goods transport operator, since, in case of payment made for plying, hiring or leasing goods carriages, an increased limit of ₹ 35,000 is applicable (i.e. payment of upto ₹ 35,000 can be made in cash without attracting disallowance under section 40A(3))
- (iii) Since drawings and investment in NSC have been given effect to in the profit and loss account, the same have to be added back to arrive at the business income.

2. Computation of "Income from other sources"

Particulars	₹
Interest on debentures	17,500
Winnings from races	<u>15,000</u>
	<u><u>32,500</u></u>

Note:

The following assumptions have been made in the above solution:

1. The figures of interest on debentures and winnings from races represent the gross income (i.e., amount received plus tax deducted at source).
2. In point no. 9 of the question, it has been given that depreciation as per Income-tax Rules, 1962 is ₹ 50,000. It has been assumed that, in the said figure of ₹ 50,000, only the proportional depreciation (i.e., 75% for business purposes) has been included in respect of motor car.

Question 6

Ms. Rachna was gifted a land by her father in December, 2001 at the occasion of her marriage. The land was allotted to her father in November, 1991 at cost of ₹ 6 lac by DDA for commercial purpose. She set up a nursery on land, earns profit of ₹ 4 lacs during the year 2013-14 from seedlings grown in nursery. She sold the nursery to her friend at ₹ 50 lacs in October, 2013. Her friend paid ₹ 20 lacs in cash and ₹ 30 lacs in the form of shares. Market value of land on date of sale was ₹ 90 lacs and shares ₹ 70 lacs. Rachna, with an intention to earn profit, invested ₹ 20 lacs in shares by purchasing shares for ₹ 15 lacs from National Stock Exchange and ₹ 5 lacs in subscription to equity shares forming part of eligible issue of capital by a public company. She spent ₹ 60,000 on purchase of computers, ₹ 20,000 on net connectivity and ₹ 2 lacs toward salary and other expenses. She paid monthly rent ₹ 2,500 for a shop which was taken in October 2013, for trading in shares. Depreciation rate on computers is 60%.

The value of shares purchased and sold during the year are as follows:

Purchases including received from friend	₹ 80,00,000
Sales	₹ 1,00,00,000

The market value of shares remains unsold as on 31.03.2014 is ₹ 40 lakhs. Ms. Rachna

- Made contribution of ₹ 20,000 to approved pension fund.
- Paid ₹ 25,000 to LIC for medical insurance premium of self and spouse.
- Repaid loan ₹ 1,00,000 and interest ₹ 20,000 to SBI taken in February, 2014 for her son's admission in Sri Ram College of Commerce B.Com.
- Contributed ₹ 25,000 to a research association, which has as its object undertaking of scientific research.

Rachna did not earn any short term capital gain during the year. Rachna has not celebrated her 40th birthday yet. Compute the total income of Ms. Rachna and tax thereon payable by her for the Assessment Year 2014-15. Cost inflation index for financial year 1991-92 is 199, 2001-02 is 426 and 2013-14 is 939.

Answer

Computation of total income of Ms. Rachna for A.Y. 2014-15

Particulars	₹	₹
Business Income (Refer Note -1)		17,03,250
Capital Gain on Sale of land		
Sale consideration (Refer Note- 2)	90,00,000	
Less: Indexed Cost of Acquisition (₹ 6,00,000 × 939/426) (Refer Note – 3)	13,22,535	<u>76,77,465</u>
Gross Total Income		93,80,715
Less: Deduction under Chapter VI-A		
Section 80CCC		
Contribution to approved pension fund	20,000	
Section 80D		
Medical insurance premium paid for self and spouse ₹ 25,000, deduction limited to ₹ 15,000	15,000	
Section 80E		
Interest paid on education loan for studies of son	<u>20,000</u>	<u>55,000</u>
Total Income		<u>93,25,715</u>

Computation of tax liability of Ms. Rachna for the Assessment Year 2014-15

Particulars	₹	₹
Agricultural income (Profit from nursery business)	4,00,000	

8.19 Income-tax

Non-agricultural income		<u>93,25,715</u>	
		<u>97,25,715</u>	
Step 1 Tax on ₹ 97,25,715 (aggregate of agricultural and non-agricultural income)			
Long term Capital Gain (₹ 76,77,465 x 20%)		15,35,493	
Tax on balance income of ₹ 20,48,250		<u>4,44,475</u>	19,79,968
Step -2 Tax on ₹ 6,00,000 (aggregate of agricultural income and basic exemption limit of ₹ 2,00,000)			50,000
Step-3 Tax on non-agricultural income (Difference of step 1 & Step 2)			19,29,968
<i>Add:</i> Education Cess @ 2%			38,599
<i>Add:</i> Secondary and Higher Education Cess @1%			<u>19,300</u>
Total Tax Liability			<u>19,87,867</u>

Notes:

(1) Computation of Business Income

Trading Account for the year ended 31.03.2014

Particulars	₹	Particulars	₹
To Purchases (₹ 80 lacs - ₹ 30 lacs + ₹ 70 lacs)	1,20,00,000	By Sales	1,00,00,000
To Gross Profit	<u>20,00,000</u>	By Closing stock (Assuming Market value is less than cost of shares)	<u>40,00,000</u>
	<u>1,40,00,000</u>		<u>1,40,00,000</u>

Particulars	₹	₹
Gross Profit as per Trading Account		20,00,000
<i>Less:</i> Expenses on net connectivity	20,000	
Salary	2,00,000	
Rent (₹ 2,500 x 6)	15,000	
Depreciation on Computers (₹ 60,000×60%×50%) (Assuming used for less than 180 days in the year)	<u>18,000</u>	<u>2,53,000</u>
		17,47,000
<i>Less:</i> Contribution to Scientific Research Institution under section 35(1) (₹ 25,000 x 175%)		<u>43,750</u>
Business Income		<u>17,03,250</u>

(2) **Computation of consideration on sale of land**

Particulars	₹
Value of cash received	20,00,000
Market value of shares received	<u>70,00,000</u>
Total Sale consideration	<u>90,00,000</u>

- (3) Since the property was acquired by Ms. Rachna by way of gift, the cost of acquisition will be cost to the previous owner.

As per the definition of indexation cost of acquisition under clause (iii) of *Explanation* below section 48, indexation benefit will be available only from the previous year in which Rachna first held the asset i.e. P.Y. 2001-02.

However, as per the view expressed by Bombay High court, in the case of *CIT v. Manjula J. Shah 16 Taxmann 42*, in case the cost of acquisition of the capital asset in the hands of the assessee is taken to be cost of such asset in the hands of the previous owner, the indexation benefit would be available from the year in which the capital asset is acquired by the previous owner. If this view is taken, the indexation cost of acquisition would be ₹ 28,31,156 and long term capital gain would be ₹ 61,68,844.

- (4) Deduction under section 80C is not provided in respect of ₹ 5 lacs subscription to equity shares forming part of eligible issue of capital by a public company, assuming it has been sold in the current year.
- (5) Repayment of principal portion of education loan does not qualify for deduction under Section 80E.
- (6) Income from seedlings grown in nursery is exempt under section 10(1) as it is agricultural income. However, the same would be aggregated for rate purposes.

Question 7

Mrs. Deepali (aged 40 years), working with M/s Good Company Ltd., a manufacturer of tyres based at Mumbai, has received the following payments during the financial year 2013-14 from her employer:

Basic salary ₹ 60,000 per month.

Dearness allowance 40% of basic salary.

Her employer has taken on rent her own house on a monthly rent of ₹ 15,000 and the same has been provided for residence of Mrs. Deepali. Company is recovering ₹ 2,000 per month as rent of house.

Mrs. Deepali has further furnished the following details:

- (i) *She has paid professional tax of ₹ 6,000 during financial year 2013-14.*

8.21 Income-tax

- (ii) She is owning only one house and payment of interest of ₹ 1,75,000 and principal of ₹ 1,00,000 was made for housing loan taken for purchase of house.
- (iii) She has also taken a loan of ₹ 2,00,000 from her employer for study of her son. SBI rate for such loan is 10%. Her employer has recovered ₹ 10,000 as interest from her salary for such loan during the year.

Compute taxable income and tax liability for assessment year 2014-15.

Answer

Computation of taxable income of Mrs. Deepali for A.Y. 2014-15

Particulars	₹	₹
Income from Salaries		
Basic salary (₹ 60,000 x 12)		7,20,000
Dearness Allowance (40% of basic salary)		2,88,000
Perquisite value of Concessional Accommodation taken on hire.	1,08,000	
Lower of:		
(i) actual rent (₹ 15,000 x 12)	₹ 1,80,000	
(ii) 15% of salary (15% of ₹ 7,20,000)	₹ 1,08,000	
(assuming that dearness allowance does not form part of pay for retirement benefits)		
Less: Rent recovered (₹ 2,000 x 12)	<u>24,000</u>	84,000
Perquisite value of concessional loan [Rule 3(7)(i)] [₹ 20,000 (10% of ₹ 2,00,000) – ₹ 10,000]		<u>10,000</u>
Gross Salary		11,02,000
Less: Deduction under section 16(iii) - Professional tax paid		<u>6,000</u>
Net Salary		10,96,000
Income from house property		
Gross Annual Value (GAV) (Rental income has been taken as GAV in the absence of other information)	1,80,000	
Less: Deduction under section 24		
(a) 30% of ₹ 1,80,000	= ₹ 54,000	
(b) Interest on loan	= ₹ <u>1,75,000</u>	
	<u>2,29,000</u>	<u>(49,000)</u>
Gross Total Income		10,47,000
Less: Deductions under Chapter – VIA		
80C – Repayment of housing loan		<u>1,00,000</u>
Total Income		<u>9,47,000</u>

Computation of tax liability for A.Y. 2014-15

Tax on ₹ 9,47,000	₹
Upto ₹ 2,00,000	Nil
200,001 -5,00,000 - 10%	30,000
5,00,001 – 9,47,000 - 20%	<u>89,400</u>
	1,19,400
<i>Add:</i> Education cess @ 2%	2,388
Secondary and higher education cess @ 1%	<u>1,194</u>
Total Tax Liability	<u>1,22,982</u>
Total Tax Liability (Rounded off)	1,22,980

Note: Mrs. Deepali cannot claim benefit of self-occupation (i.e. taking the annual value as nil and claiming a higher loss of ₹ 1,50,000) in respect of the house property owned and occupied by her, since the same has been given on rent to her employer, who has allotted the same as residence for Mrs. Deepali.

Question 8

Shri Madan (age 61 years) gifted a building owned by him to his son's wife Smt. Hema on 01.10.2013. The building fetched a rental income of ₹ 10,000 per month throughout the year. Municipal tax for the first half-year of ₹ 5,000 was paid in June 2013 and the municipal tax for the second half-year was not paid till 30.09.2014.

Incomes of Shri Madan and Smt. Hema other than income from house property are given below:

Name	Business income (₹)	Capital gain (₹)	Other sources (₹)
Shri Madan	1,00,000	50,000 (long term)	1,50,000
Smt. Hema	(75,000)	2,00,000 (short term)	50,000

Note: Capital gain does not relate to gain from shares and securities.

Compute the total income of Shri. Madan and Smt. Hema taking into account income from property given above and also compute their income-tax liability for the assessment year 2014-15.

Answer

Computation of total income and tax liability of Shri Madan for A.Y. 2014-15

Particulars	₹	₹
Income from house property (Refer Note 1)		80,500
Business Income		1,00,000
Long-term Capital Gains		50,000
Income from Other Sources		<u>1,50,000</u>
Total Income		<u>3,80,500</u>

8.23 Income-tax

Computation of tax liability		
Long-term Capital Gain of ₹ 50,000 @ 20%		10,000
Other income of ₹ 3,30,500		
(₹ 3,30,500 – ₹ 2,50,000) × 10% (Refer Note 2)		<u>8,050</u>
		18,050
Less: Rebate under section 87A		<u>2,000</u>
		16,050
Add: Education Cess @ 2%	321	
Secondary and Higher Education Cess @ 1%	<u>161</u>	<u>482</u>
Tax liability		<u>16,532</u>
Tax liability (Rounded Off)		16,530

Computation of Total Income and Tax Liability of Smt. Hema for A.Y. 2014-15

Particulars	₹	₹
Short-term Capital Gains	2,00,000	
Less: Business loss	<u>75,000</u>	1,25,000
Income from Other Sources		<u>50,000</u>
Total Income		<u>1,75,000</u>
Tax liability (Since total income is less than basic exemption limit of ₹ 2,00,000)		Nil

Notes:

- As per section 64(1)(vi), the income arising to the son's wife of an individual, directly or indirectly, from assets transferred to her, otherwise than for adequate consideration, by such individual, shall be included in the total income of the individual.

Therefore, the rental income from building transferred by Shri Madan to his son's wife Smt. Hema without consideration on 01.10.2013 is includible in the hands of Shri Madan.

Computation of Income from House Property

Particulars	Madan (₹)	Hema (₹)
	Period (01.04.2013- 30.09.2014)	Period (01.10.2013- 31.03.2014)
Gross Annual Value (₹ 10,000 × 6 months) (Rental income taken as GAV in the absence of information relating to Municipal Value, fair value and standard rent)	60,000	60,000
Less: Municipal taxes paid (paid in June for first half year only)	<u>5,000</u>	<u>Nil</u>

Net Annual Value (NAV)	55,000	60,000
Less: Deduction under section 24(a), 30% of NAV	<u>16,500</u>	<u>18,000</u>
Income from House Property	38,500	<u>42,000</u>
Income from House Property of Hema to be clubbed in the hands of Madan as per section 64(1)(vi)	<u>42,000</u>	
Income from house property	<u>80,500</u>	

2. The basic exemption limit for A.Y. 2014-15 in respect of an individual who is of the age of 60 years or more during the relevant previous year is ₹ 2,50,000. The same has been considered while calculating Madan's tax liability.

Question 9

Mr. Chandran (aged 38) owned 6 heavy goods vehicles as on 01.04.2013. He acquired 2 more heavy goods vehicles on 1.7.2013. He is solely engaged in the business of plying goods vehicles on hire since financial year 2008-09.

He did not opt for presumptive provision contained in section 44AE for the financial year 2012-13. His books were audited under section 44AB and the return of income was filed on 5.8.2013. He has unabsorbed depreciation of ₹ 70,000 and business loss of ₹ 1,00,000 for the financial year 2012-13.

Following further information is provided to you:

- (i) Deposited ₹ 20,000 in Tax Saver Deposit with UCO Bank in the name of married son.*
- (ii) Paid medical insurance premium of ₹ 23,000 for his parents (both aged above 70) by means of bank demand draft.*
- (iii) Paid premium on life insurance policy of his married daughter ₹ 25,000. The policy was taken on 1.04.2012 and the minimum sum assured is ₹ 2,00,000.*
- (iv) Repaid principal of ₹ 40,000 and interest of ₹ 15,000 to Canara Bank towards education loan of his daughter, who completed B.E. two years ago. She is employed after completion of her studies.*

Assuming that Mr. Chandran has opted for presumptive provision contained in section 44AE of the Income-tax Act, 1961, compute the total income of Mr. Chandran for the assessment year 2014-15.

Answer

Computation of total income of Mr. Chandran for the A. Y. 2014-15

Particulars	₹	₹
Income from business of plying goods vehicle (Refer Note 1)		4,50,000
Less: Brought forward business loss of financial year 2012-13 (Refer Note 2 & 3)		<u>1,00,000</u>
Gross Total Income		3,50,000

<i>Less:</i> Deduction under Chapter VI-A		
Section 80C:-		
Life insurance premium paid for insurance of married daughter (Refer Note 5)	20,000	
Section 80D:-		
Medical insurance premium paid for insurance of parents (Refer Note 6)	20,000	
Section 80E:-		
Interest paid towards education loan taken for studies of his daughter (Refer Note 7)	15,000	55,000
Total Income		<u>2,95,000</u>

Working Notes:

- (1) Computation of income from business of plying goods vehicles under section 44AE.

Particulars	₹
6 heavy goods vehicle held throughout the year (₹ 5,000×6×12)	3,60,000
2 heavy goods vehicle – held for 9 months (₹ 5,000×2×9)	<u>90,000</u>
Income under section 44AE	<u>4,50,000</u>

- (2) As per section 44AE, any deduction allowable under the provisions of sections 30 to 38 shall be deemed to have been already allowed. Therefore, the unabsorbed depreciation of ₹ 70,000 shall not be allowed as a deduction since it is covered by section 32.
- (3) Brought forward business loss of ₹ 1,00,000 shall be allowed as deduction, by virtue of section 72, as it is allowed to be carried forward for 8 assessment years following the assessment year to which it relates, since the return for A.Y. 2013-14 was filed before the due date specified under section 139(1).
- (4) Fixed deposit in the name of married son does not qualify for deduction under section 80C.
- (5) Premium paid for insurance on the life of any child of the individual, whether married or not, qualifies for deduction under section 80C. In respect of policies issued on or after 1.04.2012, only premium paid to the extent of 10% of "minimum capital sum assured" qualifies for deduction under section 80C. Therefore, out of the life insurance premium of ₹ 25,000 paid for insurance policy of married daughter, only ₹ 20,000 (being 10% of ₹ 2,00,000) is allowed as deduction under section 80C.
- (6) Deduction is allowed under section 80D for payment made for medical insurance of parents. Medical insurance premium paid for insuring the health of a person who is a senior citizen i.e. of age 60 years or more, qualifies for deduction under section 80D, subject to a maximum of ₹ 20,000. Hence, deduction of ₹ 20,000 is provided to Mr. Chandran, as his parents are senior citizens.

- (7) It is only the payment of interest on education loan which qualifies for deduction under section 80E. Deduction under section 80E is allowed in respect of interest on loan taken for education of children of the individual even if they are not dependent. Principal repayment of the education loan is not eligible for deduction under section 80E.

Question 10

Mr. Vidyasagar, a resident individual aged 64, is a partner in Oscar Musicals & Co., a partnership firm. He also runs a wholesale business in medical products. The following details are made available for the year ended 31.3.2014:

Sl. No.	Particulars	₹	₹
(i)	Interest on capital received from Oscar Musicals & Co., at 15%		1,50,000
(ii)	Interest from bank on fixed deposit (Net of TDS ₹ 1,500)		13,500
(iii)	Income-tax refund received relating to assessment year 2012-13 including interest of ₹ 2,300		34,500
(iv)	Net profit from wholesale business		5,60,000
	Amounts debited include the following:		
	Depreciation as per books	34,000	
	Motor car expenses	40,000	
	Municipal taxes for the shop (For two half years; payment for one half year made on 12.6.2014 and for the other on 14.11.2014)	7,000	
	Salary to manager by way of a single cash payment	21,000	
(v)	The WDV of the assets (as on 1.4.2013) used in above wholesale business is as under:		
	Computers	1,20,000	
	Motor car (20% used for personal use)	3,20,000	
(vi)	LIP paid for major son	60,000	
	PPF of his wife	70,000	

Compute the total income of the assessee for the assessment year 2014-15. The computation should show the proper heads of income. Also compute the WDV of the different blocks of assets as on 31.3.2014.

Answer

Computation of total income of Mr. Vidyasagar for the A.Y.2014-15

Particulars	₹	₹
Profits and gains of business or profession		
Income from wholesale business		
Net profit as per books		5,60,000

8.27 Income-tax

<i>Add:</i> Depreciation as per books	34,000	
Disallowance of municipal taxes paid for the second half-year under section 43B, since the same was paid after the due date of filing of return (₹ 7,000/2)	3,500	
Disallowance under section 40A(3) in respect of salary paid in cash since the same exceeds ₹ 20,000	21,000	
20% of car expenses for personal use	<u>8,000</u>	<u>66,500</u>
		6,26,500
<i>Less:</i> Depreciation allowable (Note 1)		<u>1,10,400</u>
		5,16,100
Income from firm		
Interest on capital from partnership firm (Note 2)		<u>1,20,000</u>
		6,36,100
Income from other sources		
Interest on bank fixed deposit (Gross)	15,000	
Interest on income-tax refund	<u>2,300</u>	<u>17,300</u>
Gross total income		6,53,400
<i>Less:</i> Deduction under Chapter VIA (Note 3)		<u>1,00,000</u>
Total Income		<u>5,53,400</u>

Notes:

(1) Depreciation allowable under the Income-tax Rules, 1962

	Opening WDV	Rate	Depre- ciation	Closing WDV
Block 1 Computers	1,20,000	60%	72,000	48,000
Block 2 Motor Car	3,20,000	15%		
			48,000	
<i>Less:</i> 20% disallowance for personal use			<u>9,600</u>	
			<u>38,400</u>	2,81,600
			<u>1,10,400</u>	

(2) Only to the extent the interest is allowed as deduction in the hands of the firm, the same is includible as business income in the hands of the partner. Maximum interest allowable as deduction in the hands of the firm is 12% p.a. It is assumed that the partnership deed provides for the same and hence is allowable to this extent in the hands of the firm. Therefore, interest @12% p.a. amounting to ₹ 1,20,000 would be treated as the business income of Mr. Vidyasagar.

(3) Deduction under Chapter VI-A

Particulars	₹	₹
Under section 80C		
LIP for major son	60,000	

PPF paid in wife's name	70,000	
	1,30,000	
As per section 80CCE, deduction is restricted to		<u>1,00,000</u>
Total deduction		<u>1,00,000</u>

Question 11

Balamurugan furnishes the following information for the year ended 31-03-2014:

Particulars	₹
<i>Income from business</i>	<i>(1,35,000)</i>
<i>Income from house property</i>	<i>(15,000)</i>
<i>Lottery winning (Gross)</i>	<i>5,00,000</i>
<i>Speculation business income</i>	<i>1,00,000</i>
<i>Income by way of salary</i>	<i>60,000</i>
<i>Long term capital gain</i>	<i>70,000</i>

Compute his total income, tax liability and advance tax obligations.

Answer

Computation of total income of Balamurugan for the year ended 31.03.2014

Particulars	₹	₹
Salaries	60,000	
<i>Less: Loss from house property</i>	<u><i>(15,000)</i></u>	
Net Salary (after set off of loss from house property)		45,000
Profits and gains of business or profession		
Speculation business income	1,00,000	
<i>Less: Business loss set-off</i>	<u><i>(1,35,000)</i></u>	
Net business loss to be set-off against long-term capital gain	<i>(35,000)</i>	
Capital Gains		
Long term capital gain	70,000	
<i>Less: Business loss set-off</i>	<u><i>(35,000)</i></u>	
Long term capital gain after set off of business loss		35,000
Income from other sources		
Lottery winnings (Gross)		<u>5,00,000</u>
Total Income		<u>5,80,000</u>

Computation of tax liability

Particulars	₹
On total income of ₹ 80,000 (excluding lottery winning)	Nil

8.29 Income-tax

On lottery winnings of ₹ 5,00,000 @ 30%	1,50,000
Add: Education Cess @ 2% and Secondary and higher education cess@1%	<u>4,500</u>
Total tax liability	<u>1,54,500</u>

The assessee need not pay advance tax since the total income (excluding lottery income) liable to tax is below the basic exemption limit. Further, in respect of lottery income, tax would have been deducted at source @ 30% under section 194B. Since the remaining tax liability of ₹ 4,500 (₹ 1,54,500 – ₹ 1,50,000) is less than ₹ 10,000, advance tax liability is not attracted.

Notes:

- (1) The basic exemption limit of ₹ 2,00,000 has to be first exhausted against salary income of ₹ 45,000. The unexhausted basic exemption limit of ₹ 1,55,000 can be adjusted against long-term capital gains of ₹ 35,000 as per section 112, but not against lottery winnings which are taxable at a flat rate of 30% under section 115BB.
- (2) The first proviso to section 234C(1) provides that since it is not possible for the assessee to estimate his income from lotteries, the entire amount of tax payable (after considering TDS) on such income should be paid in the remaining installments of advance tax which are due. Where no such installment is due, the entire tax should be paid by 31st March, 2014. The first proviso to section 234C(1) would be attracted only in case of non-deduction or short-deduction of tax at source under section 194B.

Question 12

Mr. Rajiv, aged 50 years, a resident individual and practicing Chartered Accountant, furnishes you the receipts and payments account for the financial year 2013-14.

Receipts and Payments Account

<i>Receipts</i>	<i>₹</i>	<i>Payments</i>	<i>₹</i>
<i>Opening balance (1.4.2013)</i>		<i>Staff salary, bonus and stipend to articled clerks</i>	<i>1,50,000</i>
<i>Cash on hand and at Bank</i>	<i>12,000</i>	<i>Other administrative expenses</i>	<i>48,000</i>
<i>Fee from professional services</i>	<i>9,38,000</i>	<i>Office rent</i>	<i>30,000</i>
<i>Rent</i>	<i>50,000</i>	<i>Housing loan repaid to SBI (includes interest of ₹ 88,000)</i>	<i>1,88,000</i>
<i>Motor car loan from Canara Bank (@ 9% p.a.)</i>	<i>2,50,000</i>	<i>Life insurance premium</i>	<i>24,000</i>
		<i>Motor car (acquired in Jan. 2014)</i>	<i>4,25,000</i>
		<i>Medical insurance premium (for self and wife)</i>	<i>18,000</i>
		<i>Books bought (annual publications)</i>	<i>20,000</i>

	<i>Computer acquired on 1.11.2013 (for professional use)</i>	30,000
	<i>Domestic drawings</i>	2,72,000
	<i>Public provident fund subscription</i>	20,000
	<i>Motor car maintenance</i>	10,000
	<i>Closing balance (31.3.2014)</i>	15,000
	<i>Cash on hand and at Bank</i>	
	<u>12,50,000</u>	<u>12,50,000</u>

Following further information is given to you:

- (1) He occupies 50% of the building for own residence and let out the balance for residential use at a monthly rent of ₹ 5,000. The building was constructed during the year 1997-98.
- (2) Motor car was put to use both for official and personal purpose. One-fifth of the motor car use is for personal purpose. No car loan interest was paid during the year.
- (3) The written down value of assets as on 1-4-2013 are given below:

<i>Furniture & Fittings</i>	= ₹ 60,000
<i>Plant & Machinery</i>	= ₹ 80,000
<i>(Air-conditioners, Photocopiers, etc.)</i>	
<i>Computers</i>	= ₹ 50,000

Note: Mr. Rajiv follows regularly the cash system of accounting.

Compute the total income of Mr. Rajiv for the assessment year 2014-15.

Answer

Computation of total income of Mr. Rajiv for the assessment year 2014-15

Particulars	₹	₹	₹
Income from house property			
Self-occupied			
Annual value	Nil		
<i>Less: Deduction under section 24(b)</i>			
Interest on housing loan			
50% of ₹ 88,000 = 44,000 but limited to	<u>30,000</u>		
Loss from self occupied property		(30,000)	
Let out property			
Annual value (Rent receivable has been taken as the annual value in the absence of other information)	60,000		

8.31 Income-tax

<i>Less:</i> Deductions under section 24				
(a)	30% of Net Annual Value	18,000		
(b)	Interest on housing loan (50% of ₹ 88,000)	<u>44,000</u>	<u>62,000</u>	<u>(2,000)</u>
Loss from house property				(32,000)
Profits and gains of business or profession				
Fees from professional services			9,38,000	
Less: Expenses allowable as deduction				
Staff salary, bonus and stipend		1,50,000		
Other administrative expenses		48,000		
Office rent		30,000		
Motor car maintenance (10,000 x 4/5)		8,000		
Car loan interest – not allowable (since the same has not been paid and the assessee follows cash system of accounting)		<u>Nil</u>	<u>2,36,000</u>	
			7,02,000	
Less: Depreciation				
Motor car ₹ 4,25,000 x 7.5% x 4/5		25,500		
Books being annual publications @ 100%		20,000		
Furniture and fittings @ 10% of ₹ 60,000		6,000		
Plant and machinery @ 15% of ₹ 80,000		12,000		
Computer @ 60% of ₹ 50,000		30,000		
Computer (New) ₹ 30,000 @ 60% x ½ thereon		<u>9,000</u>	<u>1,02,500</u>	<u>5,99,500</u>
Gross Total income				5,67,500
Less: Deduction under Chapter VI-A				
Deduction under section 80C				
Housing loan principal repayment		1,00,000		
PPF subscription		20,000		
Life insurance premium		<u>24,000</u>		
Total ₹ 1,44,000 but limited to			1,00,000	
Deduction under section 80D				
Medical insurance premium paid ₹ 18,000 but limited to			<u>15,000</u>	<u>1,15,000</u>
Total income				<u>4,52,500</u>

Question 13

State under which heads the following incomes are taxable:

- (i) Rental income in case of dealer in property
- (ii) Dividend on shares in case of a dealer in shares
- (iii) Salary by a partner from his partnership firm
- (iv) Rental income of machinery
- (v) Winnings from lotteries by a person having the same as business activity
- (vi) Salaries payable to a Member of Parliament
- (vii) Receipts without consideration
- (viii) In case of retirement, interest on employee's contribution if provident fund is unrecognized.

Answer

	Particulars	Head of Income
(i)	Rental income in case of dealer in property	Income from house property
(ii)	Dividend on shares in case of a dealer in shares	Income from other sources
(iii)	Salary by partner from his partnership firm	Profit and gains of business or profession
(iv)	Rental income of machinery (See Note below)	Income from other sources/ Profits and gains of business or profession
(v)	Winnings from lotteries by a person having the same as business activity	Income from other sources
(vi)	Salaries payable to a Member of Parliament	Income from other sources
(vii)	Receipts without consideration	Income from other sources
(viii)	In case of retirement, interest on employee's contribution if provident fund is unrecognized	Income from other sources

Note - As per section 56(2)(ii), rental income of machinery would be chargeable to tax under the head "Income from Other Sources", if the same is not chargeable to income-tax under the head "Profits and gains of business or profession".

Question 14

Dr. Shuba is a medical practitioner. Her age is 64 as on 1st January, 2014. The receipts and payments account of 2013-14 of her is as under:

To	₹	By	₹
Balance B/f	10,000	Purchase of commercial vehicle before 30 Sep. 2013	4,00,000
Receipts from sale of medicine	2,50,000	Drawings	2,50,000

8.33 Income-tax

Consultation fee	50,000	Deposit in bank for 5 years	1,50,000
Visiting fee	2,00,000	Surgical instrument purchased	
Lecture fees	5,000	before 30 Sep. 2013	50,000
Family pension	2,80,000	Installment of loan paid	1,21,000
		(including interest ₹ 22,333)	
Savings bank interest	1,000	Medical insurance premium	32,000
Loan from bank	3,00,000	Installment of housing loan	1,08,000
		(Principal component ₹ 48,000)	
Share from HUF	50,000	Advance tax paid	20,000
Agricultural income	1,00,000	Purchase of medicine	47,000
Income from lottery	35,000	Payment for medical journal	5,000
(net after deduction of TDS@30%)		Vehicle expenses	50,000
		Balance C/f	48,000
	12,81,000		12,81,000

Other relevant information is as under:

- She resides in her own house which was constructed in 1998 with a loan from LIC Housing of ₹ 10,00,000 out of which ₹ 6,00,000 was still due. She got it refinanced from SBI on 01-04-2013 at the rate of 10%. One-fourth portion of the house is used for clinic purposes.
 - She invested in term deposit ₹ 1,50,000 in Bank of Baroda on 01-07-2013 for a period of 5 years in the name of her minor daughter at 9% interest p.a.
 - She purchased a commercial vehicle on 1st July 2013 at ₹ 4,00,000. A loan of ₹ 3,00,000 was taken to buy the vehicle. One fourth use of vehicle is estimated to be personal.
 - She paid medical insurance premium for herself of ₹ 16,000 and for mother ₹ 16,000. Her mother is dependent on her.
 - She got her share from HUF's income of ₹ 50,000.
- Compute total income of Dr. Shuba, ignoring depreciation on building.

Answer

Computation of total income of Dr. Shuba for A.Y. 2014-15

Particulars	₹	₹	₹	₹
Income from house property:				
Annual value of self-occupied house		Nil		
Less: Interest on loan [₹ 45,000, being 3/4 th of ₹ 60,000] (Restricted to ₹ 30,000)		<u>(30,000)</u>	(30,000)	
Income from profession:				
Sale of medicine	2,50,000			

Consultation fees	50,000			
Visiting fee	<u>2,00,000</u>			
Total income		5,00,000		
Less: Expenses				
Medicine purchases	47,000			
Medical journal	5,000			
Vehicle expenses (3/4 th)	37,500			
Interest on loan (3/4 th)	16,750			
Interest on housing loan (1/4 th)	15,000			
Depreciation				
Surgical instrument(15% of ₹ 50,000)	7,500			
Vehicle (3/4 th of 15% of ₹ 4,00,000)	<u>45,000</u>			
Total expenses		<u>1,73,750</u>		
			3,26,250	
Income from other sources				
Family Pension	2,80,000			
<i>Less</i> : Deduction under section 57(iia) 33 $\frac{1}{3}$ % or ₹ 15,000, whichever is lower	<u>15,000</u>	2,65,000		
Lecture fees		5,000		
Savings bank interest		1,000		
Interest on bank FD in the name of minor daughter [₹ 1,50,000 × 9% × 9/12]	10,125			
<i>Less</i> : Exempt under section 10(32)	<u>1,500</u>	8,625		
Winnings from lottery		<u>50,000</u>		
			<u>3,29,625</u>	
Gross Total Income				6,25,875
<i>Less</i> : Deductions under Chapter VI-A				
Under section 80C				
Repayment of housing loan (₹ 48,000 × $\frac{3}{4}$)			36,000	
Under section 80D				
Medical Insurance Premium				
Own (Senior Citizen, hence fully allowed)		16,000		
Mother (Senior Citizen, hence fully allowed since premium is less than ₹ 20,000)		16,000		
Under section 80TTA				
Interest on deposit in a saving account of bank		<u>1,000</u>	<u>33,000</u>	
Total deduction				<u>69,000</u>
Total income				<u>5,56,875</u>

Notes:

1. Since the residential house was constructed before 01.04.1999, the deduction for interest is restricted to ₹ 30,000.
2. Since ¼th portion of house is used for business purposes, therefore, ¼th share of interest paid is deductible while computing business income.
3. Agricultural income is exempt under section 10(1) and share of income from HUF is exempt under section 10(2).
4. Term deposit of ₹ 1,50,000 in the name of minor daughter does not qualify for deduction under section 80C. However, principal repayment of housing loan (¾th) would qualify for deduction under section 80C. Therefore, the deduction under section 80C would be ₹ 36,000 (i.e. ¾th of ₹ 48,000).
5. Depreciation@15% has been provided on surgical instruments. It is also possible to assume that the surgical instruments mentioned in the question are life-saving medical equipment (for example, surgical laser) and therefore, eligible for depreciation@40%.

Question 15

Mr. Raghu, Marketing Manager of KL Ltd., based at Mumbai furnishes you the following information for the year ended 31.03.2014:

Basic salary -	₹ 1,00,000 per month
Dearness allowance (Forming part of salary for retirement benefits) -	₹ 50,000 per month
Bonus -	2 months basic salary
Contribution of employer to Recognized Provident Fund -	15% of basic salary plus dearness allowance

Rent free unfurnished accommodation was provided by the company at Mumbai (accommodation owned by the company).

Particulars	₹
(i) Recognised Provident Fund contribution made by Raghu	1,50,000
(ii) Health insurance premium for insurance of his wife's health	20,000
(iii) Health insurance premium in respect of parents (senior citizens)	28,000
(iv) Medical expenses of dependent brother with 'severe disability' (covered by Section 2(o) of National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disabilities Act, 1999).	6,000
(v) Interest on loan taken for education of his son studying B.Com (full-time) in a recognized college.	24,000
(vi) Interest on loan taken for education of a student for whom Mr. Raghu is the legal guardian for pursuing B.Sc. (Physics) (full-time) in a recognized university.	20,000

Compute the total income of Mr. Raghu for the assessment year 2014-15.

Answer

Computation of total income of Mr. Raghu for the A.Y. 2014-15

Particulars	₹	₹
Basic salary		12,00,000
Dearness allowance		6,00,000
Bonus		2,00,000
Employer contribution to recognized provident fund in excess of 12% is taxable (3% of ₹ 18,00,000)		54,000
Rent free accommodation @ 15% of ₹ 20 lakh (basic salary + dearness allowance + bonus)		<u>3,00,000</u>
		23,54,000
Less: Deductions under Chapter VI-A		
Section 80C		
Contribution to recognized provident fund ₹ 1,50,000 restricted to	1,00,000	
Section 80D – Health insurance premium		
Wife ₹ 20,000 restricted to	15,000	
Parents (Senior Citizens) ₹ 28,000 restricted to	<u>20,000</u>	35,000
Section 80DD		
Medical treatment of dependent brother with severe disability (flat deduction irrespective of expenditure incurred)	1,00,000	
Section 80E – Interest on loan taken for full-time education of		
- his son studying B.Com.	24,000	
- a student studying B.Sc. for whom he is the legal guardian	<u>20,000</u>	<u>44,000</u>
Total income		<u>20,75,000</u>

Question 16

Determine the total income of Mr. Chand from the following information for the Assessment Year 2014-15:

Particulars	₹
(i) Interest received on enhanced compensation (It relates to transfer of land in the financial year 2008-09. Out of the above, ₹ 65,000 relates to financial year 2013-14 and the balance relate to preceding years)	4,00,000
(ii) Business loss relating to discontinued business of the assessment year 2008-09 brought forward and eligible for set off	1,50,000

8.37 Income-tax

(iii) Current year business income (i.e. financial year 2013-14) (computed)	1,10,000
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Answer

Computation of total income of Mr. Chand for A.Y.2014-15

Particulars	₹	₹
Profits and gains of business or profession		
Current year business income	1,10,000	
Less: Brought forward business loss of discontinued business ₹ 1,50,000 set-off to the extent of current year business income as per section 72	<u>1,10,000</u>	Nil
Income from other sources		
Interest on enhanced compensation taxable on receipt basis under section 56(2)(viii)	4,00,000	
Less: Deduction under section 57(iv) @ 50%	<u>2,00,000</u>	<u>2,00,000</u>
Total Income		<u>2,00,000</u>

The unabsorbed business loss of ₹ 40,000 (₹ 1,50,000 – ₹ 1,10,000) of A.Y.2008-09 relating to discontinued business will be carried forward for set-off against income from any business in the next year i.e. A.Y.2015-16.

Question 17

Mr. Dinesh Karthik, a resident individual aged 45, furnishes the following information pertaining to the year ended 31.3.2014:

- (i) He is a partner in Badrinath & Co. He has received the following amounts from the firm:
Interest on capital at 15% : ₹ 3,00,000
Salary as working partner (at 1% of firm's sales) (allowed fully to the firm) : ₹ 90,000
- (ii) He is engaged in a business of manufacturing wheat flour from wheat. The Profit and Loss account pertaining to this business (summarised form) is as under:

To	₹	By	₹
Salaries	1,20,000	Gross profit	12,50,000
Bonus	48,000	Interest on Bank FD	45,000
Car expenses	50,000	(Net of TDS 5,000)	
Machinery repairs	2,34,000	Agricultural income	60,000
Advance tax	70,000	Pension from LIC	
		Jeevan Dhara	24,000

<i>Depreciation on:</i>		
- Car	3,00,000	
- Machinery	1,25,000	
<i>Net profit</i>	<u>4,32,000</u>	
	<u>13,79,000</u>	<u>13,79,000</u>

Opening WDV of assets are as under:

<i>Particulars</i>	<i>₹</i>
<i>Car</i>	3,00,000
<i>Machinery (Used during the year for 170 days)</i>	6,50,000
<i>Additions to machinery:</i>	
<i>New purchased on 23.9.2013</i>	2,00,000
<i>New purchased on 12.11.2013</i>	3,00,000
<i>Old purchased on 12.4.2013</i>	1,25,000

(All assets added during the year were put to use immediately after purchase)

Of the total bonus amount, ₹ 15,000 was paid on 11.10.2013.

One-fifth of the car expenses are towards estimated personal use of the assessee.

- (iii) *In March, 2012, he had sold a house at Chennai. Arrears of rent relating to this house amounting to ₹ 75,000 was received in February, 2014.*
- (iv) *Details of his Savings and Investments are as under:*

<i>Particulars</i>	<i>₹</i>
<i>Life insurance premium for policy in the name of his major son employed in LMN Ltd. at a salary of ₹ 6 lacs p.a. (Sum assured ₹ 2,00,000) (Policy taken on 1.07.2013)</i>	50,000
<i>Contribution to Pension Fund of National Housing Bank (This was met partially from out of premature withdrawal of deposit in Post Office Time Deposit made on 12.3.2006 Principal component ₹ 55,000 and Interest ₹ 5,000)</i>	70,000
<i>Medical Insurance premium for his father aged 70, who is not dependent on him</i>	22,000

You are required to compute the total income of Mr. Dinesh Karthik for the assessment year 2014-15.

Answer

Computation of total income of Mr. Dinesh Karthik for the A.Y. 2014-15

Particulars		₹	₹
Income from house property			
Arrears of rent received in respect of the Chennai house taxable under section 25B	Note 2	75,000	
Less: Deduction @ 30%		<u>22,500</u>	52,500
Profits and gains of business or profession			
(a) Own business	Note 3		5,33,250
(b) Income from partnership firm (See Note 1)			
Interest on capital		2,40,000	
[As per section 28(v), chargeable in the hands of the partner only to the extent allowable as deduction in the firm's hand i.e. @12%]			
Salary of working partner		<u>90,000</u>	3,30,000
Income from other sources			
(a) LIC Jeevan Dhara pension		24,000	
(b) Interest from bank FD (gross)		<u>50,000</u>	<u>74,000</u>
Gross Total Income			9,89,750
Less: Deductions under Chapter VIA			
Section 80C			
Life insurance premium for policy in the name of major son qualifies for deduction even though he is not dependent on the assessee. However, the same has to be restricted to 10% of sum assured i.e. 10% of ₹ 2,00,000.	20,000		
Contribution to pension fund of National Housing Bank	<u>70,000</u>	90,000	
Section 80D			
Mediclaim premium for father, a senior citizen (qualifies for deduction, even though the father is not dependent on the assessee)	22,000		
Maximum amount allowable		<u>20,000</u>	<u>1,10,000</u>
Total Income			<u>8,79,750</u>

Notes:

- (1) The income by way of interest on capital and salary of Mr. Dinesh Karthik from the firm, Badrinath & Co., in which he is a partner, to the extent allowed as deduction in the hands of the firm under section 40(b), has to be included in the business income of the partner as per section 28(v). Accordingly, ₹ 3,30,000 [i.e., ₹ 90,000 (salary) + ₹ 2,40,000 (interest@12%)] should be included in his business income.

(2) As per section 25B, any arrears of rent received will be chargeable to tax, after deducting a sum equal to 30% of such arrears, as income from house property in the year of receipt, whether or not the assessee remains the owner of the house property.

(3) **Computation of income from own business**

Particulars	₹	₹
Net profit as per profit and loss account		4,32,000
<i>Less:</i> Items credited to profit and loss account not treated as business income		
Interest on bank FD (net of TDS ₹ 5,000)	45,000	
Agricultural income	60,000	
Pension from LIC Jeevan Dhara	<u>24,000</u>	<u>1,29,000</u>
		3,03,000
<i>Add:</i> Items debited to profit and loss account to be disallowed/considered separately		
Advance tax	70,000	
Depreciation:		
Car	3,00,000	
Machinery	1,25,000	
Car expenses disallowed	<u>10,000</u>	<u>5,05,000</u>
		<u>8,08,000</u>
<i>Less:</i> Depreciation (See Working Note below)		<u>2,74,750</u>
Income from own business		<u>5,33,250</u>

Working Note

Computation of depreciation allowable under the Income-tax Act, 1961

Particulars	₹	₹
On Car-		
15% on 3,00,000	45,000	
<i>Less:</i> 1/5 th for personal use	<u>9,000</u>	36,000
On Machinery-		
Opening WDV	6,50,000	
Additions during the year (Used for more than 180 days)	<u>3,25,000</u>	
Depreciation at 15% on	9,75,000	1,46,250
Additions during the year (used for less than 180 days)		
Hence, depreciation at 7.5% on	3,00,000	<u>22,500</u>
Total normal depreciation (A)		2,04,750

Where an asset acquired during the year is put to use for less than 180 days, 50% of the rate of depreciation is allowable. This restriction does not apply to assets acquired in an earlier year.		
Additional depreciation		
New machinery		
Used for more than 180 days at 20%	₹ 2,00,000	40,000
Used for less than 180 days at 10%	₹ 3,00,000	<u>30,000</u>
Total additional depreciation (B)		<u>70,000</u>
Total permissible depreciation (A) + (B)		<u>2,74,750</u>

(4) Withdrawal from Post Office Time Deposit

The deduction under section 80C is allowable in respect of any sum deposited in a five year time deposit in an account under Post Office Time Deposit Rules, 1981 w.e.f. A.Y.2008-09. Clause (xxiv) was inserted by the Finance Act, 2008 in section 80C(2) providing this deduction with effect from A.Y.2008-09. Simultaneously, sub-section (6A) was inserted in section 80C w.e.f. A.Y.2008-09 to bring to tax pre-mature withdrawal (before five years) of the amount so deposited and interest thereon. In the question, it is clearly mentioned that the deposit was made on 12.3.2006. Therefore, no deduction under section 80C would have been allowable in the P.Y.2005-06 in respect of such deposit, since clause (xxiv) providing for deduction was inserted by the Finance Act, 2008 only w.e.f. A.Y.2008-09. Consequently, sub-section (6A) bringing to tax the withdrawal would not apply in respect of such deposit for which no deduction was allowed under section 80C.

Question 18

From the following details, compute the total income of Siddhant of Delhi and tax payable for the A.Y.2014-15:

<i>Particulars</i>	<i>₹</i>
<i>Salary including dearness allowance</i>	<i>3,35,000</i>
<i>Bonus</i>	<i>11,000</i>
<i>Salary of servant provided by the employer</i>	<i>12,000</i>
<i>Rent paid by Siddhant for his accommodation</i>	<i>49,600</i>
<i>Bills paid by the employer for gas, electricity and water provided free of cost at the above flat</i>	<i>11,000</i>

Siddhant purchased a flat in a co-operative housing society in Delhi for ₹ 4,75,000 in April, 2008, which was financed by a loan from Life Insurance Corporation of India of ₹ 1,60,000 @ 15% interest, his own savings of ₹ 65,000 and a deposit from a nationalized bank for

₹ 2,50,000 to whom this flat was given on lease for ten years. The rent payable by the bank was ₹ 3,500 per month. The following particulars are relevant:

- (a) Municipal taxes paid by Mr. Siddhant ₹ 4,300 (per annum)
- (b) Insurance ₹ 860
- (c) He earned ₹ 2,700 in share speculation business and lost ₹ 4,200 in cotton speculation business.
- (d) In the year 2008-09, he had gifted ₹ 30,000 to his wife and ₹ 20,000 to his son who was aged 11. The gifted amounts were advanced to Mr. Rajesh, who was paying interest @ 19% per annum.
- (e) Siddhant received a gift of ₹ 25,000 each from four friends.
- (f) He contributed ₹ 5,600 to Public Provident Fund and ₹ 4,000 to Unit Linked Insurance Plan.
- (g) He received national award for humanitarian work from the Central Government in the form of a land whose fair market value is ₹ 5,00,000 as on 31st March, 2014.

Answer

Computation of total income and tax liability of Siddhant for the A.Y. 2014-15

Particulars	₹	₹
Salary Income		
Salary including dearness allowance		3,35,000
Bonus		11,000
Value of perquisites:		
(i) Salary of servant	12,000	
(ii) Free gas, electricity and water	<u>11,000</u>	<u>23,000</u>
		3,69,000
Income from house property		
Gross Annual Value (GAV) (Rent receivable is taken as GAV in the absence of other information) (₹ 3,500 × 12)	42,000	
Less: Municipal taxes paid	<u>4,300</u>	
Net Annual Value (NAV)	37,700	
Less: Deductions under section 24		
(i) 30% of NAV	₹ 11,310	
(ii) Interest on loan from LIC @15% of ₹ 1,60,000 [See Note 2]	₹ <u>24,000</u>	2,390
Income from speculative business		
Income from share speculation business	2,700	

8.43 Income-tax

Less: Loss from cotton speculation business	4,200	
Net Loss	<u>1,500</u>	
Net loss from speculative business has to be carried forward as it cannot be set off against any other head of income.		
Income from Other Sources		
(i) Income on account of interest earned from advancing money gifted to his minor son is includible in the hands of Siddhant as per section 64(1A)	3,800	
Less: Exempt under section 10(32)	<u>1,500</u>	
	2,300	
(ii) Interest income earned from advancing money gifted to wife has to be clubbed with the income of the assessee as per section 64(1)	5,700	
(iii) Gift received from four friends (taxable under section 56(2)(vii) as the aggregate amount received during the year exceeds ₹ 50,000)	<u>1,00,000</u>	<u>1,08,000</u>
Gross Total Income		4,79,390
Less: Deduction under section 80C		
Contribution to Public Provident Fund	5,600	
Unit Linked Insurance Plan	<u>4,000</u>	<u>9,600</u>
Total Income		4,69,790

Particulars	₹
Tax on total income	26,979
Less: Rebate under section 87A	2,000
	<u>24,979</u>
Add: Education cess@2%	500
Add: Secondary and higher education cess@1%	<u>250</u>
	<u>25,729</u>
Tax liability (rounded off)	25,730

Notes:

- (1) National Award for humanitarian work given by the Central Government is exempt under section 10(17A) of the Income-tax Act, 1961.
- (2) It is assumed that the entire loan of ₹ 1,60,000 is outstanding as on 31.3.2014; and
- (3) Since Siddhant's own flat in a co-operative housing society, which he has rented out to a nationalised bank, is also in Delhi, he is not eligible for deduction under section 80GG in

respect of rent paid by him for his accommodation in Delhi, since one of the conditions to be satisfied for claiming deduction under section 80GG is that the assessee should not own any residential accommodation in the same place.

Question 19

Mr. Janak, working as Finance Manager in Thilagam Realty Ltd., Jaipur, retired from the company on 31.10.2013 at the age of 60. The following amounts were received from the employer from 1st April, 2013 to 31st October, 2013:

<i>Basic Salary</i>	<i>₹ 30,000 p.m.</i>
<i>Dearness Allowance</i>	<i>₹ 20,000 p.m. (40% reckoned for superannuation benefits)</i>
<i>Ex-gratia (lump sum)</i>	<i>₹ 15,000</i>

In addition to the above –

- (i) The company had taken on lease a residential house at Jaipur, paying a lease rent of ₹ 9,000 p.m. Mr. Janak, who was paying to the company ₹ 6,000 p.m. towards aforesaid rent, vacated the said premises on 31.10.2013.*
- (ii) The company had also provided to Mr. Janak a cooking range and micro-wave oven owned by it. The original cost of these assets was ₹ 40,000 and the written down value as on 1.4.2013 was ₹ 22,000.*
- (iii) Mr. Janak has two sons. His second son was studying in a school run by the employer-company throughout the financial year 2013-14. The education facility was provided free of cost. The cost of such education in a similar school is ₹ 1,800 p.m.*
- (iv) The employer-company was contributing ₹ 7,000 p.m. to Central Government Pension Scheme. Mr Janak contributed an equal amount.*
- (v) Professional tax paid by the employer ₹ 3,000.*
- (vi) Subsequent to his retirement, Mr. Janak started his own business on 15-11-2013. The results of the said business from 15.11.2013 to 31.3.2014 were:*

<i>(i) Business loss (excluding current depreciation)</i>	<i>₹ 90,000</i>
<i>(ii) Current year's depreciation</i>	<i>₹ 60,000</i>
- (vii) Mr. Janak won a prize in a TV game show. He received a sum of ₹ 42,000 after deduction of tax at source to the tune of ₹ 18,000.*
- (viii) Mr. Janak furnishes the under-mentioned data relating to savings, investments and out-goings :*
 - A. Life insurance premium, with a private insurance company ₹ 30,000 for his son and ₹ 20,000 for his married daughter.*
 - B. Medical insurance premium of ₹ 12,000 for himself and ₹ 16,000 for his father (aged 82), paid by credit card. His father is however not dependent on him.*

8.45 Income-tax

You are required to compute the total income of Mr. Janak (showing clearly the computation under various heads of income) and tax payable by him for the assessment year 2014-15.

Answer

Computation of total income of Mr. Janak for A.Y. 2014-15

Particulars	₹	₹
Basic salary = ₹ 30,000 x 7	2,10,000	
Dearness Allowance = ₹ 20,000 x 7	1,40,000	
Ex-gratia	15,000	
Employers' contribution to Central Government Pension Scheme = ₹ 7,000 x 7	49,000	
Professional tax paid by employer	3,000	
Concessional accommodation (See Notes 1 & 2)	150	
Value of furniture (See Note 3)	2,333	
Value of concessional educational facility = (₹ 1,800 x 7) (See Note 4)	<u>12,600</u>	
Gross salary	4,32,083	
Less : Deduction under section 16(iii)		
Professional tax	<u>3,000</u>	
Net salary		4,29,083
Income from other sources		
Winnings from TV Game Show (₹ 42,000 + ₹ 18,000)		<u>60,000</u>
Gross Total Income		4,89,083
Less : Deductions under Chapter VI-A		
80C Life insurance premium (₹ 30,000 + ₹ 20,000)	50,000	
80CCD(1) (See Notes 5)		
Employee's contribution to pension scheme (to be restricted to 10% of salary)	<u>26,600</u>	
Salary = (₹ 30,000 + ₹ 8,000) × 7 = ₹ 2,66,000		
Total deduction under section 80C & 80CCD(1)	76,600	
Employer's Contribution to pension scheme(to be restricted to 10% of salary) [Section 80CCD(2)] [See Note 5]	26,600	
80D (₹ 12,000 + ₹ 16,000) (See Note 6)	<u>28,000</u>	<u>1,31,200</u>
Total Income		<u>3,57,883</u>
Total income (rounded off)		3,57,880

Computation of tax liability of Mr. Janak for the A.Y. 2014-15

Particulars	₹	₹
Tax @ 30% on winnings of ₹ 60,000 from game show		18,000
Tax on balance income of ₹ 2,97,880 (See Note 8)		4,788
		22,788
Less: Rebate under section 87A		2,000
		20,788
<i>Add</i> : Education cess @ 2%	416	
Secondary and higher education cess @ 1%	208	624
Total Tax Liability		21,412
Less : TDS		18,000
Net Tax Payable		3,412

Notes:

- (1) For computation of perquisite value of concessional accommodation, 40% of dearness allowance (i.e. ₹ 8,000) should be taken into consideration as forming part of salary, since the question clearly mentions that only 40% is to be reckoned for superannuation benefits. Therefore, salary for the purpose of perquisite valuation would be ₹ 2,81,000 [i.e., (₹ 30,000 + ₹ 8,000) x 7 + 15,000].
- (2) In a case where the accommodation is taken on lease or rent by the employer and provided to the employee, the value of perquisite would be lower of the actual amount of lease rental paid or payable by the employer [i.e. ₹ 63,000, being 9,000 x 7] and 15% of salary [i.e., ₹ 42,150, being 15% of ₹ 2,81,000]. This value (i.e. ₹ 42,150) would be reduced by the rent paid by the employee (i.e., ₹ 42,000, being 6,000 x 7).
The value of concessional accommodation is ₹ 150 [i.e. ₹ 42,150 – ₹ 42,000].
- (3) The value of furniture owned by employer and provided to the employee is 10% p.a. of actual cost which amounts to ₹ 2,333 [i.e. 10% of 40,000 x 7/12].
Therefore, the value of furnished accommodation will be ₹ 2,483 (₹ 150 + ₹ 2,333) provided to the employee.
It is also possible to consider the cooking range and micro-wave oven provided by employer to the employee as a perquisite on account of use of movable assets of the employer by the employee. Even it is so assumed, there would be no change in the answer since in such a case also, the perquisite value is 10% p.a. of actual cost.
- (4) In determining the value of perquisite resulting from the provision of free or concessional educational facilities, from a plain reading of the proviso to Rule 3(5), it is apparent that if

the cost of education per child exceeds ₹ 1,000 per month, the entire cost will be taken as the value of the perquisite. Accordingly, the full amount of ₹ 1,800 per month is taxable as perquisite. In such a case, the value of the perquisite would be ₹ 12,600 (i.e. ₹ 1,800 × 7).

Note – An alternate view possible is that only the sum in excess of ₹ 1,000 per month is taxable. In such a case, the value of perquisite would be ₹ 5,600. The gross salary in that case shall be ₹ 4,25,083 and net salary would be ₹ 4,22,083. The total income and tax liability shall accordingly vary.

- (5) The entire employer's contribution to Central Government Pension scheme should be included in salary and deduction under section 80CCD(2) should be restricted to 10% of salary. The employer's contribution to pension scheme would be outside the overall limit of ₹ 1 lakh stipulated under section 80CCE. Also, the deduction for the employee's contribution to the pension scheme is restricted to 10% of salary. Salary means basic salary and dearness allowance, if provided in the terms of employment for retirement benefits.
- (6) The deduction for medical insurance premium of ₹ 16,000 paid for father is allowable in full under section 80D, as the maximum limit is ₹ 20,000, since his father is a senior citizen. Therefore, the total deduction under section 80D would be ₹ 12,000 (for self) + ₹ 16,000 (for father) = ₹ 28,000.
- (7) Winnings from TV game show is chargeable at a flat rate of 30% under section 115BB. No loss can be set-off against such income. Therefore, business loss cannot be set-off against such income.
- (8) As per section 71(2A), business loss cannot be set-off against salary income. Section 71(2A) provides that where the net result of the computation under the head "Profits and gains of business or profession" is a loss and the assessee has income chargeable under the head "Salaries", the assessee shall not be entitled to have such loss set-off against such income. From a plain reading of the provisions of section 71(2A), it is possible to take a view that even depreciation cannot be set-off against salary income. Therefore, both business loss and current depreciation cannot be set-off against salary income.

Question 20

Mr. Mahesh, a production manager working in ABC Ltd., New Delhi, receives the following emoluments during the previous year 2013-14:

	₹		₹
<i>Basic salary</i>	<i>1,75,000</i>	<i>Bonus</i>	<i>8,000</i>
<i>D.A. (not forming part of salary)</i>	<i>1,40,000</i>	<i>Medical allowance</i>	<i>5,000</i>
<i>Commission on extra production</i>	<i>12,000</i>	<i>Special allowance</i>	<i>18,000</i>

Education Allowance (including allowance for hostel expenditure) for two sons who are engineering students at Mumbai - ₹ 16,000.

- (i) His employer has provided rent free house to him in New Delhi. The house is owned by the employer.
- (ii) Electricity bills paid by ABC Ltd. for him during the previous year are of ₹ 11,500.
- (iii) On 1.1.2014, his employer company has given him a CD player for domestic use and a laptop for office and personal use. Ownership of both the assets have not been transferred. The cost of CD player is ₹ 20,000 and that of laptop is ₹ 40,000.
- (iv) His investments during the previous year are:
- | | |
|--------------------------|----------|
| (1) Notified mutual fund | ₹ 25,000 |
| (2) PPF | ₹ 15,000 |
- (v) He has paid tuition fees of his sons on 17.12.2013 of ₹ 60,000.
- (vi) He has deposited ₹ 10,000 in Five Year Time Deposit Scheme in Post Office on 25.3.2014.
- (vii) His agricultural income during the year is ₹ 45,000.
- (viii) He has received gift of ₹ 25,000 from his grandfather on 10.6.2013.
- (ix) He has gifted his car to his wife on 15.5.2013. She has earned income of ₹ 30,000 from the business of hiring the same during the previous year.
- Compute the total income and tax payable of Mr. Mahesh for the A.Y. 2014-15.

Answer

Computation of total income of Mr. Mahesh for the A.Y. 2014-15

Particulars	₹
Income from salary (as per note 3)	4,10,053
Business Income (assuming that his wife carries on the business of hiring of cars) [Income of wife from hiring of car clubbed under section 64(1)(iv)]	<u>30,000</u>
Gross Total Income	4,40,053
Less: Deduction under section 80C (as per note 5)	<u>1,00,000</u>
Total income	<u>3,40,053</u>
Total income (rounded off)	3,40,050

Computation of tax liability of Mr. Mahesh for the A.Y.2014-15

Step 1	₹	₹
Add: Agricultural income and Non-agricultural income (₹ 45,000 + ₹ 3,40,050)		
Tax on ₹ 3,85,050	18,505	

Step 2		
<i>Add:</i> Basic exemption limit to agricultural income (₹ 2,00,000 + ₹ 45,000)		
Tax on ₹ 2,45,000	<u>4,500</u>	
Step 3		
Tax on non-agricultural income (Tax under step 1 – Tax under step 2) (₹ 18,505 – ₹ 4,500)		14,005
<i>Less:</i> Rebate under section 87A		<u>2,000</u>
		12,005
<i>Add:</i> Education cess @2% and Secondary and higher education cess @ 1%		<u>360</u>
Total tax liability		<u>12,365</u>
<i>Rounded off</i>		12,370

Notes:**1. Valuation of rent free house**

Particulars	₹
Basic salary	1,75,000
D.A. (not to be considered as it is not forming part of salary)	Nil
Commission on extra production	12,000
Bonus	8,000
Special allowance	18,000
Education allowance (See Note 4)	6,400
Medical allowance	<u>5,000</u>
Salary for the purpose of valuation of rent-free house	<u>2,24,400</u>
Value of rent-free house = 15% of ₹ 2,24,400	33,660

2. Valuation of perquisite of CD Player given for use by the employee

Taxable value of this perquisite is 10% p.a. of cost of the CD player w.e.f. 1.1.2014 (i.e. for 90 days)

10% of ₹ 20,000 = 2,000 x 90/365 = ₹ 493

Provision of laptop by the employer is a tax-free perquisite.

3. Income from salary

Particulars	₹	₹
Basic pay		1,75,000
D.A.		1,40,000

Bonus		8,000
Commission		12,000
Special Allowance		18,000
Taxable education allowance (See Note-4 below)		6,400
Medical Allowance		<u>5,000</u>
Total		3,64,400
<i>Add : Taxable perquisites :</i>		
1. Rent free accommodation (Note 1)	33,660	
2. Electricity Bill paid by employer	11,500	
3. CD Player given by employer (Note 2)	<u>493</u>	<u>45,653</u>
Taxable salary		<u>4,10,053</u>

4. Education allowance exempt under section 10(14)

Education allowance of ₹ 100 per month per child for a maximum of 2 children plus hostel allowance of ₹ 300 per month per child for a maximum of 2 children is exempt.

i.e. $(₹ 100 \times 2 \times 12) + (₹ 300 \times 2 \times 12) = ₹ 2,400 + ₹ 7,200 = ₹ 9,600$

Therefore, taxable education allowance would be ₹ 16,000 – ₹ 9,600 = ₹ 6,400.

5. Investments/payments deductible under section 80C

Particulars	₹
Investment in notified mutual fund	25,000
Investment in PPF	15,000
Investment in 5 year Time Deposit in Post Office	10,000
Tuition fees of children (assumed to be paid to an eligible educational institution – hence qualifies for deduction under section 80C)	<u>60,000</u>
	<u>1,10,000</u>

However, the total deduction under section 80C cannot exceed ₹ 1,00,000. This restriction is contained in section 80CCE.

Therefore, the permissible deduction under section 80C would be ₹ 1,00,000

6. Taxability of gift received from grandfather

Gift from a relative is not taxable under section 56(2)(vii). Grandfather is a relative as per the definition of "relative" given in the Explanation to section 56(2)(vii) and hence ₹ 25,000, being gift received from grandfather, is not taxable.

Question 21

Rajat is a Chartered Accountant in practice. He maintains his accounts on cash basis. He is a Resident and ordinarily resident in India. His income and expenditure account for the year ended March 31, 2014 reads as follows:

Expenditure	₹	Income		₹
Salary to staff	5,25,000	Fees earned:		
Stipend to articled assistant	18,000	Audit	6,65,800	
Incentive to articled assistants	5,000	Taxation services	4,68,600	
Office rent	24,000	Consultancy	<u>3,82,000</u>	15,16,400
Printing and stationery	6,600	Dividend on shares of Indian companies (gross)		9,635
Meeting, seminar and conference	38,600	Income from Unit Trust of India		6,600
Repairs, maintenance and petrol of car	22,400	Profit on sale of shares (STT paid)		15,620
Subscription and periodicals	15,000	Honorarium received from various institutions for valuation of answer papers		16,350
Postage, telegram and fax	32,500	Rent received from residential flat let out		84,000
Depreciation	29,500			
Travelling expenses	55,000			
Municipal tax paid in respect of house property	1,000			
Net profit	<u>8,76,005</u>			
	<u>16,48,605</u>			<u>16,48,605</u>

Other information:

- (i) The total travelling expenses incurred on foreign tour was ₹ 20,000 which was within the RBI norms.
- (ii) Incentive to articled assistants represent amount paid to two articled assistants for passing IPCC Examination at first attempt.
- (iii) Repairs and maintenance of car includes ₹ 1,600 for the period from 1.10.2013 to 30.09.2014.

- (iv) Salary include ₹ 30,000 to a computer specialist in cash for assisting Mr. Rajat in one professional assignment.
- (v) ₹ 1,500, interest on loan paid to LIC on the security of his Life Insurance Policy and utilised for repair of computer, has been debited to the drawing account of Mr. Rajat.
- (vi) Medical Insurance Premium on the health of:

Particulars	₹	Mode of payment
Self	10,000	By Cheque
Dependent brother	5,000	By Cheque
Major son dependent on him	3,000	By Cash
Minor married daughter	2,000	By Cheque
Wife dependent on assessee	6,000	By Cheque

- (vii) Shares sold were held for 10 months before sale.
- (viii) Rajat paid life membership subscription of ₹ 1,000 to Chartered Accountants Benevolent Fund. The amount was debited to his drawings account. The Chartered Accountants Benevolent Fund is an approved fund under section 80G of Income-tax, 1961.
- (ix) Depreciation debited to income and expenditure account is as per the rates of Income-tax Rules, 1962.

Compute the total income and tax payable of Rajat for the Assessment year 2014-15.

Answer

Computation of Total Income of Mr. Rajat for Assessment Year 2014-15

Particulars	Working Note Nos.	₹
Income from House Property	1	58,100
Profit and gains of Business or Profession	2	7,73,300
Short-term capital gains	3	15,620
Income from other sources	4	<u>16,350</u>
Gross Total Income		8,63,370
Less: Deduction under Chapter VI-A	5	<u>15,500</u>
Total Income		<u>8,47,870</u>
Tax on total income		
Total Income		8,47,870
Less: Short-term capital gains (See Note 9 below)		<u>15,620</u>
Normal Income		<u>8,32,250</u>

8.53 Income-tax

Tax on normal income		96,450
Tax on short-term capital gains @15%		<u>2,343</u>
		98,793
<i>Add:</i> Education cess @ 2% and SHEC @ 1%		<u>2,964</u>
Total tax liability		<u>1,01,757</u>
Total tax liability (rounded off)		1,01,760

Notes :

(1)	Income from House Property		₹
	Gross annual value	84,000	
	<i>Less:</i> Municipal taxes paid by owner	<u>1,000</u>	
	Net Annual Value (NAV)	83,000	
	<i>Less:</i> Deduction under section 24 @ 30% of NAV	<u>24,900</u>	58,100
	Rent received has been taken as the Gross Annual Value in the absence of other information relating to Municipal Value, Fair Rent and Standard Rent.		
(2)	Income under the head "Profits & Gains of Business or Profession"		
	Net profit as per Profit & Loss Account		8,76,005
	<i>Add:</i> Expenses debited to the Profit & Loss Account but not allowable		
	(i) Salary paid to computer specialist in cash disallowed under section 40A(3), since such cash payment exceeds ₹ 20,000	30,000	
	(ii) Municipal Taxes paid in respect of residential flat let out	<u>1,000</u>	<u>31,000</u>
			9,07,005
	<i>Less:</i> Expenses allowable but not debited to profit and loss account		
	Interest paid on loan taken from LIC used for repair of computer		<u>1,500</u>
			9,05,505
	<i>Less:</i> Income credited to Profit & Loss Account but not taxable under this head:		
	(i) Dividend on shares of Indian companies	9,635	
	(ii) Income from UTI	6,600	
	(iii) Profit on sale of shares	15,620	

	(iv) Honorarium for valuation of answer papers	16,350	
	(v) Rent received from letting out of residential flat	<u>84,000</u>	<u>1,32,205</u>
			<u>7,73,300</u>
(3)	Capital gains:		
	Short term capital gain on sale of shares		15,620
(4)	Income from other sources:		
	Dividend on shares of Indian companies	9,635	
	Less: Exempt under section 10(34)	<u>9,635</u>	Nil
	Income from UTI	6,600	
	Less: Exempt under section 10(35)	<u>6,600</u>	Nil
	Honorarium for valuation of answer papers	<u>16,350</u>	16,350
(5)	Deduction under Chapter VI-A :		
	Deduction under section 80D (Medical Insurance Premium)		
	Policy holder	Amount of Premium (₹)	Amt. eligible for deduction (₹)
	Self	10,000	10,000
	Dependent brother	5,000	Nil
	Major son dependent on him	3,000	Nil
	Minor married daughter	2,000	Nil
	Wife dependent on assessee	<u>6,000</u>	<u>6,000</u>
			<u>16,000</u>
	Amount of deduction is restricted to ₹ 15,000		15,000
	Deduction under section 80G (Donation)		
	Donation to CA Benevolent Fund (50% of ₹ 1,000)		<u>500</u>
	Total deduction under Chapter VI-A		<u>15,500</u>
	<i>Note</i> – Premium paid to insure the health of brother is not eligible for deduction under section 80D. Premium paid to insure the health of son is not eligible for deduction since payment is made in cash. Premium paid to insure the health of minor married daughter is not eligible for deduction as she is not dependent on Mr.Rajat.		

- (6) ₹ 20,000 expended on foreign tour is allowable as deduction assuming that it was incurred in connection with his professional work. Therefore, it requires no further treatment.
- (7) Incentive to articled assistants passing IPCC examination in their first attempt is deductible under section 37(1).
- (8) Repairs and maintenance paid in advance for the period 1.4.2014 to 30.9.2014 i.e. for 6 months amounting to ₹ 800 will be allowed since Mr. Rajat is following the cash system of accounting.
- (9) Since securities transaction tax has been paid on the shares and the period of holding of these shares is less than 12 months, the profit arising there from is a short-term capital gain chargeable to tax at 15% under section 111A.
- (10) Since depreciation debited to income and expenditure account is as per the Income-tax Rules, 1962, no adjustment for the same has been made.

Question 22

Dr. Sparsh Kumar is running a clinic. His Income and Expenditure account for the year ending 31st March, 2014 is given below:

<i>Expenditure</i>	<i>₹</i>	<i>Income</i>	<i>₹</i>
<i>To Staff Salary</i>	<i>4,30,000</i>	<i>By Fees Receipts</i>	<i>12,63,600</i>
<i>To Consumables</i>	<i>9,250</i>	<i>By Dividend from Indian Companies</i>	<i>9,500</i>
<i>To Medicine consumed</i>	<i>3,64,800</i>	<i>By Winning from Lotteries (Net of TDS of ₹ 12,000)</i>	<i>28,000</i>
<i>To Depreciation</i>	<i>91,000</i>	<i>By Income-tax refund</i>	<i>2,750</i>
<i>To Administrative Expenses</i>	<i>1,46,000</i>		
<i>To Donation to Prime Minister's National Relief Fund</i>	<i>15,000</i>		
<i>To Excess of Income over expenditure</i>	<i><u>2,47,800</u></i>		
<i>Total</i>	<i><u>13,03,850</u></i>	<i>Total</i>	<i><u>13,03,850</u></i>

- (i) *Depreciation in respect of all assets has been ascertained at ₹ 50,000 as per Income-tax Rules, 1962.*
- (ii) *Medicines consumed include medicine of (cost) ₹ 16,000 used for his family.*
- (iii) *Fees Receipts include ₹ 14,000 honorarium for valuing medical examination answer books.*
- (iv) *He has also received ₹ 90,000 on account of Agricultural Income which had not been included in the above Income and Expenditure Account.*

- (v) He has also received ₹ 57,860 on maturity of one LIC Policy, not included in the above Income and Expenditure Account.
- (vi) He received ₹ 6,000 per month as salary from a City Care Centre. This has not been included in the 'Fees Receipts' credited to Income and Expenditure Account.
- (vii) He has sold land in June, 2013 for ₹ 6,00,000 (valuation as per stamp valuation authority ₹ 11,00,000). The land was acquired by him in October, 1999 for ₹ 4,50,000.
- (viii) He has paid premium of ₹ 12,000 for another LIC Policy which was taken on 1.04.2012 (sum assured ₹ 50,000).
- (ix) He has paid ₹ 2,500 for purchase of lottery tickets.
- (x) Donation to Prime Minister Relief Fund has been made by way of an account payee cheque.

From the above, compute the income and tax payable of Dr. Sparsh Kumar for the A.Y. 2014-15.

Cost Inflation Index: F.Y. 1999-00 – 389; F.Y. 2013-14 – 939.

Answer

Computation of total income and tax liability of Dr. Sparsh Kumar for the A.Y. 2014-15

Particulars	₹
Income from salary (Working Note – 1)	72,000
Income from business (Working Note – 2)	2,65,550
Long-term capital gains (Working Note – 3)	13,753
Income from other sources (Working Note – 4)	<u>54,000</u>
Gross Total Income	4,05,303
Less: Deduction under Chapter VI-A (Working Note – 5)	<u>20,000</u>
Total Income	<u>3,85,303</u>
Tax on total income (Working Note - 6)	27,906
Less: Rebate under section 87A	2,000
	25,906
Add: Education cess @ 2% and SHEC @1%	<u>777</u>
Total tax liability	26,683
Less: Tax deducted at source (TDS)	<u>12,000</u>
Tax payable	<u>14,683</u>
Rounded off	14,680

Working Notes:

1. Computation of salary income

Particulars	₹
Gross Salary (₹ 6,000×12)	72,000
Less: Deduction under section 16	<u>Nil</u>
Net Salary	<u>72,000</u>

2. Computation of income under the head "Profits and gains of business or profession"

Particulars	₹	₹
Net Income as per Income and Expenditure Account		2,47,800
<i>Add:</i> Expenses disallowed:		
Depreciation (₹ 91,000 – ₹ 50,000)	41,000	
Cost of medicine for self-use	16,000	
Donation to Prime Minister's Relief Fund	<u>15,000</u>	<u>72,000</u>
		3,19,800
<i>Less:</i> Dividend from Indian companies	9,500	
Income-tax refund	2,750	
Winning from Lotteries	28,000	
Honorarium for valuing answer books	<u>14,000</u>	<u>54,250</u>
		2,65,550

3. Computation of Capital Gains

Particulars	₹	₹
Sale consideration	6,00,000	
Valuation as per Stamp Valuation Authority (Value to be taken higher of actual sale consideration or valuation adopted for stamp duty purposes as per section 50C)	11,00,000	
Consideration for the purpose of capital gain		11,00,000
<i>Less:</i> Cost of acquisition = ₹ 4,50,000 x 939/389		<u>10,86,247</u>
Long term capital gain		<u>13,753</u>

4. Computation of income under the head "Income from other sources"

Particulars	₹	₹
Dividend from Indian Companies [Exempt u/s 10(34)]		-
Honorarium for valuing answer books		14,000

Winning from Lotteries (Net)	28,000	
Add: TDS	<u>12,000</u>	40,000
Income from other sources		<u>54,000</u>

Note : As per section 58(4), no expense or deduction is allowable in respect of winnings from lotteries.

5. Computation of deduction under Chapter VI-A

Particulars	₹
U/s 80C Life Insurance Premium (maximum 10% of sum assured)	5,000
U/s 80G Donation to Prime Minister's Relief Fund [See Note below]	<u>15,000</u>
Total deduction under Chapter VI-A	<u>20,000</u>

Note –The donation made to the Prime Minister's National Relief Fund qualifies for 100% deduction under section 80G.

6. Computation of tax on total income

Particulars	₹
Tax on agricultural income plus non-agricultural income i.e. tax on ₹ 4,65,303 (being ₹ 90,000 + ₹ 3,85,303) [See Note below]	36,906
Less: Tax on agricultural income plus basic exemption limit i.e. tax on ₹ 2,90,000, (being ₹ 90,000 + ₹ 2,00,000)	9,000
Tax on total income	<u>27,906</u>

Note : Tax on ₹ 3,85,303 plus agricultural income of ₹ 90,000 is computed hereunder :

Particulars	₹
Tax on long term capital gain ₹ 13,753 @ 20%	2,751
Tax on winnings from lotteries ₹ 40,000 @ 30%	12,000
Tax on balance income of (₹ 3,31,550 + 90,000)	<u>22,155</u>
	<u>36,906</u>

Note : Agricultural income is exempt from tax. It is considered for rate purpose only.

7. Any sum received under a life insurance policy is wholly exempt from tax under section 10(10D).

Question 23

Dr. Krishna furnishes you the following information:

Income and Expenditure Account for the year ended 31st March 2014

<i>Particulars</i>	<i>₹</i>	<i>Particulars</i>	<i>₹</i>
<i>To Medicines consumed</i>	<i>2,42,000</i>	<i>By Fee receipts</i>	<i>8,47,500</i>
<i>To Staff salary</i>	<i>1,65,000</i>	<i>By Rent</i>	<i>27,000</i>
<i>To Hospital consumables</i>	<i>47,500</i>	<i>By Dividend from Indian companies</i>	<i>9,000</i>
<i>To Rent paid</i>	<i>60,000</i>		
<i>To Administrative expenses</i>	<i>1,23,000</i>		
<i>To Net Income</i>	<i>2,46,000</i>		
	<i>8,83,500</i>		<i>8,83,500</i>

- (i) *Rent paid includes rent for his residential accommodation of ₹ 30,000 (paid by cheque) at Bangalore.*
- (ii) *Hospital equipments (eligible for depreciation @ 15%)*
01.04.2013 Opening WDV ₹ 5,00,000
07.12.2013 Acquire (Cost) ₹ 2,00,000
- (iii) *Medicines consumed include medicines (cost) ₹ 10,000 used for Dr. Krishna's family.*
- (iv) *Rent received – relates to a property situated at Mysore (Gross Annual Value). The municipal tax of ₹ 2,000 paid in December, 2013 has been included in the “administrative expenses”.*
- (v) *He received ₹ 5,000 per month as salary from Full Cure Hospital. This has not been included in the “fee receipts” credited to income and expenditure account.*
- (vi) *He sold a vacant site in July, 2013 for ₹ 5,00,000. It was inherited by him from his father in January, 1998. The site was acquired by his father in December, 1990 for ₹ 1,50,000.*
(Cost inflation index for F.Y 1990-91 = 182; 1997-98 = 331 and 2013-14 = 939)

Compute Dr. Krishna's taxable income for the year ended 31.03.2014.

Answer

Computation of taxable income of Dr.Krishna for the previous year ended 31.03.2014

<i>Particulars</i>	<i>₹</i>	<i>₹</i>
Income from Salaries		
Salary received @ ₹ 5,000 per month		60,000
Income from house property		
Gross Annual Value	27,000	

<i>Less:</i> Municipal tax	<u>2,000</u>	
Net Annual Value	25,000	
<i>Less:</i> Deduction under section 24 @ 30%	<u>7,500</u>	17,500
Income from business or profession		
Net income as per income & expenditure account	2,46,000	
<i>Add:</i> Rent paid to residence	30,000	
Medicines consumed – personal use	10,000	
Municipal tax relating to let out property included in administrative expenses – disallowed	<u>2,000</u>	
	2,88,000	
<i>Less:</i> Depreciation (See working note 2)	90,000	
Rent credited to income & expenditure account	27,000	
Dividend from Indian companies [Exempt u/s 10(34)]	9,000	1,62,000
Capital Gains (Long term capital gains)		
Sale consideration	5,00,000	
<i>Less:</i> Indexed cost acquisition (₹1,50,000 x 939/331) (See Note 3)	<u>4,25,529</u>	<u>74,471</u>
Gross Total income		3,13,971
<i>Less:</i> Deduction under chapter VIA – Section 80GG		
Under section 80GG, rent paid would be allowable as a deduction to the extent of the least of the following		
(i) 25% of total income = 25% of ₹ 2,39,500 (See Note 1)	59,875	
(ii) Excess of rent paid over 10% of total income (₹ 30,000 - ₹ 23,950)	6,050	
(iii) ₹ 2,000 per month	24,000	
Least of the above		<u>6,050</u>
Total Income		<u>3,07,921</u>

Note :

1. Deduction under section 80GG is to be made from Gross Total Income. Gross Total Income as defined under section 80B(5) means the total income computed in accordance with the provisions of this Act, before making any deduction under Chapter VI-A. Under section 112(2), Long term capital gains have to be reduced from Gross Total Income and Chapter VI-A deductions should be allowed as if the Gross Total income so reduced were the Gross Total Income of the assessee. Therefore, in this case, for the purpose of allowing deduction u/s 80GG, Gross Total Income = ₹ 3,13,971 – ₹ 74,471 = ₹ 2,39,500.

2. Depreciation on plant & machinery

	₹
On opening WDV of ₹ 5,00,000 @ 15%	75,000
On equipment acquired ₹ 2,00,000 @ 7.5% (50% thereon, since acquired in December)	15,000
	90,000

3. Since the property was acquired by Dr. Krishna through inheritance, the cost of acquisition to him will be the cost to the previous owner. However, indexation will be from the year in which the assessee (i.e., Dr. Krishna in this case) first held the asset i.e. F.Y. 1997-98.

Alternative view: In the case of *CIT v. Manjula J. Shah 16 Taxmann 42 (Bom.)*, the Bombay High Court held that the indexed cost of acquisition in case of gifted asset can be computed with reference to the year in which the previous owner first held the asset.

As per this view, this indexation cost of acquisition of property would be ₹ 7,73,901 and long term capital loss would be ₹ 2,73,901.

Question 24

Mr. Pankaj, aged 58 years, who retired from the services of the Central Government on 30.6.2013, furnishes particulars of his income and other details as under:

- ◆ *Salary @ ₹ 6,000 p.m.*
- ◆ *Pension @ ₹ 3,000 p.m. for July 2013 to Nov 2013.*
- ◆ *On 1.12.2013, he got 1/3rd of his pension commuted for ₹ 1,20,000.*
- ◆ *A house plot at Ernakulam sold on 1.2.2014 for ₹ 5,00,000 had been purchased by him on 3.11.1979 for ₹ 10,000. The stamp valuation authority had assessed the value of said house plot at ₹ 6,00,000 which was neither disputed by the buyer nor by him. The value of this house plot as on 1.4.1981 was ₹ 15,000 (The cost inflation index for the financial year 2013-14 is 939).*
- ◆ *Received interest on bank FDRs of ₹ 72,500, dividend on mutual fund units of ₹ 15,000 and interest on maturity of NSC of ₹ 50,000 out of which an amount of ₹ 40,000 was already disclosed by him on accrual basis in the returns upto assessment year 2013-14.*
- ◆ *Investment in purchase of NSC for ₹ 30,000 and payment for mediclaim insurance for self and wife of ₹ 12,500. Made investment in Tax Magnum units of Mutual Fund of SBI of ₹ 80,000.*

Compute the total income of Mr. Pankaj for A.Y. 2014-15.

In the event of Mr. Pankaj being ready to make appropriate investment for availing exemption in respect of capital gain arising from sale of house plot, what will be the amount to be invested and the period within which the same should be invested?

- (a) *if he wishes to avail exemption under section 54F by constructing a new residential house;*
 (b) *if he wants to avail exemption under section 54EC.*

Answer

Computation of total income of Mr. Pankaj for A.Y.2014-15

Particulars	₹
Income from salaries (See Working Note 1)	41,000
Capital gains (See Working Note 2)	4,59,150
Income from other sources (See Working Note 3)	<u>82,500</u>
Gross Total Income	5,82,650
Less: Deductions under Chapter VI-A (See Working Note 4)	<u>1,12,500</u>
Total Income	<u>4,70,150</u>

Working Notes:

1. Income from salaries

Particulars	₹
Salary for 3 months received from Government of India (₹ 6000 x 3)	18,000
Pension for 5 months from July 2013 to Nov 2013 @ ₹ 3000 p.m. (₹ 3000 x 5)	15,000
Pension for 4 months from Dec 2013 to March 2014 @ ₹ 2,000 p.m. (₹ 2,000x4)	<u>8,000</u>
	<u>41,000</u>

Note : Commuted value of pension of ₹ 1,20,000 received from the Central Government is fully exempt under section 10(10A).

2. Capital gains

Particulars	₹
Long term capital gains on sale of house plot at Ernakulam on 01.02.2014	
Sale consideration received is ₹ 5,00,000. However, since the value assessed by the stamp valuation authority (i.e. ₹ 6,00,000) is higher than the sale consideration, such value assessed is deemed to be the full value of the consideration received or accruing as a result of such transfer as per section 50C	6,00,000
Less: Indexed cost of acquisition ₹ 15,000 x 939/100	<u>1,40,850</u>
	<u>4,59,150</u>

3. Income from other sources

Particulars	₹	₹
Interest on bank FDRs		72,500
Dividend of ₹ 15,000 on units of Mutual Fund [exempt under section 10(35)]		-
Interest on maturity of NSC	50,000	
Less: Interest already shown on accrual basis in the past returns	<u>40,000</u>	<u>10,000</u>
		<u>82,500</u>

4. Deductions under Chapter VI-A

Particulars	₹	₹
Under section 80C		
Purchase of NSC	30,000	
Tax Magnum units of Mutual Fund of SBI	<u>80,000</u>	
Total	1,10,000	
Maximum deduction available under section 80C		1,00,000
Under section 80D		
Medical insurance premium paid ₹ 12,500 (assumed to have been paid by cheque)		<u>12,500</u>
		<u>1,12,500</u>

Investment in approved modes

Section 54F (by constructing a new house)

In order to avail exemption under section 54F by constructing a new residential house, the assessee should construct a residential house within three years from the date of transfer of house plot. To avail the maximum exemption, the entire net consideration received from sale of house plot should be invested. If only part of the net consideration is invested, then proportionate exemption of long term capital gains would be available i.e.

$$\text{Long term capital gain} \times \frac{\text{Amount invested in new residential house}}{\text{Net sale consideration}}$$

Section 54EC

In order to avail maximum exemption under section 54EC, the assessee should invest the entire long-term capital gain arising from transfer of the house plot, i.e. ₹ 4,59,150, within six months from the date of sale of house plot, in bonds of National Highways Authority of India (NHAI) or Rural Electrification Corporation Ltd. (RECL). If only part of the capital gain is invested, then the exemption would be restricted to the amount invested in such bonds.

Question 25

The broad break-up of tax and allied details of Mrs. Rinku, born on 30th March, 1949 are as under:

Particulars	₹
Long-term capital gains on sale of house	2,00,000
Short-term capital gains on sale of shares in B Pvt. Ltd.	30,000
Prize winning from a T.V. show	20,000
Business income	2,20,000
Net agricultural income	40,000
Mrs. Rinku has paid the following:	
LIC premium of self	40,000
LIC premium of husband	20,000

Compute the tax payable by Mrs. Rinku for the assessment year 2014-15.

Answer

Computation of tax payable by Mrs. Rinku for the A.Y.2014-15

	Particulars	₹	₹
	Step 1		
Add	Agricultural income and Non-agricultural income (₹ 40,000 + ₹ 4,10,000) [For computation of non-agricultural income, see Note 1 below]	4,50,000	
	Tax on the above income		
(i)	Tax on long-term capital gain of ₹ 1,80,000 @ 20% [₹ 2,00,000 – ₹ 20,000 (unexhausted basic exemption limit)]	36,000	
(ii)	Tax on winnings of ₹ 20,000 from a T.V. show @ 30%	6,000	
(iii)	Tax on balance income of ₹ 2,30,000	<u>Nil</u>	
	Total tax on ₹ 4,50,000		42,000
	Step 2		
Add	Basic exemption limit to agricultural income (₹ 2,50,000 + ₹ 40,000)	2,90,000	
	Tax on ₹ 2,90,000		4,000

Step 3		
Tax on non-agricultural income (Tax under step 1 – Tax under step 2) (₹ 42,000 – ₹ 4,000)		38,000
Less: Rebate under section 87A		2,000
		<u>36,000</u>
Add: Education cess @ 2%		720
Add: Secondary and higher education cess @ 1%		<u>360</u>
Tax payable by Mrs. Rinku		<u>37,080</u>

Notes :

1. Computation of total income of Mrs. Rinku for the A.Y.2014-15

Particulars	₹	₹
Business income		2,20,000
Long term capital gains on sale of house		2,00,000
Short term capital gains on sale of shares in B Pvt. Ltd		30,000
Prize winnings from a T.V. show		<u>20,000</u>
Gross Total Income		4,70,000
Less: Deduction under section 80C		
Life insurance premium of self	40,000	
Life insurance premium of husband	<u>20,000</u>	<u>60,000</u>
Total Income		<u>4,10,000</u>

- Mrs. Rinku is of 64 years of age during the P.Y.2013-14. Therefore, she is a senior citizen entitled to the higher basic exemption limit of ₹ 2,50,000.
- Short-term capital gains on sale of shares in B Pvt. Ltd. is taxable at normal rates.

Question 26

Ramdin working as Manager (Sales) with Frozen Foods Ltd., provides the following information for the year ended 31.03.2014:

– Basic Salary	₹ 15,000 p.m.
– DA (50% of it is meant for retirement benefits)	₹ 12,000 p.m.
– Commission as a percentage of turnover of the Company	0.5 %
– Turnover of the Company	₹ 50 lacs
– Bonus	₹ 50,000
– Gratuity	₹ 30,000
– Own Contribution to R.P.F.	₹ 30,000
– Employer's contribution to R.P.F.	20% of basic salary

- Interest credited in the R.P.F. account @ 15% p.a. ₹ 15,000
- Gold Ring worth ₹ 10,000 was given by employer on his 25th wedding anniversary.
- Music System purchased on 01.04.2013 by the company for ₹ 85,000 and was given to him for personal use.
- Two old heavy goods vehicles owned by him were leased to a transport company against the fixed charges of ₹ 6,500 p.m. Books of account are not maintained.
- Received interest of ₹ 5,860 on bank FDRs, dividend of ₹ 1,260 from shares of Indian Companies and interest of ₹ 7,540 from the debentures of Indian Companies.
- Made payment by cheques of ₹ 15,370 towards premium of Life Insurance policies and ₹ 12,500 for Mediclaim Insurance policy.
- Invested in NSC ₹ 30,000 and in FDR of SBI for 5 years ₹ 50,000.
- Donations of ₹ 11,000 to an institution approved u/s 80G and of ₹ 5,100 to Prime Minister's National Relief Fund were given during the year by way of cheque.

Compute the total income and tax payable thereon for the A.Y. 2014-15.

Answer

Computation of Total Income for the A.Y. 2014-15

Particulars	₹	₹
Income from Salaries		
Basic Salary (₹15,000 x 12)		1,80,000
Dearness Allowance (₹12,000 x12)		1,44,000
Commission on Turnover (0.5% of ₹ 50 lacs)		25,000
Bonus		50,000
Gratuity (Note 1)		30,000
Employer's contribution to recognized provident fund		
Actual contribution [20% of ₹ 1,80,000]	36,000	
Less: Exempt (Note 2)	<u>33,240</u>	2,760
Interest credited in recognized provident fund account @15% p.a.	15,000	
Less: Exempt upto 9.5% p.a.	<u>9,500</u>	5,500
Gift of gold ring worth ₹ 10,000 on 25 th wedding anniversary by employer (See Note 3)		10,000
Perquisite value of music system given for personal use (being 10% of actual cost) i.e. 10% of ₹ 85,000		<u>8,500</u>
		4,55,760
Profits and Gains of Business or Profession		
Lease of 2 trucks on contract basis against fixed charges of		

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₹ 6,500 p.m. In this case, presumptive tax provisions of section 44AE will apply i.e. ₹ 5,000 p.m. for each of the two trucks (5,000 x 2 x12). He cannot claim lower profits and gains since he has not maintained books of account.		1,20,000
Income from Other Sources		
Interest on bank FDRs	5,860	
Interest from debentures	7,540	
Dividend on shares [Exempt under section 10(34)]	<u>Nil</u>	<u>13,400</u>
Gross total Income		5,89,160
<i>Less:</i> Deductions under Chapter VI-A		
Section 80C		
Premium on life insurance policy	15,370	
Investment in NSC	30,000	
FDR of SBI for 5 years	50,000	
Employee's contribution to recognized provident fund	<u>30,000</u>	
Total	<u>1,25,370</u>	
Limited to	1,00,000	
Section 80D - Mediclaim Insurance	12,500	
Section 80G (Note 4)	<u>10,600</u>	<u>1,23,100</u>
Total Income		<u>4,66,060</u>
Tax on total income		
Income-tax		26,606
<i>Less:</i> Rebate under section 87A		2,000
		24,606
<i>Add:</i> Education cess @ 2%		492
<i>Add:</i> Secondary and higher education cess @ 1%		<u>246</u>
Total Tax Payable		<u>25,344</u>
Tax Payable (rounded off)		22,340

Notes:

1. Gratuity received during service is fully taxable.
2. Employer's contribution in the recognized provident fund is exempt up to 12% of the salary i.e. 12% of (Basic Salary + DA for retirement benefits + Commission based on turnover)
 - = 12% of (₹ 1,80,000+ (50% of ₹ 1,44,000)+ ₹ 25,000)
 - = 12% of 2,77,000 = ₹ 33,240

3. An alternate view possible is that only the sum in excess of ₹ 5,000 is taxable in view of the language of *Circular No. 15/2001 dated 12.12.2001* that such gifts upto ₹ 5,000 in the aggregate per annum would be exempt, beyond which it would be taxed as a perquisite. As per this view, the value of perquisite would be ₹ 5,000. In such a case the Income from Salaries would be ₹ 4,50,760.
4. Deduction under section 80G is computed as under:

Particulars	₹
Donation to PM National Relief Fund (100%)	5,100
Donation to institution approved under section 80G (50% of ₹ 11,000) (amount contributed ₹ 11,000 or 10% of Adjusted Gross Total Income i.e. ₹ 47,666, whichever is lower)	<u>5,500</u>
Total deduction	<u>10,600</u>

Adjusted Gross Total Income = Gross Total Income – Deductions under section 80C and 80D = ₹ 5,89,160 – ₹ 1,12,500 = ₹ 4,76,660.

Question 27

Dr. Niranjana, a resident individual, aged 60 years is running a clinic. Her Income and Expenditure Account for the year ending March 31st, 2014 is as under:

Expenditure	₹	Income	₹
To Medicine consumed	5,38,400	By Consultation and Medical charges	18,85,850
To Staff salary	3,80,000	By Income-tax refund (Principal ₹ 5,000, interest ₹ 450)	5,450
To Clinic consumables	1,10,000	By Dividend from units of UTI	10,500
To Rent paid	90,000	By winning from game show on T.V. (net of TDS of ₹ 15,000)	35,000
To Administrative expenses	2,55,000	By Rent	27,000
To Amount paid to scientific research association approved under section 35	1,50,000		
To Net profit	<u>4,40,400</u>		
	<u>19,63,800</u>		<u>19,63,800</u>

(i) Rent paid includes ₹ 30,000 paid by cheque towards rent for her residential house in Surat.

(ii) Clinic equipments are:

1.4.2013	Opening W.D.V.	- ₹ 5,00,000
7.12.2013	Acquired (cost)	- ₹ 2,00,000

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- (iii) Rent received relates to property situated at Surat. Gross Annual Value ₹ 27,000. The municipal tax of ₹ 2,000, paid in December, 2013, has been included in "administrative expenses".
- (iv) She received salary of ₹ 7,500 p.m. from "Full Cure Hospital" which has not been included in the "consultation and medical charges".
- (v) Dr. Niranjana availed a loan of ₹ 5,50,000 from a bank for higher education of her daughter. She repaid principal of ₹ 1,00,000, and interest thereon ₹ 55,000 during the year 2013-14.
- (vi) She paid ₹ 1,00,000 as tuition fee (not in the nature of development fees/ donation) to the university for full time education of her daughter.
- (vii) An amount of ₹ 18,000 has also been paid by cheque on 27th March, 2014 for her medical insurance premium.

From the above, compute the total income of Dr. Smt. Niranjana for the A.Y. 2014-15.

Answer

Computation of total income and tax liability of Dr. Niranjana for A.Y. 2014-15

	Particulars	₹	₹	₹
I	Income from Salary			
	Basic Salary (₹ 7,500 x 12)			90,000
II	Income from house property			
	Gross Annual Value (GAV)		27,000	
	Less : Municipal taxes paid		<u>2,000</u>	
	Net Annual Value (NAV)		25,000	
	Less : Deduction under section 24 @ 30% of ₹ 25,000		<u>7,500</u>	17,500
III	Income from profession			
	Net profit as per Income and Expenditure account		4,40,400	
	Less : Items of income to be treated separately			
	(i) Rent received	27,000		
	(ii) Dividend from units of UTI	10,500		
	(iii) Winning from game show on T.V. (net of TDS)	35,000		
	(iv) Income tax refund	<u>5,450</u>	<u>77,950</u>	
			3,62,450	
	Less : Allowable expenditure			
	Depreciation on Clinic equipments			
	on ₹ 5,00,000 @ 15%	75,000		
	on ₹ 2,00,000 @ 7.5%	15,000		

<p>(On equipments acquired during the year after September 2013 she is entitled to depreciation @ 50% of normal depreciation)</p> <p>Additional deduction of 75% for amount paid to scientific research association (Since weighted deduction of 175% is available in respect of such payment)</p>	<u>1,12,500</u>	<u>2,02,500</u>	
		1,59,950	
<p><i>Add:</i> Items of expenditure not allowable while computing business income</p> <p>(i) Rent for her residential accommodation included in Income and Expenditure A/c</p> <p>(ii) Municipal tax paid relating to residential house at Surat included in administrative expenses</p>	30,000		
	<u>2,000</u>	<u>32,000</u>	1,91,950
IV Income from other sources			
(a) Interest on income-tax refund		450	
(b) Dividend from UTI	10,500		
<i>Less:</i> Exempt under section 10(35)	<u>10,500</u>	Nil	
(c) Winnings from the game show on T.V. (₹ 35,000 + ₹ 15,000)		<u>50,000</u>	<u>50,450</u>
Gross Total Income			3,49,900
<i>Less:</i> Deductions under Chapter VI A:			
(a) Section 80C - Tuition fee paid to university for full time education of her daughter		1,00,000	
(b) Section 80D - Medical insurance premium (fully allowed since she is a senior citizen)		18,000	
(c) Deduction under section 80E - Interest on loan taken for higher education is deductible		<u>55,000</u>	<u>1,73,000</u>
Total income			<u>1,76,900</u>

Notes:

- (i) The principal amount received towards income-tax refund will be excluded from computation of total income. Interest received will be taxed under the head "Income from other sources".
- (ii) Winnings from game show on T.V. should be grossed up for the chargeability under the head "Income from other sources" (₹ 35,000 + ₹ 15,000). Thereafter, while computing

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tax liability, TDS of ₹ 15,000 should be deducted to arrive at the tax payable. Winnings from game show are subject to tax @30% as per section 115BB.

- (iii) Since Dr. Niranjana is staying in a rented premise in Surat itself, she would not be eligible for deduction u/s 80GG, since she owns a house in Surat which she has let out.

Question 28

Mr. X is a resident individual. His Profit and Loss account for the year ending 31st March, 2014 is given below:

To	₹	By	₹
General charges	35,650	Gross Profit	5,25,860
Insurance	3,500	Commission	6,800
Staff Salary	1,12,560	Rent received	37,500
Donation to political party	1,000	Interest on debentures (Net amount ₹ 22,500 plus TDS ₹ 2,500)	25,000
Depreciation	1,25,656	Agricultural income	45,000
Administrative expenses	42,500	Short term capital gain on sale of investment	29,000
Advance tax	17,000	Dividend from Indian Company	16,000
Net Profit	<u>3,47,294</u>		
	<u>6,85,160</u>		<u>6,85,160</u>

- (i) Depreciation has been calculated as per the Income-tax Rules, 1962 at ₹ 75,000
- (ii) He has deposited ₹ 35,000 in a notified scheme under Post Office Time Deposit Rules, 1981 for a five year time period.
- (iii) He had bought 200 shares of AB Co. Ltd. on 5.12.2012 @ ₹ 75 each, 150 shares of PQ Co. Ltd. on 3.8.2013 @ ₹ 112 each and 150 shares of AB Co. Ltd. on 05.09.2013 @ ₹ 60 each. He sold all the shares of AB Co. Ltd. on 15.12.2013 @ ₹ 98 each and sold the shares of PQ CO. Ltd. on 10.3.2014 @ ₹ 102 each. All shares were sold in National Stock Exchange through a registered broker.
- (iv) One of his life insurance policies matured on 14.6.2013. The sum assured was ₹ 1,00,000 and amount received on maturity was ₹ 1,62,850.
- (v) Donation to the political party represented the contribution made by cheque to a political party registered under section 29A of the Representation of the People Act, 1951.
- (vi) Income tax department refunds ₹ 42,580 (including interest of ₹ 1,470) which was directly credited in his personal savings account.
- (vii) He incurred expenditure of ₹ 40,000 on treatment of his dependent father who was suffering from specified disease as defined in rule 11DD of Income-tax Rules, 1962. The payment of medical expenses was made by cheque and an amount of ₹ 7,500 was reimbursed to him by an insurance company.

(vii) Bad debt of a business which was discontinued in earlier years, recovered during the year ₹ 15,000.

Compute total income and tax payable thereon by Mr. X for the assessment year 2014-15.

Answer

Computation of taxable income of Mr. X for the A.Y. 2014-15

	Particulars	₹	₹	₹
1.	Income from House Property (Note 1)			26,250
2.	Profits and gain of business or profession (Note 2)			2,78,450
3.	Capital gains (Note 3)			33,200
4.	Income from other sources (Note 4)			<u>26,470</u>
	Gross Total income			3,64,370
	Less : Deductions under Chapter VIA			
	(i) Deduction under section 80C (Note 5)		35,000	
	(ii) Deduction under section 80DDDB in respect of expenditure on medical treatment incurred on treatment of his father	40,000		
	Less: Expenditure reimbursed by insurance company	<u>7,500</u>	32,500	
	(iii) Deduction under section 80GGC in respect of contribution to the Political Party (Note 11)		<u>1,000</u>	<u>68,500</u>
	Total income			<u>2,95,870</u>
	Components of total income			
	Special Income			
	Short-term capital gains from sale of shares (chargeable at a special rate of 15% u/s 111A)		4,200	
	Normal income		<u>2,91,670</u>	
			<u>2,95,870</u>	

Computation of tax payable by Mr. X for the A.Y. 2014-15

Particulars	₹	₹
Tax on short-term capital gains from sale of shares @ 15% of ₹ 4,200		630
Tax on agricultural income plus non-agricultural income aggregating to ₹ 3,36,670		
First ₹ 2,00,000	NIL	
Next <u>₹ 1,36,670</u> @ 10%	<u>13,667</u>	
<u>₹ 3,36,670</u>		13,667

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		14,297
<i>Less:</i> Tax on agricultural income plus basic exemption limit aggregating to ₹ 2,45,000		
First ₹ 2,00,000	NIL	
Next <u>₹ 45,000 @ 10%</u>	<u>4,500</u>	4,500
Income tax payable		9,797
<i>Less:</i> Rebate under section 87A		2,000
		7,797
<i>Add:</i> Education cess @ 2%		156
Secondary and higher education cess@1%		<u>78</u>
Total tax liability		8,031
<i>Less:</i> Tax deducted at source		<u>2,500</u>
		5,531
<i>Less:</i> Advance tax paid		<u>17,000</u>
Tax refundable		<u>(11,469)</u>

Notes:

1. Computation of Income from House Property

Particulars	₹
Gross Annual Value (GAV)	37,500
Rent received is taken as the GAV in the absence of other information	
<i>Less:</i> Municipal taxes paid	<u>Nil</u>
Net Annual Value (NAV)	37,500
<i>Less:</i> Deduction under section 24 @ 30% of NAV	<u>11,250</u>
	<u>26,250</u>

2. Computation of Profits and gains of business or profession

Particulars	₹	₹
Net profit as per Profit & Loss account		3,47,294
<i>Add:</i> Inadmissible expenses		
Depreciation charges	1,25,656	
Advance tax (Note 9)	17,000	
Donation to political party	<u>1,000</u>	
		1,43,656
<i>Add:</i> Recovery of bad debt (Note 8)		<u>15,000</u>
		5,05,950

<i>Less:</i> Income chargeable under any other head / exempt income		
Rent received	37,500	
Interest on debentures (gross)	25,000	
Agricultural income (Note 10)	45,000	
Short term capital gain on sale of investment	29,000	
Dividend from Indian Company (Note 10)	<u>16,000</u>	<u>1,52,500</u>
		3,53,450
<i>Less:</i> Depreciation as per Income-tax Rules, 1962		<u>75,000</u>
		<u>2,78,450</u>

3. **Computation of Capital Gains**

Particulars	₹	₹
Short term capital gains on sale of investment		29,000
Short term capital gains on sale of shares		
Shares of AB Co. Ltd.		
Sale consideration 150 shares @ ₹ 98 each	₹ 14,700	
<i>Less:</i> Cost of 150 shares @ ₹ 60 each	₹ <u>9,000</u>	5,700
Shares of PQ Co. Ltd.		
Sale consideration 150 shares @ ₹ 102 each	₹ 15,300	
<i>Less:</i> Cost of 150 shares @ ₹ 112 each	₹ <u>16,800</u>	<u>(1500)</u>
		4,200
		33,200
Long term capital gains on sale of shares		
Since the holding period of 200 shares of AB Co. Ltd. is more than 12 months, the capital gain on sale of such shares is a long-term capital gain and hence, exempt from income-tax under section 10 (38).		
Capital Gains		<u>Nil</u>
		<u>33,200</u>

4. **Computation of Income from other sources**

Particulars	₹
Interest on debentures	25,000
Interest on refund from IT authority (Note 7)	<u>1,470</u>
Income from other sources	<u>26,470</u>

5. Five year time deposit in an account under Post Office Time Deposit Rules, 1981, is eligible for deduction under section 80C.
6. The maturity proceeds of the life insurance policy are exempt under section 10(10D) assuming that the policy does not fall under the exceptions stated under that section.

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7. Refund of income tax is not taxable. However, interest on such refund is chargeable to tax under the head "Income from other sources".
8. Recovery of bad debts, assumed to be allowed in full in an earlier year, is taxable under section 41(4), whether or not the business or profession in respect of which the deduction has been allowed is in existence at the time when it is recovered.
9. Advance tax is not allowable as deduction.
10. Agricultural income is exempt under section 10(1) and dividend from an Indian company is exempt from tax under section 10(34).
11. Contribution to a Political Party registered under section 29A of the Representation of the People Act, 1951 is deductible under section 80GGC, since payment is made otherwise than by way of cash.

Question 29

Dr. Parekh is a resident individual. His Income and Expenditure Account for the year ending 31st March, 2014 is given below:

<i>To</i>	<i>₹</i>	<i>By</i>	<i>₹</i>
<i>Salary to staff</i>	<i>3,78,000</i>	<i>Consultation fees</i>	<i>11,85,000</i>
<i>Cost of medicine</i>	<i>6,35,000</i>	<i>Cost of medicines recovered</i>	<i>7,85,000</i>
<i>Rent</i>	<i>66,000</i>	<i>Stock of medicine</i>	<i>25,000</i>
<i>Administrative cost</i>	<i>1,98,000</i>	<i>Interest on Post Office MIS</i>	<i>86,400</i>
<i>Advance tax</i>	<i>2,40,000</i>	<i>Interest on Time Deposit with bank (Net of TDS ₹ 3,000)</i>	<i>27,000</i>
<i>Membership fees</i>	<i>5,000</i>	<i>Rent received</i>	<i>20,000</i>
<i>Depreciation on apparatus</i>	<i>42,500</i>	<i>Winning from lotteries (Net of TDS ₹ 3,000)</i>	<i>7,000</i>
<i>Net profit</i>	<i><u>5,70,900</u></i>		
	<i><u>21,35,400</u></i>		<i><u>21,35,400</u></i>

- (i) *He has deposited ₹ 70,000 in PPF.*
- (ii) *He received salary of ₹ 1,50,000 and commission of ₹ 50,000 from a nursing home in which Dr. (Mrs.) Parekh is also an equal partner.*
- (iii) *He received fees of ₹ 50,000 from University of Trinidad as lecturer.*
- (iv) *Received pension of ₹ 84,000 from LIC Jeevan Suraksha.*
- (v) *Paid ₹ 22,500 by cheque as mediclaim insurance premium for his medical treatment.*
- (vi) *He paid LIC premium of ₹ 80,000 for his own life.*
- (vii) *Cost of administration includes ₹ 3,000 paid for municipal tax for the house let out to a tenant.*

(viii) Depreciation as per Income-tax Rules, 1962 to be computed as follows:

WDV as on 1.4.2013 Rs 3,00,000

Rate of depreciation @ 15%

(ix) Cost of lottery tickets amounting to ₹ 350 has not been debited to Income and Expenditure account.

You are required to compute the total income and tax payable thereon by Dr. Parekh for the assessment year 2014-15.

Answer

Computation of total Income and tax payable by Dr. Parekh for the A. Y. 2014-15

Particulars	₹	₹
Income from House Property (Note 1)		11,900
Profits and gains of business or profession (Note 2)		8,71,000
Income from other sources (Note 3)		<u>2,60,400</u>
Gross Total income		11,43,300
<i>Less:</i> Deductions under Chapter VIA		
(i) Deduction under section 80C		
Investment in PPF	70,000	
Life insurance premium paid	<u>80,000</u>	
	<u>1,50,000</u>	
Deduction restricted to	1,00,000	
(ii) Deduction under section 80D		
Mediclaime premium of ₹ 22,500 paid by cheque for himself. However, deduction restricted to	<u>15,000</u>	<u>1,15,000</u>
Total income		<u>10,28,300</u>
Components of Total Income		
Special income :		
Winning from lotteries (chargeable at special rate @ 30% under section 115BB)		10,000
Normal income		<u>10,18,300</u>
		<u>10,28,300</u>
Computation of Tax		
Tax on winnings from lotteries @ 30%		3,000
Tax on normal income (₹ 10,18,300)		
First ₹ 2,00,000 Nil	NIL	
Next ₹ 3,00,000 10%	30,000	
Next ₹ 5,00,000 20%	1,00,000	

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Balance	<u>₹ 18,300</u>	30%	<u>5,490</u>	<u>1,35,490</u>
	<u>₹ 10,18,300</u>			
Income tax payable				1,38,490
Add: Education cess @2%				2,770
Secondary and higher education cess @1%				<u>1,385</u>
Total Tax Payable				<u>1,42,645</u>
Total Tax Payable (Rounded off)				1,42,650
Less: Tax deducted at source				
From Interest			3,000	
From lottery income			<u>3,000</u>	<u>6,000</u>
				1,36,650
Less : Advance tax paid				<u>2,40,000</u>
Refund				(-) 1,03,350

Notes:

1. Computation of Income from House Property

Particulars	₹
Gross Annual Value – Rent received (treated as fair rent)	20,000
Less : Municipal taxes paid	<u>3,000</u>
Net Annual Value (NAV)	17,000
Less : Statutory deduction under section 24 @ 30% of NAV	<u>5,100</u>
Income from House Property	<u>11,900</u>

2. Computation of Profits and gains of business or profession

Particulars	₹	₹
Net Profit as per Income & Expenditure Account		5,70,900
Add : Depreciation charged	42,500	
Municipal Taxes paid	3,000	
Advance Tax (See Note-4)	<u>2,40,000</u>	<u>2,85,500</u>
		8,56,400
Less: Rent received	20,000	
Interest on Post Office MIS	86,400	
Interest on Term Deposit with bank (Net of TDS)	27,000	
Winning from lotteries (Net of TDS)	7,000	
Depreciation as per Income-tax Act, 1961	<u>45,000</u>	<u>1,85,400</u>

Salary from Nursing Home as partner	1,50,000	6,71,000
Commission from Nursing home as partner	<u>50,000</u>	<u>2,00,000</u>
Income from business		<u>8,71,000</u>

3. Computation of Income from Other Sources

Particulars	₹
Interest Post Office MIS	86,400
Interest on Term Deposit with Bank (Gross)	30,000
Winning from lotteries (Gross)	10,000
Fees from University of Trinidad	50,000
Pension from LIC Jeevan Suraksha	<u>84,000</u>
Income from Other Sources	<u>2,60,400</u>

4. Advance Tax is not allowable as deduction.

5. Depreciation of Apparatus :

	₹
WDV as on 1.4.2013	3,00,000
Depreciation @15%	<u>45,000</u>
WDV as on 31.3.2014	<u>2,55,000</u>

6. Any salary, bonus, commission or remuneration by whatever name called due to or received by a partner of a firm from the firm shall not be treated as salary but it shall be treated as income from business or profession for the purposes of section 28.

7. As per section 58(4), no expenditure can be allowed against winnings from lotteries. Therefore, amount spent on lottery tickets being ₹ 350, cannot be allowed as deduction from income from winnings of lotteries.

8. Pension from LIC Jeevan Suraksha is taxable as Income from other sources.

Question 30

From the following particulars furnished by Mr. X for the year ended 31.3.2014, you are requested to compute his total income and tax payable for the assessment year 2014-15.

- (a) *Mr. X retired on 31.12.2013 at the age of 58, after putting in 25 years and 9 months of service, from a private company at Mumbai.*
- (b) *He was paid a salary of ₹ 25,000 p.m. and house rent allowance of ₹ 6,000 p.m. He paid rent of ₹ 6,500 p.m. during his tenure of service.*
- (c) *On retirement, he was paid a gratuity of ₹ 3,50,000. He was not covered by the payment of Gratuity Act. His average salary in this regard may be taken as ₹ 24,500. Mr. X had not received any other gratuity at any point of time earlier, other than this gratuity.*

8.79 Income-tax

- (d) He had accumulated leave of 15 days per annum during the period of his service; this was encashed by Mr. X at the time of his retirement. A sum of ₹ 3,15,000 was received by him in this regard. His average salary may be taken as ₹ 24,500. Employer allowed 30 days leave per annum.
- (e) After retirement, he ventured into textile business and incurred a loss of ₹ 80,000 for the period upto 31.3.2014.
- (f) Mr. X has invested ₹ 62,500 in public provident fund and ₹ 37,500 in National Savings Certificates.

Answer

Computation of total income of Mr. X for A.Y.2014-15

Particulars	₹	₹
Income from Salaries		
Basic salary (₹ 25,000 x 9 months)		2,25,000
House rent allowance		
Actual amount received	54,000	
Less: Exemption under section 10(13A)(Note 1)	<u>36,000</u>	18,000
Gratuity		
Actual amount received	3,50,000	
Less: Exemption under section 10(10)(iii) (Note 2)	<u>3,06,250</u>	43,750
Leave encashment		
Actual amount received	3,15,000	
Less: Exemption under section 10(10AA) (Note 3)	<u>2,45,000</u>	<u>70,000</u>
Gross Salary		3,56,750
Profits and gains of business or profession		
Business loss of ₹ 80,000 to be carried forward as the same cannot be set off against salary income		<u>Nil</u>
Gross Total income		3,56,750
Less: Deduction under section 80C		
Investment in public provident fund	62,500	
Investment in NSC	<u>37,500</u>	<u>1,00,000</u>
Total income		2,56,750
Tax on total income		5,675
Less: Rebate under section 87A		<u>2,000</u>

Add: Education cess @ 2% and SHEC @ 1%	3,675
	<u>110</u>
Tax payable	<u>3,785</u>
Tax payable (rounded off)	3,790

Note :

(1) As per section 10(13A), house rent allowance will be exempt to the extent of least of the following three amounts:

(i) HRA actually received (6,000 x 9)	54,000
(ii) Rent paid in excess of 10% of salary (₹ 6,500 – ₹ 2,500) x 9 months	36,000
(iii) 50% salary	1,12,500

(2) Gratuity of ₹ 3,06,250 is exempt under section 10(10)(iii), being the minimum of the following amounts :

(i) Actual amount received	3,50,000
(ii) Half month average salary for each year of completed service (1/2 x 24,500 x 25)	3,06,250
(iii) Statutory limit	10,00,000

(3) Leave encashment is exempt upto the least of the following:

(i) Actual amount received	3,15,000
(ii) 10 months average salary (24,500 x 10)	2,45,000
(iii) Cash equivalent of unavailed leave calculated on the basis of maximum 30 days for every year of actual service rendered to the employer from whose service he retired (see note 4 below)	3,06,250
(iv) Statutory limit	3,00,000

(4) Since the leave entitlement of Mr. X as per his employer's rules is 30 days credit for each year of service and he had accumulated 15 days per annum during the period of his service, he would have availed/taken the balance 15 days leave every year.

Leave entitlement of Mr.X on the basis of 30 days for every year of actual service rendered by him to the employer	= 30 days/year x 25 = 750 days
Less: Leave taken /availed by Mr.X during the period of his service	= 15 days/year x 25 = <u>375 days</u>
Earned leave to the credit of Mr.X at the time of his retirement	<u>375 days</u>
Cash equivalent of earned leave to the credit of Mr.X at the time of his retirement	= 375 × 24,500 /30 = ₹ 3,06,250

Question 31

- (i) Smt. Savita Rani was born on 01.07.1950. She is a Deputy Manager in a Company in Mumbai. She is getting a monthly salary and D.A. of ₹ 45,000 and ₹ 12,000 respectively. 50% of DA forms part of pay. She also gets a House Rent Allowance of ₹ 6,000 per month. She is a member of Recognised P.F. wherein she contributes 15% of her salary of ₹ 51,000 p.m. (45,000 + 6,000, being 50% of DA). Her employer also contributes an equal amount.
- (ii) She is living in the house of her minor son in Mumbai.
- (iii) During the previous year 2013-14, her minor son has earned an income of ₹ 30,000 (computed) as rent from a House Property, which had been transferred to him by Smt. Savita Rani without consideration a few years back.
- (iv) During the previous year 2013-14, she sold Government of India Capital Indexed Bonds for ₹ 1,50,000 on 30.09.2013, which she purchased on 01.07.2001 for ₹ 80,000 (Cost inflation index – F.Y. 2001-2002: 426 and for the F.Y. 2013-14: 939).
- (v) Her employer gave her an interest free loan of ₹ 1,50,000 on 01.10.2013 to one of her son's wife for the purchase of an Alto Maruti Car. Nothing has been repaid to the company towards the loan. The lending rate on SBI for a similar loan is 8% as on 01.04.2013.
- (vi) During the previous year 2013-14 she paid ₹ 15,000 by cheque to GIC towards Medical Insurance Premium of her dependent mother.

Compute the taxable income and tax liability of Mrs. Savita Rani for the A.Y. 2014-15.

Answer

Computation of taxable income and tax liability of Smt. Savita Rani for A.Y. 2014-15

Particulars	₹	₹
Income from salary		
Basic salary (₹ 45,000 x 12)		5,40,000
Dearness Allowance (₹ 12,000 x 12)		1,44,000
House Rent allowance (fully taxable)		72,000
Employer's contribution to recognized provident fund in excess of 12% is taxable as salary income		
12% of salary is ₹ 73,440. Employer's contribution is 15% of salary, which is ₹ 91,800		
Excess contribution is (₹ 91,800 – ₹ 73,440)		18,360
Perquisite in respect of interest free loan (₹ 1,50,000 x 8% x ½)		6,000
Net Salary		<u>7,80,360</u>
Income from house property (See Note below)		30,000
Long term Capital Gain:		
Sale consideration of GOI capital indexed bonds	1,50,000	

Less: Indexed cost of acquisition (₹ 80,000 x 939/426)	1,76,338	
Long-term capital loss (to be carried forward)	<u>26,338</u>	
Gross Total Income		8,10,360
Deduction under section 80C – in respect of recognized provident fund contribution	91,800	
Deduction under section 80D – Mediclaim	<u>15,000</u>	<u>1,06,800</u>
Total Income		<u>7,03,560</u>
Tax Payable on ₹ 7,03,560		65,712
Add : Education cess and Secondary and higher education cess @ 3%		<u>1,971</u>
Total tax payable		<u>67,683</u>
Total tax payable (rounded off)		67,680

Note: As per section 27, any property transferred to the minor child without adequate consideration would be deemed to be the property of the assessee. Therefore, the income from house property of ₹ 30,000 (computed) is to be assessed in the hands of Smt. Savita Rani.

Question 32

Ramesh retired as General manager of XYZ Co. Ltd. on 30.11.2013 after rendering service for 20 years and 10 months. He received ₹ 3,00,000 as gratuity from the employer. (He is not covered by Gratuity Act, 1972).

His salary particulars are given below :

Basic pay	₹ 10,000 per month up to 30.6.2013
Basic pay	₹ 12,000 per month from 1.7.2013
Dearness allowance (Eligible for retirement benefits)	50% of basic pay
Transport allowance	₹ 1,500 per month

He resides in his own house. Interest on monies borrowed for the self occupied house is ₹ 24,000 for the year ended 31.03.2014.

From a fixed deposit with a bank, he earned interest income of ₹ 18,000 for the year ended 31.03.2014.

Compute taxable income of Ramesh for the year ended 31.03.2014.

Answer

Computation of taxable income of Ramesh for the A.Y. 2014-15

Particulars	₹	₹
Income from salary		
Basic pay : April to June (₹ 10,000 x 3)		30,000
Basic pay : July to November (₹ 12,000 x 5)		60,000

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Dearness allowance @ 50% basic pay		45,000
Transport allowance (₹ 1500 x 8) less exemption @ ₹ 800 per month (₹ 12,000 – ₹ 6,400)		5,600
Gratuity		
(i) Statutory limit ₹ 10,00,000		
(ii) Half month average salary [See Note below] ₹ 8,100 x 20 yrs = ₹ 1,62,000		
(iii) Actual amount received = ₹ 3,00,000		
Least of the above i.e. ₹ 1,62,000 is exempt. Balance is taxable (₹ 3,00,000 – ₹ 1,62,000)		<u>1,38,000</u>
		2,78,600
Income from house property:		
Self occupied – ALV	Nil	
Less: Interest on monies borrowed under section 24(b)	<u>24,000</u>	(24,000)
Income from other sources:		
Fixed deposit interest		<u>18,000</u>
Total income		<u>2,72,600</u>

Note :

Average salary of 10 months preceding the month of retirement is to be computed : ₹	
Basic pay ₹ 10,000 x 6	60,000
Basic pay ₹ 12,000 x 4	<u>48,000</u>
Total	1,08,000
Add: 50% of Dearness Allowance–eligible for retirement benefits	<u>54,000</u>
	<u>1,62,000</u>
Average salary : ₹ 1,62,000/10	16,200
Half month average salary ₹ 16,200 / 2	8,100

Question 33

Rosy and Mary are sisters, born and brought up at Mumbai. Rosy got married in 1982 and settled at Canada since 1982. Mary got married and settled in Mumbai. Both of them are below 60 years. The following are the details of their income for the previous year ended 31.3.2014:

S.No.	Particulars	Rosy ₹	Mary ₹
1.	Pension received from State Government	--	10,000
2.	Pension received from Canadian Government	20,000	--

3.	Long-term capital gain on sale of land at Mumbai	1,00,000	50,000
4.	Short-term capital gain on sale of shares of Indian listed companies in respect of which STT was paid	20,000	2,00,000
5.	LIC premium paid	--	10,000
6.	Premium paid to Canadian Life Insurance Corporation at Canada	10,000	--
7.	Mediclaime policy premium paid	--	5,000
8.	Tax saving bond purchased in March, 2014	30,000	20,000
9.	Rent received in respect of house property at Mumbai	60,000	30,000

Compute the taxable income and tax liability of Mrs. Rosy and Mrs. Mary for the Assessment Year 2014-15 and tax thereon.

Answer

Computation of taxable income of Mrs. Rosy and Mrs. Mary for the A.Y.2014-15

S. No.	Particulars	Mrs. Rosy	Mrs. Mary
		₹	₹
(I)	Salaries		
	Pension received from State Government	-	10,000
	Pension received from Canadian Government is not taxable in the case of a non-resident since it is earned and received outside India	-	-
		-	10,000
(II)	Income from house property		
	Rent received from house property at Mumbai (assumed to be the annual value in the absence of other information i.e. municipal value, fair rent and standard rent)	60,000	30,000
	Less: Deduction under section 24(a) @ 30%	18,000	9,000
		42,000	21,000
(III)	Capital gains		
	Long-term capital gain on sale of land at Mumbai	1,00,000	50,000
	Short term capital gain on sale of shares of Indian listed companies in respect of which STT was paid	20,000	2,00,000
		1,20,000	2,50,000
(A)	Gross Total Income [(I)+(II)+(III)]	1,62,000	2,81,000

8.85 Income-tax

	<i>Less: Deductions under Chapter VIA</i>		
1.	Deduction under section 80C		
	1. LIC Premium paid	-	10,000
	2. Premium paid to Canadian Life Insurance Corporation	10,000	
	3. Tax Saving Bond (assuming that they are notified infrastructure bonds eligible for deduction under section 80C)		
		<u>30,000</u>	<u>20,000</u>
		40,000	30,000
2.	Deduction under section 80D – Medclaim premium paid (assuming that the same is paid by cheque)		<u>5,000</u>
		40,000	35,000
(B)	Total deduction under Chapter VIA is restricted to income other than capital gains taxable under sections 111A & 112	<u>40,000</u>	<u>31,000</u>
(C)	Total income (A-B)	<u>1,22,000</u>	<u>2,50,000</u>
	Tax liability of Mrs. Rosy for A.Y. 2014-15		
	Tax on long-term capital gains @ 20%	20,000	Nil
	Tax on short-term capital gains @ 15%	<u>3,000</u>	
		23,000	
	Tax liability of Mrs. Mary for A.Y.2014-15		
	Tax on short-term capital gains @ 15% of ₹ 50,000 [i.e. ₹ 2,00,000 less ₹ 1,50,000, being the unexhausted basic exemption limit as per proviso to section 111A]		7,500
	<i>Less: Rebate under section 87A</i>		<u>2,000</u>
			5,500
	Education cess @ 2% & SHEC@ 1%	<u>690</u>	<u>165</u>
	Total tax payable	<u>23,690</u>	<u>5,665</u>

Note :

- (1) Long-term capital gains is chargeable to tax @ 20% as per section 112.
- (2) Short-term capital gains on transfer of equity shares in respect of which securities transaction tax is paid is subject to tax @ 15% as per section 111A.
- (3) In case of resident individuals, if the basic exemption limit is not fully exhausted against other income, then the long-term capital gains/short-term capital gains will be reduced by the unexhausted basic exemption limit and only the balance will be taxed at 20%/15% respectively. However, this benefit is not available to non-residents. Therefore, while Mrs. Mary can set-off unexhausted basic exemption limit against long-term capital gains and short-term capital gains taxable under section 111A, Mrs. Rosy cannot do so.

- (4) Since long-term capital gains is taxable at the rate of 20% and short-term capital gains is taxable at the rate of 15%, it is more beneficial for Mrs. Mary to first exhaust her basic exemption limit of ₹ 2,00,000 against long-term capital gains of ₹ 50,000 and the balance limit of ₹ 1,50,000 (i.e., 2,00,000 – 50,000) against short-term capital gains.

Question 34

Mr. Rajesh is serving in a public limited company as General Manager (Finance). His total emoluments for the year ended 31st March, 2014 are as follows:

Basic Salary	₹ 5,40,000
HRA (Computed)	₹ 1,80,000
Transport allowance	₹ 12,400

Apart from the above, his employer has sold the following assets to him on 1st January, 2014:

- (i) Laptop computer for ₹ 20,000 (Acquired in September, 2012 for ₹ 1,20,000)
- (ii) Car 1800 cc for ₹ 3,20,000 (purchased in April, 2011 for ₹ 8,50,000)

He also owns a residential house, let out for a monthly rent of ₹ 15,000. The fair rental value of the property for the let out period is ₹ 1,50,000. The house was self-occupied by him from 1st January, 2014 to 31st March, 2014. He has taken a loan from Bank of ₹ 20 lacs for the construction of the property, and has repaid ₹ 1,05,000 (including interest ₹ 40,000) during the year.

Mr. Rajesh sold shares of different Indian companies on 14th April, 2013:

Name	Sale value (per share)	Purchase price (per share)	Acquired on	No. of shares
A Ltd.	₹ 150	₹ 120	2 nd May, 2007	200
B Ltd.	₹ 82	₹ 65	16 th April, 2012	125

Sale proceeds were subject to brokerage of 0.1% and securities transaction tax of 0.125% on the gross consideration. He received income-tax refund of ₹ 5,750 (including interest ₹ 750) relating to the assessment year 2012-13.

Compute the total income of Mr. Rajesh for the Assessment Year 2014-15.

Answer

Computation of total income of Mr. Rajesh for the A.Y. 2014-15

Particulars	₹
Income from salaries (Working note 1)	9,86,800
Income from house property (Working note 2)	1,00,000
Capital gains	
Short-term capital gains (Working note 3)	2,115

8.87 Income-tax

Income from other sources: Interest on Income-tax refund	<u>750</u>
Gross Total Income	10,89,665
<i>Less: Deduction under Chapter VIA</i>	
Deduction under section 80C	
Repayment of housing loan (principal) [See Note below]	<u>65,000</u>
Total Income	<u>10,24,665</u>
Total Income (rounded off)	10,24,670

Working Notes :

	Particulars	₹	₹
1.	Income from salaries		
	Basic Salary		5,40,000
	HRA (computed)		1,80,000
	Transport allowance	12,400	
	<i>Less: Exempt under section 10(14) [₹ 800 × 12]</i>	<u>9,600</u>	2,800
	Perquisites (relating to sale of movable assets by employer)		
	<i>Laptop Computer</i>		
	Cost [September, 2012]	1,20,000	
	<i>Less: Depreciation at 50% for one completed year</i>	<u>60,000</u>	
	WDV [September, 2013]	60,000	
	<i>Less: Amount paid to the employer</i>	<u>20,000</u>	
	Perquisite value of laptop (A)	<u>40,000</u>	
	<i>Car</i>		
	Cost [April, 2011]	8,50,000	
	<i>Less: Depreciation for the 1st year</i> (April'11 to March'12) @ 20% of WDV	<u>1,70,000</u>	
	WDV [April, 2012]	6,80,000	
	<i>Less: Depreciation for the 2nd year</i> (April'12 to March'13) @ 20% of WDV	<u>1,36,000</u>	
	WDV [April, 2013]	5,44,000	
	<i>Less: Amount paid to the employer</i>	<u>3,20,000</u>	
	Perquisite value of car (B)	<u>2,24,000</u>	
	Perquisite value (A) + (B)		<u>2,64,000</u>
	Income chargeable under the head "Salaries"		<u>9,86,800</u>

2.	<p>Income from house property</p> <p>Section 23(2) provides that the annual value of a self-occupied house shall be taken as Nil. However, section 23(3) provides that the benefit of self-occupation would not be available if the house is actually let during the whole or part of the previous year. This implies that the benefit of taking the annual value as nil would be available only if the house is self-occupied for the whole year.</p> <p>In this case, therefore, the benefit of taking annual value as Nil is not available since the house is self-occupied only for 3 months. In such a case, the gross annual value has to be computed as per section 23(1). Accordingly, the fair rent for the whole year should be compared with the actual rent for the let-out period and whichever is higher shall be adopted as the Gross Annual Value.</p>						
Particulars		₹	₹				
Gross Annual Value (higher of fair rent for the whole year and actual rent for the let-out period)			2,00,000				
Fair rent for the whole year = ₹ 1,50,000 × 12/9		2,00,000					
Actual rent received = ₹ 15,000 × 9		1,35,000					
<i>Less:</i> Municipal taxes			<u>Nil</u>				
Net Annual Value (NAV)			2,00,000				
<i>Less:</i> Deductions under section 24							
30% of NAV		60,000					
Interest on loan [See Note below]		<u>40,000</u>	<u>1,00,000</u>				
Income from house property			<u>1,00,000</u>				
<i>Note : It is presumed that the interest of ₹ 40,000 paid on housing loan represents the interest actually due for the year.</i>							
3.	<p>Income chargeable as "Capital Gains"</p> <p>Section 10(38) exempts long-term capital gain on sale of equity shares of a company, if such transaction is chargeable to securities transaction tax. Since Mr.Rajesh has held shares of A Ltd. for more than 12 months, the gains arising from sale of such shares is a long-term capital gain, which is exempt under section 10(38), since securities transaction tax has been paid on such sale.</p> <p>Shares in B Ltd. are held for less than 12 months and hence the capital gains arising on sale of such shares is a short-term capital gain chargeable to tax @15% as per section 111A, since the transaction is subject to securities transaction tax. It may be noted, however, that securities transaction tax is not a deductible expenditure.</p> <p>Short-term capital gains arising from sale of shares of B Ltd.</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 60%; padding: 5px;">Sale consideration (82 × 125)</td> <td style="border-left: 1px solid black; border-right: 1px solid black; text-align: right; padding: 5px;">10,250</td> </tr> <tr> <td style="padding: 5px;"><i>Less:</i> Brokerage @ 0.1%</td> <td style="border-left: 1px solid black; border-right: 1px solid black; text-align: right; padding: 5px;"><u>10</u></td> </tr> <tr> <td style="padding: 5px;">Net sale consideration</td> <td style="border-left: 1px solid black; border-right: 1px solid black; text-align: right; padding: 5px;">10,240</td> </tr> </table>	Sale consideration (82 × 125)	10,250	<i>Less:</i> Brokerage @ 0.1%	<u>10</u>	Net sale consideration	10,240
Sale consideration (82 × 125)	10,250						
<i>Less:</i> Brokerage @ 0.1%	<u>10</u>						
Net sale consideration	10,240						

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Cost of acquisition (65 x 125)	<u>8,125</u>
Short-term capital gains	<u>2,115</u>

Question 35

Mr. Ram, who does not maintain books of account for the year ended 31.3.2014, requests you to compute his total income and the tax payable thereon for the assessment year 2014-15 from the following:

- ₹
- (i) Basic Salary - 20,000 p.m.
 CCA - 1,000 p.m.
 HRA - 5,000 p.m.
- (ii) Ram resides in Chennai, paying a rent of ₹ 6,000 per month.
- (iii) Ram is paid an education allowance of ₹ 500 per month per child for all the three of his children. Actual expenses (tuition fees only) amounts to ₹ 15,000, ₹ 10,000 and ₹ 5,000 respectively.
- (iv) He bought a heavy goods vehicle on 7.6.2013 and has been letting it on hire from the same date. He declares an income of ₹ 34,900 from the same.
- (v) Interest from company deposits is ₹ 15,000 and bank interest from saving bank account is ₹ 5,000.
- (vi) Interest is payable on bank loans availed for buying the truck and making company deposits as follows:-

Purpose	Date of loan	Amount	Interest rate
Truck purchase	1.4.2013	5 lakhs	10% p.a.
Company deposit	1.10.2013	1 lakh	9 % p.a.

- (vii) Loss carried forward arising from speculating in shares during the preceding previous year and eligible for set-off is ₹ 1,00,000.
- (viii) Ram has invested ₹ 12,000 in notified equity linked saving scheme of UTI, ₹ 52,000 in PPF, ₹ 9,000 as premium on life insurance policy taken on 31.07.2012 on his own life (sum assured ₹ 40,000) and ₹ 15,000 towards pension fund of LIC.

Answer

Computation of total income of Mr. Ram for the Assessment Year 2014-15

Particulars	₹	₹
Income from Salary		
Basic Salary (₹ 20,000 × 12)		2,40,000
CCA (₹ 1,000 × 12)		12,000
HRA (₹ 5,000 × 12)	60,000	

<i>Less:</i> Exempt under section 10(13A) [See Note 1 below]	<u>48,000</u>	12,000
Education Allowance (₹ 500×12×3)	18,000	
<i>Less:</i> Exempt under section 10(14) (₹ 100×12×2)	<u>2,400</u>	<u>15,600</u>
Income from Salary		2,79,600
Profits and gains from business or profession		
Income from the business of letting on hire, a heavy vehicle under section 44AE (₹ 5,000×10) [See Note 2 below]		50,000
Income from Other Sources		
Interest from company deposits	15,000	
Interest from Saving Bank Account	<u>5,000</u>	
	20,000	
<i>Less:</i> Deduction under section 57		
₹ 1,00,000 @ 9% for 6 months—towards loan interest	<u>4,500</u>	<u>15,500</u>
Gross Total Income		3,45,100
<i>Less:</i> Deduction under Chapter VI-A		
Under section 80C [See Note 4 below]	93,000	
Under section 80CCC	<u>15,000</u>	
	<u>1,08,000</u>	
restricted to	1,00,000	
Under section 80TTA- Interest from Saving Bank Account (See Note-7 below)	<u>5,000</u>	<u>1,05,000</u>
Total Income		<u>2,40,100</u>

Computation of tax payable for the A.Y.2014-15

Tax on ₹ 2,40,100	4,010
<i>Less:</i> Rebate under section 87A	<u>2,000</u>
	2,010
<i>Add:</i> Education cess @ 2% and SHEC @ 1%	60
Tax Payable	<u>2,070</u>

Notes :

- (1) HRA is exempt to the extent of the least of the following under section 10(13A)
- (1) 50% of salary (as the city is Chennai) i.e. 50% of ₹ 2,40,000 = ₹ 1,20,000
 - (2) Excess of rent paid over 10% of salary = ₹ 72,000 – ₹ 24,000 = ₹ 48,000
 - (3) Actual HRA received = 5,000 × 12 = ₹ 60,000
- Least of the above i.e. ₹ 48,000 is exempt under section 10(13A)

- (2) In the case of a person owning not more than 10 vehicles at any time during the previous year, estimated income from each heavy vehicle will be deemed to be ₹ 5,000/- for every month or part of the month during which the heavy vehicle is owned by the assessee during the previous year [Section 44AE].

Presumptive income = ₹ 5,000 × 10 = 50,000

If, however, the assessee declares a higher amount, such amount will be considered as income. In the instant case, since the assessee declares a lower amount, it cannot be considered, since no books of account are maintained. Also, interest is not deductible, since under section 44AE, all deductions under sections 30 to 38 are deemed to have been allowed.

- (3) Brought forward loss from speculation business can be set off only against income from speculation business and not against other business income.

- (4) Deduction under section 80C:

Investment in notified equity linked saving scheme of UTI	12,000
Investment in PPF	52,000
Life insurance premium on own life restricted to 10% of sum assured	4,000
Tuition fees paid for two of his children (Most favourable to Ram)	25,000
	93,000

- (5) Contribution to pension fund of LIC ₹ 15,000 is deductible under section 80CCC.
- (6) Total deduction under sections 80C, 80CC and 80CCD is limited to ₹ 1,00,000 as per section 80CCE.
- (7) Deduction under section 80TTA is allowed in respect of interest from Saving Bank Account upto a maximum of ₹ 10,000. Therefore, interest from Saving Bank Account of ₹ 5,000 is allowed as deduction.

Question 36

Mr. Ashok owns a property consisting of two blocks of identical size. The first block is used for business purposes. The other block has been let out from 1.4.2013 to his cousin for ₹ 10,000 p.m. The cost of construction of each block is ₹ 5 lacs (fully met from bank loan), rate of interest on bank loan is 10% p.a. The construction was completed on 31.3.2013. During the year ended 31.3.2014, he had to pay a penal interest of ₹ 2,000 in respect of each block on account of delayed payments to the bank for the borrowings. The normal interest paid by him in respect of each block was ₹ 42,000. Principal repayment for each block was ₹ 23,000 made at the end of the year. An identical block in the same neighbourhood fetches a rent of ₹ 15,000 per month. Municipal tax paid in respect of each block was ₹ 12,000.

The income computed in respect of business prior to adjustment towards depreciation on any asset is ₹ 2,20,000.

Depreciation on equipments used for business is ₹ 30,000.

On 23.3.2014, he sold shares of B Ltd., a listed share in BSE for ₹ 2,30,000. The share had been purchased 10 months back for ₹ 1,80,000. Securities transaction tax paid may be taken as ₹ 220.

Brought forward business loss of a business discontinued on 12.1.2013 is ₹ 80,000. This loss has been determined in pursuance of a return of income filed in time and the current year is the seventh year.

The following payments were effected by him during the year :

- (i) LIP of ₹ 20,000 on his life and ₹ 12,000 for his son aged 22, engaged as a software engineer and drawing salary of ₹ 25,000 p.m.
- (ii) Mediclaim premium of ₹ 6,000 for himself and ₹ 5,000 for above son. The premiums were paid by cheque.

You are required to compute the total income for the assessment year 2014-15 and the tax payable. The various heads of income should be properly shown. Ignore the interest on bank loan for the period prior to 1.4.2013, as the bank had waived the same.

Answer

Computation of total income of Mr. Ashok for the A.Y.2014-15

Particulars	₹	₹	₹
Income from house property [See Note I]			
House block 1 used for business, hence ALV		Nil	
House block 2 let out (higher of fair rent and rent receivable)		1,80,000	
Less: Municipal tax paid		<u>12,000</u>	
Net annual value (NAV)		1,68,000	
Less: Deductions under section 24			
(a) 30% of NAV	50,400		
(b) Interest on bank loan @ 10% on ₹ 5,00,000	<u>50,000</u>	<u>1,00,400</u>	67,600
Profits and gains of business or profession [See Note II]			
Income prior to adjustment for depreciation		2,20,000	
Less : Depreciation on equipments used for business	30,000		
Depreciation on building ₹ 5,00,000 @ 10%	<u>50,000</u>	<u>80,000</u>	
		1,40,000	
Less: Set off of brought forward business loss relating to discontinued business [See Note III]		<u>80,000</u>	60,000

Capital Gains [See Note IV]			
Short term capital gains from sale of listed shares			
Full value of consideration		2,30,000	
Less: Cost of acquisition		<u>1,80,000</u>	<u>50,000</u>
Gross Total Income			1,77,600
Less: Deduction under section 80C in respect of LIP ₹ 32,000 and housing loan repayment in respect of II block ₹ 23,000	55,000		
Deduction under section 80D (for self)	<u>6,000</u>		<u>61,000</u>
Total income			<u>1,16,600</u>
Tax on total income			Nil

Notes :**I – On computation of Income from house property**

- (i) The annual value of the house property which is used for business would not fall under the head "Income from house property". Therefore, the annual value of the first block is not chargeable to tax under the head "Income from house property". However, depreciation there on at 10% has been claimed while computing the income from business.
- (ii) As regards the second block, the sum for which the property may be reasonably expected to be let is ₹ 15,000 per month. The Gross Annual Value (GAV) of the block is the higher of fair rent (i.e., ₹ 15,000 p.m.) or the actual rent received (₹ 10,000 p.m.) Hence, the GAV of the second block is ₹ 1,80,000 (i.e. ₹ 15,000 p.m.)
- (iii) Under section 24(b), interest on bank loan for construction of house is deductible. However, penal interest is not deductible. Interest due during the year in respect of the second block is ₹ 50,000 (i.e. 10% of ₹ 5 lakhs), which is allowable as deduction under section 24(b).

II – On computation of Profits and gains of business or profession

Mr. Ashok can claim depreciation @ 10% on the building used by him for business purposes. The depreciation on the first block is ₹ 50,000 (being 10% of ₹ 5,00,000) and depreciation on equipments used for business is ₹ 30,000. Hence the depreciation allowable during the year is ₹ 80,000.

III – On set off of business loss

As per section 72, business loss relating to discontinued business is eligible for set off.

IV – On treatment of short-term capital gains (STCG)

The listed shares have been sold and securities transaction tax is paid, hence it is taxable at 15% as per section 111A. For the purpose of providing deduction under Chapter VI-A, the gross total income should be reduced by the STCG on listed shares.

V – On computation of deductions under sections 80C and 80D

Deduction under section 80C can be claimed in respect of life insurance premium paid for major son, even though he is not dependent on the assessee. It is assumed Block 2 let out to cousin was used for residential purpose and accordingly principal repayment was considered for deduction under section 80C.

However, deduction under section 80D cannot be claimed in respect of mediclaim premium paid for non-dependant son. Mediclaim premium paid for self of ₹ 6,000 is eligible for deduction.

Question 37

Total income of Mrs. Priti, aged 59, a resident of Mumbai for the financial year 2013-14 is ₹ 2,10,500. It includes an income of ₹ 22,000 from the business of dealing in shares on which she has paid securities transaction tax of ₹ 1,500. She has also deposited ₹ 15,000 in her P.P.F. account with the State Bank of India. Compute her tax liability for the A.Y. 2014-15.

Answer

Computation of tax liability of Mrs. Priti for A.Y. 2014-15

Particulars	₹	₹
Total income other than business of dealing in shares (₹ 2,10,500 – ₹ 22,000) (before deduction under section 80C)		1,88,500
Income from business of dealing in shares – See Note		20,500
Gross Total Income		2,09,000
Less : Deduction under section 80C in respect of PPF deposit		15,000
Total income		1,94,000
Tax on total income		Nil
Note: ₹ 22,000 less amount of ₹ 1,500 paid towards securities transaction tax eligible for deduction under section 36(1)(xv).		

Question 38

Mr. A, a senior citizen, has furnished the following particulars relating to his house properties:

Nature of occupation	House I Self occupied ₹	House II Let out ₹
<i>Municipal valuation</i>	60,000	1,20,000
<i>Fair rent</i>	90,000	1,50,000
<i>Standard rent</i>	75,000	90,000
<i>Actual rent per month</i>		9,000
<i>Municipal taxes paid</i>	6,000	12,000

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Interest on capital borrowed	70,000	90,000
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Loan for both houses were taken on 1.4.2007. House II remained vacant for 4 months.

Besides the above two houses, A has inherited during the year an old house from his grand father. Due to business commitments, he sold the house immediately for a sum of ₹ 250 lakhs. The house was purchased in 1960 by his grand father for a sum of ₹ 2 lakhs. However, the fair market value as on 1.4.1981 was ₹ 20 lakhs. With the sale proceeds, A purchased a new house in March, 2014 for a sum of ₹ 100 lakhs and the balance was used in his business.

The other income particulars of Mr. A besides the above are as follows (A.Y. 2014-15)

Business loss	₹ 2 lakhs
Income from other sources (Fixed Deposit interest)	₹ 1 lakh
Investments made during the year : PPF	₹ 1,00,000
Cost inflation index (F.Y. 2013-14)	939

Compute total income of Mr. A and his tax liability for the assessment year 2014-15

Answer

Computation of Total Income and Tax liability of Mr. A for A.Y. 2014-15

Particulars	₹	₹
1. Income from house property – House I	(70,000)	
– House II	<u>(48,000)</u>	
(See working note 1)		(1,18,000)
2. Profits and gains of business		(2,00,000)
3. Capital gains – long term (See working note 2)		1,30,00,000
4. Income from other sources – Bank interest		<u>1,00,000</u>
Gross total income		1,27,82,000
Less : Deduction under chapter VI-A		
Deduction under section 80C (PPF)		<u>1,00,000</u>
Total income		<u>1,26,82,000</u>
Tax liability		
Total income other than long term capital gain is Nil.		
Taxable long term capital gain is = 1,24,32,000		
[i.e. ₹ 1,30,00,000 – ₹ 3,18,000 – basic exemption limit of ₹ 2,50,000]		
On long term capital gains of ₹ 1,24,32,000 @ 20%		24,86,400
Surcharge @ 10%		2,48,640
		<u>27,35,040</u>
Education cess@2% and Secondary and higher education cess@1%		<u>82,051</u>
Total tax payable		<u>28,17,091</u>

Working notes:

1. Calculation of income from house property

House I – Self occupied		₹
Annual value		Nil
Less : Interest as per section 24(b)		<u>70,000</u>
Loss from house property (House I)		<u>(70,000)</u>
House II - Let out		₹
Gross annual value (₹ 9,000 x 8)		72,000
Less :Municipal taxes		<u>12,000</u>
Net Annual Value (NAV)		60,000
Less : Deductions under section 24		
30% of NAV	18,000	
Interest on borrowed capital	<u>90,000</u>	
		<u>1,08,000</u>
Loss from house property (house II)		<u>(48,000)</u>

Note : Interest on capital borrowed will be allowed in full for let out properties. As per section 23(1)(c), where the property or any part of the property is let and was vacant during the whole or any part of the previous year and owing to such vacancy the actual rent received or receivable by the owner in respect thereof is less than the annual letting value, then the actual rent received or receivable would be the Gross Annual Value of the property. In this case, the actual rent received (i.e. ₹ 72,000) is less than the annual letting value on (i.e. ₹ 90,000) account of vacancy and therefore, the actual rent received is taken as the Gross Annual Value.

2. Computation of Capital Gains

Particulars	₹	₹
Sale consideration	2,50,00,000	
Less: Indexed Cost of acquisition (₹ 20,00,000 x 939/939)	<u>20,00,000</u>	
	2,30,00,000	
Less : Exemption under section 54	<u>1,00,00,000</u>	
Taxable long term capital gain		1,30,00,000

As per the definition of the indexed cost of acquisition under clause (iii) of *Explanation to* section 48, indexation benefit will be available only from the previous year in which Mr. A first held the asset i.e. P.Y. 2013-14. Since Mr. A sold the asset in the same year in which it was held by him, cost of acquisition and indexed cost of acquisition would be same.

Note: As per the view expressed by Bombay High Court, in the case of *CIT v. Manjula J. Shah 16 Taxmann 42*, in case the cost of acquisition of the capital asset in the hands of the assessee is taken to be cost of such asset in the hands of the previous owner, the indexation benefit would be available from the year in which the capital asset is acquired by the previous owner. If this view is taken, the indexed cost of acquisition would be ₹ 1,87,80,000 and long term capital gain (before exemption under section 54) would be ₹ 62,20,000. Therefore, exemption under section 54 would be restricted to ₹ 62,20,000 and the taxable long term capital gain would be Nil.

3. It has been assumed that the loss from house property and business loss have been set-off fully against long term capital gains. Therefore, ₹ 1 lakh relating to section 80C investments are deducted against "Income from other sources". The taxable income represents long term capital gains only and the tax liability is computed accordingly.

Question 39

Mr. Balaji furnishes you the following information for the financial year ended 31st March, 2014:

Pension from Central Government	2,47,000
Rent from let out property	2,40,000
Interest on moneys borrowed for let out property - paid	1,60,000
Interest on moneys borrowed for let our property - unpaid	12,000
Income from business in trade in grains and pulses	4,10,000
Loss from speculation in Jewellery	80,000
Unabsorbed depreciation of discontinued textiles business of assessment year 2012-13	2,00,000

He let out a factory building with machinery for a monthly rent of ₹ 20,000.

The WDV of factory building as on 01-04-2013 was ₹ 8,10,000 (depreciation rate 10%) and WDV of machineries being ₹ 4,91,300 (depreciation rate 15%).

Compute the total income of Mr. Balaji for the Assessment year 2014-15.

Answer

Computation of total income of Mr. Balaji for the A.Y. 2014-15

Particulars	₹	₹	₹
Income from salaries			
Pension from Central Government (See Note 1)			2,47,000
Income from house property			
Gross Annual Value		2,40,000	

<i>(Rent received has been taken as the Gross Annual Value in the absence of other information relating to Municipal Value, Fair Rent and Standard Rent)</i>			
Less: Municipal Taxes paid		<u>NIL</u>	
Net Annual Value (NAV)		2,40,000	
<i>Less: Deduction under section 24</i>			
(a) Standard deduction @ 30% of NAV	72,000		
(b) Interest on borrowed capital (₹1,60,000+ ₹12,000) (See Note 2)	<u>1,72,000</u>	<u>2,44,000</u>	(4,000)
Income from business or profession			
Income from business of trading in grains and pulses		4,10,000	
Rent of factory building with machinery (₹20,000 x 12) (See Note 3)		2,40,000	
<i>Less: Depreciation</i>			
- Factory building (8,10,000 x 10%)	81,000		
- Machinery (4,91,300 x 15%)	<u>73,695</u>	<u>85,305</u>	4,95,305
			7,38,305
<i>Less: Brought forward depreciation relating to A.Y. 2012-13 from discontinued textile business (See Note 4)</i>			
			<u>2,00,000</u>
Total Income			<u>5,38,305</u>

Notes:

1. Uncommuted pension is fully taxable in the hands of both government and non-government employees. It is presumed that pension received by Mr. Balaji is uncommuted pension.
2. Interest accrued is allowable as deduction under section 24(b). Therefore, interest of ₹ 12,000 accrued but not paid during the year can also be claimed as deduction.
3. Composite rent from letting out of building along with machinery is not taxable under the head "Income from house property", if the two lettings are not separable. It would be taxable either as business income or income from other sources.

It has been assumed that the composite rent received by Mr. Balaji from letting out of factory building and machinery is not separable and letting out of factory building by Mr. Balaji is incidental to his main business of trading in grains and pulses and therefore, such income would be taxable under the head "Profit and gains from business or profession".

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4. Unabsorbed depreciation under section 32 can be carried forward indefinitely and set-off against income under any head, even if it relates to a discontinued business.
5. As per section 73, loss from a speculation business can be set off only against profit of another speculation business. Therefore, loss from speculation in jewellery of ₹ 80,000 cannot be set off in the current year since there is no profit from any other speculation business. The loss of ₹ 80,000 from speculation business has to be carried forward for set off against profit and gains of any speculation business in the succeeding 4 years.

Question 40

Mr. Hari, aged 54 years, provides the following information for the year ending 31-03-2014 :

	₹
(i) Rent from vacant site let on lease	1,12,000
(ii) Rent from house property at Delhi	20,000
	<i>per month</i>
(iii) Turnover from retail trade in grains (No books of account maintained)	24,37,500
(iv) Arrears of salary received from ex-employer	40,000
(v) Purchase of 10,000 shares of X Co. Ltd., on 01-01-2010	1,00,000
He received a 1 : 1 bonus on 01-01-2011. Sale of 5,000 bonus shares in September, 2013	2,20,000
(vi) Received ₹ 1,50,000 on 12-02-2014 being amount due from Mr. A, relating to goods supplied by Hari's father, which was written off as bad debt by his father in Assessment Year 2012-13 and allowed as deduction. Hari's father died in July 2012.	
(vii) Brought forward business loss relating to discontinued textile business of Hari relating to the Assessment Year 2012-13.	1,97,500
(viii) Brought forward depreciation relating to discontinued textile business of Hari	1,50,000
(ix) Hari contributed ₹ 30,000 to National Children's Fund and ₹ 40,000 to Charitable Trust enjoying exemption under section 80G.	

Compute the total income and the tax thereon of Mr. Hari for the Assessment Year 2014-15.

Answer

Computation of total income and tax liability of Mr. Hari for the A.Y. 2014-15

Particulars	₹	₹
Income from Salaries		
Arrears of salary received from ex-employer		40,000
Income from house property (See Note 1)		1,68,000

Profit and gains of business or profession		
Income from business of retail trade in grains (See Note 2)	1,95,000	
<i>Less:</i> Set-off of brought forward business loss relating to A.Y.2012-13 of discontinued textile business (See Note 5)	<u>1,95,000</u>	Nil
Capital gains (See Note 3)		
Sale consideration on sale of bonus shares	2,20,000	
<i>Less:</i> Indexed cost of acquisition	<u>Nil</u>	
Long term capital gains		2,20,000
Income from other sources		
Rent from vacant site let on lease		<u>1,12,000</u>
		5,40,000
<i>Less:</i> Set-off of unabsorbed depreciation relating to textile business (See Note 6)		<u>1,50,000</u>
Gross Total Income		3,90,000
<i>Less:</i> Deductions under Chapter VI-A (See Note 7)		<u>46,000</u>
Total Income		<u>3,44,000</u>
Tax on total income		
Tax on long-term capital gains@20% of ₹ 70,000 (₹ 2,20,000 - ₹ 1,50,000, being unabsorbed depreciation set-off)	14,000	
Tax on balance income of ₹ 2,74,000 (i.e. ₹ 3,44,000 – ₹ 70,000, being long term capital gains taxable@20%)	<u>7,400</u>	21,400
<i>Less:</i> Rebate under section 87A		<u>2,000</u>
		19,400
<i>Add:</i> Education cess @ 2%		388
Secondary and higher education cess @ 1%		<u>194</u>
Total tax liability		<u>19,982</u>

Notes:

(1) Income from House Property at Delhi

Particulars	₹
Gross Annual Value (GAV)	2,40,000
<i>Less:</i> Municipal taxes paid	<u>Nil</u>
Net Annual Value (NAV)	2,40,000
<i>Less:</i> Deduction under section 24 @ 30% of NAV	<u>72,000</u>
Income from house property	<u>1,68,000</u>

Note: Rent received has been taken as the Gross Annual Value in the absence of other information relating to Municipal Value, Fair Rent and Standard Rent.

- (2) Since Mr. Hari has not maintained books of accounts in respect of the business of retail trade in grains and the turnover from such business is less than ₹ 100 lacs, the income from such business would be computed on a presumptive basis under section 44AD @ 8% of turnover. The income under section 44AD is, therefore, ₹ 1,95,000, being 8% × ₹ 24,37,500.
- (3) Cost of acquisition of bonus shares is Nil as per section 55. Since the bonus shares were allotted on 1.1.2011, the period of holding of bonus shares exceeds 1 year, therefore, it is a long-term capital asset and the gain arising from sale of such shares shall be long-term capital gains.

Note – The problem has been solved by assuming that the shares are not listed and securities transaction tax is not paid on sale of such shares, and hence such long-term capital gains is taxable.

- (4) ₹ 1,50,000 represents the amount due from Mr. A relating to goods supplied by Mr. Hari's father, which was written off as a bad debt by his father in the A.Y.2012-13 and allowed as deduction to him. The said sum recovered by Mr. Hari, in the A.Y.2014-15, would not be treated as his income since there is no such provision under section 41(4) to treat the sum recovered by the successor in business as his income.
- (5) Business loss of a discontinued business can be carried forward and set-off against the profits of an existing business in the subsequent years. Brought forward business loss of ₹ 1,97,500 from discontinued textile business can be set-off against the current year income of ₹ 1,95,000 from the business of retail trade. The balance loss of ₹ 2,500 can be carried forward to the next year to be set-off against the business income of that year. It can be carried forward upto a maximum of 6 more assessment years to be set-off against the business income of those years.
- (6) Unabsorbed depreciation under section 32 can be carried forward indefinitely and set-off against income under any head.

Section 44AD specifically provides that while computing income of an eligible business on presumptive basis, any deduction allowable under sections 30 to 38 shall be deemed to have been given full effect to and no further deduction under those sections shall be allowed. However, in the given problem, the unabsorbed depreciation relates to discontinued textile business and not to the retail trade business (eligible business) in respect of which income is computed on a presumptive basis under section 44AD.

Therefore, it is possible to take a view that such unabsorbed depreciation not relating to the eligible business under section 44AD, can be set-off against income of the current year.

- (7) In the above solution, the deduction under Chapter VI-A and computation of tax liability has been worked out by setting-off the unabsorbed depreciation against long-term capital gains, which would be most beneficial for Mr. Hari, since the long-term capital gain is taxable @ 20%, whereas the normal income of Mr. Hari (i.e., ₹ 2,74,000) after such set-

off would be taxable at 10%, which is the rate applicable to the income slab which Mr. Hari falls in. Therefore, the deduction under Chapter VI-A be as follows -

Deduction under Chapter VI-A :

Particulars	₹	₹
Deduction under section 80G		
Contribution to National Children's Fund (Eligible for 100% deduction w.e.f. A.Y. 2014-15)		30,000
Contribution to Charitable trust recognized for section 80G purposes	40,000	
Deduction restricted to 50% of 10% of Adjusted Total Income i.e. $50\% \times (10\% \times ₹ 3,20,000)$		<u>16,000</u>
Total deduction under Chapter VI-A		<u>46,000</u>

Adjusted total income (for the purpose of computation of deduction under section 80G):

Gross total income	3,90,000
Less: Long term capital gains (₹ 2,20,000 - ₹ 1,50,000)	<u>70,000</u>
Adjusted total income	<u>3,20,000</u>

Question 41

Mr. Rahul, an assessee aged 61 years, gives the following information for the previous year ended 31-03-2014 :

Sl. No.	Particulars	₹
a.	Loss from profession	1,05,000
b.	Capital loss on the sale of property - short term	55,000
c.	Capital gains on sale of shares - long term	2,05,000
d.	Loss in respect of self occupied property	15,000
e.	Loss in respect of let out property	30,000
f.	Share of loss from firm	1,60,000
g.	Income from card games	55,000
h.	Winnings from lotteries	1,00,000
i.	Loss from horse races in Mumbai	40,000
j.	Medical Insurance premium paid by cheque	18,000

Compute the total income of Mr. Rahul for the assessment year 2014-15.

Answer

Computation of total income of Mr. Rahul for the A.Y. 2014-15

Particulars	₹	₹
Income from house property		
Loss (₹ 15,000 + ₹ 30,000)	(45,000)	
Profits and gains from business or profession		
Loss from profession	(1,05,000)	
Capital Gains		
Long-term capital gains on sale of shares		2,05,000
Less: Short-term capital loss on sale of property (Note 1)		<u>55,000</u>
Income under the head "Capital Gains"		1,50,000
Less: Set-off of losses under other heads of income (Note 2)		
Loss from profession	1,05,000	
Loss under the head "Income from house property" (₹ 15,000 + ₹ 30,000)	<u>45,000</u>	<u>1,50,000</u>
		Nil
Income from other sources		
Income from card games	55,000	
Winnings from lotteries	<u>1,00,000</u>	<u>1,55,000</u>
Gross total income		1,55,000
Less: Deductions under Chapter VIA (Note 4)		<u>Nil</u>
Total Income		<u>1,55,000</u>

Notes:

- (1) As per section 74, short-term capital loss can be set-off against both short-term capital gains and long-term capital gains. Hence, short term capital loss of ₹ 55,000 can be set-off against long-term capital gains of ₹ 2,05,000 on sale of shares. The net income under the head "Capital gains" would be ₹ 1,50,000.
- (2) Section 71 provides for set-off of loss from one head against income from another. As per section 71(2), loss under any head of income, other than capital gains, can be set-off against income under any head, including capital gains. Therefore, loss of ₹ 1,05,000 from profession and loss of ₹ 45,000 from house property (both let out and self-occupied) can be set-off against the net income of ₹ 1,50,000 under the head "Capital Gains".
- (3) Loss from an exempt source cannot be set-off against profit from a taxable source. Therefore, share of loss from a firm cannot be set-off against any other income, since share of profit from firm is exempt under section 10(2A).
- (4) As per section 58(4), no deduction in respect of any expenditure or allowance in connection with income by way of winnings from lotteries and income from card games is allowable under any provision of the Income-tax Act, 1961. Therefore, since the total income comprises only of income from card games and winnings from lotteries,

deduction under Chapter VI-A is not allowable from such income. Therefore, Mr. Rahul will not be entitled to claim deduction under section 80D in respect of medical insurance premium paid by cheque.

- (5) Further, loss from horse races can neither be set-off against winnings from lotteries and income from card games nor can it be carried forward.

Question 42

Mr. Vishal is a resident individual. His Profit & Loss Account for the year ended 31st March, 2014 is given below:

	₹		₹
To Staff Salary	3,57,500	By Gross profit	13,55,500
To Office Rent	78,000	By Interest on Post Office Monthly Income scheme	98,400
To Administrative Expenses	2,14,000	By Bank F.D. interest (Net of TDS 7,000)	63,000
To Income-tax	1,60,000	By Rent (on let out property)	66,000
To Depreciation	67,500	By Winning from lotteries (Net of TDS 7,500)	17,500
To Net Profit	7,23,400		
	16,00,400		16,00,400

Following further information is given to you:

- (i) During the financial year 2013-14, he deposited ₹ 85,000 in to his Public Provident Fund Account (i.e. on 27-3-2014)
 - (ii) He received annual salary of ₹ 1,20,000 and annual Commission of ₹ 60,000 from a partnership firm in the capacity of working partner. It is fully chargeable to tax under section 28 (v).
 - (iii) Received annuity pension of ₹ 72,500 from LIC of India.
 - (iv) Paid medical insurance premium of ₹ 21,850. The medical insurance was on self. Mr. Vishal is not a senior citizen.
 - (v) Life Insurance Premium of ₹ 25,000 was paid on the policy standing in the name of his wife Sujatha.
 - (vi) Administrative expenses include ₹ 5,000 being municipal tax on let out property.
 - (vii) Depreciation eligible as per the Income-tax Act, 1961 amounts to ₹ 57,000.
- Compute the total income of Mr. Vishal for the Assessment year 2014-15.

Answer

Computation of total income of Mr. Vishal for the A.Y. 2014-15

Particulars	₹	₹	₹
Income from House Property			
Gross Annual Value – Rent received (Note 1)		66,000	

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Less: Municipal taxes paid		<u>5,000</u>	
Net Annual Value		61,000	
Less: Deduction under section 24 @ 30% of NAV		<u>18,300</u>	42,700
Profits and gains of business or profession			
Net Profit as per Profit & Loss Account		7,23,400	
Add: Expenses not allowable			
Income-tax	1,60,000		
Depreciation charged	67,500		
Municipal Taxes paid on let out property	<u>5,000</u>	<u>2,32,500</u>	
		9,55,900	
Less: Income not forming part of business income			
Interest on Post Office Monthly Income scheme	98,400		
Interest on Bank Fixed Deposit	63,000		
Rent received	66,000		
Winning from lotteries	<u>17,500</u>	<u>2,44,900</u>	
		7,11,000	
Less: Depreciation as per Income-tax Act, 1961		<u>57,000</u>	
		6,54,000	
Add: Salary received from partnership firm (Note 2)		1,20,000	
Commission received from partnership firm (Note 2)		<u>60,000</u>	8,34,000
Income from other sources			
Interest on Post Office Monthly Income scheme		98,400	
Interest on Bank Fixed Deposit (₹63,000 + ₹7,000)		70,000	
Winning from lotteries (₹17,500 + ₹7,500)		25,000	
Annuity pension received from LIC of India		<u>72,500</u>	<u>2,65,900</u>
Gross Total income			11,42,600
Less: Deductions under Chapter VI-A			
(i) <u>Deduction under section 80C</u>			
Investment in PPF		85,000	
Life insurance premium paid for his wife		<u>25,000</u>	
		<u>1,10,000</u>	
Deduction restricted to		1,00,000	
(ii) <u>Deduction under section 80D</u>			
Mediclaime premium of ₹21,850 paid for insurance on self. However, the deduction is restricted to ₹15,000.		<u>15,000</u>	<u>1,15,000</u>
Total income			<u>10,27,600</u>

Notes: (1) Rent received is assumed to be the gross annual value of the let out property in absence of any information regarding municipal value, fair rental value and standard rent.

(2) Any salary, bonus, commission or remuneration, by whatever name called, due to or received by a partner of a firm shall not be treated as salary but it shall be treated as income from business or profession for the purposes of section 28.

EXERCISES

1. Income under the Income-tax Act, 1961, is to be computed under -
 - a) five heads
 - b) six heads
 - c) four heads
2. What is the basic exemption limit for a woman assessee below the age of 60 years at any time during the previous year 2013-14?
 - a) ₹ 1,80,000
 - b) ₹ 2,50,000
 - c) ₹ 2,00,000
3. What is the rate of surcharge applicable to individuals having total income exceeding ₹ 1 crore?
 - a) 10%
 - b) 2.5%
 - c) Nil
4. What is the basic exemption limit for Mrs. X, who is of the age of 80 years as on 30.3.2014?
 - a) ₹ 5,00,000
 - b) ₹ 2,40,000
 - c) ₹ 2,50,000
5. Share of profit of Mr. P, who is a partner in M/s PQR is –
 - a) exempt from tax
 - b) taxable as his business income
 - c) taxable as his salary
6. Explain briefly the tax treatment of the following income of Mr. X, who is a partner in the firm M/s. XYZ –
 - (i) Salary received by Mr. X from M/s. XYZ.
 - (ii) Interest (on loan) received from M/s. XYZ.
 - (iii) Share of profit from the firm.
7. Discuss the tax treatment of the following income of Mr. A, who is a member of a HUF-
 - (i) Share of income from HUF.
 - (ii) Income from an impartible estate of the HUF.
 - (iii) Income from self-acquired property converted into joint family property.

Answers

1. a; 2. c; 3. a; 4. a; 5. a

Provisions Concerning Advance Tax and Tax Deducted at Source

Key Points	
Advance Tax	
<u>Installments of advance tax and due dates</u>	
<u>Companies - four installments</u>	
Due date of installment	Amount payable
On or before 15 th June	Not less than 15% of advance tax liability.
On or before 15 th September	Not less than 45% of advance tax liability <i>less</i> amount paid in earlier installment.
On or before 15 th December	Not less than 75% of advance tax liability <i>less</i> amount paid in earlier installment or installments.
On or before 15 th March	Whole amount of advance tax liability <i>less</i> amount paid in earlier installment or installments.
<u>Non-corporate assessees - three installments</u>	
Due date of installment	Amount payable
On or before 15 th September	Not less than 30% of advance tax liability.
On or before 15 th December	Not less than 60% of advance tax liability <i>less</i> amount paid in earlier installment.
On or before 15 th March	Whole amount of advance tax liability <i>less</i> amount paid in earlier installment or installments.

<u>Interest for non-payment or short-payment of advance tax [Section 234B]</u>	
(1)	Interest under section 234B is attracted for non-payment of advance tax or payment of advance tax of an amount less than 90% of assessed tax.
(2)	The interest liability would be 1% per month or part of the month from 1 st April following the financial year upto the date of determination of income under section 143(1).
(3)	Such interest is calculated on the amount of difference between the assessed tax and the advance tax paid.
(4)	Assessed tax is the tax calculated on total income less tax deducted at source.
<u>Interest payable for deferment of advance tax [Section 234C]</u>	
(1)	Interest under section 234C is attracted for deferment of advance tax beyond the due dates.
(2)	The interest liability would be 1% per month, for a period of 3 months, for every deferment.
(3)	However, for the last installment of 15 th March, the interest liability under this section would be 1% for one month.
(4)	The interest is to be calculated on the difference between the amount arrived at by applying the specified percentage of tax on returned income and the actual amount paid by the due date

9.3 Income-tax

Deduction of Tax at source

Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
192	Salary	Basic exemption limit (₹ 2,00,000 / ₹ 2,50,000, as the case may be)	Any person	Individual	Average rate of income-tax computed on the basis of the rates in force.	At the time of payment	Allowances, to the extent exempt under section 10, and exempt perquisites would be excluded.
193	Interest on Securities	8% Savings (Taxable) Bonds, 2003 – ₹ 10,000 Interest on debentures issued by a company in which the public are substantially	Any person	Any resident	10%	At the time of credit of such income to the account of the payee or at the time of payment, whichever is earlier.	Some exempted interest payments are interest - - On any security of the Central Government or a State Government. - Payable to LIC, GIC or any of the four public sector insurance companies formed by GIC in respect of any securities owned by it or in which it has full beneficial interest. - Payable to any other insurer in respect of any securities owned by it or in which it

Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time deduction of	Payments / Income exempted from TDS
		interested, paid or credited to a resident individual or HUF - ₹ 5,000					has full beneficial interest. - Payable on any security issued by a company, where such security is in dematerialized form and is listed on a recognized stock exchange in India.
194	Dividend	₹ 2,500 in a financial year	The Principal Officer of a domestic company	Resident Individual	10%	At the time of payment	Dividend credited or paid to LIC, GIC or any of the four public sector insurance companies formed by GIC, or any other insurer, in respect of shares owned by it or in which it has full beneficial interest. Dividend referred to in section 115-O, since the domestic company distributing dividend has paid dividend distribution tax on such dividend.
194A	Interest other than interest on securities	₹ 10,000 in a financial year, in case of interest paid by – (i) a banking company;	Any person, other than an individual or HUF not liable to tax audit u/s 44AB in the	Any Resident	10%	At the time of credit of such income to the account of the payee or at the time of	Interest credited or paid to: - any banking company, or a cooperative society engaged in the business of banking - any financial corporation established by

9.5 Income-tax

Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
		(ii) a co-operative society engaged in banking business; and (iii) deposits with post office. ₹ 5,000 in a financial year, in other cases.	immediately preceding financial year.			payment, whichever is earlier.	<ul style="list-style-type: none"> - or under a Central, State or Provincial Act. - the Life Insurance Corporation of India. - the Unit Trust of India; - any company and cooperative society carrying on the business of insurance. - notified institution, association, body or class of institutions, associations or bodies <p>Interest credited or paid by a firm to a partner Interest credited or paid by a co-operative society to its member or to any other co-operative society, etc.</p>
194B	Winnings from any lottery, crossword puzzle or card game or other game of any sort	Payment of an amount exceeding ₹ 10,000	Any Person	Any Person	30%	At the time of payment	-

Provisions concerning Advance Tax and Tax Deducted at Source 9.6

Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
194BB	Winnings from horse race	Payment of an amount exceeding ₹ 5,000	Book Maker or a person holding licence for horse racing, wagering or betting in any race course.	Any Person	30%	At the time of payment	-
194C	Payments to Contractors	Single sum credited or paid exceeding ₹ 30,000 or The aggregate of sums credited or paid during the financial year exceeding ₹ 75,000	Central/State Govt., Local authority, Central/ State/Provin-cial Corp., company, firm, trust, co- operative society, individuals/ HUFs liable to tax audit in the immediately preceding financial year.	Any Resident contractor for carrying out any work (including supply of labour)	1% of sum paid or credited, if the payee is an Individual or HUF 2% of sum paid or credited, if the payee is any other person.	At the time of credit of such sum to the account of the contractor or at the time of payment, whichever is earlier.	(i) Any sum credited or paid to a contractor in transport business, if the contractor furnishes his PAN to the person paying or crediting such sum. (ii) Any sum credited or paid by an individual or HUF exclusively for personal purposes of such individual or HUF.

9.7 Income-tax

Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
194D	Insurance Commission	₹ 20,000 in a financial year	Any person	Any Resident	10%	At the time of credit of such income to the account of the payee or at the time of payment, whichever is earlier.	
194H	Commission or brokerage	₹ 5,000 in a financial year	Any person, other than an individual or HUF not liable to tax audit u/s 44AB in the immediately preceding financial year.	Any Resident	10%	At the time of credit of such income to the account of the payee or at the time of payment, whichever is earlier.	Commission or brokerage payable by BSNL or MTNL to their PCO franchisees.

Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
194-I	Rent	₹ 1,80,000 in a financial year	Any person, other than an individual or HUF not liable to tax audit u/s 44AB in the immediately preceding financial year.	Any Resident	For P & M or equipment-2% For land, building, furniture or fixtures - 10%	At the time of credit of such income to the account of the payee or at the time of payment, whichever is earlier.	-
194-IA	Payment on transfer of certain immovable property	₹ 50 lakh (Consideration for transfer)	Any person, being a transferee	Resident transferor	1%	At the time of credit of such sum to the account of the transferor or at the time of payment, whichever is earlier.	Payment for transfer of agricultural land

9.9 Income-tax

Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
194J	Fees for professional or technical services/ Royalty/ Non-compete fees/ Director remuneration	₹ 30,000 in a financial year, for each category of income. (However, this limit does not apply in case of payment made to director of a company).	Any person, other than an individual or HUF not liable to tax audit u/s 44AB in the immediately preceding financial year.	Any Resident	10%	At the time of credit of such sum to the account of the payee or at the time of payment, whichever is earlier.	Any sum by way of fees for professional services credited or paid by an individual or HUF exclusively for personal purposes of such individual or any member of HUF.
194LA	Compensation on acquisition of certain immovable property	₹ 2,00,000 in a financial year	Any person	Any Resident	10%	At the time of payment	Compensation on acquisition of agricultural land.

Question 1

Compute the amount of tax deduction at source on the following payments made by M/s. S Ltd. during the financial year 2013-14 as per the provisions of the Income-tax Act, 1961.

Sr. No.	Date	Nature of Payment
(i)	1-10-2013	Payment of ₹ 2,00,000 to Mr. "R" a transporter who is having PAN.
(ii)	1-11-2013	Payment of fee for technical services of ₹ 25,000 and Royalty of ₹ 20,000 to Mr. Shyam who is having PAN.
(iii)	30-06-2013	Payment of ₹ 25,000 to M/s X Ltd. for repair of building.
(iv)	01-01-2014	Payment of ₹ 2,00,000 made to Mr. A for purchase of diaries made according to specifications of M/s S Ltd. However, no material was supplied for such diaries to Mr. A by M/s S Ltd.
(v)	01-01-2014	Payment made ₹ 1,80,000 to Mr. Bharat for compulsory acquisition of his house as per law of the State Government.
(vi)	01-02-2014	Payment of commission of ₹ 6,000 to Mr. Y.

Answer

- (i) No tax is required to be deducted at source under section 194C by M/s S Ltd. on payment to transporter Mr. R, provided he furnishes his PAN to M/s. S Ltd.
- (ii) As per section 194J, liability to deduct tax is attracted only in case the payment made as fees for technical services and royalty, individually, exceeds ₹ 30,000 during the financial year. In the given case, since, the individual payments for fee of technical services i.e. ₹ 25,000 and royalty ₹ 20,000 is less than ₹ 30,000 each, there is no liability to deduct tax at source. It is assumed that no other payment towards fees for technical services and royalty were made during the year to Mr. Shyam.
- (iii) Provisions of section 194C are not attracted in this case, since the payment for repair of building on 30.06.2013 to M/s. X Ltd. is less than the threshold limit of ₹ 30,000.
- (iv) According to section 194C, the definition of "work" does not include the manufacturing or supply of product according to the specification by customer in case the material is purchased from a person other than the customer.
Therefore, there is no liability to deduct tax at source in respect of payment of ₹ 2,00,000 to Mr. A, since the contract is a contract for 'sale'.
- (v) As per section 194LA, any person responsible for payment to a resident, any sum in the nature of compensation or consideration on account of compulsory acquisition under any law, of any immovable property, is responsible for deduction of tax at source if such payment or the aggregate amount of such payments to the resident during the financial year exceeds ₹ 2,00,000.

In the given case, no liability to deduct tax at source is attracted as the payment made does not exceed ₹ 2,00,000.

- (vi) As per section 194H, any person (other than an individual or HUF) who is responsible for paying commission or brokerage to a resident shall deduct tax at source if the amount of such income or the aggregate of the amounts of such income credited or paid during the financial year exceeds ₹ 5,000.

Since the commission payment made to Mr. Y exceeds ₹ 5,000, the provisions of section 194H are attracted.

The tax to be deducted at source shall be - ₹ 6,000 x 10% = ₹ 600.

Question 2

State the applicability of TDS provisions and TDS amount in the following cases:

- (a) *Rent paid for hire of machinery by B Ltd. to Mr. Raman ₹ 2,10,000.*
(b) *Fee paid to Dr. Srivatsan by Sundar (HUF) ₹ 35,000 for surgery performed to a member of the family.*

Answer

- (a) Since the rent paid for hire of machinery by B. Ltd. to Mr. Raman exceeds ₹ 1,80,000, the provisions of section 194-I for deduction of tax at source are attracted.

The rate applicable for deduction of tax at source under section 194-I on rent paid for hire of plant and machinery is 2% assuming that Mr. Raman had furnished his permanent account number to B Ltd.

Therefore, the amount of tax to be deducted at source:

$$= ₹ 2,10,000 \times 2\% = ₹ 4200.$$

Note: In case Mr. Raman does not furnish his permanent account number to B Ltd., tax shall be deducted @ 20% on ₹ 2,10,000, by virtue of provisions of section 206AA.

- (b) As per the provisions of section 194J, a Hindu Undivided Family is required to deduct tax at source on fees paid for professional services only if it is subject to tax audit under section 44AB in the financial year preceding the current financial year.

However, if such payment made for professional services is exclusively for the personal purpose of any member of Hindu Undivided Family, then, the liability to deduct tax is not attracted.

Therefore, in the given case, even if Sundar (HUF) is liable to tax audit in the immediately preceding financial year, the liability to deduct tax at source is not attracted in this case since, the fees for professional service to Dr. Srivatsan is paid for a personal purpose i.e. the surgery of a member of the family.

Question 3

Ashwin doing manufacture and wholesale trade furnishes you the following information :

Total turnover for the financial year

Particulars	₹
2012-13	1,05,00,000
2013-14	95,00,000

State whether tax deduction at source provisions are attracted for the below said expenses incurred during the financial year 2012-13:

Particulars	₹
Interest paid to UCO Bank	41,000
Contract payment to Raj (2 contracts of ₹ 12,000 each)	24,000
Shop rent paid (one payee)	1,90,000
Commission paid to Balu	7,000

Answer

As the turnover of Ashwin for F.Y.2012-13, i.e. ₹ 105 lakh, has exceeded the monetary limit of ₹ 100 lakh prescribed under section 44AB, he has to comply with the tax deduction provisions during the financial year 2013-14, subject to, however, the exemptions provided for under the relevant sections for applicability of TDS provisions.

Interest paid to UCO Bank

TDS under section 194A is not attracted in respect of interest paid to a banking company.

Contract payment of ₹ 24,000 to Raj for 2 contracts of ₹ 12,000 each

TDS provisions under section 194C would not be attracted if the amount paid to a contractor does not exceed ₹ 30,000 in a single payment or ₹ 75,000 in the aggregate during the financial year. Therefore, TDS provisions under section 194C are not attracted in this case.

Shop Rent paid to one payee – Tax has to be deducted under section 194-I as the rental payment exceeds ₹ 1,80,000.

Commission paid to Balu – Tax has to be deducted under section 194-H as the commission exceeds ₹ 5,000.

Question 4

State in brief the applicability of tax deduction at source provisions, the rate and amount of tax deduction in the following cases for the financial year 2013-14:

- (i) Winning by way of jackpot in a horse race ₹ 1,00,000.
- (ii) Payment made by a firm to sub-contractor ₹ 3,00,000 with outstanding balance of ₹ 1,20,000 shown in the books as on 31-03-2014.

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- (iii) Rent paid for plant and machinery ₹ 1,50,000 by a partnership firm having sales turnover of ₹ 20,00,000 and net loss of ₹ 15,000.
- (iv) Payment made to Ricky Ponting, an Australian cricketer, by a newspaper for contribution of articles ₹ 25,000.

Answer

- (i) Provisions for tax deduction at source under section 194BB @ 30% are attracted if the amount exceeds ₹ 5,000 in respect of income arising by way of winning a jackpot in horse races.

Tax to be deducted = ₹ 1,00,000 x 30% = ₹ 30,000

- (ii) Provisions of tax deduction at source under section 194C are attracted in respect of payment by a firm to a sub-contractor. Under section 194C, tax is deductible at the time of credit or payment, whichever is earlier @ 1% if the payment is made to an individual or HUF and 2% for others.

Assuming that sub-contractor to whom payment has been made is an individual and the aggregate amount credited during the year is ₹ 4,20,000, tax is deductible @ 1% on ₹ 4,20,000.

Tax to be deducted = ₹ 4,20,000 x 1% = ₹ 4,200

- (iii) As per section 194-I, tax is to be deducted @ 2% on payment of rent for plant and machinery, only if the payment exceeds ₹ 1,80,000 during the financial year. Since rent of ₹ 1,50,000 paid by a partnership firm does not exceed ₹ 1,80,000, tax is not deductible.
- (iv) Under section 194E, the person responsible for payment of any amount to a non-resident sportsman for contribution of articles relating to any game or sport in India in a newspaper shall deduct tax @ 20%. Further, since Ricky Ponting is a non-resident, education cess @2% and secondary and higher education cess @ 1% on TDS would also be added.

Therefore, tax to be deducted = ₹ 25,000 x 20.60% = ₹ 5,150.

Question 5

State the concessions granted to transport operators onwards in the context of cash payments under section 40A(3) and deduction of tax at source under section 194-C.

Answer

Section 40A(3) provides for disallowance of expenditure incurred in respect of which payment or aggregate of payments made to a person in a day exceeds ₹ 20,000, and such payment or payments are made otherwise than by account payee cheque or account payee bank draft.

However, in case of payment made to transport operators for plying, hiring or leasing goods carriages, the disallowance will be attracted only if the payments made to a person in a day

exceeds ₹ 35,000. Therefore, payment or aggregate of payments up to ₹ 35,000 in a day can be made to a transport operator otherwise than by way of account payee cheque or account payee bank draft, without attracting disallowance under section 40A(3).

Under section 194C, tax had to be deducted in respect of payments made to contractors at the rate of 1% in case the payment is made to individual or Hindu Undivided Family or at the rate of 2% in any other case.

However, no deduction is required to be made from any sum credited or paid or likely to be credited or paid during the previous year to the account of a contractor, during the course of the business of plying, hiring or leasing goods carriages, if the contractor furnishes his permanent account number (PAN) to the person paying or crediting such sum.

Question 6

Briefly discuss the provisions relating to payment of advance tax on income arising from capital gains and casual income.

Answer

The proviso to section 234C contains the provisions for payment of advance tax in case of capital gains and casual income.

Advance tax is payable by an assessee on his/its total income, which includes capital gains and casual income like income from lotteries, crossword puzzles, etc.

Since it is not possible for the assessee to estimate his capital gains, or income from lotteries etc., it has been provided that if any such income arises after the due date for any installment, then, the entire amount of the tax payable (after considering tax deducted at source) on such capital gains or casual income should be paid in the remaining installments of advance tax, which are due.

Where no such installment is due, the entire tax should be paid by 31st March of the relevant financial year.

No interest liability on late payment would arise if the entire tax liability is so paid.

Note: In case of casual income the entire tax liability is fully deductible at source @30% under section 194B and 194BB. Therefore, advance tax liability would arise only in respect of the education cess and secondary and higher education cess element of such tax, if the same along with tax liability in respect of other income, if any, is ₹ 10,000 or more.

Question 7

Mrs. Indira, a landlord, derived income from rent from letting a house property to M/s Vaibhav Corporation Ltd. of ₹ 1,00,000 per month. She charged service tax @ 12.36% on lease rent charges. Calculate the deduction of tax at source (TDS) to be made by M/s Vaibhavi Corporation Ltd. on payment made to Mrs. Indira and narrate related formalities in relation to TDS.

Answer

- (1) As per *Circular No. 4/2008 dated 28th April, 2008* issued by the CBDT, the service tax paid by the tenant does not partake the nature of income of the landlord. The landlord only acts as a collecting agency for collection of service tax. Therefore, tax deducted at source under section 194-I would be required to be made on the amount of rent paid or payable excluding the amount of service tax, i.e. tax has to be deducted under section 194-I on ₹ 12 lakh.
- (2) Tax is deductible @ 10% under section 194-I.
- (3) Hence, in the given case, TDS under section 194-I would amount to ₹ 10,000, to be deducted every month.
- (4) Tax deducted should be deposited within prescribed time i.e. on or before seven days from the end of the month in which the deduction is made and upto 30th April for the month of march.

Question 8

Explain the difference between tax deduction at source and tax collection at source.

Answer

Tax deduction at source means any tax which has been deducted at source by the payer at the time of accrual or payment to the payee. Persons responsible for making payment of income covered by the scheme of tax deduction are required to deduct tax at source at the prescribed rates. Tax so deducted should be deposited within the prescribed time. Tax is largely deducted on expense and not supply of goods.

Tax collection at source is effected by the seller from the buyer at the time of debiting the amount to the account of the buyer or at the time of receipt of amount, whichever is earlier. Certain specified goods when sold must be subjected to tax collection at source and taxes collected thereon must be remitted into government's account within the prescribed time.

Question 9

Bharghav doing textiles business furnishes you the following information:

Total turnover for the financial year:

	₹
2012-13	105,00,000
2013-14	95,00,000

State whether the provisions of tax deduction at source are attracted for the following expenses incurred during the financial year 2013-14:

	₹
<i>Interest paid to Indian Bank on Term Loan</i>	92,800
<i>Advertisement expenses to R (two individual payments of ₹ 24,000 and ₹ 34,000)</i>	58,000

Factory rent paid to C	1,85,000
Brokerage paid to B, a sub-broker	6,000

Answer

Since the turnover of Mr. Bharghav for F.Y.2012-13, i.e., ₹ 105 lakhs, has exceeded the monetary limit of ₹ 100 lakhs prescribed under section 44AB, he has to comply with the tax deduction provisions during the financial year 2013-14, subject to, however, the exemptions provided for under the relevant sections for applicability of TDS provisions.

(i) **Interest paid to Indian Bank on term loan**

TDS under section 194A is not attracted in respect of interest paid to a banking company.

(ii) **Advertisement expenses to R (two individual payments of ₹ 24,000 and ₹ 34,000)**

Under section 194C, the provisions for tax deduction at source would not be attracted if the amount paid to a contractor does not exceed ₹ 30,000 in a single payment or ₹ 75,000 in the aggregate during the financial year. Therefore, provisions for deduction of tax at source under section 194C are not attracted in respect of payment of ₹ 24,000 to R.

However, payment of ₹ 34,000 to R would attract TDS@1% under section 194C, since it exceeds ₹ 30,000.

Note - The tax to be deducted would be ₹ 340, being 1% of ₹ 34,000.

(iii) **Factory rent of ₹ 1,85,000 paid to C**

Tax has to be deducted under section 194-I as the rental payment exceeds ₹ 1,80,000.

Note - The tax to be deducted is ₹ 18,500, being 10% of ₹ 1,85,000.

(iv) **Brokerage of ₹ 6,000 paid to B, a sub-broker**

Tax has to be deducted@10% under section 194-H as the brokerage exceeds ₹ 5,000 during the F.Y. 2013-14.

Note - The tax to be deducted is ₹ 600, being 10% of ₹ 6,000.

EXERCISES

- Any person responsible for paying to a resident any sum exceeding ₹ 2 lakh towards compensation for compulsory acquisition of his urban industrial land under any law has to deduct income-tax at the rate of -
 - 10%
 - 15%
 - 20%
- The rate of TDS on rental payments of plant, machinery or equipment is -
 - 2%

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- b) 5%
 - c) 10%
3. For non-payment or short payment of advance tax -
 - a) interest is payable under section 234A
 - b) interest is payable under section 234B
 - c) interest is payable under section 234C
 4. For deferment of advance tax -
 - a) interest is payable under section 234A
 - b) interest is payable under section 234B
 - c) interest is payable under section 234C
 5. Write short notes on -
 - (a) Certificate for deduction of tax at lower rate
 - (b) Installments of advance tax and due dates for payment of advance tax
 - (c) Payment of advance tax in case of capital gains
 6. Explain the meaning of the following terms in the context of section 194J -
 - (a) Professional services
 - (b) Fees for technical services
 7. Who are the "persons responsible for paying" taxes deducted at source as per section 204?
 8. Which are the payments for which individuals and HUFs, who are liable to get their accounts audited under section 44AB, are vested with the liability to deduct tax at source? Discuss.

Answers

1. a; 2. a; 3. b; 4. c.

Provisions for Filing Return of Income

Key Points	
Section	Particulars
139(1)	<p><u>Assesseees required to file return of income compulsorily</u></p> <p>(i) Companies and firms (whether having profit or loss or nil income);</p> <p>(ii) a person, being a resident other than not ordinarily resident, having any asset (including any financial interest in any entity) located outside India or signing authority in any account located outside India, whether or not having income chargeable to tax;</p> <p>(iii) Individuals, HUFs, AOPs or BOIs and artificial judicial persons whose gross total income (i.e., total income before giving effect to the provisions of Chapter VI-A) exceeds the basic exemption limit.</p> <p><u>Due date of filing return of income</u></p> <p>30th September of the assessment year, in case the assessee is:</p> <p>(i) a company;</p> <p>(ii) a person (other than company) whose accounts are required to be audited; or</p> <p>(iii) a working partner of a firm whose accounts are required to be audited.</p> <p>31st July of the assessment year, in case of any other assessee (other than assesseees who are required to furnish report under section 92E, for whom the due date is 30th November of the assessment year).</p>
139(3)	<p><u>Return of loss</u></p> <p>An assessee can carry forward or set off his/its losses provided he/it has filed his/its return under section 139(3), within the due date specified under section 139(1).</p> <p><u>Exceptions</u></p> <p>Loss from house property and unabsorbed depreciation can be carried forward for set-off even though return not been filed before the due date.</p>

139(4)	<p><u>Belated Return</u></p> <p>A return of income for any previous year, which has not been furnished within the time allowed u/s 139(1) or under a notice issued u/s 142(1), may be furnished at any time before the:</p> <p>(i) expiry of one year from the end of the relevant assessment year; or</p> <p>(ii) completion of the assessment,</p> <p>whichever is earlier.</p> <p>A belated return cannot, however, be revised.</p>
139(5)	<p><u>Revised Return</u></p> <p>If any omission or any wrong statement is discovered in a return furnished u/s 139(1) or in pursuance of a notice u/s 142(1), a revised return may be furnished by the assessee at any time:</p> <p>(i) before the expiry of one year from the end of the relevant assessment year; or</p> <p>(ii) before the completion of assessment,</p> <p>whichever is earlier.</p>
139(4A)	<p><u>Return of Income of Charitable Trusts and Institutions</u></p> <p>Every person in receipt of income derived -</p> <p>(i) from property held under trust wholly or partly for charitable or religious purpose; or</p> <p>(ii) by way of voluntary contributions on behalf of such trust or institution,</p> <p>must furnish a return of income if the total income, in respect of which he is assessable as a representative assessee (computed before allowing any exemption u/s 11 & 12) exceeds the basic exemption limit.</p>
139(4B)	<p><u>Return of Income of Political Parties</u></p> <p>A political party is required to file a return of income if its total income (before claiming any exemption u/s 13A) exceeds the basic exemption limit.</p> <p>Grant of exemption under section 13A is subject to the condition of the political party filing a return of income within the time limit prescribed u/s 139(1).</p>
139(4C)	<p><u>Mandatory filing of returns by Scientific Research Associations, News agency, Trade unions etc.</u></p> <p>It is mandatory for a research association, news agency or trade union to file a return of income on or before the due date under section 139(1), if its total income (before giving effect to the exemption under section 10) exceeds the basic exemption limit.</p>

10.3 Income-tax

Authorised Signatories to the Return of Income [Section 140]			
This section specifies the persons who are authorized to sign and verify the return of income under section 139.			
	Assessee	Circumstance	Authorised signatory
1.	Individual	(i) In circumstances not covered under (ii), (iii) & (iv) below	- the individual himself
		(ii) where he is absent from India	- the individual himself; or - any person duly authorised by him in this behalf holding a valid power of attorney from the individual (Such power of attorney should be attached to the return of income)
		(iii) where he is mentally incapacitated from attending to his affairs	- his guardian; or - any other person competent to act on his behalf
		(iv) where, for any other reason, it is not possible for the individual to sign the return	- any person duly authorised by him in this behalf holding a valid power of attorney from the individual (Such power of attorney should be attached to the return of income)
2.	Hindu Undivided Family	(i) in circumstances not covered under (ii) and (iii) below	- the karta
		(ii) where the karta is absent from India	- any other adult member of the HUF
		(iii) where the karta is mentally incapacitated from attending to his affairs	- any other adult member of the HUF
3.	Company	(i) in circumstances not covered under (ii) to (v) below	- the managing director of the company
		(ii) (a) where for any unavoidable reason such managing director is not able to sign and verify the return; or (b) where there is no managing director	- any director of the company - any director of the company

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		(iii) where the company is not resident in India	- a person who holds a valid power of attorney from such company to do so (such power of attorney should be attached to the return).
		(iv) (a) Where the company is being wound up (whether under the orders of a court or otherwise); or (b) where any person has been appointed as the receiver of any assets of the company	- Liquidator - Liquidator
		(v) Where the management of the company has been taken over by the Central Government or any State Government under any law	- the principal officer of the company
4.	Firm	(i) in circumstances not covered under (ii) below	- the managing partner of the firm
		(ii) (a) where for any unavoidable reason such managing partner is not able to sign and verify the return; or (b) where there is no managing partner.	- any partner of the firm, not being a minor - any partner of the firm, not being a minor
5	Local authority	-	- the principal officer
6	Political party [referred to in section 139(4B)]	-	- the chief executive officer of such party (whether he is known as secretary or by any other designation)
7	Any other association	-	- any member of the association or the principal officer of such association
8	Any other person	-	- that person or some other person competent to act on his behalf.

Question 1

Paras is resident of India. During the F.Y. 2013-14, interest of ₹ 1,88,000 was credited to his Non-resident (External) Account with SBI. ₹ 30,000, being interest on fixed deposit with SBI, was credited to his saving bank account during this period. He also earned ₹ 3,000 as interest on this saving account. Is Paras required to file return of income?

What will be your answer, if he owns one shop in Kerala having area of 150 sq. ft.?

Answer

An individual is required to furnish a return of income under section 139(1) if his total income, before giving effect to the deductions under Chapter VI-A, exceeds the maximum amount not chargeable to tax i.e., ₹ 2,00,000 (for A.Y. 2014-15).

Computation of total income of Mr. Paras for A.Y. 2014-15

Particulars	₹
Income from other sources	
Interest earned from Non-resident (External) Account ₹ 1,88,000 [Exempt under section 10(4)(ii), assuming that Mr. Paras has been permitted by RBI to maintain the aforesaid account]	NIL
Interest on fixed deposit with SBI	30,000
Interest on savings bank account	3,000
Gross Total Income	33,000
<i>Less:</i> Deduction under section 80TTA (Interest on saving bank account)	3,000
Total Income	30,000

Since the total income of Mr. Paras for A.Y.2014-15, before giving effect to the deductions under Chapter VI-A, is less than the basic exemption limit of ₹ 2,00,000, he is not required to file return of income for A.Y.2014-15.

Owning a shop having area of 150 sq.ft in Kerala would not make any difference to the answer.

Note: In the above solution, interest of ₹ 1,88,000 earned from Non-resident (External) account has been taken as exempt on the assumption that Mr. Paras, a resident, has been permitted by RBI to maintain the aforesaid account. However, in case he has not been so permitted, the said interest would be taxable. In such a case, his total income, before giving effect to the deductions under Chapter VIA, would be ₹ 2,21,000 (₹ 30,000 + ₹ 1,88,000 + ₹ 3,000), which is higher than the basic exemption limit of ₹ 2,00,000. Consequently, he would be required to file return of income for A.Y.2014-15. Here again, ownership of shop in Kerala is immaterial.

Question 2

State with reasons whether you agree or disagree with the following statements:

- (a) Return of income of Limited Liability Partnership (LLP) could be signed by any partner.
- (b) Time limit for filing return under section 139(1) in the case of Mr. A having total turnover of ₹ 60 lakhs for the year ended 31.03.2014, whether or not opting to offer presumptive income under section 44AD, is 30th September 2014.

Answer

(a) Disagree

The return of income of LLP should be signed by a designated partner.

Any other partner can sign the Return of Income of LLP **only** in the following cases:-

- (i) where for any unavoidable reason such designated partner is not able to sign and verify the return, or,
- (ii) where there is no designated partner.

(b) Disagree

In case Mr. A opts to offer his income as per the presumptive taxation provisions of section 44AD, then, the due date under section 139(1) for filing of return of income for the year ended 31.03.2014, shall be 31st July, 2014.

It is only in case Mr. A does not opt for presumptive taxation provisions under section 44AD and offers income to be lower than 8% of total turnover and his total income exceeds the basic exemption limit, he has to keep books of account as per section 44AA and get his accounts audited under section 44AB, in which case the due date for filing return would be 30th September, 2014.

Question 3

Specify the persons who are authorized to sign and verify under section 140, the return of income filed under section 139 of the Income-tax Act, 1961 in the case of:

- (i) Political party;
- (ii) Local authority;
- (iii) Association of persons, and
- (iv) Limited Liability Partnership (LLP).

Answer

The following persons (mentioned in Column III below) are authorised as per section 140, to sign and verify the return of income filed under section 139:

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I	II	III
(i)	Political party	Chief Executive Officer of such party (whether known as secretary or by any other designation).
(ii)	Local authority	Principal Officer thereof.
(iii)	Association of Persons	Any member of the association or the principal officer thereof.
(iv)	LLP	Designated partner, or Any partner, - where the designated partner is not able to sign and verify the return for any unavoidable reason; - where there is no designated partner.

Question 4

State whether filing of income-tax return is mandatory for the assessment year 2014-15 in respect of the following cases:

- (i) Research association eligible for exemption under section 10(21) having total income of ₹ 2,10,000
- (ii) Registered trade union eligible for exemption under section 10(24) having following incomes:
- | | |
|---------------------------------------|----------|
| Income from house property (computed) | ₹ 60,000 |
| Income from other sources (computed) | ₹ 40,000 |
- (iii) A charitable trust registered under section 12AA, having total income of ₹ 2,10,000.
- (iv) A Limited Liability Partnership (LLP) with business loss of ₹ 1,30,000.

Answer

- (i) As per section 139(4C), a research association referred to in section 10(21) must file its return of income within the due date under section 139(1) if its total income, without giving effect to the provisions of section 10, exceeds the maximum amount which is not chargeable to income-tax.

Since the total income of the research association exceeds the basic exemption limit of ₹ 2,00,000, it has to file its return of income for the A.Y. 2014-15.

- (ii) As per section 139(4C), a registered trade union referred to in section 10(24) must file its return of income if the total income exceeds the basic exemption limit without giving effect to the provisions of section 10.

Since the total income of the trade union is less than the basic exemption limit of ₹ 2,00,000, it need not file its return of income for the A.Y. 2014-15.

- (iii) As per section 139(4A), a charitable trust registered under section 12AA must file its return of income, if its total income computed as per the provisions of the Income-tax Act, 1961, without giving effect to the provisions of sections 11 and 12, exceeds the maximum amount which is not chargeable to income-tax. Since the total income of the charitable trust exceeds ₹ 2,00,000, it has to file its return of income for the A.Y. 2014-15.
- (iv) As per third proviso to section 139(1), every company or firm shall furnish on or before the due date the return in respect of its income or loss in every previous year. Since LLP is included in the definition of "firm" under the Income-tax Act, 1961, it has to file its return mandatorily, even though it has incurred a loss.

Question 5

State with reasons, whether the following statements are true or false, with regard to the provisions of the Income-tax Act, 1961:

- (i) *The Assessing Officer has the power, inter alia, to allot PAN to any person by whom no tax is payable.*
- (ii) *Where the Karta of a HUF is absent from India, the return of income can be signed by any male member of the family.*

Answer

- (i) **True** : Section 139A(2) provides that the Assessing Officer may, having regard to the nature of transactions as may be prescribed, also allot a PAN to any other person, whether any tax is payable by him or not, in the manner and in accordance with the procedure as may be prescribed.
- (ii) **False** : Section 140(b) provides that where the Karta of a HUF is absent from India, the return of income can be signed by any other adult member of the family; such member can be a male or female member.

Question 6

The total income of a university without giving effect to exemption under section 10(23C) is ₹ 46 lacs. Its total income, however, is nil. Should the University file its return of income?

Answer

Section 139(4C) enjoins that, a university referred to in section 10(23C), should file the return of income if its total income without giving effect to the exemption under section 10, exceeds the basic exemption limit. The provisions of the Act will apply as if it were a return required to be furnished under section 139(1). In the given case, since the total income of the University before giving effect to the exemption exceeds the basic exemption limit, it has to file its return of income.

Question 7

Mrs. Hetal, an individual engaged in the business of Beauty Parlour, has got her books of account for the Financial year ended on 31st March, 2014 audited under section 44AB. Her total income for the assessment year 2014-15 is ₹ 2,35,000. She wants to furnish her return of income for assessment year 2014-15 through a tax return preparer. Can she do so?

Answer

Section 139B provides a scheme for submission of return of income for any assessment year through a tax return preparer. However, it is not applicable to persons whose books of account are required to be audited under section 44AB. Therefore, Mrs. Hetal cannot furnish her return of income for A.Y.2014-15 through a tax return preparer.

Question 8

Can an individual, who is not in India, sign the return of income from outside India? Is there any other option?

Answer

As per section 140, return of income can be signed by an individual even if he is absent from India. Hence, an individual can himself sign the return of income from a place outside India. Alternatively, any person holding a valid power of attorney and duly authorised by the individual can also sign the return of income. However, such power of attorney should be attached along with the return of income.

Question 9

Explain with brief reasons whether the return of income can be revised under section 139(5) of the Income-tax Act, 1961 in the following cases:

- (i) *Belated return filed under section 139(4).*
- (ii) *Return already revised once under section 139(5).*
- (iii) *Return of loss filed under section 139(3).*

Answer

Any person who has furnished a return under section 139(1) or in pursuance of a notice issued under section 142(1) can file a revised return if he discovers any omission or any wrong statement in the return filed earlier. Accordingly,

- (i) A belated return filed under section 139(4) cannot be revised. Only a return furnished under section 139(1) or in pursuance of a notice issued under section 142(1) can be revised.
- (ii) A return revised earlier can be revised again as the first revised return replaces the original return. Therefore, if the assessee discovers any omission or wrong statement in such a revised return, he can furnish a second revised return within the prescribed time i.e. within one year from the end of the relevant assessment year or before the completion of assessment, whichever is earlier.
- (iii) A return of loss filed under section 139(3) is deemed to be return filed under section 139(1), and therefore, can be revised under section 139(5).

Question 10

Enumerate the circumstances in which an individual assessee is empowered to sign & verify his return of income under section 139 by himself or otherwise by an authorized signatory.

Answer**Signatory to return of income in case of individual [Section 140(a)]**

The following table enumerates the specific circumstances and the authorized signatories empowered to sign and verify the return of income of an individual assessee filed under section 139(1) in each such circumstance:

	Circumstance	Return of income, to be signed by
(i)	Where he is absent from India	- the individual himself; or - any person duly authorised by him in this behalf holding a valid power of attorney from the individual. (Such power of attorney should be attached to the return of income)
(ii)	Where he is mentally incapacitated from attending to his affairs	- his guardian; or - any other person competent to act on his behalf.
(iii)	Where, for any other reason, it is not possible for the individual to sign the return	- any person duly authorised by him in this behalf holding a valid power of attorney from the individual (Such power of attorney should be attached to the return of income)
(iv)	In circumstances not covered under (i), (ii) & (iii) above	- the individual himself

EXERCISES

- Akash, who is 32 years old, has to file a return of income if his gross total income is in excess of -
 - ₹ 1,50,000
 - ₹ 2,00,000
 - ₹ 1,60,000
- The due date for filing of a return of income for a company for Assessment year 2014-15 is -
 - 31st July, 2014
 - 30th September, 2014
 - 31st October, 2014
 - 31st August, 2014
- For filing returns of income in respect of various entities, the Income-tax Act, 1961 has prescribed -
 - Two due dates

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- b) Three due dates
 - c) Four due dates
4. Political parties -
- a) need not file their return of income
 - b) should always file their return of income
 - c) should file their return of income if the total income computed without giving effect to the provisions of section 13A exceeds the basic exemption limit.
5. The return of a company has to be signed by -
- a) the Managing Director or Director
 - b) the General Manager
 - c) The Secretary
6. An assessee can file a revised return of income at any time before the completion of assessment or before expiry of the following period, whichever is earlier -
- a) one year from the end of the relevant assessment year
 - b) two years from the end of the relevant assessment year
 - c) six months from the end of the relevant assessment year
7. As per section 139(1), filing of returns is compulsory for -
- a) companies only
 - b) firms only
 - c) both companies and firms
8. Write short notes on the following -
- a) Belated return
 - b) Revised return
9. Filing of return of income on or before due date is necessary for carry forward of losses - Discuss the correctness of this statement.
10. Who are the persons authorised to sign the return of income in the case of -
- a) Hindu Undivided Family
 - b) Company
 - c) Partnership firm
11. List ten transactions for which quoting of permanent account number is mandatory.

10.12 Income-tax

12. Mr. Bhuvan, an individual, has got his books of account for the year ending 31.3.2014 audited under section 44AB. His total income for the A.Y. 2014-15 is ₹ 2,50,000. He desires to know if he can furnish his return of income for the A.Y. 2014-15 through a Tax Return Preparer.
13. Discuss briefly about the scheme to facilitate submission of return of income through Tax Return Preparers.
14. Enumerate eight transactions, for which quoting of Permanent Account Number is mandatory.
15. Briefly discuss about the interest chargeable under section 234A for delay or default in furnishing return of income.

Answers

1. b; 2. b; 3. b; 4. c; 5. a; 6. a; 7. c.