

UNIVERSITY OF JAMMU
B.COM. FOURTH SEMESTER
INCOME TAX LAW AND PRACTICE - II

Course No. BCG-402

Max Marks = 100

Internal assessment = 20

External exam. = 80

OBJECTIVES: OBJECTIVE: To impart knowledge about basic concepts pertaining to theory and practice of income tax

UNIT I: CAPITAL GAINS

Meaning of capital assets; Short term and long term capital gain and loss, computation of capital gain, indexing of cost of acquisition and improvement.

Deductions u/s 54, 54B, 54D, 54EC, 54ED, 54F

Income from Other Sources: Computation of general income u/s 56(1) and specific income u/s 56(2), and grossing up of income falling under other sources, Interest on securities, types of securities.

UNIT II:

Set off and carry forward of losses, aggregation of income, deductions from gross total income for individuals, HUF's and Firms

UNIT III: Assessment of individuals and H.U.F including computation of tax liability.

UNIT IV: Assessment of firms and association of persons. including computation of tax liability

SKILL DEVELOPMENT (GUIDELINES FOR CLASS ROOM TEACHING AND INTERNALASSESSMENT)

- Create deep understanding of all concepts specified in the syllabus.

- Enable the students in computing income and tax liability of various assesses as specified above.

BOOKS RECOMMENDED

1. Income Tax Law & Accounts by Dr H C Meharotra and Dr S P Goyal : Sahitya Bhavan Publications.
2. Income tax Law and Practice by V.P.Gaur & D.B. Narang: Kalyani Publishers.
3. Direct taxes Law and Practices by V.K. Singhania & Kapil Singhania- Taxman publication.
4. Income tax Law and Practices by Mahesh Chandra, D.C. Shukla, K.A.Mahajan, M.A. Shah – Pragati publication, New Delhi.
5. Conceptual clarity on Income Tax & Wealth Tax by Arvind Tuli & Dr. Mrs. Neeru chadda – Kalyani Publication, New Delhi

NOTE FOR PAPER SETTER

Equal weightage shall be given to all the units of the syllabus. The external Paper shall be of the two sections viz, A & B of three hours duration.

Section-A: This section shall contain four short answer questions selecting one from each unit. Each question shall carry 5 marks .A candidate shall be required to attempt all the four questions. Total weightage to this section shall be of 20 marks.

Section-B: This section shall contain eight long answer questions of 15 marks each. Two questions with internal choice shall be set from each unit. A candidate shall have to attempt any four questions selecting one from each unit. Total weightage to this section shall be of 60 marks.

MODEL QUESTION PAPER
INCOME TAX LAW AND PRACTICE – II

Max Marks: -80

Time allowed: 3hrs

Section- A (Marks 20) (5 Marks x 4)

Attempt all questions. Each question carries five marks.

1. Discuss the concept of book profit with suitable example.
2. Write a short note on set off and carry forward of losses.
3. Calculate tax payable in case of individual for the assessment year with suitable example.
4. Discuss long term capital gain & short term capital gain.

Section- B (Marks 60) (15 Marks x 4)

Attempt any four questions selecting one from each unit. Each question carries 15 marks.

UNIT-I

1. Mr. X purchased a house in 1976 for Rs. 1,00,000. He incurred the following expenses for the improvement of the house.

Renovation of the house for Rs. 25,000 and addition of 2 rooms after one year for Rs. 50,000. The F.M.V. of the house on 1-4-81 was Rs. 110,000. He sold the house in May 2012 for Rs. 14,00,000.

He purchased another house property within 2 months for Rs. 3,00,000 and invested in capital gains account scheme Rs. 50,000. Calculate taxable capital gain for the previous year _____. Cost inflation index for 1981-82 was 100 and for 1912-13 is 852.

OR

Following are the particulars for the year _____. Compute income under the head other sources.

	Rs.
(i) Card games loss	12,000
(ii) From the activity of owning and Maintaining horses for race purpose	
(a) Loss at Bombay	40,000
(b) Profit at Banglore	20,000
(iii) Dividend (gross)	6,000
(iv) Betting in horse races	400

UNIT-II

2. Mr. X earned gross total income of Rs. 5,00,000. In the previous year _____ and made the following donation during the year.

- (i) Rs. 10,000 to chief Minister's earthquake relief fund.
- (ii) Rs. 15,000 to National foundation for communal harmony.
- (iii) Rs. 20,000 for municipal corporation approved for promotion of family planning.
- (iv) Rs. 45,000 to approved institutions.

Calculate the amount of deduction admissible to him u/s 80G

OR

Discuss with suitable example rules regarding set off and carry forward of losses.

UNIT-III

3. Mr. K.L Seth a resident of Delhi [population above 25 lakhs] submits the following details of his income for the financial year.....

Salary	7000 p.m
DA	6000 p.m
Entertainment allowance	350 p.m
City compensatory allowance	250 p.m
Bonus	7000
Employer's contribution to RPF	12000
His own contribution to RPF	12000
Interest on RPF balance @ 13%	7800

He is provided with an unfurnished accommodation for which employer charges Rs. 200 p.m. The municipal value of the house owned by employer is Rs. 22050 p.a. He is also provided by employer with chauffeur driven car of 1.8 lt. capacity. The car is used for official purposes only and the entire expenses of its running and maintenance are met by the employer.

During the year Mr. K.L Seth has received dividends from co-op, society amounting to Rs. 14000. He paid insurance premium of Rs. 3000 on a policy taken on his the life of his father who is not dependent on him. During the year he had following income also.

- (a) Winnings from lottery Rs. 50000 out of which tax @30% has been deducted at source.
- (b) He went to Nepal and won Rs. 35000 from gambling in a casino.
- (c) He lost Rs. 20000 in card games during Diwali season.
- (d) He earned Rs. 14910 from his term deposits with a bank.

Computes his total income and tax liability for the assessment year.....

OR

HUF with more than one co-parcener entitled to claim partition, owns a property which is let out at Rs. 600 p.m per unit. The property consists of 10 identical residential units. The municipal rental value of the property is Rs. 60,000p.a.

Following deductions are claimed as expenses: Rs.

Municipal taxes	4200
Lift maintenance	2000
Water pump expenses	800
Actual expenses on repairs	8000
Cost of renovation of the property	50000
Education cess levied by the state govt.	2000
Rent collector monthly salary	200
Interest on loan taken by mortgaging the property and loan was used for the family business	5000

Income from the family business for the assessment yearwas Rs. 160000 after charging interest on loan. A lottery ticket worth Rs. 100 was purchased out of family funds on the name HUF. It won a prize of rs. 100000. The Karta had acquired a shop out of his own savings which he wife. Shop has an annual income (computed under the head house property) of Rs. 24000.

Compute total income of HUF and tax payable for the assessment year

UNIT-IV

4. From the information given below find out the amount of remuneration which can be debited to P & L A/c of the firm and how much income of partners shall be chargeable to tax under the head profits and gains. Salary and interest to partners has been paid as per deed.

	Rs.
Books profit (after debiting the following)	40000
Following payments have been made as per partnership deed, which had been submitted along with return for the assessment year.....	
Salary to X (working partner)	84000
Salary to Y (non working partner)	20000
Commission to Z (working partner)	60000
Interest on capital to partners @ 16%	
To X	12000
To Y	9000
To Z	6000

OR

Mr. K, Mrs. L and Mr. M are members of an AOP sharing profits and losses equally. During the year endingtotal income of AOP was Rs. 237000. The details of individual incomes of its members are given below:

Mrs. K	Rs.
Rent from house property:	60000
Interest on deposits with HUDCO	36000
Bank interest	50000
Mrs. L	
House property income (computed)	20000

Bank interest on fixed deposits:	96000
Interest on debentures (gross)	30000
Mr. M	
Pension from government	136000
Interest accrued on NSC VIII issue	12600
Interest on Govt. securities	15000

Compute tax liability of AOP and its members.

CAPITAL GAINS

STRUCTURE:

1.1 Introduction

1.2 Objective

1.3 Concept of Capital Gain

1.4 Meaning of Capital Asset

1.4.1 Kinds of capital assets

- Short-Term Capital Asset
- Long-Term Capital Asset

1.4.2 Transfer of capital asset

1.4.3 Transactions which do not constitute transfer [Sections 46 and 47]

1.4.4 Year of chargeability to tax

1.5 Meaning of Capital Gain

1.5.1 Short-term Capital Gain

1.5.2 Long-Term Capital Gain

1.6 The method of computing capital gains.

1.7 Differences between Long term capital gains and Short term capital gains

- 1.8 Full value of consideration
- 1.9 Cost of Acquisition
- 1.10 Cost of Improvement
- 1.11 Cost Inflation Index
- 1.12 Exemption from Capital Gains
- 1.13 Income from Other Source
- 1.14 Interest on securities
 - 1.14.1 Interest on Securities exempted from Tax. U/S 10(15)
- 1.15 Kinds of securities
- 1.16 Summary
- 1.17 Glossary
- 1.18 Self-Assessment Questions
- 1.19 Books Recommended

1.1 INTRODUCTION

The provisions for computation of Income from capital gains are covered under sections 45 to 55. Section 2(14) defines the term capital gain and section 45, the charging section lays down basis of charge for taxability of capital gain/loss arises on transfer of capital asset. Taxability of capital gain depends upon the nature of capital gain arises, i.e., short term capital gain or long term capital gain. The type of capital gain depends upon the period for which the capital asset is held. The taxability of capital gain shall satisfy the conditions like there should be capital asset, the asset is transferred by the assessee, such transfer takes place during the previous year, etc. To give relief to the assessee, the concept of exemption introduced under section 54, 54B, 54D, 54EC, 54F, 54G, 54GA and 54GB. Further this lesson will give some insight regarding the concept of 'income from other sources'. Income chargeable under Income-tax Act, which does not specifically fall for

assessment under any of the heads, must be charged to tax as "income from other sources". This head is thus a residuary head of income under which income can be computed only after deciding whether the particular item of income is otherwise assessable under any of the first four heads. In addition to the taxation of income not covered by the other heads, Section 56 (1) provides the general income details and Section 56(2) specifically provides certain items of incomes as being chargeable to tax under the head in every case.

1.2 OBJECTIVES

At the end of this lesson, you will learn

- The conditions to be satisfied for income to be chargeable under this head,
- Which assets are classified as capital asset,
- The year in which the capital gains are chargeable to tax,
- Classification of capital gain into long term and short term,
- Which are the transactions not regarded as transfer,
- What are the exemptions available in respect of capital gains.
- Which are the income chargeable under the head income from other sources.
- What are admissible deductions.

1.3 CONCEPT OF CAPITAL GAINS

Profits or gains arising from the transfer of a capital asset made in a previous year are taxable as capital gains under the head "Capital Gains". Sections 45 to 55A of the Income-tax Act, 1961 deal with capital gains. Section 45 of the Act, provides that any profits or gains arising from the transfer of a capital asset effected in the previous year shall, save as otherwise provided in Sections 54, 54B, 54D, 54EC, 54ED, 54F, 54G, 54GA and 54H be chargeable to income-tax under the head "Capital Gains" and shall be deemed to be the income of the previous year in which the transfer took place. Doubts may arise as to whether 'Capital Gains' being a capital receipt can be brought to tax as income. It may be noted that the ordinary accounting canons of distinctions between a capital receipt and a

revenue receipt are not always followed under the Income-tax Act. Section 2(24)(vi) of the Income-tax Act specifically provides that "Income" includes "any capital gains chargeable under Section 45(1)". It may not be out of place to mention here that in the absence of a specific provision in Section 2(24) capital gains have no logic to be taxed as income. The constitutional validity of the provisions of the Act relating to capital gains was challenged in *Navin Chandra Mafatlal v. C.I.T.* (1955) 27 ITR 245. The Supreme Court while upholding the competence of parliament in legislating with regard to capital gains as part of income, observed that the term income should be given the widest connotation so as to include capital gains within its scope. However, all capital profits do not necessarily constitute capital gains. For instance, profits on re-issue of forfeited shares, profits on redemption of debentures, premium on issue of shares, 'pagri' from tenants etc. are capital profits and not capital gains, hence, not liable to tax. The capital gain is chargeable to income tax if the following conditions are satisfied:

1. There is a capital asset.
2. Assessee should transfer the capital asset.
3. Transfer of capital assets should take place during the previous year.
4. There should be gain or loss on account of such transfer of capital asset.

1.4 Capital Asset: Sec. 2(14): Capital Asset means property of any kind (Fixed, Circulating, movable, immovable, tangible or intangible) whether or not connected with business or profession. In other words property of any kind held by an assessee whether or not connected with his business or profession but does not include:

(i) Any stock-in-trade, consumable stores or raw-materials held for the purposes of his business or profession;

(ii) Personal effects that is to say, movable property (including wearing apparel and furniture but excluding jewellery) held for personal use by the assessee or any member of his family dependent on him. Jewellery includes ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals, whether or not containing any precious or semi-precious stone, and whether or not worked

or sewn into any wearing apparel and precious or semi-precious stones, whether or not set in any furniture, utensil or other article or worked or sewn into any wearing apparel;

(iii) Agricultural land in India, not being land situate (a) within the jurisdiction of a municipality or a cantonment board and which has a population of not less than 10,000, or (b) in any area within the distance, measured aerially, -

(I) not being more than two kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten thousand but not exceeding one lakh; or

(II) not being more than six kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than one lakh but not exceeding ten lakh; or (III) not being more than eight kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten lakh.

Explanation: - For the purposes of this sub-clause, "population" means the population according to the last preceding census of which the relevant figures have been published before the first day of the previous year;

(iv) 6 % per cent Gold Bonds, 1977 or 7% per cent Gold Bonds, 1980 or National Defence Gold Bonds, 1980 issued by the Central Government;

(v) Special Bearer Bonds 1991 issued by the Central Government.

(vi) Gold Deposit Bonds issued under the Gold Deposit Scheme, 1999 notified by the Central Government.

(vii) Deposit certificates issued under gold monetization scheme, 2015 [w.e.f.A.Y 2016-17]

1.4.1 Kinds of capital assets

There are two kinds of capital assets

Short-term capital asset: Sec. 2(42A): means a capital asset held by an assessee for not more than thirty six months immediately preceding the date of its transfer. But following

assets shall be treated as short term capital assets if these assets are held by its owner (before transfer) for not more than 12 months. (i) a security and shares of companies listed in a recognized stock exchange in India. (ii) A unit of equity oriented fund (iii) a zero coupon bonds.

Following assets shall be treated as short term capital assets if such assets are held by its owner before transfer for not more than 24 months.

- (i) Unlisted shares of companies
- (ii) An immovable property being land and building or both.

Any gain or loss occurring to the assessee on such assets shall be known as short term capital gain or loss [2 (42B)]

Long-term capital asset: Sec. 2(29A): means a capital asset which is not a short-term capital asset. i.e., the assets which are held by the assessee for a period exceeding 36 /24 months / 12 months as the case may be, months immediately preceding the date of their transfer, are called long term capital assets.

Any gain or loss occurring on such assets shall be known as long term capital gain or loss, [2 (42B)]

Types of capital gains

Short term capital gains: Any gain on transfer of short term capital assets is called short term capital gain.

It is calculated as follows:

Full value of consideration		+ + +
Less: Expenses of transfer		+ + +
Net consideration		+ + +
Less: cost of acquisition	+ + +	
Cost of improvement	+ + +	

Short term capital gain		+++
Long term capital gains: Any gain on transfer of long term capital asset is called long term capital gain . It is calculated as follows:		
Full value of consideration		+++
Less: Expenses of transfer		+++
Net consideration		+++
Less: cost of acquisition	+++	
Cost of improvement	+++	
Long term capital gain		+++

1.4.2 Transfer of capital asset [Section 2 (47)]

Transfer includes:

- Sale of asset
- Exchange of asset
- Relinquishment of asset (means surrender of asset)
- Extinguishments of any right on asset (means reducing any right on asset)
- Compulsory acquisition of asset.
 - In a case where the asset is converted by the owner there of into, or is treated by him as stock in trade of a business carried on by him, such conversion or treatment, or
 - Any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53 A of the transfer of property act, 1882; or

- Any transaction (whether by way of becoming a member of , a acquiring shares in, a co- operative society, company or other association of persons or by way of any agreement or any arrangement or in any other manner whatsoever) which has the effect of transferring or enabling the enjoyment of , any immovable property.
- Maturity or redemption of a zero coupon bond.

The definition of transfer is inclusive, thus transfer includes only above said five ways. In other words, transfer can take place only on these five ways. If there is any other way where an asset is given to other such as by way of gift, inheritance etc. it will not be termed as transfer.

1.4.3 Transactions which do not constitute transfer [Sections 46 and 47]

(i) Any distribution of capital assets on liquidation of a company to its shareholders [section 46 (1)]

(ii) any transfer of a capital asset under a gift or will or an irrevocable trust; Provided that this clause shall not apply to transfer under a gift or an irrevocable trust of a capital asset being shares, debentures or warrants allotted by a company directly or indirectly to its employees under the Employees' Stock Option Plan or stock purchase Scheme;

(iii) Any transfer of a capital asset by a company to its subsidiary company, if- (a) the parent company or its nominees hold the whole of the share capital of the subsidiary company, and (b) the subsidiary company is an Indian company;

(iv) Any transfer of a capital asset by a subsidiary company to the holding company, if - (a) the parent company or its nominees hold the whole of the share capital of the subsidiary company is, and (b) the subsidiary company is an Indian company[section 47 (iv)];

(v) Any transfer, in a scheme of amalgamation, of a capital asset by the amalgamating company to the amalgamated company if the amalgamated company is an Indian company;

(vi) any transfer in a scheme of amalgamation of a capital asset being share or shares held in an Indian Company, by the amalgamating foreign company to the amalgamated foreign company, if -

(a) at least twenty-five per cent of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; and

(b) such transfer does not attract tax on capital gains in the country, in which the amalgamating company is incorporated (applicable from the assessment year 1993-94);

(viaa) any transfer in a scheme of amalgamation of a banking company with a banking institution sanctioned and brought into force by the Central Government under Sub-section (7) of Section 45 of the Banking Regulation Act, 1949, of a capital asset by the banking company to the banking institution. (vib) any transfer, in a demerger, of a capital asset by the demerged company to the resulting company, if the resulting company is an Indian company.

(vic) any transfer in a demerger, of a capital asset, being a share or shares held in an Indian company, by the demerged foreign company to the resulting foreign company, if -

(a) the shareholders holding not less than three-fourths in value of the shares of the demerged foreign company continue to remain shareholders of the resulting foreign company; and

(b) such transfer does not attract tax on capital gains in the country in which the demerged foreign company is incorporated provided that the provisions of Sections 391 to 394 of the Companies Act, 1956 (1 of 1956) shall not apply in case of demerger referred to in this clause.

(vid) any transfer or issue of shares by the resulting company in a scheme of demerger to the shareholders of the demerged company if the transfer or issue is made in consideration of demerger of the undertaking.

(vii) any transfer by a shareholder, in a scheme of amalgamation, of a capital asset being a share or shares held by him in the amalgamating company, if -

(a) the transfer is made in consideration of the allotment to him of any share or shares in the amalgamated company except where the shareholders itself is the amalgamated company, and

(b) the amalgamated company is an Indian company;

(viiia) any transfer of a capital asset of such foreign currency convertible bonds or Global Depository Receipts as are referred to in Section 115AC(1) or rupee denominated bond of an Indian company or derivative, made by a non-resident on a recognized stock exchange located in any International financial services centre and where the consideration for such transaction is paid or payable in foreign currency, shall not be regarded as transfer. [Section 47 (viiiab)]

(viii) any transfer of agricultural land in India effected before the first day of March, 1970;

(ix) any transfer of a capital asset being any work of art, archaeological, scientific or art collection, book, manuscript, drawing, painting, photograph or print to the Government or a University or the National Museum, National Art Gallery, National Archives or any such other public museum or institution as may be notified by the Central Government in the Official Gazette to be of national importance or to be of renown throughout any State or States [Section 47 (ix)];

(x) any transfer by way of conversion of bonds or debentures, debenture stock or deposit certificates in any form, of a company, into shares or debentures of that company [Section 47 (x)].

(xi) any transfer made on or before 31.12.1998 by a person not being a company of a capital asset being membership of a recognised stock exchange to a company in exchange for shares allotted by that company to him (transferor). The shares cannot be transferred for 3 years.

(xii) any transfer of land by a sick industrial company under a scheme prepared and sanctioned under section 18 of the sick industrial companies (Special provisions) Act, 1985 (1 of 1986) where such industrial company is being managed by its workers co-operative: provided that such transfer is made during the period commencing from the previous year in which such has become a sick industrial company and ending with the previous year in which the entire networth of such company becomes equal to or exceeds the accumulated losses [Section 47 (xii)]

(xiii) where a firm is succeeded by a company in the business carried on by it as a result of which the firm sells or otherwise transfers any capital asset or intangible asset to the company. Any transfer of a capital asset or intangible asset by a firm to a company as a result of

succession of the firm by a company in the business carried on by the firm, or any transfer of a capital asset to a company in the course of the demutualisation or corporatisation of a recognised stock exchange in India as a result of which an association of persons or body of individuals is succeeded by such company.

Provided that -

(a) all the assets and liabilities of the firm or of the association of persons or body of individuals relating to the business immediately before the succession become the assets and liabilities of the company,

(b) all the partners of the firm immediately before the succession become the shareholders of the company in the same proportion in which their capital account stood in the books of the firm on the date of succession.

(c) the partners of the firm do not receive any consideration or benefit, directly or indirectly in any form or manner, other than by way of allotment of shares in the company, and

(d) the aggregate of the share holding in the company of the partners of the firm is not less than fifty per cent of the total voting power in the company and their shareholding continue to be as such for a period of five years from the date of succession.

(e) the demutualisation or corporatisation of a recognised stock exchange in India is carried out in accordance with a scheme for corporatisation which is approved by the Securities and Exchange Board of India established under Section 3 of the Securities and Exchange Board of India Act, 1992.

(xiiia) any transfer of a capital asset being a membership right held by a member of a recognised stock exchange in India for acquisition of shares and trading or clearing rights acquired by such member in that recognised stock exchange in accordance with a scheme for demutualisation or corporatisation which is approved by the Securities and Exchange Board of India established under Section 3 of the Securities and Exchange Board of India Act, 1992 (15 of 1992).

(xiiib) any transfer of a capital asset or intangible asset by a private company or unlisted public company (hereafter in this clause referred to as the company) to a limited liability partnership or any transfer of a share or shares held in the company by a shareholder as a

result of conversion of the company into a limited liability partnership under the provisions of section 56 and 57 of limited liability partnership act, 2008 shall not be regarded as transfer on fulfillment of the following conditions: (a) all the assets and liabilities of the company immediately before the conversion become the assets and liability of the limited liability partnership (b) all the shareholders of the company immediately before the conversion become the partner of the limited liability partnership and their capital distribution and profit sharing profit ratio in the LLP are in the same proportion as their shareholding in the company on the date of conversion. (c) the aggregate of the profit sharing profit ratio of the shareholders of the company in the LLP shall not be less than 50 % at any time during the period of 5 years from the date of conversion.

1.4.4 Year of chargeability to tax

Capital gains are generally charged to tax in the year in which 'transfer' takes place.

1.5 MEANING OF CAPITAL GAIN

Any profits or gains arising from the transfer of a capital asset is called capital gain. Capital gain is an increase in the value of a capital asset (investment or real estate) that gives it a higher worth than the purchase price. The gain is not realized until the asset is sold. A capital gain may be short-term (one year or less) or long-term (more than one year) and must be claimed on income taxes.

In other words, A capital gain refers to profit that results from a sale of a capital asset, such as stock, bond or real estate, where the sale price exceeds the purchase price. The gain is the difference between a higher selling price and a lower purchase price. Conversely, a capital loss arises if the proceeds from the sale of a capital asset are less than the purchase price.

Capital gains may also refer to a different form of profit received from an asset which refers to "investment income" in the form of cash flow or passive income that arises in relation to real assets, such as property; financial assets, such as shares/stocks or bonds; and intangible assets.

Under section 45 (1) any profits or gains arising from the transfer of a capital asset effected in the previous year shall, save as otherwise provided in section 54, be chargeable

to income tax under the head capital gains and shall be deemed to be the income of the previous year in which the transfer took place unless such capital gains are exempt under section 54, 54B, 54EC, 54F, 54G, 54GA or 54GB.

1.5.1 Short-term Capital Gain

Any capital gain arising as a result of transfer of a short-term capital asset is known as short-term capital gain. According to Section 2(42A) of the Income-tax Act: "Short term" capital asset means a capital asset held by an assessee for not more than thirty-six months immediately preceding the date of its transfer. In the case of capital assets (being equity or preference share in a company) held by an assessee for not more than 12 months immediately prior to its transfer. (i) a security and shares of companies listed in a recognized stock exchange in India. (ii) A unit of equity oriented fund (iii) a zero coupon bonds.

Following assets shall be treated as short term capital assets if such assets are held by its owner before transfer for not more than 24 months.

- (i) Unlisted shares of companies
- (ii) An immovable property being land and building or both.

Any gain or loss occurring to the assessee on such assets shall be known as short term capital gain or loss [2 (42B)]

1.5.2 Long term capital gains

Long-term capital asset: Sec. 2(29A): means a capital asset which is not a short-term capital asset. i.e., the assets which are held by the assessee for a period exceeding 36 /24 months / 12 months as the case may be, months immediately preceding the date of their transfer, are called long term capital assets.

Any gain or loss occurring on such assets shall be known as long term capital gain or loss, [2 (42B)]

Any capital gain arising as a result of transfer of a long-term capital asset is known as long-term capital gain. Long term Capital gains are computed by deducting from the full value of consideration for the transfer of a capital asset the following:

- Expenditure connected exclusively with the transfer;
- The indexed cost of acquisition of the asset, and
- The indexed cost of improvement, if any, of that asset.

1.6 The method of computing capital gains

Short-term Capital Gain	Long-term Capital Gain
A. Find out Full Value of Consideration	A. Find out Full Value of Consideration
B. Deduct	B. Deduct
(i) Expenditure incurred wholly and exclusively in connection with such Transfer.	(i) Expenditure incurred wholly and exclusively in connection with such Transfer.
(ii) Indexed Cost of Acquisition	(ii) Indexed Cost of Acquisition
(iii) Indexed Cost of Improvement	(iii) Indexed Cost of Improvement
(iv) Exemption provided by Ss. 54, 54B, 54D, & 54G, 54GA	(iv) Exemption provided by Ss. 54B, 54D 54EC, 54ED, 54F & 54G, 54GA
C. (A-B) is the short-term capital gain	C. (A-B) is the long-term capital gain

1.7 Differences between Long term capital gains and Short term capital gains

Long Term Capital Gain	Short Term Capital Gain
It arises out of transfer of long term capital assets	It arises out of transfer of short capital assets
Tax rate is 20%	Rates Applicable is 15 %
Cost of acquisition and cost of improvement are indexed on the basis of CII	No indexing is done.
If LTCA is acquired before 1-4-2001, then the fair market value of the asset as on 1-4-2001 is taken as the value of acquisition.	No such option is available to STCA
Long term capital loss can be set off only against long term capital gain.	Short term capital loss can be set off against short term capital gain or long term capital gain.

1.8 FULL VALUE OF CONSIDERATION

Full value of consideration means the whole or complete sale price or exchange value or compensation including enhanced compensation received in respect of capital asset in transfer. The following points are important to note in relation to full value of consideration.

1. The consideration may be in cash or kind.
2. The consideration received in kind is valued at its fair market value.
3. It may be received or receivable.
4. The consideration must be actual irrespective of its adequacy.

When shares, debentures or warrants are received under employees stock option plan or scheme are transferred under a gift or an irrecoverable trust, the market value on the date of transfer shall be deemed to be the full value of consideration received or accruing as a result of transfer for computation of capital gains.

1.9 COST OF ACQUISITION

Cost of Acquisition (COA) means any capital expense at the time of acquiring capital asset under transfer, i.e., to include the purchase price, expenses incurred up to acquiring date in the form of registration, storage etc. expenses incurred on completing transfer. In other words, cost of acquisition of an asset is the value for which it was acquired by the assessee. Expenses of capital nature for completing or acquiring the title are included in the cost of acquisition. Cost inflation index for the first year in which the asset was held by the assessee or for the year beginning on the 1st day of April, 2001, whichever is later.

➤ **Cost to the previous owner deemed to be the cost of acquisition:** If the asset is acquired by an assessee in the *following* circumstances the cost of acquisition of the asset shall be deemed to be the cost for which the previous owner of the property acquired it.

1. On any distribution of asset on the total or partial partition of a HUF or
2. Under gift or will
3. By succession, inheritance or devolution or

4. On any distribution of assets on the dissolution of a firm, body of individuals or other association of persons at any time before 1-04-1987. Or
 5. On Any distribution of asset on the liquidation of a company or
 6. Under a transfer to a revocable or an irrevocable trust or
 7. On transfer by a parent company to its Indian subsidiary company which is wholly owned by a parent company or
 8. On the transfer by a subsidiary company to its Indian holding company which owns whole of the share capital of the subsidiary company or
 9. On the transfer of capital asset by the amalgamating company to the amalgamated company if the amalgamated company is an Indian company. Or
 10. On transfer of shares of an Indian company by amalgamated foreign company to the amalgamated foreign company. Or
 11. On the transfer of capital asset in a scheme of amalgamation of a banking company with a banking institution sanctioned and brought into force by the central government or
 12. When any members of HUF converts his self acquired property into HUF property or
 13. On transfer of capital asset by the predecessor cooperative bank to the successor cooperative bank in a business organization or
 14. On transfer of shares in the predecessor cooperative bank in lieu of shares allotted in the successor cooperative bank in a business reorganization or
 15. On transfer of capital asset or intangible asset by a firm to a company as a result of succession of the firm by a company or
 16. On succession of a sole proprietary concern by a company.
- **Cost of share or security** : With effect from assessment year 2010-11 , where the capital gain arises from the transfer of specified security or sweat equity shares referred to in section 17 (2) (vi), the cost of acquisition of such security or shares shall

be the fair market value which has been taken into account for the purposes of section 17 (2) (vi)

- **Cost of bonus shares** The cost of bonus shares or security which is received by the assessee without any payment on the basis of his holding any financial asset will be as under (a) Where bonus share or security was received prior to 1st April 1981, the fair market value on 1st April 1981. (b) In any other case- nil
- **Cost of acquisition of goodwill** If the asset is purchased from the previous owner – purchase price In any other case – Nil **The finance act ,1994 has amended the above provision in following manner (a)** In case the capital asset is goodwill, tenancy rights, stage carriage permits or lorry hours the cost of acquisition will be : (i) purchase price , if such asset was purchased, and (ii) nil in all other cases except those covered u/s 49 (1) (1) to (iv).

(b) in case a person is holding shares or other securities and assessee becomes entitled to subscribe to an additional financial asset, the cost of such additional asset shall be :

(i) cost of original asset shall be its purchase price paid

(ii) In case such right to subscribe is renounced in favour of some other person, the cost of such renounced right is taken as NIL.

(i) In case assessee subscribes to such additional asset, the amount actually paid shall be its cost.

(ii) In case asset is acquired by renounce the cost shall be price paid by him to renounce and amount paid to the company or institution for such renounced asset.

(iii) With effect from assessment year 1998-99 the above mentioned provisions relating to cost of goodwill have been made applicable to a right to manufacture, produce or process any article or thing

Cost of acquisition of shares or debentures- shares or debentures acquired in consideration of conversion of debenture, debenture stock or deposit certificate shall be deemed to be the cost of original debentures, debenture stocks or deposit certificates converted.

Cost of acquisition shall have to be adjusted by the Cost Inflation Index to arrive at the indexed cost of acquisition, as follows:

Situation	Indexing
Long term capital assets acquired before 1-4-01 under gift, will, partition HUF , Inheritance i.e. u/s 49 (1)	Actual cost or FMV on 1-4-01 which ever is more x CII of the year of transfer / CII of 2001-02 i.e 100
Cost of improvement incurred on or after 1-4-01 on above mentioned assets	Cost of improvement x CII of year of transfer CII of the year of improvement
Long term capital assets acquired on or after 1-4-01 (Not under any of the modes mentioned above) Cost of improvement year incurred after 1-4-01	Actual cost x CII of the year of transfer CII of the year of acquisition Cost of improvement x CII of the improvement year incurred after 1-4-01 of transfer CII of the year of improvement
Long term capital assets acquired by present seller u/s 49 (1) on or after 1-4-01 but was acquired by previous owner before 1-4-01	Actual cost of FMV on 1-04-01 whichever is more x CII of the transfer /CII of the year in which present seller became its owner. Contrary views of high courts regarding base year for indexation benefit if asset is acquired u/s 49 (1) . However, in the case of CIT vs. Manjula J.Shah (2011) 16 Taxmann 42 (Bombay) the honourable bombay high court has held that while computing capital gains arising on transfer of a capital asset acquired by an assessee under a gift, indexed cost of acquisition has to be computed with reference to the year in which previous year first held the asset, and not from the year in which the assessee become owner of that asset.

	Similar decision has been given by the honorable Delhi high court, in the case of Arun Shungloo trust vs. CIT (2012) 18 Taxmann 216 (Delhi).
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1.10 COST OF IMPROVEMENT [SECTION 55 (1)]

Cost of improvement is the capital expenditure incurred by an assessee for making any addition or improvement in the capital asset. It also includes any expenditure incurred in protecting or curing the title. In other words, cost of improvement includes all those expenditures, which are incurred to increase the value of the capital asset. It means the amount which bears the cost of improvement the same proportion as cost inflation index for the year in which the assets is sold bears to the cost inflation index for the year in which improvement to the asset took place.

According to section 55 (1) : (a) In relation to a capital asset being goodwill of a business cost of improvement shall be taken to be nil and (b) In relation to any asset – the amount spent by assessee on Improving the asset after its acquisition.

The improvement to be so taken into account should be of such capital nature as it does not fall in deductions allowed while computing the income chargeable under the heads:

- (i) The income from the house property
- (ii) profits and gains of business or profession
- (iii) Income from other sources

Cost of improvement incurred on or after = $\frac{\text{Cost of improvement} \times \text{CII of year of transfer}}{\text{CII of the year of improvement}}$

1-4- 01

CII of the year of improvement

1.11 COST INFLATION INDEX SPECIFIED FOR PURPOSE OF COMPUTATION OF CAPITAL GAIN

Vide notifications issued u/s 48, the central govt. has notified the following cost inflation index (C.II)

Sl. No.	Financial year	Cost Inflation Index
1.	2001-02	100
2.	2002-03	105
3.	2003-04	109
4.	2004-05	113
5.	2005-06	117
6.	2006-07	122
7.	2007-08	129
8.	2008-09	137
9.	2009-10	148
10.	2010-11	167
11.	2011-12	184
12.	2012-13	200
13.	2013-14	220
14.	2014-15	240
15.	2015-16	254
16.	2016-17	264
17.	2017-18	272
18.	2018-19	280

Computation of capital gains in case of slump sale: Any gain arising from the slump sale effected in the previous year shall be chargeable as long term capital gains of the previous year in which the transfer take place.

Expenditure on transfer

Expenditure incurred wholly and exclusively for transfer of capital asset is called expenditure on transfer. It is fully deductible from the full value of consideration while calculating the capital gain. Examples of expenditure on transfer are the commission or brokerage paid by seller, any fees like registration fees, and cost of stamp papers etc., travelling expenses, and litigation expenses incurred for transferring the capital assets are expenditure on transfer.

Note: Expenditure incurred by buyer at the time of buying the capital assets like brokerage, commission, registration fees, cost of stamp paper etc. are to be added in the cost of acquisition before indexation.

1.12 EXEMPTION FROM CAPITAL GAINS

- **Capital gain arising on the transfer of property used for residence u/s 54:** The exemption u/s 54 relates to the capital gain arising out of transfer of residential house. The exemption is available to only Individual assesses or HUF, There occurs some long term capital gain and such capital gain is re-invested in:
 - (a) Purchase of another residential house with in one year before or two years after the sale of the house or
 - (b) Construction of new residential house within three years after the sale of the house.

The amount of capital gain so invested shall be exempted from tax w.e.f assessment year 2015-16, exemption u/s 54 (1) shall be available if the investment is made in purchase or construction of one residential house situated in India subject to the existing time limits.

With regard to pre- investment of long term capital gain for the purchase or construction of a residential house, following points should be noted:-

- (1) Construction of a new house must be completed within 3 years from the date of transfer of the house. Construction may have started before the sale of the house but completion is required to be made within 3 years of sale.
- (2) Exemption is allowed even if a part of the capital gain is invested to buy an old house and the remaining part is invested to renovate it or to expand it by constructed new rooms or adding another floor.
- (3) This exemption is allowed even if assessee purchase or constructs one house or he may sell two houses and invests the amount of long term capital gain to buy or construct only one house.
- (4) In case a residential house property is compulsorily acquired by government , the time limits prescribed for purchase or constructed of a residential house shall apply from the date of receipt of compensation.

Amount deposited in capital gain deposit account scheme.

In case the amount of capital gain is not re – invested for the purchase or construction of the new house upto the last date of filing of return of income u/s 139 then it should be deposited in the capital gain deposit scheme with a specified bank authorized by the central

government in accordance with the scheme. Any amount already utilized by the assessee for the purchase or construction of the new house together with the amount so deposited shall be deemed to be the cost of new house.

The amount deposited in the deposit account scheme must be utilized to purchase or construct the new house within 3 years from the date of transfer of the old house.

If the amount deposited in this scheme is not utilized wholly or partly for the purchase or construction of the new house within specified period, then,

- (i) The amount not so utilized shall be charged u/s 45 as the income of the previous year in which period of 3 years from the date of the transfer of the original asset expires, and
- (ii) The assessee shall be entitled to withdraw such amount in accordance with the scheme.

The transfer of newly acquired house property within 3 years

A residential house property purchased or constructed by re-invested capital gain cannot be transferred within 3 years of its purchase or construction.

If the house so acquired by reinvesting capital gain is sold within a period of 3 years from the date of its purchase or construction, the previously exempted capital gain will be taxable along with the capital gain on the sale of such house, if any, in the current previous year. In the event of loss on sale of new house, it shall be adjusted out of old exempted capital gain [section 54]

- **Capital gain arising from the transfer of agricultural land (sec 54 B):**

Any capital gain arising on the transfer of agricultural land situated in an urban area is exempt subject to the following conditions

The agriculture land is owned by an individual or a HUF. Agricultural land situated in rural areas is not treated as capital asset and so capital gain arising from sale of agricultural land in rural areas is not chargeable to tax.

Amount deposited in capital gain deposit account scheme:

In case the amount of capital gain is not reinvested for the purchase of agricultural land upto the last date of filing of return of income u/s 139 then the amount of capital gain should

be deposited in the capital gain deposit account scheme with a specified bank upto the last date of filing of return. The proof of deposit is required to be attached with the return of income of that year.

The amount deposited under this scheme must be utilized to purchase agricultural land within 2 years from the date of transfer of agricultural land. In case amount deposited is not utilized to purchase agricultural land within the stipulated period, than the amount which remains unutilized shall be treated as capital gain of the previous year in which the period of 2 years would expire.

Transfer of new agricultural land with in 3 years.

If land, so purchased by re – investing the capital gain, is transferred within a period of 3 years from the date of its purchase, the previously exempted capital gain will be taxable along with the new capital gain on the sale of such land, if any, in the current previous year.

Capital gain on compulsory acquisition of land and buildings (sec 54 D): This exemption is available to all categories of taxpayers. To get exemption the following conditions are to be satisfied.

1. The asset transferred is land or building or any right in land or building which formed part of new industrial undertaking belonging to the tax payer.
2. Asset in question is transferred by way of compulsory acquisition under any law.
3. The asset in question was used for the purpose of industrial undertaking at least for two years immediately before the date of compulsory acquisition.
4. Assessee has purchased any other land or building with in a period of three years from the date of receipt of compensation or constructed a building within such a period.

If the new asset is not acquired by the due date for furnishing the return of income for the relevant assessment year, the unutilized amount of capital gains must be deposited in a Capital Gains Deposit Account. The cost of acquisition of the new asset is reduced by the exemption granted from LTCG for a period of 3 years from its date of acquisition.

- **Investment in Financial Assets (Section -54 EC):** This exemption is available to all categories of taxpayers. To get exemption the following conditions are to be satisfied.
 - (i) In case the capital gain arises from the transfer of a long term capital asset of land or building or both (to be called as the original asset) and the assessee has , at any time with a period of six months after the date of transfer , invested the whole or any part of capital gains in the long term specified asset, such capital gain shall be exempted in accordance with the following provisions of this section:
 - (a) If whole of such capital gain is reinvested in the long term specified asset, the whole of such capital gain shall be exempted.
 - (b) If the amount of the long term capital gain reinvested in specified asset is less than the capital gain arising from the transfer of the original asset, amount so invested in specified asset shall be exempted [section 54 EC (1)]
 - (ii) Where the long term specified asset is transferred or converted otherwise than by transfer into money at any time within a period of 3 or 5 years (If bond is issued on or after 1-4-18) from the date of its acquisition , the amount of capital gains arising from the transfer of the original asset not charged u/s 45 on the basis of the cost of such long term specified asset as provided in clause (a) or as the case may be, clause (b) of sub section (1) shall be deemed to be the income chargeable under the head capital gain relating to long term capital asset of the previous year in which the long term specified asset is transferred or converted (Otherwise than by transfer) in to money.

In a case, where the original asset is transferred and the assessee invests the whole or any part of the capital gain received or accrued as a result of transfer of the original asset in any long term specified asset and such assessee takes any loan or advance on the security of such specified asset, he shall be deemed to have converted such specified asset into money on the date

- (iii) The investment made on or after 1.4.2007 in the long term specified asset by an assessee during any financial year shall not exceed fifty lakh rupees. The investment is to be made within six months from the date of transfer of the original capital asset. This means that exemption u/s 54EC shall be restricted upto 50 lakhs only on investments made in the financial year in which original asset/assets are transferred and in the subsequent financial years.
- (iv) Cost in relation to long term specified asset being land or building or both, means the amount invested in such specified asset out of capital gains received or accruing as a result of the transfer of the original asset.
- (v) Long term specified asset shall mean any bond redeemable after 5 years and issued on or after 1st April, 2007 by the NHAI or by rural electrification corporation limited and bonds issued after 1-4-18 by power finance corporation limited (Notified on 08.06.2017).

So, if land or building or both are transferred and there is a capital gain then the same can be got exempted if the net sale considerations is re- invested within 6 months of sale in the following bonds.

- (a) Bonds issued by National highway authority of India.
- (b) Bonds issued by rural electrification corporation of India.
- (c) Bonds issued by power finance corporation Limited.

In case only a part of net sale consideration is re-invested then only the proportionate part of capital gain shall be exempted.

- **Investment into a residential house (Section 54F):** If an individual or a HUF having LTCG arising out of sale of capital asset other than a residential house invests in the purchase or construction of a residential house, then, he/it is eligible for exemption. In case an individual and HUF transfer any long term capital asset i.e. after holding for 24 months and constructs a residential house within 3 years after the sale or purchases another residential house within one year before or two years after the sale, so much of capital gain shall be exempted as is in proportion of amount invested to net consideration.

$$\text{Amount of exemption} = \frac{\text{Amount invested to purchase or construct a residential house X}}{\text{Capital Gains}} \\ \text{Net Consideration}$$

Where net consideration = full value of consideration - cost of transfer.

Exemption u/s 54 F shall be allowed, if following conditions are fulfilled.

- (i) The assessee is only an individual or a HUF.
- (ii) The assessee does not own more than one residential house on the date of transfer of the assets.
- (iii) The assessee transfers above mentioned assets or assets other than a residential building and there is a long term capital gain.
- (iv) The assessee invests the net sale consideration of above mentioned assets to construct a residential house within 3 years of the sale of the asset or purchases an already built house within one year before or two years after the sale of the above mentioned asset. W.e.f assessment year 2015-16 , exemption u/s 54 F shall be available if the investment is made in purchase or construction of one residential house situated in India, subject to existing time limits.
- (v) The assessee is required not to purchase another residential house within a period of one year after or constructs within a period of 3 year after the date of transfer of the mentioned asset/ assets.

Claim of exemption u/s 54 F if more than one asset is sold.

The assessee can claim exemption u/s 54 F , in such a manner, which is most beneficial to him. In this context, he has two options:

- (i) He may calculate the exemption u/s 54 F for each asset separately and then compare the most beneficial alternative or
- (ii) He may calculate the exemption in following manner and then choose the beneficial alternative
 - (a) Calculate capital gain for each asset separately

(b) Calculate percentage of LTTCG to net consideration

(c) Allow exemption u/s 54 F out of LTTCG of that asset whose percentage is highest.

(d) If amount invested in house is more than net consideration of one asset, the balance investment is to be taken up out of that asset whose percentage is next highest and so on.

w.e.f assessment year 2018-19, if house property acquired after getting examples u/s 54 F is transferred after 2 years but before 3 years, capital gain so arising shall be long term capital gain and the benefit of indexation shall also be available.

Exemption of capital gain on transfer of assets in case of shifting of industrial undertaking from an urban area to any special economic zones (SEZ) [Section 54 GA]

W.e.f assessment year 2006-07, this exemption has been introduced to encourage industrial undertaking situated in an urban area to shift to a special economic zone. This exemption is expected to help those industrial undertaking which may shift their premises from an urban area to a special economic zone.

To avail this exemption, following points are to be noted:

1. There is a transfer of assets like land and building or any right in land and building , plant and machinery of an industrial undertaking situated in an urban area.
2. The above mentioned transfer has been made with the intention of shifting of an industrial undertaking from an urban area to a special economic zone.
3. In connection with transfer of an industrial unit from an urban area to a special economic zone, the assessee has set up an industrial unit in an economic zone within a period of one year before or 3 years after the date on which such transfer took place.

This means that the assessee has bought land or acquired or constructed a building , purchased plant and machinery or has shifted the original assets and has transferred the establishment from an urban area to a special economic zone within the time frame

of one year before and 3 years after the date on which the above mentioned transfer took place.

Amount of exemption

Least of following two amounts shall be the exemption:

- (a) Amount of capital gain earned on the transfer of capital asset.
- (b) Amount spent on the purchase, construction, etc of new assets in a SEZ within specified time frame.

No transfer of new assets within 3 years

New assets acquired by invested the amount of capital gain are not supposed to be transferred within 3 years from the date of their purchase, construction, etc. and if transferred exemption allowed earlier u/s 54 GA Shall be withdrawn and so capital gain arising from such transfer and capital gain got exempted earlier, both will be taxed in the year in which transferred.

Illustrations

Illustration 1: Mr. ghosh sold a house on 1-09- 2018 for Rs 15,00,000. The house was inherited by him during 2001-02 from his father who had constructed it in 1991-92 for Rs 50,000. Mr. ghosh spent Rs 50,000 on renovation of the house in 2006-07. Fair market value of the house as on 1-04-2001 was Rs 450,000. This house was under negotiations for sale in May, 2010 and he received Rs 20,000 as advance money. The contract could not materialize and the advance money was forfeited. Compute the amount of capital gain assuming that he does not qualify for examination. [C.II for 2001-02 = 100; 2006-07 = 122; 2010-11 = 167 & 2018-19 = 280]

Solution 1: Computation of capital gain for assessment year 2019-20

Sale price on 1-09-2018		Rs 15,00,000
Less: Cost of acquisition	450,000	
Less: Advance money forfeited	20,000	
Net cost	430,000	

Indexed cost [430,000 x 280/100]	12,04,000	
Indexed cost of improvement [50,000 x 280 /122]	114,754	Rs 13,18,754
Long term capital gain		Rs 181,246

Note: Advance money forfeited has been deducted from cost of acquisition as advance was received and forfeited prior to 1-04-2014 i.e. , during the previous year 2013-14

Solution 2:

(a) Calculation of taxable capital gain of Mr. A for assessment year 2019-20

Full value of consideration		Rs 20,00,000
Less: Expenses on transfer		NIL
Net consideration		20,00,000
Less: Indexed cost of acquisition		
Cost in 2001-02	500,000	
Less: Advance forfeited in 2005-06	50,000	
[450,000 x 280/100]	<u>450,000</u>	12,60,000
Indexed cost of improvement		<u>NIL</u> <u>12,60,000</u>
Taxable LTCG		<u>740,000</u>

Note: Advance money forfeited has been deducted from cost of acquisition as it was forfeited prior to 1-4-2014.

(b) Calculation of taxable capital gain for the assessment year 2019-20

Full consideration value		Rs 20,00,000
Less: expenses on sale		<u>NIL</u>
Net consideration		<u>20,00,000</u>
Less: Indexed cost of acquisition		
Cost in 2001-02	Rs 500,000 [500,000 x 280 /100]	<u>14,00,000</u>
Taxable LTCG		<u>600,000</u>

(c) Calculation of taxable capital gain for the assessment year 2019-20

Full value of consideration		Rs 20,00,000
Less: expenses on sale		<u>NIL</u>
Net consideration		<u>20,00,000</u>

Less: Indexed cost of acquisition		
Cost to previous owner Rs 500,000 [500,000 x 280 /200]		7,00,000
Indexed cost of improvement	<u>Nil</u>	<u>700,000</u>
Taxable LTCG		13,00,000

Illustration 3: Find out taxable capital gain from the particulars given below:

Net consideration of a residential house Rs 10 lakh (2-06-18) [C II = 280]

Cost of acquisition of this house Rs 210,000 (1-05-07) [CII = 129]

New house acquired on 1-9-18 for 200,000

Solution 3:

Computation of capital gain

Net consideration		Rs 10,00,000
Less : Cost (indexed 210,000 x 280/129)		<u>455,814</u>
Long term capital gain		544,186
Less: Exempted u/s 54 (1)		
Cost of new house		<u>200,000</u>
Taxable long term capital gain		<u>344,186</u>

Illustration 4 : Mr. Rehman purchased a house on 1-11-2001 for Rs 200,000 and its was improved in 2010-11 at a cost of Rs 100,000. What will be indexed cost during 2018-19 if CII for 2001-02 is 100 , for 2010-11 is 167 and for 2018-19 = 280

Solution 4:

Computation of indexed cost

Cost of acquisition		200,000
Indexed cost of acquisition	$200,000 \times 280 / 100$	= 560,000
Cost of improvement		100,000
Indexed cost of improvement	$100,000 \times 280 / 167$	= <u>167,665</u>
Total indexed cost		= <u>727,665</u>

Illustration 5: Find out indexed cost and capital gain in the following cases:

- (a) WDV of office furniture as on 1-4-18 Rs 18,000 (Which was purchased on 15-9-08 for Rs 20,000 and sold on 1-9-18 [CII = 280] for Rs 26,000)
- (b) Bonds purchased on 1-11- 06 [CII = 122] for 260,000 were sold on 1-1-19 [CII = 280] for Rs 400,000
- (c) Cost of acquisition of house in mumbai in 1996-97 Rs 100,000
 Cost of improvement made in 1999-00 Rs 50,000
 FMV on 1-4-01 [CII = 100] Rs 400,000
 Cost of additions made in 2008-09 [CII = 137] Rs 320,000
 Sale price of the house on 1-11- 18 [CII = 280] Rs 28,60,000
 Expenses on sale Rs 60,000

- (a) Mr. Mohan inherited a house at Jammu from his father Mr. Rohit on 1-1- 2006 [CII = 117]. The house was acquired by Mr. Rohit in 1989-90 for Rs 60,000 and its FMV at on 1-4-2001 was Rs 520,000 and its was sold in 2018-19 [CII = 280] for 13,50,000

Solution 5: Computation of Capital gain

- (a) STCG

Sale price	Rs 26,000
Less: WDV as on date	Rs <u>18,000</u>
STCG	Rs <u>8,000</u>

- (b) LTCG

Sale price	Rs 400,000
Less: Cost price [no indexing]	Rs 260,000
LTCG	Rs 140,000

- (c) LTCG

Sale price	Rs 28,60,000
Less : Expenses on sale	Rs <u>60,000</u>
Net consideration	Rs 28,00,000
Less:	
Indexed cost [$460,000 \times 280/100$]	12,88,000
Indexed cost of additions [$320,000 \times 280/137$]	<u>654,015</u>
	Rs <u>19,42,015</u>

LTCG	Rs <u>857,985</u>
(d) LTCG	
Sale price	Rs 13,50,000
Less: expenses on sale	<u>NIL</u>
Net consideration	Rs 13,50,000
Less: Indexed cost [520,000 x 280 / 117]	Rs <u>12,44,444</u>
LTCG	Rs 105,556

Illustration 6 : Mr. Avtar Singh purchased a plot in 2002-03 for Rs 400,000 and it was sold on 15-1-19 for Rs 14,80,000 . He paid Rs 20,000 as brokerage charges. He invested Rs 200,000 in bonds issued by NHAI on 31-3-19 and Rs 310,000 in Bonds issued by Rural electrification corporation on 1-6- 2019 (Both notified u/s 54 EC)

Compute the taxable amount of capital gain if CII for 2002-03 is 105 and for 2018-19 is 280.

Solution 6 : Computation of Taxable capital gain

Sale price of plot	Rs 14,80,000
Less: Expenses on sale	Rs <u>20,000</u>
Net consideration	14,60,000
Less: indexed cost [400,000 x 280 / 105]	<u>1066,667</u>
LTCG	393,333

Less: Exemption u/s 54 EC

Amount invested in NHAI	Rs 200,000
Amount invested in bonds of rural electrification	Rs <u>310,000</u>
	Rs 510,000

But exemption restricted to Rs 393,333

As the investment made within 6 months of

Investment	<u>393,333</u>
LTCG	NIL

Illustration 7: Mr. X provides the following information regarding the transaction for the sale of residential house during the assessment year 2019-20

House purchased in 1988 for Rs 150,000

FMV on 1-4-01 [CII = 100] Rs 620,000

Sold in oct, 2018 [CII = 280] Rs 28,00,000

Amount invested in purchase of another house in April , 2018 Rs 800,000.

Find out Taxable Capital gain

Solution 7:

Computation of capital gain

Sale price of house / Net consideration	Rs <u>28,00,000</u>
Less: Indexed FMV [620,000 x 280/100]	<u>17,36,000</u>
LTCG	10,64,000
Less: Exemption u/s 54	
Amount invested in new house within 2 years after sale	<u>800,000</u>
Taxable	<u>264,000</u>

Illustration 8: Mr. Z acquired a plot of land on 30-6-2006 [CII = 122] for Rs 750,000 and spent Rs 28,500 on its registration and brokerage ,etc. This plot was sold for Rs 21,00,000 on 30-6-2018 [CII = 280]. He had purchased a house for Rs 400,000 on 1-8-2017 for his own residence. He had paid Rs 5,000 as ground rent of plot held by him. Compute the amount of taxable capital gain for the assessment year 2018-19.

Solution 8:

Computation of capital gain

Sale price of plot on 30-6-18	21,00,000
Less:	
Indexed cost [750,000 + 28,500]	
778,500 x 280 / 122	<u>17,86,721</u>
LTCG	313,279
Less: Exemption u/s 54 F	
Amount invested in new house within 1 year before sale	
[313,279 x 400,000 /21,00,000]	<u>59,672</u>
Taxable LTCG	253,607

1.13 INCOME FROM OTHER SOURCE

“Income from other sources” is the fifth and last head of income included while computing the gross total income of an assessee. Under the Income Tax act, income of every kind which is not to be excluded from the total income shall be chargeable to income tax under the head ‘Income from other sources’, if it is not chargeable to income tax under any of the other heads of income. Thus, income from other sources is a residuary head of income i.e. income not chargeable under any other head is chargeable to tax under this head. All income other than income from salary, house property, business and profession or capital gains is covered under ‘Income from other sources’

Section 56, 57, 58 and 59 of the Income Tax Act deal with the computation of income under this head.

According to section 56 (1), every kind of income which is included in the total income under this Act and which is not charged to tax under any first four heads specified in section 14 is chargeable to income-tax under the head “Income from Other Sources”.

1.13.1 There are two types of income included in this head

- General Incomes covered under section 56(1), and
- Specific Incomes covered under section 56(2).

General Incomes section 56 (1) as ‘Income from Other Sources’

- 1) Income earned by the assessee from licenses granted to brick-makers, to erect brick kilns upon his land and making use of the brick-earth for making bricks.
- 2) Interest on loans, securities, deposits, cooperative debentures and current accounts.
- 3) Income from agriculture land situated outside India.
- 4) Income derived by a coal mine owner from rent and royalties.
- 5) Any withdrawal from the National Saving Scheme up to an amount on which deduction under section 80CCA has been claimed.

- 6) Remuneration received for being as a director, not as employee.
- 7) Income received from a person other than the employer like University remuneration.
- 8) Family pension received by the legal heirs of employee.
- 9) Income received by a professional man as a university examiner.
- 10) Income received from sub-letting of house.
- 11) Remuneration from lectures delivered outside India.
- 12) Tips received by a waiter or taxi driver not from their employer.
- 13) Any amount or pension received from LIC or other insurer under section 80CCC.
- 14) Deemed incomes.
- 15) Income from writing articles by a non-journalist.
- 17) Gratuity received by a non-employee director.
- 18) Commission received by an agent of Life Insurance Corporation, Postal Savings, Unit Trust of India or other type of mutual funds if it is not his regular business.
- 19) Commission received by a director for standing as a guarantor.
- 20) Commission received by a director for under righting the shares of a new company.

Specific Incomes section 56 (2) as ‘Income from Other Sources’

- 1) Any winning from lotteries, crossword puzzles, races including horse races, car games or any other games or from gambling or betting of any form or natural.
- 2) Dividends (except dividend covered u/s 115-O).
- 3) Income from plant, machinery or furniture let on hire, provided such income is not charged to tax under the head ‘profits and Gains of Business or Profession’.
- 4) Any sum received by the assessee from his employees as contribution to any provident fund or superannuation fund or any fund set up under provisions of the Employees State Insurance Act 1948, or from any other fund from the welfare of

such employees, provided such income is not charged to tax under the head 'Profits and Gains of Business or Profession'.

- 5) Income received in the form of interest on securities, provided such income is not charged to tax under the head 'Profits and Gains of Business or Profession.
- 6) Income from let-out of building along with plant, machinery or furniture and letout of building is inseparable from such plant, machinery or furniture, provided income from such let-out is not charged to tax under the head 'Profits and Gains from Business or Profession'.
- 7) Any sum or bonus received from key man insurance policy if such sum is not chargeable to tax as salary or bonus income.
- 8) Any sum of money received without consideration by an individual or HUF, the aggregate value of which exceeds Rs.50, 000, from any person on or after 1 April 2006 but before 1 October 2009. The whole amount will be charged to tax under the head 'Income from Other Sources'.
- 9) Income received by in the form of interest on compensation or on enhanced compensation.
- 10) Any consideration received by a closely held company for the issue of shares that exceeded the face value of such shares.
- 11) Any sum received as an advance or otherwise in the course of negotiation for the transfer of a capital asset and such amount is forfeited due to non transfer of such capital asset.
- 12) If a firm or closely held company receives any property in the form of shares of a closely held company in any previous from any person:
 - a) Without any consideration, the aggregate fair market value of which exceeds Rs.50,000, such aggregate fair market value of shares shall be taxable under the head 'Income from Other Sources'.
 - b) For a consideration which is less than the fair market value of such shares by an amount exceeding Rs. 50000, the excess of aggregate fair market value of such

shares over such consideration shall be taxable under the head 'Income from Other Sources'.

13) The treatment of Gifts by an Individual or HUF:

a) Any sum of money received by an individual or HUF from any person without consideration exceeds Rs.50000 in aggregate during the previous year, whole of such amount shall be chargeable to tax under the head 'Income from other sources'.

b) Immovable property:

(i)- Any immovable property received by an individual or HUF from any person without any consideration having stamp duty exceeding Rs.50000, the stamp duty value shall be taxable under the head 'Income from other sources'.

(ii)- Any immovable property received by an individual or HUF on or after 1 April 2015 for a consideration which is less than the stamp duty value of such property by an amount exceeding Rs. 50000, the stamp duty value of such property as exceeding such consideration is taxable under the head 'Income from other sources'.

c) Other than Immovable Property;

(i)- Property other than immovable property received by an individual or HUF from any person without any consideration, the aggregate fair market value of which exceeds Rs.50000, whole of the aggregate fair market value of such property shall be taxable under the head 'income from other sources'.

(ii)- Property other than immovable property received by an individual or HUF from any person for a consideration, which is less than the aggregate fair market value of the property by an amount exceeding Rs. 50000, the excess of aggregate fair market value of such property over such consideration is taxable under the head 'Income from other sources'.

1.14 INTEREST ON SECURITIES

The income from interest on securities shall be chargeable to tax under income from other sources, if it is not taxable under the head income from business or profession. The following amounts due to an assessee in the previous year shall be chargeable to income tax as interest on securities.

1. Interest on any security of the central or state govts.

2. Interest on debentures or other securities issued by a local authority Or a company or a corporation established by a central , state or provincial act, [Section 2 (28 B)]

What is interest

Interest in the return which a person receives from another person for bearing the risk of parting with the money and losing the income which he would have received on such money had he deposited it in a bank. It simply means the return received by a creditor who has given his money as debt.

What is security

A security is a document acknowledging the debt taken by a specific authority from general public . It may be named as debt or loan or paper or debenture or security or certificate. It is secured in some manner.

Content of security

It contains face value of security , date of maturity, rate of interest, date , place and period of payment of interest, etc. These are transferable.

Who can issue a security?

As per section 18, securities may be issued by following authorities:

- The central government
- A state government
- A local authority
- A company
- A statutory corporation

Taxability of interest

- Any interest which accrues after a fixed period as mentioned on the face of the security itself. In India, generally, interest accrues after a period of 6 months.

Any interest which accrues to a person during the previous year is added in his gross total interest.

- Interest is taxable on due basis whether received or not. It is immaterial whether the assessee has received it or not.
- Interest on securities issued by the Govt. of India is considered to be accrued in India even if enforced to pay outside India.
- Interest accrues on the name of the person on whose name securities stand on the date of accrual of interest. It is immaterial that he purchased these securities a few days earlier than the date of accrual of interest. He has to include full interest in his gross total income.

Deduction of Tax at source. It is the duty of the security issuing authority to deduct tax at source before making the payment of interest on securities at the prescribed rate. Rates in force means the rate or rates specified for the purpose of deduction by finance act of the year in which deduction is to be made. The tax deducted at source will be deposited in the government treasury on behalf of the security holder. The security holder account is credited with the amount and while paying the tax on the total income the amount deducted at source will be deducted.

However, in the case of the following securities tax is not deducted at source:

- (i) Interest payable on 4 $\frac{1}{4}$ % national defence bonds, 1972 where the bonds are held by an individual, not being a non- resident or
- (ii) 4 $\frac{1}{4}$ % National defence loan, 1968 or 4 $\frac{3}{4}$ % national defence loan, 1972, provided the interest is payable to an individual or
- (iii) Interest payable on national development bonds
- (iv) 7 year national savings certificates (IVth Issue)
- (v) Debentures issued by any co- operative society or any other institution notified by the central government or

- (vi) 6 ½ % gold bonds, 1977 or 7 % gold bonds, 1980 where the bonds are held by an individual , not being a non- resident and the holder thereof makes a declaration in writing before, the person responsible for paying the interest that the total nominal value of gold bonds held by him did not exceed Rs 10,000 at any time during the period to which the interest relates or
- (vii) No tax will be deducted at source from any security issued by central government or a state government
- (viii) No tax will be deducted at source if interest on term deposit with a bank does not exceed Rs 10,000 in a previous year.

1.14.1 Interest on Securities exempted from Tax. U/S 10(15)

A. Interest on certain type of Bonds issued by public sector companies/undertakings has been exempted from tax, these are:

1. 7% capital investment bonds.
2. 10% secured redeemable NTPC bonds 1986. (Ist series)
3. 9% and 10% secured redeemable non-convertible bonds issued by Indian Railway Finance Corporation.
4. 10% secured redeemable non-convertible bonds issued by Mahanagar Telephone Nigam Ltd.
5. 10% secured redeemable non-convertible bonds 1987 (B series) issued by National Hydro Electric Power Corporation Ltd.
6. 9% (Tax free) secured redeemable bonds issued by Power Finance Corporation Ltd.
7. 6.5%, 8%, 9%, and 10% National Relief Bonds.
8. 10% (Tax free) secured redeemable non-convertible bonds issued by Indian Telephone Industries Ltd.
9. 10-years 9% (Tax free) secured redeemable non-convertible PFC bonds- II series (private placement) issued by Power Finance Corporation.

10. 10-years 9% (Tax free) secured redeemable non-convertible NTPC bonds-IV issue (private placement).
11. 10-years 9% (Tax free) secured redeemable non-convertible REC bonds issued by the Rural Electrification Corporation Ltd.
12. 10-years 9% (Tax free) secured redeemable non-convertible (C series) issue by Neyveli Lignite Corporation Ltd.

B. Interest on Securities exempted from Tax.

- Interests on securities earned by the following types of assesseees are exempted from tax.

- 1) Political parties.
- 2) A local authority.
- 3) A registered trade union.
- 4) Trustees of a recognized provident fund.
- 5) An approved scientific research association.
- 6) Members of scheduled tribes living in tribal areas.
- 7) A non-resident of Indian origin and securities and bonds were issued before June 1, 2002.
- 8) Public charitable and religion trusts.

1.15 KINDS OF SECURITIES

There are four types of securities.

1. Tax free government securities: The interest on these securities is fully exempt from tax. The interest on such securities is neither included in total income nor taxed.

2. Less tax government securities: These securities are issued by central govt or state government. These securities are taxable securities. But no tax is deducted at source on such securities. Therefore the interest on such securities will not be grossed up.

3. Tax free commercial securities: These securities are issued by local authority or Statuary Corporation or a company in the form of debentures or bonds. Actually the interest is not tax free. Income tax due on this interest is payable by the company or authority or Statuary Corporation. These are called tax free because the assessee is not required to pay tax on it. The interest due to an assessee is grossed up and this grossed up amount is included in the total income.

4. Less tax commercial securities: These are taxable securities. In this case income tax is deducted at source on the amount of interest calculated at the percentage stated on the securities. In this type of securities, if the net amount of interest is given, it has got to be grossed up. If the rate of percentage of interest is given it is not grossed up.

Deduction [Section 57]

The taxable income under the head income from other sources shall be computed after allowing the following deductions as provided in section 57:

1. In case of Dividends and Interest on securities: From the dividend income, a deduction shall be allowed in respect of any sum spent by way of commission or remuneration to a banker or any other person as collection charges for realizing the dividend or interest on securities.
2. Repairs, depreciation ,etc in case of letting of machinery, plant or furniture with or without building. The following deductions shall be allowed from the income earned by letting of machinery , plant or furniture with or without building
 - (i) Expenditure incurred on current repairs of plant, machinery, furniture or building
 - (ii) Insurance premium paid regarding these assets.
 - (iii) Depreciation on plant, machinery and furniture. Depreciation in respect of buildings will be allowed only if the assessee is the owner. It will not be allowed if the assessee is lessee or mortgage in possession of the building.

3. Deduction in respect of employee's contribution in staff welfare schemes [57 (ia)]. Any amount received by employer from his employees as their contribution of provident fund, ESI Fund or superannuation fund is deemed as income u/s 59 (ic) if not taxable under the head profits and gains of business or profession.

In case employer deposits any amount out of these incomes in these funds before prescribed due date, such amount is allowed as deduction u/s 57 (ia).

4. Standard deduction out of family pension [section 57 (iia)] . In case of income in the nature of family pension, a deduction of a sum equal to 33 1/3 % of such pension or Rs 15,000 whichever is less , shall be allowed.

Family pension means a regular monthly amount payable by employer to the legal heirs of deceased employee.

5. Deduction from any other income [Section 57 (iii)]. Any expenditure which is spent to earn an income chargeable to tax under this head shall be deducted from such income.

This deduction is not admissible to assessee being a foreign company.

To claim this deduction following conditions must be satisfied

- (i) The expenditure should be incurred solely for earning such income
 - (ii) It should not be in the nature of capital expenditure.
 - (iii) It should not be in the nature of personal expense
 - (iv) It should be incurred in the relevant accounting year.
6. Deduction from royalties received by authors: Other than those writing for films- Actual expenses can be claimed as deduction.
7. Deduction regarding interest on compensation or enhanced compensation: In case assessee has received any income of this type, a deduction of a sum equal to 50 % of such income shall be allowed and no deduction shall be allowed under other clause of this section.

Amount expressly disallowed [Section 58]

The following expenses are not allowed to be deducted from such income:

In case of any assessee —

- (i) Any personal expenses of the assessee
- (ii) Any interest chargeable under this act which is payable outside India on which tax has not been paid or deducted at source.
- (iii) Any payment which is chargeable under the head salaries if it is payable outside India unless tax has been paid or deducted at source.
- (iv) In case an assessee has income from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever, such assessee shall not be allowed any deduction in respect of any expenditure or allowance in connection with such incomes.

In case of every assessee any payment to relatives and associates made in cash may be disallowed under section 40 A in certain circumstances. The provisions of section 40 A are made applicable under this head also by sub section 2 of section 58.

Profits chargeable to tax [section 59]

Under section 59 (i) the provisions of sub section (1) of section 41 have been made applicable in computing the income of an assessee under section 56 as they are applicable in computing the income under the head profits and gains of business or profession.

This provision deals with any allowance or deduction which has been allowed under this head in the assessment of income in any earlier year in respect of any expenditure, loss or trading liability incurred by the assessee subsequently during any previous year, the same amount is received or recovered in cash or in any other manner shall be deemed to be the income of that previous year in which it is recovered irrespective of the fact whether the source of income continues to exist in that year or not.

Avoidance of tax by certain transactions in securities (Bond washing) [Section 94]

1. In case a person sells his securities to another person a few days before the accrual of interest and purchases them back after the date of accrual, and assessing office is satisfied that the transaction has been made with intention of avoiding tax, such interest shall be deemed as income of the transferor and not transferee [Section 94 (1)]
2. In case a person has any beneficial interest in any securities and as a result of some arrangement either no income is received by such person or the income received by him is lower than the amount which he would have received, the interest, which would have accrued on such securities had there been no such arrangement, would be included in the income of person making such arrangement. [section 94 (2)]
3. The above provisions will not be applicable , if such person proves to the satisfaction of the assessing officer that the transaction has not resulted into any avoidance of tax or if at all there was some avoidance it was exceptional as there had not been any avoidance of tax in any of three preceeding previous years [section 94 (3)]
4. In case of dealer of securities, if there is a transaction of sale or purchase of securities and as a result the interest becomes receivable by him but is not deemed to be his income due to the above provisions , no account shall be taken of the transaction in computing profits arising from or loss sustained in the business[section 94(4)]
5. The assessing officer may direct any person to furnish a detail of securities held by him by serving upon him a notice for not less than 28 days [section 94 (5)]

TDS rates

- | | |
|-------------------------------------------------------------------------|------|
| 1. Interest on securities issued by local authority or statutory bodies | 10 % |
| 2. Listed debentures of a company | 10 % |
| 3. Unlisted debentures | 10 % |
| 4. Bank interest | 10 % |
| 5. Casual incomes | 30 % |

No TDS

1. Interest on government securities
2. In case of winning from bettings
3. Deemed dividend u/s 2 (22) (c)
4. Interest on any security notified u/s 193
5. Interest paid to an individual and HUF in account payee cheque for an amount not exceeding Rs 5,000 by certain companies
6. Bank interest on fixed deposit credited or paid up to Rs 10,000
7. Race winnings if it is up to Rs 5,000
8. Winnings from lotteries and puzzle amount if up to Rs 10,000
9. In case of card game and games of other sort if up to Rs 10,000

1.16 SUMMARY

Any income arising from the transfer of a capital asset in the relevant previous year shall be chargeable to income tax under the head 'Capital Gains' and shall be deemed to be the income of the previous year in which transfer of asset takes place. It means tax is to be levied on any profit or gain occurring on the transfer of a capital asset. The term capital assets includes all types of properties, whether tangible or intangible, movable or immovable, fixed or floating. Further two types of capital assets are there: Short term capital assets and long term capital assets. If the assessee holds the capital asset up to 36 months, then asset is considered as long term whereas, if the assessee holds the capital asset up to less than 26 months, then asset is considered as short term. The gain from capital asset arises only on its transfer. If the asset transferred is not a capital asset, then no capital gain shall arise. The transfer includes, sale, exchange or relinquishment of the capital assets; or the extinguishment of any rights therein; or the compulsory acquisition thereof under any law. In other words long and short term gains arise only when there is transfer of an asset. Any capital gain arising as a result of transfer of a short-term capital asset is known as short-term capital gain whereas any gain arising as a result of transfer of long-term capital asset is known as long term capital gain. In addition, the value for which the asset was acquired by

the assessee is known as the cost of acquisition. In other words Cost of Acquisition (COA) means any capital expense at the time of acquiring capital asset under transfer, i.e., to include the purchase price, expenses incurred up to acquiring date in the form of registration, storage etc. expenses incurred on completing transfer. Expenses of capital nature for completing or acquiring the title are included in the cost of acquisition. Further if the assessee makes any addition or improvement in the capital asset as an addition over and above the cost of acquisition such cost or capital expenditure is termed as Cost of improvement. It also includes any expenditure incurred in protecting or curing the title. In other words, cost of improvement includes all those expenditures, which are incurred to increase the value of the capital asset. The assessee has been provided the opportunity by the Act to avail tax deduction arising out of capital gains by way of many specific sections. Under Sections 54, 54B, 54D, 54EC, 54F, 54G and 54H of the Act, capital gains arising from the transfer of certain capital assets are exempt from tax under certain circumstances.

Under the Income Tax act, income of every kind which is not to be excluded from the total income shall be chargeable to income tax under the head 'Income from other sources', if it is not chargeable to income tax under any of the other heads of income. Thus, income from other sources is a residuary head of income i.e. income not chargeable under any other head is chargeable to tax under this head. All income other than income from salary, house property, business and profession or capital gains is covered under 'Income from other sources'. Two types of income are included in this head, General Incomes covered under section 56(1), and Specific Incomes covered under section 56(2).

Lastly we have discussed some issues related interest on securities. The income from interest on securities shall be chargeable to tax under income from other sources, if it is not taxable under the head income from business or profession. The following amounts due to an assessee in the previous year shall be chargeable to income tax as interest on securities. Interest on any security of the central or state govts, Interest on debentures or other securities issued by a local authority, Interest on debentures issued by a company (whether Indian or foreign), Interest on debentures or other securities issued by statutory corporation. Interest on Securities is exempted from Tax. U/S 10(15).

ILLUSTRATION 1

Mr. R held the following Investments:

- a) Rs 9000 10% (tax-free) Debentures of a listed company (rate of TDS 10%)
- b) Rs 100000 12% Punjab govt. loan.

Compute his income from interest on securities for the year ending 31-3-2019.

SOLUTION

Computation of Income from interest on securities

	Rs
a) Rs 90,000 10% (tax free) Debentures (listed) [9000 x 100/90]	10,000
b) Rs 100000 12% Punjab Govt. Loan	12,000
Income from Interest on securities	22,000

ILLUSTRATION 2

Calculate income from other source from information given below:

- i) Winning from lottery
- ii) Amount received from race winnings

Gifts received during the previous year 2018-19

- i) Received Rs 20000 gift from his friend
- ii) Received Rs 100000 as gift from his elder brother
- iii) Received Rs 140000 as gift on his marriage
- iv) Received 80000 as gift from his NRI friend on 1.1.2019
- v) Another gift of Rs 18000 received from his cousin

SOLUTION

Computation of income from other source

Income	Rs	Rs
i) Winning from lottery		100000
ii) Amount received from race winning		50,000
to be grossed up [$35000 \times 100/70$]		
Gifts Received		
i) Received Rs 20000 gift from his friend	20000	
ii) Received Rs 100000 as gift from his elder brother	Nil	
(Gifts from relatives are exempted)		
iii) Received Rs 140000 as gift on his marriage	Nil	
(Gifts from marriage are exempted)		
iv) Received 80000 as gift from his NRI friend on 1.1.2019	80000	
v) Another gift of Rs 18000 received from his cousin	18000	<u>1,18,000</u>
Income from other sources		<u>2,68,000</u>

Illustration 3 : Mr. Mukundu furnishes the following information about his income for the previous year 2018-19 . Compute his income under the head other sources

Dividend on equity shares Rs 600

Dividend On preference shares Rs 3,200

Income from letting on hire of building and machinery under composite lease Rs 17,000

Interest on bank deposits Rs 2,500

Director's fees Rs 1,200

Ground rent Rs 600

Income from undisclosed sources (Unexplained) Rs 10,000

Income from lotteries (Gross) Rs 10,000

The following deductions are claimed by him:

Collection charges of dividend Rs 20

Allowable depreciation on building and machinery Rs 4,000

Fire insurance premium on building and machinery Rs 100

Solution 3:

Computation of income from other sources

General income u/s 56 (1)		
Interest on bank deposit	2,500	
Director's fees	1,200	
Ground rent	600	
Income from undisclosed sources	<u>10,000</u>	14,300
Specific income u/s 56 (2)		
Dividend on equity shares (exempted)	Nil	
Dividend on preference shares (Exempted)	Nil	
Winnings from lotteries	10,000	
Rent of building and machinery	17,000	
Less: expenses:		
Depreciation	4,000	
Fire insurance premium	100	
	<u>12,900</u>	12,900
Income from other sources		37,200

Illustration 4 : Compute income from other sources of Mr. Krishna Murthy who held the following investments during the previous year 2018-19

11,000 , 10 % central government securities

Rs 36,000, 10 % tax free commercial securities of a closely held company

Rs 6,300 received as interest on tax free public limited company securities (Listed)

Rs 7,200 received interest on karnatka government securities

Rs 4,000 received as interest on debentures of Deepak fertilizers (Listed)

Rs 30,000 , 13.5 % securities of paper mill co. (Listed)

Rs 35,000, 11 % securities of paper mill co. (Listed)

Rs 10,000 , 15 % jaipur municipal corporation bonds

Dividend from carona ltd. Rs 4,000

During the year, he also got a prize in karnatka state lottery . The net amount received by him was Rs 35,000 . Interest on all securities is payable on 1ST January every year. Bank charged Rs 200 as collection charges.

Solution 4: Computation of income from other sources

Specified incomes 56 (2)		
Dividend from carona Ltd. (Exempted)	Nil	
Interest on securities		
Rs 11,000 10 % central government securities	1,100	
Rs 36,000 10 % tax free commercial (3600 x 100 /90)	4,000	
Rs 6,300 received as interest on listed debentures [6,300 x 100 /90]	7,000	
Rs 7,200 received as interest on karnatka government securities (No TDS)	7,200	
Rs 4,000 received as interest on listed debentures of Deepak fertilizers [no TDS]	4,000	
Rs 35,000 11 % securities of paper mill	3,850	
Rs 30,000 13.5 % securities	4,050	
Rs 10,000 15 % Jaipur municipal Bonds	1,500	32,700
Winning from lottery [35,000 x 100 /70]		50,000

Winning from lottery [35,000 x 100 /70]		82,700
Gross income		200
Less: Deduction of collection charges		82,500
Income from other sources		

1.17GLOSSARY

- Sections 45 to 55A of the Income-tax Act, 1961 deal with capital gains. Section 45 of the Act, provides that any profits or gains arising from the transfer of a capital asset effected in the previous year shall, save as otherwise provided in Sections 54, 54B, 54D, 54EC, 54ED, 54F, 54G, 54GA and 54H be chargeable to income-tax under the head “Capital Gains” and shall be deemed to be the income of the previous year in which the transfer took place.
- Section 2(14) of the Income-tax Act defines the term “capital asset” to mean Property of any kind held by an assessee whether or not connected with his business or profession but does not include any stock-in-trade, personal effects, agricultural land in India, 6½ per cent Gold Bonds, Special Bearer Bonds, Gold Deposit Bonds.
- The essential requirement for the incidence of tax on capital gains is the transfer of a ‘capital asset’. Any capital gain arising as a result of transfer of a short-term capital asset is known as short-term capital gain. “Short term” capital asset means a capital asset held by an assessee for not more than thirty-six months immediately preceding the date of its transfer. In the case of capital assets (being equity or preference share in a company) held by an assessee for not more than 12 months immediately prior to its transfer.
- Assets other than short-term capital assets are known as ‘long-term capital assets’ and the gains arising therefrom are known as ‘long-term capital gains’. Section 48 of the Act provides that the income chargeable under the head ‘capital gains’ shall be computed by deducting from the full value of consideration received or accruing as a result of the transfer of the capital asset the amount of expenditure incurred wholly and exclusively in connection with such transfer and the cost of acquisition of the capital asset and the cost of any improvement thereto.

- ‘Cost of acquisition’ of goodwill of a business or a right to manufacture, produce or process any article or thing, tenancy rights, stage carriage permits or loom hours is in the case of acquisition of such asset by the assessee by purchase from a previous owner, cost of acquisition means the amount of the purchase price; and in any other case cost of acquisition shall be Nil.
- Cost of improvement means all capital expenditure in making any additions or alterations by the assessee after it became his property and where the capital asset became the property of the assessee by any of the modes specified in Section 49(1) by the previous owner as the case may be.
- Under Sections 54, 54B, 54D, 54EC, 54F, 54G and 54H of the Act, capital gains arising from the transfer of certain capital assets are exempt from tax under certain circumstances.
- Income chargeable under Income-tax Act, which does not specifically fall for assessment under any of the heads discussed earlier, must be charged to tax as “income from other sources”.
- Section 56(2) specifically provides for the certain items of incomes as being chargeable to tax under the head such as Dividend, Keyman Insurance policy, Winnings from lotteries, Contribution to Provident fund, Income by way of interest on securities, Income from hiring machinery etc, Hiring out of building with machinery, Money Gifts, Share premiums in excess of the fair market value to be treated as income, income by way of interest received on compensation.
- The entire income of winnings, without any expenditure or allowance or deductions under Sections 80C to 80U, will be taxable. However, expenses relating to the activity of owning and maintaining race horses are allowable. Further, such income is taxable at a special rate of income-tax i.e., 30% + surcharge + cess @ 3%.
- Admissible Deductions : The income chargeable under the head “Income from other sources” is the income after making the deductions such as
 - sum paid by way of commission or remuneration to a banker or any other person for the purpose of realising such interest;

- deduction shall be allowable in accordance with the provisions of Section 36(1)(va), i.e., if the employer has credited the employee's accounts in the respective funds;
 - a sum equal to 33-1/3% of the income or ₹ 15,000, whichever is less, is allowable as a deduction from family pension;
 - a deduction of a sum equal to 50% of from Interest on compensation or enhanced compensation, and
 - any other expenditure (not being in the nature of capital expenditure) laid out or expended wholly and exclusively for the purpose of making or earning such income.
- Inadmissible deductions: The following amounts shall not be deducted in computing income chargeable under the head 'Income from other sources':
 - Any personal expenses of the assessee.
 - Any interest chargeable under the Income-tax Act which is payable outside India and from which income-tax has not been paid or deducted at source.
 - Any payment which is chargeable under the head "Salaries" if it is payable outside India unless tax has been paid thereon or deducted therefrom at source.
 - Any expenditure referred to in Section 40A of Income-tax Act.
 - The basis of charge on income by way of interest on securities is on "receipt" basis if books of account are maintained on cash basis. If the assessee does not maintain books of account or, when he maintains books of account on the basis of "mercantile system", it is taxable on "due" basis.

1.18 SELF ASSESSMENT QUESTIONS

1. What do you mean by "Capital Gain"?

2. Difference between Long-term Capital Gain and Short –Term Capital Gain .

3. Explain with the help of suitable illustration how capital gains are computed under section 45(2) in case of conversion of capital asset into stock-in-trade.

4. What is Cost of Acquisition and Cost of Improvement?

5. What are the incomes chargeable under the head “Income from other sources”?

6. What deductions are allowed under the head “Income from other sources”?

7. What are 'capital assets'? What items are not included in capital assets?

8. Explain the deduction given in respect of certain incomes.

9. Explain Specific Income. What are the items to be included under general and Specific Income?

1.19 BOOKS RECOMMENDED

1. Dr. V.K. Singhania: Students Guide to Income-tax; Taxmann Publications Pvt. Ltd., New Delhi.
2. Girish Ahuja and Ravi Gupta: Systematic Approach to Income-tax and Sales-tax; Bharat Law House, New Delhi.
3. Dr. H.C Meharotra and Dr S. P Goyal: Income Tax Law and Accounts; Sahitya Bhavan Publications.
4. V. P Gaur & D. B Narang: Income Tax Law & Practice; Kalyani Publishers.

5. V. K Singhanian & Kapil Singhanian: Direct Taxes Law & Practices; Taxman Publications.
6. Mahesh Chandra, D. C Shukla, K. A Mahajan & M. A Shah: Income Tax Law & Practices; pragati Publication, New Delhi.
7. Arvind Tuli & Dr. Neeru Chadda: Conceptual Clarity on Income Tax and Wealth Tax; Kalyani Publication, New Delhi.

**SETT OFF AND CARRY FORWARD OF LOSSES, AGGREGATION OF
INCOME, DEDUCTIONS FROM GROSS TOTAL INCOME FOR
INDIVIDUALS, HUF'S AND FIRMS.**

STRUCTURE:

2.1 Introduction

2.2 Objective

2.3 Concept of set-off and carry-forward of losses

2.3.1 Set-off of Losses

2.3.2 Carry-forward of Losses

2.4 Aggregation of Income

2.4.1 Income of other persons to be included in the income of individual (Section 60-645).

2.4.2 Income received from firm assessed as firm and Association of Persons (Section 66 & 67).

2.4.3 Deemed Incomes (Section 68-69).

2.5 Deductions from Gross Total Income

2.5.1 Deduction in respect of certain payments (section 80C to 80GGC).

2.5.2 Deduction in respect of certain incomes (section 80IA to 80U).

2.6 Summary

2.7 Glossary

2.8 Self-Assessment Questions

2.9 Books Recommended

2.1 INTRODUCTION

This lesson discusses the provisions for set-off and carry forward of losses. Sometimes the assessee incurs a loss from a source of income and unless such loss is set-off against any income, the net result of the assessee's activities during the particular accounting year cannot be ascertained and consequently the tax payable would also be incapable of determination. For this purpose, the Income-tax Act contains specific provisions (Sections 70 to 79) for the set-off and carryforward of losses.

This lesson also discusses the deductions from gross total income. The deductions are available only to the assessee where the gross total income is positive. If however, the gross total income is nil or negative, the question of any deduction from the gross total income does not arise. For this purpose, the expression 'gross total income' means the total income of the assessee computed in accordance with the provisions of the Income-tax Act before making any deduction under Chapter VIA. The aggregate of income computed under each head, after giving effect to the provisions for clubbing of income and set off of losses, is known as "Gross Total Income". Sections 80A to 80U of the Income-tax Act lay down the provisions relating to the deductions allowable to assessee from their gross total income. The income arises after deduction under section 80C to 80U is called Total Income.

2.2 OBJECTIVES

At the end of this lesson, you will learn

- What are the provisions of set off/carry forward and set off of losses
- How losses can be set off inter-head and intra-head.
- The conditions to be satisfied for carry forward and set off of loss from house property, business loss and unabsorbed depreciation.

- Up to what period the loss can be carried forward and set-off.
- The type of deductions allowable from gross total income
- What are the permissible deductions in respect of payments
- What are the permissible deductions in respect of incomes
- What are the deductions allowable in the case of a person with disability.

2.3 SET-OFF AND CARRY FORWARD OF LOSSES

Income tax is levied on the total income of previous year of an assessee. Hence it is necessary to ascertain the total income by aggregating the income of different heads. An assessee may have both positive income and negative income (loss). The department of income tax have given relief to assesseees that if there is loss from one head of income it can be set off from other heads of income. But if a loss cannot be set off in the same assessment year it can be forward and set off in future against income of that year. Therefore the topic is divided into two headings namely: i) set-off of losses; and ii) carry forward and set off losses. So when the income of the different sources is put together the loss one source is to be adjusted against the income of other two sources. It is therefore, follows that where the net results in respect of any source is a negative figure, it can be set off against a positive figure in respect of another source of income under the same head of income. Similarly, when the income of all heads is aggregated, the loss under one head is set off against the income of another head and if at all the total result in loss, the same in carried forward over future years for setting out.

Sections 70 -79 of income tax act deals with the provisions regarding set off and carry forward and set off losses. All these provisions are divided under following two headings.

- a) Set off of losses
- b) Carry forward and set off of losses.

2.3.1 A. Set-off of Losses

A loss can be set-off primarily within the same head and if it still remains unadjusted it can be set off from other heads of income. It has been divided into following two types:

1. Set-off of loss from one source against income from another source within the same head of income. [Section 70].

The general rule is that loss from one source can be set-off from another source falling under the same head of income. The income under one head is computed by adding together the incomes from different sources which falls under the same head. Section 70 of the income tax reveals that the loss of one source is adjusted against the income of another source falling under the same head of income. Suppose the assessee is running two three different businesses and the income of the head is calculated by combining different sources. So it is automatic that if there is loss under one source, the same is adjusted or set off against the available income under other sources in the same head of income For example, an assessee is running two businesses A and B. There is a profit of Rs 200,000 in business A whereas there is a loss of Rs. 100,000 in business B. The assessee can setoff loss from business B with the income of business A and his total income will be Rs 100,000. However there are six exceptions to the rule that a loss can be set-off against any other income under the same head.

- Loss from speculation business cannot be set off against income from other sources.[Section 73 (1)] This loss can be set off only against income from another speculation business. It cannot be set off against any non- speculation business income . However, non-speculation business loss can also be set off against speculation business income. Loss in trading in derivates is to be treated as non- speculation business loss and not as speculation loss.

The business of purchase and sale of shares not be treated as speculation business[explanation to section 73] [w.e.f A.Y 2015-16]

The business of purchase and sale of shares carried on by a company shall not be deemed as a speculation business, if the principal business of such company is the business of trading in shares.

- Loss of specified business under section 35AD cannot be set off against income from other business. This loss can be set off only against income from other specified business. For example, business of cold chain facility, warehousing business for storage of agricultural produce,etc. it cannot be set off against income from any other business. [section 73 A (1)]

- Long term capital loss cannot be set off against short term capital gain. This loss can be set off only against long term capital gain. This loss cannot be set off from short term capital gain. However, short term capital loss shall be allowed to be adjusted out of long term as well as short term capital gain.

- Loss from the activity of owning and maintaining race horses shall be set off against income from owning and maintaining race horses only and not against any other income under the head other sources. This means that loss from the activity of owning and maintaining race horses cannot be set off against any other income falling under the head other sources.

- Loss in respect of casual income falling under section 56(2)(ib), viz, lottery, gambling, betting, winning from races (including horse races) cannot be set-off against any income falling under head other sources. In fact, such a loss can't be set off at all.

- Loss from an exempted source can't be set-off from a source of income which is taxable. For example, agriculture income can't be set-off from non-agriculture income.

- No set off of loss against deemed incomes referred to in sections 68,69 , 69 A , 69B, 69C or 69D [Amendments to Section 115 BBE (2)] [w.e.f A.Y 2017-18]

Set off of any loss shall also be not allowable in respect of income under the aforesaid sections.

2. Set-off of loss of one head against the income of another head in the same assessment year, i.e., inter-head set-off [Section 71]:

The general rule is that loss under one head of income can be adjusted against income under another head. However, there are certain exceptions to this rule as:

- Where the net result of the computation under any head of income (other than 'Capital Gains') is a loss, the assessee can set-off such loss against his income assessable for that assessment year under any other head, including 'Capital Gains'. If any capital loss or part of a loss remains unadjusted then such loss shall be allowed to be carry forward to be set off out of income under the head capital gains only in future years.

Long term capital gains on sale of long term asset of shares on which STT has been paid exempt from tax u/s 10 (38) , hence long term capital loss on sale of such shares cannot be set off out of any other long term capital gain and so such loss is to be ignored.

- Where the net result of the computation under the head “Profits and gains of business or profession” is a loss, such loss cannot be set off against income under the head “Salaries”. The assessee shall not be entitled to have such loss set off against such income. It simply means that loss under the head profits and gains of business or profession cannot be set off from income under the head salaries.[Section 71 (2A)]
 - Where the net result of computation under the head ‘Capital Gains’ is a loss, such capital loss cannot be set-off against income under any other head.
 - Speculation loss and loss from the activity of owning and maintaining race horses cannot be set off against income under any other head.
- loss from a source whose income is exempted: If a person has loss from a source of income which is exempted under any provision of this act, such loss cannot be set off out of taxable income if any other head.
- share of loss from Firm/AOP: Share of loss from a firm assessed u/s 184 or 185 from an association of person cannot be set off from the individual income of partners/ members.
- No Set off of loss against deemed incomes referred to in sections 68, 69, 69 A, 69B , 69 C or 69 D [Amendment to Section 115BBE (2)] [w.e.f.A.Y 2017-18] : Set off of any loss shall also be not allowable in respect of incomes under the aforesaid sections.

2.3.2 B. Carry forward and set off of losses

If it is not possible to set off the losses during the same assessment year in which they occurred, so much of the loss as the assessee has not been able to set off out of the following losses can be carried forward for being set off against his income in the succeeding years provided the losses have been determined in pursuance of a return filed by the assessee within the time allowed and it is the same assessee who sustained the loss.

- **Loss under the head income form house property[Section 71 B]:** Any loss under this head can be carried forward up to 8 assessment years immediately following the assessment year for which the loss was first computed and set off from the same head. Up to assessment year 1998-99, loss under the head house property was not allowed to be carried forward to future assessment years and hence section 71 B is not applicable on house property loss prior to assessment year 1999-2000. Thus, loss under the head house property can be carried forward even if the return if such loss is not filed on or before due

date. However, for carry forward of other losses, return of loss is required to be filed on or before due date.

- **Loss of non-speculation business or profession[Section 72 (1):** Any non-speculation business loss can be carried forward up to 8 assessment years immediately following the assessment year for which the loss was first computed and set off against any income falling under the business or profession.

- **Loss of speculation business[Section 73]:** Any speculation business loss can be carried forward up to 4 assessment years immediately following the assessment year for which the loss was first computed and set off against the profit of any speculation business carried on by assessee.

- **Loss of specified business referred to in section 35 AD [Section 73A]:** No limit is prescribed by the Act which means it can be carried forward till it is set off. But loss can be set-off against profits and gains of any specified business carried on by assessee assessable for that assessment year.

- **Short term capital loss or long term capital loss[Section 74]:** Any loss under this can be carried forward up to 8 assessment years immediately following the assessment year for which the loss was first computed. Mode of set-off: A brought forward long term capital loss can be set-off against long term capital gain while as brought forward short term capital loss can be set off against any capital gain.

- **Loss from activity of owning and maintaining race horses[Section 74 A]:** such loss can be carried forward up to 4 assessment years and can be set off against income from owning and maintaining of horses.

Rules regarding unabsorbed depreciation:

With effect from AY 2003-04, unadjusted depreciation can be carried forward till it is fully adjusted from any income during the succeeding previous years. It shall be treated as depreciation of succeeding previous years. In case there is carry forward business loss as well as carry forward unabsorbed depreciation, then the following order should be followed for set off

- Firstly current depreciation secondly brought forward business loss and thirdly brought forward unabsorbed depreciation.

2.4 AGGREGATION OF INCOME

Clubbing of income means Income of other person included in assessee's total income, for example: Income of husband which is shown to be the income of his wife is clubbed in the income of Husband and is taxable in the hands of the husband. Under the Income Tax Act a person has to pay taxes on his income. A person cannot transfer his income or an asset which is his one of source of his income to some other person or in other words we can say that a person cannot divert his income to any other person and says that it is not his income. If he do so the income shown to be earned by any other person is included in the assessee's total income and the assessee has to pay tax on it. Inclusion of other's Incomes in the income of the assessee is called Clubbing of Income and the income which is so included is called Deemed Income. It is as per the provisions contained in Sections 60 to 64 of the Income Tax Act. For example: A purchased a house property in the name of his wife B. A let out this house property. The rental income earned by A in name of his wife B is taxable in the hands of A.

While aggregating the income of an assessee, following are also included in the total income:

- (i) Income of other persons to be included in the income of individual (Section 60-65).
- (ii) Income received from firm assessed as firm and Association of Persons (Section 66 & 67).
- (iii) Deemed Incomes (Section 68-69).

2.4.1 Incomes of other persons to be included in the income of individual (Section 60-65).

Section 60-65 deal with such cases where a particular income is earned or received by another person and does not belong to the assessee but for Income-Tax purposes, such incomes are included in the total income of the assessee.

1. Transfer of income without transfer of Asset [Section 60]: If any person transfers income without transferring the ownership of the asset, such income will be taxable in the hands of the transferor. Example, Mr. Rahul owns a property from which he earns a rental income amounting to Rs 100,000. Now, suppose he transfers such rental income to his wife either by directing the tenant to pay the rent directly to her or by otherwise. In this

case, although rent will be received by his wife yet it shall be included in the income of rahul i.e., transferor of income.

2. Revocable transfer of Asset[Section 61]: If any person transfers any asset to any other person in such form and condition that such transfer is revocable at any time during the lifetime of the transferee , the income earned through such asset is chargeable to tax as the income of the transferor. Section 63 has defined the words “transfer” and “revocable transfer” as under:

(a) a transfer shall be deemed to be revocable if:

(i) It contains any provision for the re-transfer directly or indirectly of the whole or any part of the income or assets of the transferor, or

(ii) It, in any way, gives the transferor a right to reassume power directly or indirectly over the whole or any part of the income or assets.

(b) “Transfer” Includes any settlement, trust, covenant, agreement or arrangement.

(c) Specified revocable transfers excluded from clubbing provisions [section 62 (1)] . The provisions of section 61 shall not be applicable in the case of following revocable transfers

(i) If the transfer is by way of trust which is not revocable during the life time of the beneficiary or

(ii) If transfer is otherwise than by way of trust and is not revocable during the life time of the transferee or

(iii) If transfer is made before the 1st day of April, 1961 , which is not revocable for a period exceeding 6 years

For ex. X transfers a house property to A. However, X has right to revoke the transfer during the life time of A . It is a revocable transfer and income arising from the house property is taxable in the hands of X.

3. Remuneration to Spouse[Section 64(1)(ii)]: An individual is chargeable to tax in respect of any remuneration received by the spouse from a concern in which the individual

has *substantial interest. This provision has an exception. The income to the spouse may be by way of salary, bonus, commission, fee or any other remuneration.

However, if above income derived by the employed spouse from such concern is due to his/ her knowledge, technical qualification or professional qualification or work experience, etc, it shall not be clubbed with the income of the spouse holding substantial interest. In other words, the income shall be taxable in the hands of the employed spouse.

Substantial interest means

In case of company – A person having atleast 20% of the equity shares carrying voting rights.

In case of cases- A person entitled to atleast 20% of the voting power of the concern.

4. Income from assets transferred to spouse[Section 64(1)(iv)]: Where an asset is transferred by an individual to his spouse directly or indirectly, otherwise than for adequate consideration or in connection with an agreement to live apart, any income from such asset is deemed to be the income of the transferor. For ex. Mrs. A transfer's 100 debentures of IFCI to her husband without adequate consideration. Interest income on these debentures will be included in the income of Mrs. A.

5. Income from asset transferred to son's wife[Section 64(1)(vi)]: If an individual, directly or indirectly transfers asset, without adequate consideration to son's wife, income arising from such asset is included in the income of the transferor after 1-6-1973. For ex. Mrs. A transfer's 100 debentures of IFCI to her son's wife without adequate consideration. Interest income on these debentures will be included in the income of Mrs. A.

6. Income from asset transfer to a person for the benefit of spouse/ son's wife [Section 64(1)(vii)]: If an individual, directly or indirectly transfers asset, without adequate consideration to a person or an association of persons for the benefit of his/her spouse / son's wife, income arising from such asset directly or indirectly is included in the income of the transferor.

It simply means that when assets are transferred without adequate consideration to some person or association of person, the ultimate benefit of which shall be of the spouse of the

transferor, the income from such assets is considered to be the transferor's income and so added in his total income.

Where, from the assets transferred, only a portion of the income is meant for the immediate or deferred benefit of the spouse of the transferor, then only such income is to be added in the total income of the transferor

For Ex. X transfers Government bonds without consideration to an association of persons, subject to the condition that the interest income from these bonds will be utilized for the benefit of Mrs. X or Mrs. X son's wife. Interest from bonds will be included in the income of X

7. Income of a minor child [Section 64(iA)]: All income which arises to the minor shall be clubbed in the income of his parents. Income will be included in the income of that parent whose total income is greater. This case has two exceptions.

(1) Income of minor child suffering from specified disability.

(2) Income of minor child on account of manual work or involving application of his skill/ talent etc.

*Substantial Interest: An individual is deemed to have substantial interest if he beneficially holds equity shares carrying not less than 20% voting powering case of a company or is entitled to not less than 20% of the profits in case of a concern other than a company, at any time during the previous year.

Some special points to remember:

1. If an individual makes a gift in cash or by cheque to his spouse and that money is utilized by the spouse for purchase of an asset. The income earned by the spouse from that asset will not be clubbed in the income of the individual.

2. In order to invoke clubbing provisions there must be relation of husband and wife. That means if a person transfers asset to his would be spouse before marriage income arising from such asset will not be included in the income of transferor.

3. Negative income is also income. Under the Income Tax Act income does not means positive income only. The term income includes negative income or loss also.

4. Income from accretion to asset is not taxable in the hands of the transferor.
5. Income from saving out of pin money is not included in the income of husband.
6. Income of minor child is clubbed with the income of the parent whose income after excluding the share of minor's income is greater.
7. If trust is created for the benefit of minor child and income during minority of child is being accumulated and added to corpus of trust and income from increased corpus is given to the child after attaining majority, clubbing provisions are not applicable.

2.4.2 Income received from AOP[Section 67A]

In the aggregation process of total income of the assessee following income is included in the total income of the assessee but this income is tax free(Section 67A). It is:

If the assessee is a member of an association of persons or body of individuals other than Hindu Undivided Family, any portion of the amount which he is entitled to rebate on the income received from the association or body on which income-tax has already been paid by the association or body.

2.4.3 Deemed Incomes[Section 68-69]

In certain cases, some amounts are deemed as income in the hands of the assessee though they are actually not in the nature of income. These cases are contained in sections 68, 69, 69A, 69B, 69C and 69D. The Assessing Officer may require the assessee to furnish explanation in such cases. If the assessee does not offer any explanation or the explanation offered by the assessee is not satisfactory, the amounts referred to in these sections would be deemed to be the income of the assessee. Such amounts have to be aggregated with the assessee's income.

Cash credits (sec 68)

Where any sum is found credited in the books of an assessee maintained for any previous year, and the assessee offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the sum so credited may be charged to income-tax as the income of the assessee of that previous year.

If the assessee fails to submit any satisfactory explanation or the A.O is not satisfied with the explanation, the income is treated income from undisclosed sources

Unexplained investments (sec 69)

Where in the financial year immediately preceding the assessment year the assessee has made investments which are not recorded in the books of account, if any, maintained by him for any source of income, and the assessee offers no explanation about the nature and source of the investments or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the value of the investments may be deemed to be the income of the assessee of such financial year.

Unexplained money, etc (Sec 69A)

Where in any financial year the assessee is found to be the owner of any money, bullion, jewellery or other valuable article and such money, bullion, jewellery or valuable article is not recorded in the books of account, if any, maintained by him for any source of income, and the assessee offers no explanation about the nature and source of acquisition of the money, bullion, jewellery or other valuable article, or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the money and the value of the bullion, jewellery or other valuable article may be deemed to be the income of the assessee for such financial year.

Amount of investments, etc., not fully disclosed in books of account(69B.)

Where in any financial year the assessee has made investments or is found to be the owner of any bullion, jewellery or other valuable article, and the Assessing Officer finds that the amount expended on making such investments or in acquiring such bullion, jewellery or other valuable article exceeds the amount recorded in this behalf in the books of account maintained by the assessee for any source of income, and the assessee offers no explanation about such excess amount or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the excess amount may be deemed to be the income of the assessee for such financial

Unexplained expenditure, etc (69C).

Where in any financial year an assessee has incurred any expenditure and he offers no explanation about the source of such expenditure or part thereof, or the explanation, if any, offered by him is not, in the opinion of the Assessing Officer, satisfactory, the amount covered by such expenditure or part thereof, as the case may be, may be deemed to be the income of the assessee for such financial year:

Provided that, notwithstanding anything contained in any other provision of this Act, such unexplained expenditure which is deemed to be the income of the assessee shall not be allowed as a deduction under any head of income.

Amount borrowed or repaid on hundi (69D)

Where any amount is borrowed on a hundi from, or any amount due thereon is repaid to, any person otherwise than through an account payee cheque drawn on a bank, the amount so borrowed or repaid shall be deemed to be the income of the person borrowing or repaying the amount aforesaid for the previous year in which the amount was borrowed or repaid, as the case may be:

Provided that, if in any case any amount borrowed on a hundi has been deemed under the provisions of this section to be the income of any person, such person shall not be liable to be assessed again in respect of such amount under the provisions of this section on repayment of such amount. For the purposes of this section, the amount repaid shall include the amount of interest paid on the amount borrowed.

2.5 DEDUCTIONS TO BE MADE FROM GROSS TOTAL INCOME

The deduction from gross total income is available only where the gross total income is positive. If however income is negative, the question of any deduction does not arise. Section 80A to 80 U of the Income-tax Act lays down the provisions relating to the deductions available to assesseees from their gross total income.

Deductions are available in two categories:

- a. Deduction in respect of certain payments (section 80C to 80GGC).
- b. Deduction in respect of certain incomes (section 80IA to 80U).

2.5.1 A. Deduction in respect of certain payments

A1. Deduction regarding approved savings in P.F., LIC Premium etc (80C)

Eligible assesses: Individual and HUF

Entitlement: Deduction from the Gross Total Income of an amount equal to the investments made, subject to a maximum amount of Rs. 150,000.

Nature of Investments:

- a. Life Insurance policy taken on the life of an individual assessee or spouse and any child of such individual, and any member of the Hindu Undivided Family.
- b. Amounts paid to effect or to keep in force a contract for a non-cumulative deferred annuity not being an annuity plan.
- c. Deduction from the salary payable by or on behalf of the Government to any individual, in accordance with the conditions of his service, for securing to him a deferred annuity or making provision for his wife or children, to the extent of one-fifth of salary.
- d. Any contribution made by an individual only to any provident fund to which the Provident Funds Act, 1925, applies; a Recognised provident fund; an approved superannuation fund.
- e. Subscription to the notified securities of the Central Government.
- f. Any contribution to a PPF by individual or HUF.
- g. Subscription to other notified savings certificates defined in Section 2(c) of the Government Savings Certificates Act, 1959.
- h. Contributions made by an individual or HUF, for participation in the Unit-Linked Insurance Plan, 1971.
- i. Any contribution to effect or keep in force any notified annuity plan of the LIC or any other insurer.
- j. Any subscription, to any units of any Mutual Fund or the Unit Trust of India under any notified plan formulated by the Central Government.

k. Subscription to the notified deposit scheme of or contribution to any such pension fund set up by the National Housing Bank established under Section 3 of the National Housing Bank Act, 1987.

l. Tuition fees (excluding any payment towards any development fees or donation or payment of similar nature), whether at the time of admission or thereafter, to any university, college, school or other educational institution situated within India;

m. For purchase or construction of a residential house property, the income of which is chargeable to tax under the head “Income from House Property”, where such payments are made towards or by way of:

a. Any instalment or part payment of the amount due under any self- financing or other scheme of any development authority, housing board or other authority engaged in the construction and sale of house property on ownership basis; or

b. Any instalment or part payment of the amount due to any company or cooperative society of which the assessee is a shareholder or member towards the cost of the house property allotted to him; or

c. Re-payment of the amount borrowed by the assessee from:

(1) The Central Government or any State Government; or

(2) Any bank, including a co-operative bank, or

(3) The Life Insurance Corporation, or

(4) The National Housing Bank, or

(5) Any public company formed and registered repayment of principal part only not interest in India with the main object of carrying on the business of providing long-term finance for the construction or purchase of houses in India for residential purposes, eligible for deduction under Section 36(1)(viii), or

(6) Any company in which the public are substantially interested or any co-operative society, where such company or co-operative society is engaged in the business of financing the construction of houses; or

(7) The assessee's employer where such employer is a public company or a public sector company or a university established by law or a college affiliated to such university or a local authority or a cooperative society;

(8) The assessee's employer where such employer is an authority or a board or a corporation or any other body established under a Central or State Act (w.e.f. A. Y. 2006-07).

d. Stamp duty, registration fee and other expenses for the purpose of transfer of such house property to the assessee.

n. Subscription to equity shares or debentures or units forming part of any eligible issue of capital.

o. Fixed deposits for a minimum period of 5 years in any Scheduled Banks (w.e.f. A. Y. 2007-08).

p. As subscription to such bonds issued by the National Bank for Agriculture and Rural Development, as the Central Government may, by notification in the Official Gazette specify in this behalf.

q. In an account under the Senior Citizens Savings Scheme Rules, 2004.

r. As five year time deposit in an account under the Post Office Time Deposit Rules, 1981.

A-2. Deduction in respect of contribution to certain pension funds persons (80CCC)

Covered- individual.

Eligible Amount- Deposit or payment made to LIC or any other insurer in the approved annuity plan for receiving pension.

Extent of Deduction- Least of amount paid or Rs. 1,50,000/- .

A-3. Deduction in Respect of Contribution to Pension Scheme of Central Govt., or of any other Employer (80CCD).

Covered - Individual.

Eligible Amount: the amount of deduction shall be as follows

1. For employees (Govt., or Non-Govt.): Employees own contribution or 10% of salary whichever is less and contribution of central govt. / other employer or 10% of salary whichever is less.

2. For other employees (self-employed): depositors own contribution or 20% of gross total income [A.Y 2017-18], whichever is less [Section 80 CCD (1)].

The maximum amount of deduction u/s CCD is Rs 1,50,000 only.

A-4. deduction in respect of investment made under any notified saving scheme (80CCG)

Deduction is allowed if the following conditions are satisfied:

1. The assessee is a resident individual.
2. His gross total income does not exceed 12 Lakh.
3. He has acquired listed shares or listed units of an equity oriented funds in accordance with a notified scheme
4. The investment is locked in for a period of 3 years from the date of acquisition in accordance with the above scheme.
5. The assessee satisfies any other condition as may be prescribed.
6. Investments can be made for 3 consecutive previous year
7. Investments made in listed units of an equity oriented fund shall also be eligible.

If the above conditions are satisfied, a deduction will be allowed under section 80CCG. The amount of deduction is 50% of the amount invested in equity shares. However, the amount of deduction under this section cannot be more than ₹ 25,000. The deduction shall be allowed for 3 consecutive assessment years beginning with assessment years in which listed equity shares or units were first acquired. In case assessee fails to comply with any of the above mentioned conditions, the deduction originally allowed shall be deemed to be the owner of assessee of such previous year in which default is committed.

A-5. Deductions in Respect of Medical Insurance Premia, Preventive health check up and Contribution made to the central govt. health scheme (CGHS) (80D)

Deduction regarding health insurance is allowed to individuals and HUFs. Where the assessee is an individual, the sum referred to in sub-section (1) shall be the aggregate of the following:

(a) the whole of the amount paid to effect or to keep in force an insurance on the health of the assessee or his family or “any contribution made to the Central Government Health Scheme” or such other scheme as may be notified by the Central Government in this behalf or any payment made on account of preventive health check-up of the assessee or his family and the sum does not exceed in the aggregate Rs 25000 (Rs 50000 in case of senior citizens) OR actual premium deposited in any mode other than cash regarding medical insurance policy or policies of assessee, his / her spouse and all dependent children put together and preventive health check up amount upto Rs 5,000 only and contribution made to CGHS.

(b) the whole of the amount paid to effect or to keep in force an insurance on the health of the parent or parents of the assessee or any payment made on account of preventive health check-up of the assessee or his family as does not exceed in the aggregate Rs 25000 (Rs 50000 in case of senior citizens). The deduction in respect of payment made on account of preventive health check up shall not exceed Rs 5,000.

Where the assessee is a Hindu undivided family, the sum referred to in sub-section (1) shall be the whole of the amount paid to effect or to keep in force an insurance on the health of any member of that Hindu undivided family as does not exceed in the aggregate Rs 25000 (Rs 50000 in case of senior citizens).

(C) In case a senior citizen has not got health insurance coverage (sometimes insurance companies do not provide such coverage to senior citizens,) a deduction upto maximum of Rs 350,000 shall be allowed regarding any payment made on account of medical expenditure incurred in respect of a senior citizen. In case one parent has been medically insured and the other being senior citizen is not medically insured but has to incur medical expenses, the aggregate deduction regarding health insurance premium and medical expenditure incurred will be allowed but is shall be limited to Rs 50,000.

A-6. Deductions in respect of maintenance including medical treatment of a dependent who is a person with disability (80DD)

Persons Covered- Resident Individual/HUF.

Eligible Amount-

(a) Expenditure incurred on medical treatment [including nursing], training and rehabilitation of a disabled dependent, or

(b) Any payment or deposit made under a scheme framed by LIC or any other insurer or the administrator or the specified company and approved by the Board for payment of lump sum amount or annuity for the benefit of dependent with disability.

Extent of Deduction: (a) Rs. 75,000/- in case of normal disability or (b) Rs. 125,000/- in case of severe disability.

A-7. Deduction in respect of medical treatment, etc. (80DDB)

An individual (*less than 60 years of age*) can claim up to Rs 40,000 for the treatment of specified critical ailments. This can also be claimed on behalf of the dependents. Where the amount actually paid in respect is in respect of the assessee or his dependent or any member of a hindu undivided family of the assessee and who is a senior citizen, the deduction under this section shall be allowed for Rs 10,00,000

To claim Tax deductions under Section 80DDB, it is mandatory for an individual to obtain 'Doctor Certificate' or 'Prescription' from a specialist working in a Govt. or Private hospital.

For the purposes of section 80DDB, the following shall be the eligible diseases or ailments:

- Neurological Diseases where the disability level has been certified to be of 40% and above;

(a) Dementia

(b) Dystonia Musculorum Deformans

(c) Motor Neuron Disease

(d) Ataxia

(e) Chorea

(f) Hemiballismus

(g) Aphasia

(h) Parkinson's Disease

- Malignant Cancers
- Full Blown Acquired Immuno-Deficiency Syndrome (AIDS) ;
- Chronic Renal failure
- Hematological disorders
- Hemophilia
- Thalassaemia

A-8. Deduction in respect of interest on loan taken for education (80E).

Persons Covered- Individual.

Extent of Deduction- Entire amount of interest.

Eligible Amount- Any amount paid by way of interest on loan taken from any financial institution or any approved charitable institution for his/her higher education or w.e.f. 14-2008 for the purpose of higher education of his/her spouse, children and legal guardian of the Individual. Relevant Conditions/Points:

1. Amount should be paid out of income chargeable to tax.
2. All field of studies including vocational studies pursued after passing the senior secondary examination or its equivalent from any school, board or university recognized by the central govt. or state govt. or local authority or by any other authority authorised by the central govt. or state govt. or local authority to do so.

3. Approved charitable institution means an institution established for charitable purposes and notified by the Central Government u/s. 10(23C) or referred in 80G(2)(a).

4. Financial institution means banking company or financial institution notified by Central Government. 5. The deduction is allowed in the initial assessment year (i.e., the assessment year relevant to the previous year, in which the assessee starts paying the interest on loan) and 7 assessment years. Immediately succeeding the initial assessment year or until the interest is paid in full whichever is earlier.

A-9 Deduction In Respect of Donations to Certain Funds, Charitable Institutions, Etc. (80G)

Persons Covered-All assessees [except for 80G (2)(c), which is applicable for donations made only by company] to the Indian Olympic Association or to any other Association or Institution for the development of infrastructure for sports & games or the sponsorship of sports & games, in India.

Eligible Amount- Any sums paid in the previous year as Donations to certain funds, charitable institutions etc. specified u/s. 80G (2).

Relevant Conditions/Points

1. Donation in kind is not eligible for deduction.
2. Donations paid out of another year's income or out of income not includible in the assessment of current year are also eligible for deduction. Lt. F. No. 45/313/66 – ITJ (61) dt. 2-12-1966.

Extent of Deduction

Without any ceiling of 10% of adjusted Gross Total Income:—

(a) 100% of donation if donation given to

- (i) National Defence Fund set up by the Central Government;
- (ii) Prime Minister's National Relief Fund;

- (iii) Prime Minister's Armenia Earthquake Relief Fund;
- (iv) Africa (Public Contributions — India) Fund;
- (v) National Foundation for Communal Harmony;
- (vii) An approved university/educational institution of National eminence;
- (viii) The Maharashtra Chief Minister's Relief Fund
- (ix) Chief Minister's Earthquake Relief Fund, Maharashtra;
- (x) Any fund set up by the State Government of Gujarat exclusively for providing relief to the victims of earthquake in Gujarat;
- (xi) Any Zila Saksharta Samiti constituted in any district under the chairmanship of the Collector of that district;
- (xii) National Blood Transfusion Council or to any State Blood Transfusion Council;
- (xiii) Any fund set up by a State Government for the medical relief to the poor;
- (xiv) The Army Central Welfare Fund or the Indian Naval Benevolent Fund or the Air Force Central Welfare Fund,
- (xv) Andhra Pradesh Chief Minister's Cyclone Relief Fund, 1996;
- (xvi) National Illness Assistance Fund;
- (xvii) Chief Minister's Relief Fund or Lieutenant Governor's Relief Fund in respect of any State or Union Territory;
- (xviii) National Sports Fund;
- (xix) National Cultural Fund;
- (xx) Fund for Technology Development and Application;
- (xxi) National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disabilities;

(xxii) Any trust, institution or fund to which Section 80G(5C) applies for providing relief to the victims of earthquake in Gujarat (contribution made during January 26, 2001 and September 30, 2001) or

(b) 50% of donation if donation given to:

Jawaharlal Nehru Memorial Fund; Prime Minister's Drought Relief Fund; National Children's Fund (deduction shall be allowed 100% w.e.f. A.Y 2014- 15); Indira Gandhi Memorial Trust; Rajiv Gandhi Foundation.

With ceiling of 10% of adjusted Gross Total Income:—

Where the aggregate of sums exceed 10% of adjusted gross total income, then such excess amount is ignored for computing such aggregate.

(a) 100% of qualifying amount, if donation given to Government or any approved local authority, institution or association to be utilised for the purpose of promoting family planning; Donation by a Company to the Indian Olympic Association or to any other notified association or institution established in India for the development of infrastructure for sports and games in India or the sponsorship of sports and games in India.

(b) 50% of qualifying amount if donation given to any other fund or any institution which satisfies conditions mentioned in Section 80G(5); Government or any local authority to be utilised for any charitable purpose other than the purpose of promoting family planning, Any authority constituted in India for the purpose of dealing with and satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns, villages or both; Any corporation referred in Section 10(26BB) for promoting interest of minority community; For repairs or renovation of any notified temple, mosque, gurudwara, church or other place.

A-10. Deduction in respect of expenditure incurred on payment of house rent (80GG):

Persons Covered- Individual.

Deductions admissible under this Section is:

i. Statutory limit Rs 5000;

ii. Actual rent paid less 10% of 'Adjusted Total Income'.

iii. 25% of such 'Adjusted Total Income'. Whichever is less. Adjusted GTI = GTI - (LTCG + STCG on shares covered under STT + income referred to in section 115A + all other deductions u/s 80 except 80GG).

A-11. Deduction in respect of contribution given by companies to political parties or electoral trust (80GGB)

Any sum contributed by an Indian Company, other than cash, in the previous year to any political party or to an electoral trust shall be allowed as deduction while computing its total income.

A-12. Deduction in respect of contribution given by any person to political parties or electoral trust (80GGC)

Any sum contributed by an assessee, other than cash, in the previous year to any political party or to an electoral trust except local authority and every artificial juridical person wholly or partly funded by the government shall be allowed as deduction while computing its total income.

No deduction shall be allowed in case donation is given in cash

The term political party means a political party registered under section 29A of the representation of the people act, 1951.

2.5.2 B. Deduction in respect of certain incomes

B-1. Deduction in respect of profits and gains from industrial undertakings or enterprise engaged in infrastructure development (section 80-IA).

Where gross total income of assessee includes any profits and gains derived by an undertaking or an enterprise from any eligible business, a deduction shall be allowed to stated percentage of profit and gains from such business for stated number of years.

1. Undertaking engaged in providing infrastructure facility (80IA(40(i)))

Eligible business: developing, operating and maintaining or developing operating and maintaining infrastructure facility.

Form of organisation: industrial undertaking owned by a company registered in India or by a consortium of such companies.

Rate of deduction: @100% of profits of such eligible business.

Commencement of operation: on or after 1-4-1995

Period of deduction: 10 years out of 20 years (out of 15 years in case of ports airport etc)beginning with the year in which undertakings develops such infrastructural facility.

2. Telecommunication services (80IA(4)(ii))

Eligible business: telecommunication services, radio paging, domestic satellite services, network of trunking, broadband network and internet services.

Form of organisation: all enterprises whether corporate or not.

Commencement of operation: on or after 1-4-1995 but on or before 31-3-2005.

Rate of deduction: 100% of profits and gains from such business for first 5 consecutive AY's out of first 15 years.

30 % of profits and gains for next 5 consecutive assessment years out of first 15 years starting from the date of commencement of operations.

3. Industrial Park (80IA(4)(iii))

Eligible business : developing, developing and operating or maintaining and operationg an industrial park or special economic zone notified by central govt. with scheme framed and notifies

Form of organization : The deduction is available to all industrial undertakings enterprises whether in corporate sector or in non- corporate sector i.e., sole proprietor firms, etc.

Specific conditions of commencement of operations

For industrial park During 1-4-2006 to 31-3-2011

For special economic zone During 1-4-1997 to 31-3-2005

4. Power Sector (80IA(4)(iv))

Eligible business: generation of power; or generation and distribution of power; or transmission or distribution by laying a network of new transmission; or undertakingsubstantial renovation and modernisation of the existing transmission or distribution lines.

Form of organisation: all enterprises whether corporate or not. Commencement of operation: after 1-4-1993 to 31-3-2017.

Rate of deduction: 100% of profits and gains from such business for any 10 consecutive AY's out of first 15 years beginning from the year in which undertaking starts operation.

5. Undertaking setup for reconstruction or revival of power generating plant (80IA(4)(v)) Eligible business: reconstruction or revival of power generating plant.

Form of organisation: Indian Co.

Commencement of operation: before 31-3-2017. Rate of deduction: 100% of profits and gains from such business for any 10 consecutive AY's out of first 15 years beginning from the year in which undertaking starts operation.

B-2. Deduction in respect of profits and gains from certain industrial undertakings other than infra-structure development undertakings (section 80-IB).

The deduction under section 80-IB is available to an assessee whose gross total income includes profits and gains derived from the following business. **for details refer to bare Act.

B-3. Special provision in respect of certain undertakings or enterprises in certain special category states (section 80-IC). **for details refer to bare Act.

B-4. Deduction in respect of employment of new workmen (80JJAA).

Eligible assessee: Indian co.

GTI should include should include profits and gains derived from manufacture of goods in factory.

Amount of deduction: 30% of additional wages paid to new regular workmen employed by the assessee in the previous year for three assessment years including the assessment year relevant to the previous year in which such employment is provided.

Additional wages means the wages paid to new regular workman in excess of 100 workmen employed during the previous year.

However in case of an existing factory additional wages shall be nil if the increase in the number of regular workmen employed during the year is less than 10% of the existing number of workmen employed in such factory as on the last day of the preceding year.

B-5. Deduction in respect of royalty income etc., of authors of certain books other than text books (80QQB).

Amount of deduction: the gross total income of assessee pertaining to the previous year includes royalty or the copyright fees, there shall, in accordance with and subject to the provisions of this section, be allowed a deduction of 100% of such income or Rs. 300,000, whichever is less.

B-6. Deduction in respect of royalty on patents (80RRB):

(1) Where in the case of an assessee, being an individual, who is –

(a) Resident in India;

(b) A patentee;

(c) In receipt of any income by way of royalty in respect of a patent registered on or after the 1st day of April, 2003 under the Patents Act, 1970, and his gross total

income of the previous year includes royalty, there shall, in accordance with and subject to the provisions of this section, be allowed a deduction of 100% of such income or Rs 300,000, whichever is less.

B-7. Deduction in respect of interest on deposits in savings account (80TTA):

Eligible assessee: individual or HUF.

Eligible income: interest on deposits in saving accounts with:

a) A banking company to which the Banking Regulation Act, 1949 (10 of 1949), applies (including

any bank or banking institution referred to in section 51 of that Act);

(b) A co-operative society engaged in carrying on the business of banking (including a cooperative

land mortgage bank or a co-operative land development bank); or

(c) A Post Office as defined in clause (k) of section 2 of the Indian Post Office Act, 1898.

Amount of deduction: actual interest or Rs 10,000 whichever is less.

B-8. Deduction in case of a person with disability (80U):

Amount of deduction: In computing the total income of an individual, being a resident, who, at

any time during the previous year, is certified by the medical authority to be a person with

disability, there shall be allowed a deduction of a sum of Rs 75,000; or a person with severe

disability shall be allowed a deduction of a sum of Rs 1,25,000.

Deductions for senior citizens in respect of interest on deposits with bank and post office [Section 80 TTB] [w.e.f AY 2019-20]

A deduction of upto Rs 50,000 shall be allowed to a senior citizen in respect of interest income from deposits with banks or post office or co- operative banks. It is important to note that interest earned on every type of deposit shall be eligible for deduction under this section.

2.6 SUMMARY

Income tax is levied on the total income of previous year of an assessee. Hence it is necessary to ascertain the total income by aggregating the income of different heads. An assessee may have both positive income and negative income (loss). The department of income tax have given relief to assesseees that if there is loss from one head of income it can be set off from other heads of income. But if a loss cannot be set off in the same assessment year it can be forward and set off in future against income of that year.

Set-Off of Losses from one source against Income from another source under the same Head of Income [Section 70]: If the net result for any assessment year in respect of any source falling under any head of income is a loss, the assessee is entitled to set off the amount of such loss against his income from any other source under the same head. However, Loss from Speculation Business, Loss from the activity of owning and maintaining race horses, long-term capital loss can be set-off from any other source of income.

Where any individual transfers directly or indirectly any asset (other than a house property) to the spouse, the income from such asset shall be included in the income of the transferor

Carry-Forward and Set-Off of Losses If it is not possible to set-off the losses during the same assessment year in which these occurred, so much of the loss as has not been so set-off out of the following losses, can be carried forward to the following assessment year and so on to be set-off against the income of those years provided the losses have been determined in pursuance of a return filed by the assessee and it is the same assessee who sustained the loss.

However, losses suffered under the following heads are not allowed to be carried forward and set off:

(1) Losses under the head 'salaries'.

(2) Losses under the head 'Income from other sources' (excepting loss suffered from the activity of owning and maintaining race horses).

– W.e.f. assessment year 2000-2001, Section 72A has been substituted by new section to provide for carry forward and set off of accumulated loss and unabsorbed depreciation allowance in case of:

- (i) Amalgamation [Section 72A(1), (2) and (3)], or
- (ii) Demerger [Section 72A(4) and (5)], or
- (iii) Reorganisation of business [Section 72A(6)].

Submission of Return for Loss (Section 80): An assessee is not entitled to carry-forward a loss unless he has filed a return of loss to the Department in time and in the prescribed form. It is obligatory on the part of the assessee to file such return; otherwise he will be deprived of the benefit of carryforward of losses. In fact, only that amount of loss is allowed to be carried-forward which has been computed by the Assessing Officer and not by the assessee.

Similarly aggregation of Income was discussed. The aggregate of income computed under each head, after giving effect to the provisions for clubbing of income and set off of losses, is known as "Gross Total Income". Clubbing of income means Income of other person included in assessee's total income, for example: Income of husband which is shown to be the income of his wife is clubbed in the income of Husband and is taxable in the hands of the husband. Under the Income Tax Act a person has to pay taxes on his income. A person cannot transfer his income or an asset which is his one of source of his income to some other person or in other words we can say that a person cannot divert his income to any other person and says that it is not his income. If he do so the income shown to be earned by any other person is included in the assessee's total income and the assessee has to pay tax on it. Inclusion of other's Incomes in the income of the assessee is called Clubbing of Income and the income which is so included is called Deemed Income. It is as per the provisions contained in Sections 60 to 64 of the Income Tax Act. For example: A purchased a house property in the name of his wife B. A let out this house property. The rental income earned by A in name of his wife B is taxable in the hands of A.

Sections 80A to 80U of the Income-tax Act lay down the provisions relating to the deductions allowable to assesseees from their gross total income. In order to further the Government Policy of attracting investment and activity in the desired direction and to provide stimulus to growth or to meet social objectives, concession in the form of 'deduction' from Taxable Income is allowed. Chapter VI-A of the Income-tax Act, 1961 contains such deduction provisions. With the advent of new philosophy of giving direct assistance to the desired goal and avoiding indirect route of tax concessions, the numbers of deductions are being omitted. This is also with a view to avoid complexity of tax law. In computing Total Income of an assessee deductions under sections 80CCC to 80U are permissible from "Gross Total Income". [Section 80A(1)]

Deduction not to be allowed unless return furnished [Sec. 80AC]

Where in computing the Total Income of an assessee of the Previous Year relevant to the Assessment Year commencing on the 1st day of April, 2006 or any subsequent Assessment Year, any deduction is admissible under Section 80-IA or Section 80-IAB or Section 80-IB or Section 80-IC or Section 80-ID or Section 80-IE, no such deduction shall be allowed to him unless he furnishes a return of his income for such Assessment Year on or before the due date specified under sub-section (1) of section 139.

"Gross Total Income" means the aggregate of income computed under each head as per provisions of the

Act, after giving effect to the provisions for clubbing of incomes (Sections 60 to 64) and set off of losses

and but before making any deductions under this chapter. [Section 80B(5)].

The deductions under Chapter VIA are not available from the following incomes though these are included in the "Gross Total Income":

- (i) Long Term Capital Gains;
- (ii) Winnings from lotteries, cross word puzzles etc.
- (iii) Incomes referred to in Sections 115A to AD, 115BBA and 115D.

The aggregate amount of deductions under Chapter VIA [Sections 80CCC to 80U] shall not exceed the

“Gross Total Income” of the assessee. [Section 80A (2)]

PRACTICAL PROBLEMS

ILLUSTRATION I

The following are the particulars of income and loss of an individual under different heads of income . Set off losses in the assessment year 2019-20 and find out the net result

Income from house property A Rs 5,000
 Income from house property B Rs (8,000)
 Income from interest on securities Rs 20,000
 Income from a cycle business Rs (20,000)
 Profit from speculation business Rs 20,000
 Loss from short term capital asset Rs 6,000
 Long term capital loss Rs 25,000
 Long term capital gain investment Rs 21,000

Solution 1:

House property income:		
Income from house property A	5,000	
Income from house property B		
Can be set off	<u>(8,000)</u>	
Business income :		
Profit from speculation business	20,000	NIL
Profit from cycle business	<u>(20,000)</u>	
Capital gains		
Long term capital gains	21,000	
Income from another long term capital asset	<u>(25,000)</u>	
Long term capital loss to be C/F	(4,000)	
Short term capital Loss to be C/F	6,000	
Income from other sources:		
Interest on securities		<u>20,000</u>
Gross total income		<u>17,000</u>

Illustration 2 :

Compute taxable income and loss to be C/F

Business profit for the previous year 2018-19 Rs 20,000

B/F business loss of 2016-17 Rs 10,000

Capital loss on shares Rs 60,000

Loss from self occupies house u/s 24 Rs 5,000

Solution 2:

Adjustment of losses during assessment year 2019-20

House property	
Self occupied house - Loss	(5,000)
Profit and Gains: Business Profit	<u>20,000</u>
Available income	15,000
B/F Business loss of 2016-17	<u>10,000</u>
Total Income	5,000
Capital gain: Capital loss to be C/F	60,000

Long term capital loss of shares (STT Paid) not allowed to be C/F and so it is ignored.

Illustration 3 : The following are the particulars of income/loss of Mr. A. You are required to set off losses and carry forward and set off where necessary

	Assessment Year 2018-19	Assessment Year 2019-20
Income from salary – computed	15,000	15,000
Income from interest on securities (Gross)	5,000	5,000
Loss from business	53,000	15,000
STCG	8,000	-
LTCG (Land)	21,000	-

Solution 3:

Assessment Year 2018-19

	In Rs.	In Rs.
Salary income – Computed		15,000
Business loss		(53,000)
Capital gain		
Short term	8,000	
Long term	<u>21,000</u>	29,000
Other sources: Interest on securities		<u>5,000</u>
Gross total income (Salary income)		<u>15,000</u>

Note: Business loss of Rs 53,000 shall be adjusted against income of all other heads except income under the head ‘salaries’ and business loss to be C/F

Assessment Year 2019-20

	In Rs.
Salary income – Computed	15,000
Business loss	-15,000
Other sources: Interest on securities	<u>5,000</u>
Gross Total Income	<u>15,000</u>

Note: Business loss B/F from Assessment year 2018-19 cannot be set off as assessee has no income under the head profits and gains of business or Profession . Hence, he can C/F loss of assessment year 2018-19 . i.e., Rs 19,000. Business loss of assessment year 2019-20 i.e., Rs 10,000 will also be carried forward as it cannot be set off from salary income

Illustration 4:

From the following particulars of income of assesses A,B and C . How the capital losses shall be set off and carried forward for the previous year ending on 31-3-2019.

Assessee - A

- (i) Business income Rs 15,000
- (ii) Short term capital loss Rs 1,200
- (iii) Long term capital gain – Plot Rs 7,200

Assessee - B

- (iv) Long term capital gain on sale of jewellery Rs 20,000
- (v) Business income Rs 30,000
- (vi) Short term capital loss Rs 40,000
- (vii) Business income Rs 60,000

Assessee C

- (viii) Short term capital gain Rs 20,000
- (ix) Long term capital gain – land Rs 17,000
- (x) Carry forward loss- short term capital assets Rs 50,000

Solution 4

Assessee- A			15,000
Business income			
Long term capital gain – Plot	7,200		
Long term capital gain on sale of jewellery	<u>20,000</u>	27,200	
Set off short term capital loss		<u>(1,200)</u>	
Net capital gain			<u>26,000</u>
Gross total income			<u>41,000</u>
Assessee B			
Business income			
Short term capital loss to be C/F	Rs. 40,000		30,000
Gross total income			=
Assessee C			<u>30,000</u>
Business income		17,000	
Long term capital gain – Land		<u>20,000</u>	60,000
Short term capital gain		37,000	
Set off short term capital loss B/F		<u>50,000</u>	
S.T capital loss still to be C/F		<u>13,000</u>	<u>NIL</u>
Gross total income			<u>60,000</u>

Illustration 5 : Mr. Singh a resident of India, submits the following particulars of his income for the assessment year 2019-2020.

	Rupees
I. Income from house let out (computed)	9,500
II. Profit from radio business	19,600
III. Profit from electric business	1,800
IV. Speculation income	19,00
V. Short-term capital gain	32,00
VI. Long –term capital gain (jewellery)	9,250
Current year’s depreciation amounted to	2,500
The following items have been brought forward from preceding assessment year:	
I. Loss from cycle businesses discontinued (2017-18)	3,900
II. Loss from electric business	2,700
III. Loss from radio business	1,900
IV. Unabsorbed depreciation of electric business	1,000
V. Unabsorbed family planning expenditure	2,600
VI. Speculation loss	3,200
VII. STCL from the year 2015-16	4,100
VIII. LTCL from the year 2016-17	6,450

You are required to compute his gross total income and deal with the carry forward of losses.

SOLUTION 5

Computation of total Income of Mr. Singh

House Property	Rupees	Rupees	Rupees
I. Income from let out house (computed)			9,500
Business Income			
i. Profit from radio business	19,600		
ii. Share of profit from electric business	<u>1,800</u>		
	21,400		

Less: Current year's depreciation	<u>2,500</u>	18,900
Set off B/F loss from cycle business	3,900	
	Rupees	Rupees
Set off B/F loss from radio business	1,900	
Set off B/F loss from electric business	<u>2,700</u>	8,500
		10,400
Set off B/F unabsorbed depreciation		<u>1,000</u>
		9,400
iii. Speculation Business income	1,900	
Set off B/F loss from speculation business	<u>-3,200</u>	
This loss shall be C/F to be set off against speculation income of future	<u>-1,300</u>	Nil
		9,400

Capital Gains

STCG	3,200	
Set off STCL of 2015-16	<u>4,100</u>	-900
LTCG	9,250	
Set off LTCL loss B/F	<u>6,450</u>	+2800
Taxable Capital gain		<u>1,900</u>
Total income		<u>20,800</u>

Note:

1. Loss from speculation business is not allowed to be set off out of the profits of a non-speculation business.
2. Unabsorbed expenditure on family planning is not allowed to be deducted in case of non-company assesses.
3. Loss of a discontinued business can set off out of profits of a continuing business.

ILLUSTRATION 6

Mr. M Rafiq submits the following information of his incomes and losses for the year ending 31-3-2019. Compute his total income :

	Rs
1. Salary income (computed)	24,000
2. Income from house property :	
House A (income)	10,000
House B (loss)	40,000
House C (self-occupied)	28,000
3. Income from business:	
Cloth business (profit)	10,000
Hardware business (loss)	12,000
Speculation (profit)	12,000
Speculation (loss)	17,000
4. Capital gains:	
Short-term (gain)	8,000
Short-term (loss)	24,000
	8,000
5. Other Sources:	
Income from betting	12,000
Income from card games	9,000
Interest from securities (gross)	8,000

SOLUTION 6

Computation of total income of Mr.Rafiq

	Rupees	Rupees	Rupees
Salaries			
Salary income (computed)			24,000
House property			
House A		+10,000	
House B		40,000	
House C		<u>28,000</u>	
House property loss to be set off from other heads			-58,000

Profits & Gains:

	Rupees	Rupees	Rupees
Cloth business	+10,000		
Set off Hardware business loss	<u>-12,000</u>	-2,000	
Speculation (profit)	+12,000		
Set off speculation loss	<u>- 5,000</u>	Nil	
Business loss to be set off from other heads			-2,000

Capital Gains:

STCG	+8,000		
Set off STCL	<u>-24,000</u>		
	-16,000		
LTCG	<u>+8,000</u>		
STCL to be C/F	<u>-8,000</u>		<u>Nil</u>

Other sources:

Income from betting	12,000		
Income from cards	<u>9,000</u>	21,000	
Interest on securities	<u>8,000</u>	<u>29,000</u>	
<u>Total income</u> (Casual income)			<u>21,000</u>

Note:

1. Business loss shall be set off from income from interest on securities.
2. House property loss of 58,000 shall be set off from salary income of 24,000 and balance from interest on securities 6,000. Unadjusted house property loss 28,000 shall be C/F.
3. No loss can be set off from casual incomes.

ILLUSTRATION 7

The assessment of M & Bros. for the assessment years 2018-19 and 2019-20 shows the following results:

	Ass. Year 2018-19	Ass. Year 2019-20
I Interest on securities	-2,000	+2,000
Ii Income from house property	+8,000	+8,000
PGBP:		
a. Dealing in fruits	-30,000	-12,000
b. Manufacturing glass:		
Profit before depreciation	+50,000	+1,40,000
Depreciation	+80,000	+75,000
c. Speculative transactions	+6,000	-9,000
Iv Income from other sources (bank interest)	+2,000	+5,000
V Short term capital gain	Nil	-25,000

Compute net assessable results for each of the two years giving full reasons for your working.

SOLUTION 7

Calculation of total income of M& Bros. for assessment year 2018-2019

	Rupees	Rupees	Rupees
Income from house property			+8,000
Profits & gains:			
a. Dealing in fruits		30,000	
b. Glass Manufacturing	+ 50,000		
Less: Current depreciation	<u>-80,000</u>		
Unabsorbed depreciation	<u>-30,000</u>	Nil	
c. Speculation profit		<u>+6,000</u>	
Net loss from business			-24,000
Income from other sources:			
a. Bank interest		+2,000	
Interest on securities		<u>-2,000</u>	<u>Nil</u>
Gross total income			<u>Nil</u>

Note: Loses to be C/F

a. Unabsorbed Depreciation	30,000
b. Business loss to be C/F	16,000
(After adjusting 8,000 from HP income)	

Calculation of total Income of M & bros. for assessment year 2019-2020:

Income from house property **+8,000**

Profits & Gains:

a. Dealing in fruits		12,000
b. Glass Manufacturing	+1,40,000	
<i>Less:</i> Current Depreciation	<u>75,000</u>	
Business profit		<u>+65,000</u>
Balance business income		53,000
B/F business loss		<u>-16,000</u>
		37,000
Unabsorbed <u>depreciation</u>	<u>-30,000</u>	<u>+7,000</u>
c. Speculation loss to be C/F	<u>9,000</u>	

Income from other sources:

a. Bank interest	+5,000	
b. Interest on securities	<u>+2,000</u>	<u>+7,000</u>
Total income		<u>22,000</u>

Notes:

1. Capital loss of 25,000 to be C/F as it cannot be set off from any other income.
2. Speculation loss to be C/F 9,000.

2.7 GLOSSARY

- Set-Off Losses: When any loss relating to any particular previous year is set-off against the income of same previous year, it is called set-off of losses.
- Carry forward of loss: If any loss related to any previous year (or assessment year) cannot be set-off either under the same head or against the incomes of other

heads during same previous year(or assessment year), such a loss can be carried forward to future previous years for setting off against incomes of future previous years(or assessment years).

- Speculation Loss: Any loss computed in respect of speculation business. Such a loss carried by an assessee shall not be set-off except against profits and gains, if any, of another speculation business.
- Transfer of Income (section 60): Where a person transfers to any other person income (whether revocable or not) from an asset without transferring that asset, the income shall be included in the total income of the transferor. “Transfer” includes any settlement, trust, covenant, agreement or arrangement.
- Revocable transfer: Where a person transfers any asset to any other person with a right to revoke the transfer, all income accruing to the transferee from the asset shall be included in the total income of the transferor.
- The income under revocable transfer of asset shall be included in the income of transferor even when only a part of income from transferred asset has been applied for the transferor.
- Irrevocable Transfer: In case of an irrevocable transfer of assets for a specified period, the income from such assets shall not be included in the income of transferor.
- Income to spouse from a concern in which such individual has substantial interest [Section 64(1)(ii)]: All such income as arises directly or indirectly, to the spouse of an individual by way of salary, commission, fees or any other remuneration, whether in cash or kind from a concern in which such individual has a substantial interest, shall be included in the income of the individual.
- Income to spouse from the assets transferred [Section 64(1)(iv)]: Where any individual transfers directly or indirectly any asset (other than a house property) to the spouse, the income from such asset shall be included in the income of the transferor.
- Income to Son’s Wife [Section 64(1)(vi)]: Where any individual transfers, directly or indirectly, any asset to his/her son’s wife without adequate consideration, after

1.6.1973, the income from such asset shall be included in the income of the transferor.

- **Transfer for Immediate or Deferred Benefit of Son's Wife [Section 64(1)(viii)]:** Any income arising, directly or indirectly, to any person or association of persons from assets transferred directly or indirectly after June 1, 1973, otherwise than for adequate consideration to the person or association of persons by such individual shall, to the extent to which the income from such assets is for the immediate or deferred benefit of his son's wife be included in computing the total income of such individual.
- **Income to spouse through a third person [Section 64(1)(Vii)]:** Where a person transfers some assets directly or indirectly to a person or association of persons (trustee or body of trustees or juristic person) without adequate consideration for the immediate or deferred benefit of his or her spouse, all such income as arises directly or indirectly from assets transferred shall be included in the income of the transferor.
- **Clubbing of Income of Minor Child [Section 64(1a)]:** All income which arises or accrues to the minor child (not being a minor child suffering from any disability of the nature specified in Section 80U) shall be clubbed in the income of his parent. However, any income which is derived by the minor from manual work or from any activity involving application of his skill, talent or specialised knowledge and experience will not be included in the income of his parent. In case the income of an individual includes any income of his minor child in terms of this section [i.e. Section 64(1A)], such individual shall be entitled to exemption of the amount of such income or Rs. 1,500 whichever is less.

2.8 SELF ASSESSMENT QUESTIONS

1. What do you mean by "Set-off and carry forward of losses"? Which losses can be carried forward?

2. Discuss the provisions of the Income-tax Act relating to the set-off of losses.

3. Discuss the provisions of the Income-tax Act relating to carry-forward and set-off of losses, with particular reference to the provisions of Section 72A of the Act.

4. Explain in brief the deduction for the medical insurance premium paid by the assessee.

5. Enumerate the various rebates and reliefs available to individuals under the Income-tax Act, 1961.

6. What conditions are to be satisfied in order to claim a deduction for donations made to certain funds or/ and charitable institutions? Illustrate.

7. Explain the deduction given in respect of certain payments.

8. Explain the deduction given in respect of certain incomes.

9. Explain Deemed income. Elaborate the incomes that are treated as deemed incomes.

2.9 BOOKS RECOMMENDED

1. Dr. V.K. Singhania: Students Guide to Income-tax; Taxmann Publications Pvt. Ltd., New Delhi.
2. Girish Ahuja and Ravi Gupta: Systematic Approach to Income-tax and Sales-tax; Bharat Law House, New Delhi.
3. Dr. H.C Meharotra and Dr S. P Goyal: Income Tax Law and Accounts; SahityaBhavan Publications.
4. V. P Gaur & D. B Narang: Income Tax Law & Practice; Kalyani Publishers.
5. V. K Singhania & Kapil Singhania: Direct Taxes Law & Practices; Taxman Publications.
6. Mahesh Chandra, D. C Shukla, K. A Mahajan & M. A Shah: Income Tax Law & Practices; pragati Publication, New Delhi.
7. Arvind Tuli & Dr. Neeru Chadda: Conceptual Clarity on Income Tax and Wealth Tax; Kalyani Publication, New Delhi.

**ASSESSMENT OF INDIVIDUALS AND H.U.F INCLUDING
COMPUTATION OF TAX LIABILITY.**

STRUCTURE:

3.1 Introduction

3.2 Objective

3.3 Assessment of Individuals

3.4 Tax treatment of income received from different institutions

3.5 Income of other persons to be included in the total income of an individual

3.6 Computation of Gross Total Income

3.7 Computation tax liability

3.8 Concept of H.U.F

3.9 Types of members

3.10 Joint Property of the family

3.11 Position under Hindu Succession Act, 1956

3.12 Computation of Income of the H.U.F.

3.13 Partition of a Hindu undivided family (Section 171)

- Who is entitled to share on partition
- Assessment after partition (Section 171)

- A partition of the HUF can be both total and partial

3.14 Summary

3.15 Glossary

3.16 Self-Assessment Questions

3.17 Books Recommended

3.1 INTRODUCTION

Income tax is that percentage of your income that you pay to the government to fund infrastructural development, pay the salaries of those employed by the state or central governments, etc. All taxes are levied based on the passing of a law, and the law that governs the provisions for our income tax is the Income Tax Act, 1961.

Income tax is only of the direct means of taxation like capital gains tax, securities transaction tax, etc., and there are many other indirect taxes that we pay like sales tax, VAT, Octroi, service tax, GST etc.

The income tax you pay every month or upon every contractual earning is what forms a large part of the revenue for the Government of India. These revenue functions are managed by the Ministry of Finance, which has delegated the responsibility to managing direct taxes (like income tax, wealth tax, etc.) to the Central Board of Direct Taxes (CBDT).

Income tax is applicable for individuals, businesses, corporate, and all other establishments that generate income. The Income Tax Act, 1961 regulates the collection, recovery, and administration of income tax in India. The government requires the tax amount for various purposes ranging from building the infrastructure to paying the state and central government's employees. It helps the government in generating a steady source of income that is used for the development of the nation.

The income tax is paid every month from the monthly earnings, however, it is calculated on an annual basis. The amount of income tax an individual has to pay depends on many factors.

Under the Department of Revenue of the Ministry of Finance, the Income Tax Department (IT Department) is responsible for monitoring the collection of Income Tax, Expenditure

Tax, and various other Financial Acts that are passed every year in the Union Budget. The Central Board of Direct Taxes (CBDT) regulates the policy and planning of taxes. CBDT is also responsible for administering the direct tax laws through the IT Department. In addition to the collection of taxes, the IT department is also involved in prevention and detection of tax avoidance.

Income tax has to be paid by every individual person, Hindu Undivided Family (HUF), Association of Persons (AOP), Body of Individuals (BOI), corporate firms, companies, local authorities and all other artificial juridical persons that generate income.

Taxes are calculated on the annual income of a person, and an annual cycle (year) in the eyes of the Income Tax law starts on the 1st of April and ends on the 31st of March of the next calendar year. The law recognizes and classifies the year as “Previous Year” and “Assessment Year”.

*The year in which income is earned is called the **previous year** and the year in which it is charged to tax is called the **assessment year**.*

*For example: Income earned between April 1st 2018 and March 31st 2019 is called the **income of the previous year** and will be charged to tax in the **next year, or the assessment year** that starts on April 1st 2019.*

Taxes are collected by the government in three primary ways:

1. Voluntary payment by taxpayers into designated banks, like advance tax and self-assessment tax.
2. Taxes Deducted at Source (TDS) which is deducted from your monthly salary, before you receive it.
3. Taxes Collected (TCS).

In this lesson the Income Tax Treatment with relation to Hindu Undivided Families (HUF) and individuals is being discussed. The tax implications, rates of tax and other issues relating to the above persons have been discussed elaborately. Hindu undivided family is treated as a separate taxable entity for the purpose of income tax assessment.

3.2 OBJECTIVES.

At the end of this lesson, you will learn

- What is a HUF, how it comes into existence
- When and how it can be partitioned and what are the tax implications before and after its partition.
- What is an individual.
- What are the rates applicable for taxing individual.
- How to calculate tax liability of Individual.
- What is Hindu Succession Act 1956.
- Computation of the income of H.U.F.
- Partition of a Hindu undivided family.

3.3 ASSESSMENT OF INDIVIDUALS

Section 4 of the income tax, 1961 read with section 2 (31) provides the different units of assessment. These are:

- (i) Individual
- (ii) Hindu undivided family (HUF)
- (iii) Firm
- (iv) Association of persons or a body of individuals
- (v) Local authority
- (vi) Company
- (vii) Artificial juridical person.

Individual includes both male and female assesseees. The total income has to be computed as per the provisions of the Income-tax Act, 1961. In addition to individuals own income, income of other persons received by him in some other capacity or received by other

persons is to be clubbed with individual assessee's income. It is important to note that no special formalities are required to be fulfilled as in case of firm to claim the status of individual for assessment purposes. An individual may have income under any/ all of the following 5 heads:

- (i) Income from head salary
- (ii) Income under head house property
- (iii) Income under head business or profession
- (iv) Income under head capital gain
- (v) Income under head from other sources.

Following steps are considered for computing total income and to charge tax.

Step 1 – Determination of the residential status of the Assessee: First all we want to determine the residential status of the assessee. The residential status of a person has to be determined to find out which income is to be included in computing the total income. It decides whether the individual is to be taxed or not. The residential status of an individual is determined on the basis of the duration of time spent by him in India. . Based on the time spent by him, he may be (a) resident and ordinarily resident, (b) resident but not ordinarily resident, or (c) non-resident.

Step 2 – Classification of income under different heads: The Act specifies five heads of income. These heads of income consist of all possible types of income that can accrue to or be received by an individual. An individual is required to classify the income earned by him under the appropriate heads of income.

Step 3 – Exclusion of income not chargeable to tax: There are certain incomes which are wholly exempt from income-tax e.g. agricultural income. These incomes have to be excluded while calculating Gross Total Income. At the same time certain incomes are partially exempt from income tax e.g. House Rent Allowance, Education Allowance etc.. These incomes are excluded only to the extent of the limits specified in the Act. The balance income over and above the prescribed limits would enter computation of total income and have to be classified under the relevant head of income.

Step 4 – Computation of income under each head: Income is to be computed in accordance with the provisions governing a particular head of income. As per the rules certain deductions and allowances are allowed. These deductions are allowed while computing income under each head.

Step 5 – Clubbing of income of spouse, minor child etc.: In case of individuals, income-tax is levied on a slab system on the total income. The tax system is progressive. That means if income increases the tax amount to be paid also increases. We can see that some taxpayers who have the higher income bracket have a tendency to divert some portion of their income to their spouse, minor child etc. to minimize their tax burden. In order to prevent such tax avoidance, clubbing provisions have been included in the Income-tax Act. As per the provisions of income tax act income arising to certain persons (like spouse, minor child etc.) have to be included in the income of the person when it is seen that the income is diverted for avoiding tax.

Step 6 – Set-off or carry forward and set-off of losses: An individual may have different sources of income under the same head of income. He might have profit from one source and loss from the other. As per the provision we can set off the losses under one head or form other heads or can carry forwards for the coming assessment years. All provisions related to that should be considered while computing total income of the Assessee.

Step 7 – Computation of Gross Total Income: The final figures of income or loss under each head of income, after allowing the deductions, allowances and other adjustments, are then aggregated, after giving effect to the provisions for clubbing of income and set-off and carry forward of losses, to arrive at the gross total income.

Step 8 – Deductions from Gross Total Income: There are deductions prescribed from gross total income. The allowable deductions in case of an individual are deductions under sections 80C, 80CCC, 80CCD, 80CCF, 80D, 80DD, 80DDB, 80E, 80G, 80GG, 80GGA, 80GGC, 80-IA, 80-IAB, 80-IB, 80-IC, 80-ID, 80-IE, 80JJA, 80QQB, 80RRB, 80TTA and 80U. These deductions are allowed as per the rules prescribed in the income tax act.

Step 9 – Compute Total income: After allowing all deductions allowable, we can compute total income. **Step 10 – Application of the rates of tax on the total income:** Different slab of

tax rates are available on basis of status and age of individual. . There also will be basic exemption limit.

3.4 TAX TREATMENT OF INCOME RECEIVED FROM DIFFERENT INSTITUTIONS:

1. As a member of HUF: Exempted u/s 10(2). But where an individual converts his individual property into common pool of HUF of which he is a member, income from such property shall be included in his individual income.

If the member earns his own income, besides being the member of HUF, he will pay tax on his own earned income.

But u/s 64 (2) where an individual converts his individual property into the common part of HUF of which he is a member, income from such property shall be included in his individual income.

2. Income received as share from AOP. Share from AOP is treated as: If the individual income of all partners does not exceed the exempted first income slab, then share from such AOP is to fully added. However, if the individual income of any partner exceeds the first exempted income slab, then share from such AOP is not to be added in the income of the individual.

For determining rates of tax, the individual income of each member or partner is to be taken in to account as under:

- (a) If individual income of all partners / members does not exceed Rs 250,000 whether a male or female (For a resident senior citizen Rs 300,000 and for resident super senior citizen Rs 500,000) each, the AOP shall pay tax at the rates applicable to an individual .
- (b) Share from such AOP is fully added in the individual income of the each partner and is fully taxable again as partner's individual income.
- (c) Out of the tax a rebate of tax on share from AOP is allowed at average rate.
Average rate = Total tax / Total income x 100.
- (d) No rebate of tax if total income of such AOP does not exceed Rs 250,000.

If total income of any one or more partners /members of AOP exceed Rs 250,000 , the AOP shall pay tax at MMR i.e, 30 % on whole of its total income.

Share from such AOP shall be fully exempted while calculating individual income of partners partners are not allowed any rebate u/s 86 .

3. As a partner of firm assessed as firm u/s 184. Exempted But remuneration and interest on capital received is taxable under the head profits and gains to the extent it is allowed as deduction to the firm.

4. As a partner of firm assessed as firm u/s 185. Exempted But remuneration and interest on capital received from such firm is also exempted u/s 10 (2A). The following sums received by partner from such firm shall also be exempted in the hands of the partner. : (a) Any remuneration, Bonus, fees, commission, etc. (b) Interest on loan/ capital from such firm.

5. As a shareholder of a company. The gross amount of dividend received by an individual is to be included in his total income. The gross amount means, the net dividend received plus tax deducted at source. The shareholder is liable to pay tax on whole of his income from dividend i.e., the gross amount of dividend declared by the company. The assessee shall get credit of the tax deducted at source out of his total tax liability. The individual shall be entitled to the deduction as provided by the different sections of income tax act.

with effect from assessment year 1998-99 dividend received from or declared or distributed by an Indian company on or after 1-6- 97 shall be fully exempted and shall not form part of total income.

3.5 INCOME OF OTHER PERSONS TO BE INCLUDED IN THE TOTAL INCOME OF AN INDIVIDUAL

The following incomes although accruing to other persons are included in the income of individual assessee:

1. Transfer of an income without transfer of asset: The income shall be included in the total income of transferor.

2. Revocable transfer of asset: The income from such assets is also included in the total income of the transferor. If the assets is not revocable during the life time of the transferor, it shall be regarded as irrevocable transferor for this purpose.

3. Income of minor child: With effect from assessment year 1993-94 , income of a minor from whatsoever sources shall be added in the income of that parent whose other income is higher. In case, income is included in the income of one parent shall always be included in the income of that parent. Income of a minor handicapped or mentally retarded child shall not be clubbed.

4. Income from asset transferred to spouse, daughter in law by an individual without adequate consideration shall be included in the income of that individual. The relationship must exist on the date on which asset is transferred . On a particular date on which transferor and transferee have on relationship with each other, but subsequently, such relationship is formed, the income from such asset shall remain to be the income of transferee.

5. Income from the asset transferred by an individual in such a way that benefit accrues directly or indirectly to the spouse or minor child of the transferor, the income from such transferred assets shall be included in the total income of the transferor.

6. Share of income arising to spouse for being member of a trust or to minor child who is beneficiary under a trust. The finance act, 1979 provides that any income arising to the spouse or minor child from a trust shall be deemed to be the income accruing indirectly to the spouse or minor child of such individual from the membership of the spouse to or from the admission of minor to the benefits of a firm in which such individual is partner.

3.6 COMPUTATION OF GROSS TOTAL INCOME

The final figures of income or loss under each head of income, after allowing the deductions, allowances and other adjustments, are then aggregated, after giving effect to the provisions for clubbing of income and set-off and carry forward of losses, to arrive at the gross total income.

Deductions from Gross Total Income:

There are deductions prescribed from gross total income. The allowable deductions in case of an individual are deductions under sections 80C, 80CCC, 80CCD, 80CCF,

80D, 80DD, 80DDB, 80E, 80G, 80GG, 80GGA, 80GGC, 80-IA, 80-IAB, 80-IB, 80-IC, 80-ID, 80-IE, 80JJA, 80QQB, 80RRB, 80TTA and 80U. These deductions are allowed as per the rules prescribed in the income-tax act.

3.7 COMPUTATION OF TAX LIABILITY

After computing the total income, next step is to compute the tax liability. The following steps are to be followed:

1. Round of total income to the nearest multiple of 10.
2. Divide the total income into four parts:
 - i. LTCG - calculate tax @20%.
 - ii. STCG on shares which are subject to STT- calculate tax @15%.
 - iii. On casual income- calculate tax @30%.
 - iv. Balance is total income.

Calculate tax at following rate:

Application of the rates of tax on the total income:

The basic exemption limit is Rs 2, 50,000 for the assessment year 2016-17.

A) Normal Rates (individual whether male or female):

Up to Rs: 2,50,000: Nil

Rs: 2, 50,000 to 5,00,000: 5%

Rs: 5, 00,000 to 10,00,000: 20%

Above Rs: 10,00,000: 30%

B) Individual- Senior citizen (60 years or more but less than 80 years):

Up to Rs: 3,00,000: Nil

Rs: 300,000 to 5,00,000: 5%

Rs: 5,00,000 to 10,00,000: 20%

Above Rs:10,00,000: 30%

C) Individual- Super senior citizen (80 years or more):

Up to Rs: 5,00,000: Nil

Rs: 5,00,000 to 10,00,000: 20%

Above Rs: 10,00,000: 30%

3. Rebate u/s 87A. In case of resident individuals, a rebate of Rs 3,500 or tax calculated whichever is less, shall be allowed provided their total income does not exceed Rs 350,000.

4. Surcharge- if total income exceeds Rs 50 lakhs but does not exceed 1 crore surcharge @ 10% of tax and if total income exceeds Rs 1 crore surcharge @ 15% of tax shall be added.

5. Health and education cess @ 4% of tax and surcharge, if any

6. After adding education cess, rebates u/s 86 for share from AOP. This rebate is allowed at average rate and relief u/s 89 (1) for arrears.

7. Balance is tax payable which will be rounded off to the nearest multiple of Rs 10.

Applicability of alternate minimum tax (AMT) on individual [Section 115 JC TO JF]

The finance act, 2011 introduced the concept of alternate minimum tax on limited liability partnership. However, the finance act, 2012 has extended the system of alternate minimum tax on all persons other than a company subject to certain conditions. Thus, w.e.f Assessment year 2013-14, Alternate minimum tax is also applicable on individuals.

Individual covered under AMT [Section 115 JEE (1)]

The provisions of alternate minimum tax shall apply to an individual:

(1) Who has claimed any deduction under:

u/s 35 AD or

Any section (Other than Section 80 P) included in Chapter VI-A under the following Heading “C” – Deduction in respect of certain incomes” [i.e. Under section 80IA to section 80 RRB],

Or section 10 AA (SEZ) and

(2) Whose adjusted total income exceeds Rs 20, 00,000.

Individual not covered under AMT [Section 115 JEE (2)]

The provisions of alternate minimum tax shall not apply to an individual whose ‘ Adjusted total income’ does not exceed Rs 20 Lakh.

Scheme of AMT [Section 115 JC (1)]

Where the regular income tax payable by an individual for a particular previous year is less than the alternate minimum tax payable for such previous year, the adjusted total income shall be deemed to be the total income of such individual for such previous year and it shall be liable to pay income tax on such total income @ 18 .5 %

Thus, AMT is an alternate amount of tax which an individual has to pay if the regular income tax for any previous year is less than 18 .5 % of its adjusted total income as defined for this purpose. Section 115 JC is an overriding section and provides a specific tax rate on a specific figure for certain individuals. It provides a new concept of adjusted total income for individuals, which is to be treated as total income of the individual and on this total income , tax is required to be calculated @ 18.5 % . This tax is called ‘alternate minimum tax’. AMT has brought into tax net those individuals who were earning profits but were not paying any income tax due to various deductions or exemptions available to them under the income tax , 1961.

Ultimate tax liability of Individual

Regular income tax payable as per normal provisions of IT act

Or

Tax @ 18.5 % on adjusted total income

Whichever is higher.

Note: In the case of unit located in an international financial services centre (IFSC) which desires its income solely in convertible foreign exchange, AMT shall be charged @ 9% [w.e.f.A.Y 2019-20]

Surcharge

Surcharge on AMT for Assessment year 2019-20 shall be as under: -

- | | |
|-----------------------------------------------------------------------|-------------|
| (i) If adjusted total income does not exceed Rs 50 lakhs | NIL |
| (ii) If adjusted total income Rs 50 lakhs but does not exceed 1 Crore | 10 % of tax |
| (iii) If adjusted total income exceeds Rs 1 Crore | 15 % of tax |

Meaning of Adjusted Total income [Section 115 JC (2)]

Adjusted total income means the total income before giving effect to this newly inserted chapter XII BA as increased by:

- (i) Deductions claimed under any sections included in chapter VI-A under the heading C i.e., deductions in respect of certain incomes (Except section 80 P) and
- (ii) Deduction claimed , if any , u/s 10AA
- (iii) Deduction claimed , u/s 35 AD less depreciation allowable u/s 32 on the cost of that asset.

Total income shall be increased by the deduction claimed u/s 35 AD for the purpose of computing adjusted total income, but the amount of depreciation allowable u/s 32 shall be reduced while calculating adjusted total income.

It is important to note that part C of Chapter VI- A covers various deductions u/s 80 in respect of certain incomes. These deductions (For an individual) are as follows:

- (i) Deductions u/s 80 IA
- (ii) Deductions u/s 80 I- AB
- (iii) Deductions u/s 80 IB
- (iv) Deductions u/s 80 IBA

- (v) Deductions u/s 80 IC
- (vi) Deductions u/s 80 ID
- (vii) Deductions u/s 80 IE
- (viii) Deductions u/s 80 JJA
- (ix) Deductions u/s 80 JJAA
- (x) Deductions u/s 80QQB
- (xi) Deductions u/s 80 RRB
- (xii) Deductions u/s 80TTA
- (xiii) Deductions u/s 80 TTB

In other words, adjusted total income for the purposes of section 115 JC (1) shall be calculated as follows:

Total income as per normal provisions of IT act

Add: Deductions in respect of certain incomes [Section 80 IA to 80 RRB]

[Except section 80 P]

Add: Deductions u/s 10 AA

Add: Deductions allowable u/s 35 AD

Less: Depreciation allowable u/s 32

Adjusted Total Income

Meaning of Regular Income tax [Section 115 JF (d)]

It means the income tax payable for a previous year by an individual on its total income in accordance with provisions of IT act, 1961 other than the provisions of this chapter XIIB.

Furnishing of report obtained from chartered accountant [Section 115 JC (3)]

Every individual covered u/s 115 JC shall obtain a report, in prescribed form (29 C) from an accountant [as defined in section 288 (2)] certifying that the adjusted total income and

the alternate minimum tax have been computed in accordance with the provisions of this chapter . Such report shall be furnished to income tax department on or before the due date of filling of return u/s 139 (1).

Tax credit for alternate minimum tax [Section 115 JD]

1. The credit for tax paid by an individual under section 115 JC shall be allowed to it in accordance with the provisions of this section [Section 115 JD (1)]
2. Computation of amount of tax credit [Section 115 JD (2)] The tax credit of an assessment year shall be the excess of alternate minimum tax paid over the regular income tax payable for that year. In other words,

Amount of tax credit = Alternate minimum tax - tax payable on total income computed as per normal provisions of the income tax act.

3. Time limit to carry forward tax credit : [Section 115 JD (4)] The tax credit for any assessment year can be carried forward up to fifteenth assessment year immediately succeeding the assessment year for which tax credit becomes allowable u/s 115 JC (1).
4. Set off of tax credit [Section 115 JD (5)] : Tax credit shall be allowed in any assessment year, in which the regular income tax exceeds the alternate minimum tax . Such set off shall be allowed to the extent of the excess of regular income tax over the alternate minimum tax and the balance of the tax credit, if any, shall be carried forward.

Note: No interest shall be payable on tax credit allowed [Section 115 JD (3)]

Increase/Decrease of tax credit [Section 115 JD (6)]

If the amount of regular income tax or the alternate minimum tax is reduced or increased as a result of any order passed under this act, the amount of tax credit allowed under this section shall also be adjusted/ varied accordingly.

Application of other provisions of this act [Section 115 JE]

Same as otherwise provided in this chapter, all other provisions of this act shall apply to an individual referred to in this chapter

PROBLEMS

ILLUSTRATION 1 :

Compute the total income of Mr. Ram from the particulars given below:	Rs.
i) Interest on securities	27000
ii) Rental Value of a house Rs 7500 p.m. self-acquired but transferred to HUF Pool. Computed income from this house is	25200
iii) Share from firm assessed u/s 184 in which he has 1/3 rd share	45000
iv) Commission received by his wife from above mentioned firm for acting as its selling agent	25000

SOLUTION 1 :

Computation of Total Income of Mr. Ram	Rs.	Rs.
Profits and Gains		
1/3 rd Share from the firm assessed u/s 184 (Exempted)		Nil
Other Sources:		
a) Commission received by wife from a firm in which spouse has substantial interest u/s 64(1)(ii)	25000	
b) Income from self- acquired asset converted into common pool of HUF u/s 64(2)	25200	
c) Interest on Securities	27000	77200
Total Income		77200

ILLUSTRATION 2

For the accounting year ended 31st, March 2019 Mr. Shashi Kant furnishes the following particulars of his Income. Rs.

i) Salary received in India	60000
ii) Profit from business in Germany but received in India	15000
iii) Income from house property in Pakistan deposited in bank there	12000
iv) Profit from business established in Bangladesh but business is controlled from India	46000
v) Income accrued in India but received in Sweden	25000
vi) In this accounting year Mr. Shashi Kant has brought into India foreign income of earlier years	42700
vii) Profit from sale of plant at Mumbai (50% received in Bangkok)	160000
viii) Interest on Japan development bonds (60% received in India)	100000
compute his total Income if	
a) <i>He is resident,</i>	
b) <i>He is not ordinarily resident, or</i>	
c) <i>He is non-resident.</i>	

SOLUTION 2

Calculation of Total Income of Mr. Shashi Kant

	Resident	Not ordinarily	Non-Resident
a) Income accrued and received in India			
<i>Salary received being salary income</i>	60000	60000	60000
b) Income accrued in India but received outside India			
i) <i>Income accrued in India</i>	25000	25000	25000
ii) <i>Profit from sale of plant</i>	160000	160000	160000
c) Income accrued outside India but received in India			

<i>i) Profit from business in Germany but 15000 received in India</i>	15000	15000	15000
<i>ii) Interest on Japan Development Bonds</i>	100000	60000	60000
d) Income accrued and received outside India			
<i>i) Income from house property in Pakistan</i>	12000	—	—
<i>ii) Profit from business establishment in Bangladesh</i>	46000	46000	—
<i>iii) Foreign income of past previous years brought into India during the year</i>	—	—	—
Grand Total Income & Total Income	4,18,000	3,66,000	3,20,000

ILLUSTRATION 3

Mr. Verma is the manager of Punjab Cotton Mills Ltd. He draws a salary of Rs. 33,000 p.m. His other items of income are:

- a) Interest on fixed deposits with Andhra Bank Rs. 10800 and interest credited in the savings a/c in the bank Rs. 12000.*
- b) Winning from Lottery Rs. 60000.*
- c) Dividend from an Indian Company Rs. 3600.*
- d) Long term capital gains from sale of his residential house, occupied for the last 20 years Rs. 115000.*
- e) Short Term capital loss Rs. 10000.*
- f) Long term capital loss from Gold brought forward from the assessment year 2017-18 Rs. 20000.*

The following deductions are claimed:

- i) Life Insurance premium (policy for 100000 taken 2005) Rs. 14500.*
- ii) Donation for Punjabi University Rs. 5000.*

iii) Donation to clean Ganga fund setup by Central Govt. Rs. 5000.

iv) Education of his children Rs. 4500.

Compute his total income and Tax payable for the assessment year 2019-20.

SOLUTION 3

Computation of Total Income

Salaries	Rs.	Rs.
Salary @ 33,000 p.m	3,60,000	
Deduction u/s 16	40,000	
		3,56,000
Capital Gains		
L.T.C from house	1,15,000	
Less: Exemption u/s 54	1,05,000	10000
Set off S.T.C. Loss of the same year	10000	Nil
L.T.C Loss b/f still to be c/f	10000	Nil
Other Sources		
Interest on fixed deposit with bank	10800	
Interest on savings a/c with the bank	12000	
Winning from Lottery	60000	
Dividend from indian company: Exempted	Nil	82,800
Gross Total Income		4,42,800
Deduction u/s 80		
i) u/s 80 C: Q.A of savings	14500	
ii) u/s 80 G: Donation to a university Rs.5000, Q.A= 100%	5000	
Donation to clean Ganga Fund Rs. 5000, Q.A= 100%	5000	
iii) u/s 80TTA: Interest in savings a/c-restricted to 10000	10000	34,500
Total Income		4,08,300

Computation of Tax liability

Lottery Income Rs. 60000@30%		18000
Other Income (4,08,300-60000)=348,300		
On 2,50,000	Nil	
On balance Rs. 98,300@5%	4915	
Tax		4915
22,915		
Less rebate u/s 87A		NIL
		22,915
Add: 4% health and Education Cess@ 4%of tax		917
Total tax		23,832
Tax Payable rounded off to 23,830		

Note : (1) Since total income of the asseesee exceeds Rs 350,000 so he is not entitled for a rebate u/s 87 A (2) He is entitled to get deduction u/s 80TTA but he will not get deduction u/s 87TTB regarding his interest on Fixed deposits in banks as he is not a senior citizen.

ILLUSTRATION 4

The total income of an individual (45 years old) computed under the normal provisions of income tax act is Rs 10 lakh. However, the adjusted total income of the individual [computed as per section 115 JC(2)] amounted to Rs 30 lakh. Calculate the final tax liability of the individual for assessment year 2019-20.

Computation of tax liability as per normal provisions of Income tax act.

Case 1

Total given income = 10,00,000

Tax on Rs 10,00,000 as per slabs	112,500
Add: Surcharge	<u>NIL</u>
Add: 4% health and education cess	<u>4,500</u>
Tax liability	<u>117,000</u>

Case 2

Tax liability under AMT [i.e., u/s 115 JC]	
Adjusted total income given	30,00,000

ILLUSTRATION 5

From the particulars given below, compute the total income and tax payable of Mr. dev a central govt. employee working at Chandigarh.

- (1) Salary Rs 25,000 P.m
- (2) T A bill Rs 5,000 P.a actual expenditure Rs 6,000 p.a
- (3) Bonus Rs 25,000 p.a
- (4) His contribution to statutory provident fund Rs 1,700 p.m
- (5) Employers contribution of SPF 10 % of Salary
- (6) Interest on accumulated balance of SPF @ 13 %
- (7) Entertainment allowance Rs 1,000 P.m
- (8) He owns two houses, one of which is let out at a rent of Rs 4,000 p.m and other whose annual value is Rs 10,000 remained vacant through out the year on account of his employment at ambala where he has taken a house on rent. The two houses are subject to municipal taxes of Rs 5,000 and Rs 1,000 respectively.
- (9) During the year he sold shares of hero Honda ltd. And earned a STCG of Rs 50,000 [STT paid]
- (10) He earned Rs 11,500 as interest from the government securities and bank interest on SBI fixed deposits Rs 11,000 and on a saving account Rs 10,600 . He

pays life insurance premium of Rs 25,000 on his life policy of Rs 400,000. He deposited Rs 10,000 in home deposit account.

Solution 5

Computation of total income of Mr. Dev for the assessment year 2019-20

Salary		
Basic pay @ Rs 25,000 p.m	25000p.m.	300,000
Travelling allowance – exempted	exempted	Nil
Entertainment allowance	1000p.m.	12000
Bonus	--	25000
Gross salary		337000
Deduction u/s 16		
Std deduction 40,000		
Entertainment allowance 5,000		45,000
Salary income		292000
Income from house property		
Rent/ ARV (4000p.m.)	48000	
Less: Municipal taxes	5000	
NAV	<u>43000</u>	
Less: Deductions u/s 24		
Standard deduction 30 % of NAV (43000x30%)	12900	
Let out income		30100
The other house is exempted u/s 23 (2)		Nil
Capital gain : STCG on shares		50,000
Income from other sources		
Bank interest on fixed deposits	11000	
Interest on saving account	10600	
Interest on govt. securities	10500	
Gross total income		32,100
Deductions u/s 80		404200
80 C		
Contribution to SPF 20,000		
Premium of life insurance 25,000		

Contribution to home deposit account	10,000		
80 TTA			
Interest credited in SBI saving bank a/c restricted to			55000
Total income			339800

Working notes:

Deduction u/s 16 (ii)

Entertainment allowance Govt. employee least of 3 items shall be the deduction

Statutory limit 5,000

1/5th of 300,000 60,000

Actual Entertainment allowance 12,000

Interest credited on credit balance in SPF is fully exempted

Computation of tax liability

Total income = Rs 339,800	
Tax on short term capital gain = 50,000 X 15 %	7,500
Tax on balance income = 339,800 – Rs 50,000 = Rs 289,000	
On first Rs 250,000	Nil
On balance Rs 39,800 @ 5 %	<u>1,990</u>
Tax	9,490
Less: Rebate u/s 87 A (Total income does not exceed Rs 350,000)	<u>2,500</u>
Tax liability	6,990
Add: 4 % Health and education cess	<u>280</u>
Total tax liability	7,270

Illustration 6

The following are particulars of the income of the GND university teacher during the year ending 31ST March, 2019

- (a) Salary Rs 37,400 p.m plus Rs 9,000 p.m as grade pay from which 10 % is deducted for statutory provident fund to which the university contributes 12 %

- (b) Rent free bungalow of the annual letting value of Rs 18,000
- (c) Wardenship allowance Rs 2,000 p.m
- (d) 12 % interest on government loan of Rs 65,000
- (e) Income from house property computed Rs 29,560
- (f) He received Rs 3,500 for writing articles in a journal
- (g) He paid Rs 2,000 by cheque to GIC under mediclaim
- (h) Interest gross Rs 2,500
- (i) Examinership remuneration Rs 3,500
- (j) During the year, he sold his plot and earned a long term capital gain of Rs 40,000

During the year he paid Rs 24,000 as life insurance premium on his own policies and spent Rs 600 on books purchased for his own use.

Find out his total income , tax and exempted income . population of Amritsar is 12 lakhs.

Solution 6

Computation of total income

Salary income	
Pay Rs 37,400 P.m	448,800
Grade pay Rs 9,000 P.m	108,000
Wardenship Allowance Rs 2,000 p.m	24,000
Rent free accommodation at Amritsar	
10 % of salary i.e., 448,800 + 108,000 + 24,000 = Rs 580,800	58,080
Employer's contribution to SPF- exempted	<u>Nil</u>
Gross salary	<u>638,880</u>
Less: Deductions u/s 16 : Standard deduction u/s 16 (i)	<u>40,000</u>
Salary income	<u>598,880</u>
Income from house property	29,560
Capital gain	
LTTCG on sale of plot	40,000

Income from other sources		
Interest – gross	2,500	
Examinership remuneration	3,500	
Interest on govt. Loan	7,800	
Remuneration for writing articles	3,500	
Interest on postal saving bank deposit	6,500	
Less : Exempted u/s 10 (15)	<u>3,500</u>	<u>3,000</u>
Gross total income		<u>20,300</u>
Less: Deductions u/s 80		688,740
80C : Own contribution to SPF	55,680	
Life insurance premium	<u>24,000</u>	79,680
80 D : Medclaim		2,000
80 TTA: Interest on postal saving bank account		<u>3,000</u>
Total income		<u>604,060</u>

Computation of tax on total income of Rs 604,060

LTCG Rs 40,000 @ 20 %		8,000
Balance income = 604,000 – 40,000 = 564,060		
On first Rs 250,000 of total income		Nil
On next Rs 250,000 of total income	5 %	12,500
On balance Rs 64,060	20 %	12,812
Tax		33,312
Add: 4 % Health and education cess		<u>1,332</u>
Total tax liability		<u>34,644</u>

Total tax liability round off Rs 34,640

3.8 CONCEPT OF HINDU UNDIVIDED FAMILIES

The term ‘Hindu undivided family’ has not been defined in the Income-tax Act. However, in general parlance it means an undivided family of Hindus. Creation of a HUF is a God-

gifted phenomenon. As soon as a married Hindu gets a child, a new HUF comes into existence. It is not at all necessary that every HUF must have joint property or family income. [R.SubramaniaIyer v. CIT (1955) 28, ITR, 352]. However, to become an assessee under the Income-tax Act, there must be 'income-yielding' joint property of the family.

A HUF may consist of a number of smaller HUFs. A smaller HUF has a legal existence and may be assessable as a unit distinct from the apex joint family even when the bigger HUF is in place [CIT v. Khanna (1963) 49 ITR 232].

Under Hindu Law, a Joint Hindu Family consists of all persons lineally descended from a common ancestor (except those who have separated from the joint family by partitioning of assets) and includes their wives and unmarried daughters, and also a stranger who has been adopted by the family. [Surjit lal Chhabra v. CIT (1975) 101, ITR, p.776 (S.C.)].

The Supreme Court's decision in the case of Surjit Lal Chhabra v. CIT (1975 101 ITR 776) has come to stay as one of the leading case laws. The ratio laid down by the Supreme Court had been applied by the Andhra Pradesh, Orissa and Madras High Courts, followed by Bombay, Patna, Madhya Pradesh and Delhi High Courts and relied upon by the Punjab High Court. In the latest case, the Delhi High Court held in Commissioner of Income-tax v. S.P. Chopra (1991, 191 ITR 455) that the income from the half share of the property had to be treated as the individual income of the assessee under the personal law and not as income of the family. The character of the property had to be determined in accordance with the personal law of the assessee and not on the basis of how the property had been treated by the revenue in respect of earlier assessments.

A son conceived or in his mother's womb is equal in many respects to a son actually in existence, viz., inheritance, partition, survivorship etc. But this doctrine does not apply to the Income-tax Act. Hence, a son conceived is not treated a member of the H.U.F. for Income-tax purposes. [T.S. Srinivasan v. C.I.T., (1966) 60, ITR, p.36 (S.C.)].

Jain and Sikh undivided families are also treated as Hindu undivided families unless, under special circumstances, the assessee claims not to be treated as such. If such claim is made, the assessee shall have to prove that there is some such custom in his family on account of which it cannot be treated as a Hindu undivided family.

A Hindu does not cease to be a Hindu merely because he declared for the purpose of the Special Marriage Act, 1872, that he does not profess Hindu Religion. Such a Hindu does form an H.U.F. with his children from such marriage. [CIT v. Partap Chand (1959), 36 ITR, 262]. Similarly, a Muslim family governed by the Marumakkathayam law constitutes 'Tarwad' or 'Thavazhi' and falls within the definition of a H.U.F. [V.K.P. Abdul Kadar Haji v. Ag. ITO (1967) 66, ITR, 173].

If a Hindu gets converted as a Christian, the family of such a person will not be a HUF. However a Hindu, along with his son (by a christian wife) who has been brought up as a Hindu will be a HUF. [CWT v. R. Sridharan (1976) 104, ITR, 436 (S.C.)].

To claim the status of hindu undivided family, a family must satisfy the following two conditions:

1. Existence of common property in the family: The common property may consist of ancestral property inherited from a male ancestor, property acquired with the aid of ancestral property and property acquired by an individual from his own sources but put into common pool of hindu undivided family.
2. Existence of hindu coparcenary: When there is a person who can claim share in the property of HUF on partition, he is known as coparcener. In order to assess a family as HUF, there must be coparcenary. All HUF's may not have coparcenary and hence all HUF's cannot be treated as HUF for assessment purposes. The coparcenary implies the existence of more than one coparcenary in HUF members of HUF and coparcenary of HUF do not mean the same. As HUF may have many members- Male or female, minor or major, etc. and all members are not coparceners. A Hindu coparcenary includes only those members who (i) Acquire by birth an interest in joint or coparcenary property and (ii) Have the right to claim partition of such property. Such coparceners are the male ancestor with his lineal descendants in the male line within three degrees, i.e., sons, grandson, and great grandsons. However, w.e.f 1.9.2015, a daughter born in the family's also a coparcener like male members of the family.

3.9 TYPES OF MEMBERS

A Hindu Joint Family consists of two types of members:

(i) Coparceners: The lineal male descendants of a person up to the third generation of such person are known as coparceners. The coparceners acquire, on birth, ownership in the ancestral properties of such ascendant and have a right to claim partition of such property at any time. However, w.e.f. 9.9.2005 due to amendment of Hindu Succession Act, the daughter of a coparcener shall by birth become a coparcener in her own right in the same manner as the son. Hence, the daughter can also ask for partition.

(ii) Other members: Such members include wives of male members of the family and other male members.

Thus, a Hindu Joint Family may consist of:

(a) All persons lineally descended from a common ancestor and includes their wives and daughters (w.e.f. 9.9.2005).

(b) A male and widow or widows of deceased male member or members. [GowliBuddanna v. C.I.T. (1966) 60, ITR, p. 293 (S.C.)]

However, an unmarried coparcener who receives share on the partition of joint family properties, cannot form a Hindu undivided family unless he marries. After his marriage, he can hold the property received from family as joint family property consisting of himself and his wife. [C. Krishna Prasad v. C.I.T. (1974) 97, p. 493 (S.C.)].

Karta: Property of the family is ordinarily managed by the father or other senior member for the time being of the family. He is called Karta. However, the senior member may give up his right of management and a junior member may be appointed as Karta with the consent of all other members. [Narendra Kumar J. Modi v. CIT (1976) 105, ITR, 109 (S.C.)]. In the absence of a male member in the family or when all male members are minors, a woman member can be treated as manager of the family for income-tax purposes. [Smt. ChampaKumariSinghi v. Addl. Member of the Board of Revenue (1962) 46, ITR, p. 81].

Since daughter is also a coparcener w.e.f. 9.9.05, it may be presumed that daughter can also be karta of her father's HUF.

3.10 JOINT PROPERTY OF THE FAMILY

It consists of:

(i) Ancestral property;

(ii) Accretion thereto;

(iii) Acquisition with joint funds; and

(iv) Self-acquired property of any member thrown by him into the common stock to be treated as family property. In the case of Pushpa Devi v. C.I.T. the Supreme Court has held that a Hindu female, not being a coparcener, cannot blend her separate property with Joint family property. However, she can make a gift of her property to the family. [(1977) 109, ITR p. 730].

The Supreme Court's decision in the case of Pushpa Devi v. Commissioner of Income-tax (1977, 109 ITR 730) had been later followed by the Calcutta, Andhra Pradesh and Madras High Courts. In the latest case, the Madras High Court held in the case of RajathyAmmal v. Commissioner of Wealth-tax (1987, 164 ITR 605) that a female member could not throw her property into the family hotchpotch and the only way she could achieve her purpose was either by gifting it or selling to the family.

Further, Section 64(2) provides that where an individual being a member of Hindu undivided family transfers his separate property after 31st December, 1969 to the family for the common benefit of the family, otherwise than for adequate consideration, such property is known as converted property. The income derived from the converted property or any part thereof shall be included in the total income of the transferor individual and not in the income of the family.

School of Hindu Law: According to Hindu Law, HUFs are governed by two schools viz. **Mitakshara and Dayabhaga.**

Mitakshara School applies to whole of India except the states of West Bengal and Assam.

Dayabhaga School applies to the States of West Bengal and Assam. The difference between the two schools is as under:

(i) Foundation: In the Mitakashara School, the foundation of a coparcenary is laid down when a son is born to the Mitakshara father. Under the Dayabhaga School the foundation of a coparcenary is laid on the death of the father leaving, as survivors, one or more sons.

(ii) Right to partition: A Mitakshara son, in whom the interest in family property is vested by birth, all along possesses a right to demand partition. A Dayabhaga son, on the other hand acquires no interest in the family property by birth and, consequently, has no right to demand partition of the HUF property from his father.

(iii) Quantum of share: Under Mitakshara Law, each coparcener takes as undefined share in the coparcenary property. The share of the members decreases by birth in the family and increases upon death of a coparcener. A Dayabhaga coparcener, on the other hand, always takes a defined share in the property left by his deceased father. Thus, the heirs of a deceased governed by the Dayabhaga School do not constitute a HUF automatically on the death of the deceased and cannot be assessed as a HUF unless they have by mutual consent agreed to form a joint family.

(iv) Gift out of ancestral property: A Mitakshara Karta may make a gift of movable property of the family, out of love and affection, within reasonable limits. He can also make a gift of immovable properties, within reasonable limits for pious purposes; i.e., for charitable and religious purposes or to a daughter in fulfilment of a nuptial promise etc. However, a gift to a stranger is void. On the contrary, a Dayabhaga father can alienate ancestral property, both movable as well as immovable, by sale, gift, will or otherwise in the same way as he can dispose of his separate property.

3.11 POSITION UNDER HINDU SUCCESSION ACT, 1956

This Act came into force on and from 17th June, 1956. It lays down a uniform and comprehensive system of inheritance and applies to persons governed by the Mitakshara as well as the Dayabhaga Schools, superseding and abrogating all previous law or customs or usage having the force of law. Under this Act, the heirs of a male Hindu dying intestate on or after 17th June, 1956 are divided into three classes. Class I heirs get the right to the deceased's property simultaneously to the exclusion of all other Classes of heirs. Class II relations succeed only if there is no class I relation and, the heirs in the first entry of class II being preferred to heirs in the second entry, and so on, but heirs in any one entry taking in equal shares amongst themselves.

The students should note that Section 4 of the Hindu Succession Act, 1956 clearly lays down that "save as otherwise expressly provided in the Act, any text, rule or interpretation of Hindu Law or any custom or usage as part of that law in force immediately before the

commencement of the Act shall cease to have effect with respect to any matter for which provision is made in the Act.” And, Section 8 of the Hindu Succession Act, 1956, lays down the scheme of succession to the property of a Hindu dying intestate. The schedule classifies the heirs on which such property shall devolve.

The preferential heirs of class I are as under:

(1) Son (2) Daughter (3) Widow (4) Mother (5) Son/daughter/widow of a predeceased son (6) son/daughter of a predeceased daughter (7) Son/daughter/ widow of a predeceased son of a predeceased son.

A son's son is not mentioned as an heir under Class I of the schedule and, therefore, he cannot get any right in the property of his grandfather under the provision. The right of a son's son in his grandfather's property during the lifetime of his father which existed under the Hindu Law as in force before the Act, is not saved expressly by the Act and, therefore the earlier interpretation of Hindu Law giving a right by birth in such property 'ceased to have effect'.

Therefore, the property which devolves on a Hindu on the death of his father intestate after coming into force of the Hindu Succession Act, 1956, does not constitute H.U.F. property consisting of his own branch including his sons. [Shri VallabhdasModani v. C.I.T. (1982) 138, ITR, p. 673].

The Allahabad High Court's decision supra in the case of Shri VallabhdasModani v. Commissioner of Incometax was followed by the Andhra Pradesh High Court (1983, 144 ITR 18) and later approved by the Supreme Court in the case of Commissioner of Wealth-Tax v. Chander Sen (1986, 161 ITR 370) holding that it is not possible to say that when a son inherits the property in the situation contemplated by the Hindu Succession Act, 1956, he takes as Karta of his own undivided family.

3.12 COMPUTATION OF INCOME OF THE H.U.F.

The gross total income of the family for the relevant previous year shall be computed under the relevant heads (as per the provisions of the Income-tax Act) as it is computed for other assesseees. However, in this connection the following points are worth noting:

Clubbing of Income

(i) If the funds of a Hindu Undivided family are invested in a company or a firm, fees or remuneration received by the member as a director, or a partner in the company or firm may be treated as income of the family in case the fees or remuneration is earned essentially as a result of investment of funds. But, if the fees or remuneration is earned essentially for services rendered by the member in his personal capacity, the income shall constitute the personal income of the member.

(ii) For determining whether a particular income belongs to a member of the family or to his undivided family, the Supreme Court has enunciated certain principles. The question to be considered in such cases is, whether the remuneration received by the coparcener is in substance merely a mode of return made to the family because of the investment of the family funds in the business or whether it is a compensation for services rendered by the coparcener. If it is the former, it is an income of the HUF but if it is the latter it is the income of the individual. If the income was essentially earned as a result of the funds invested, the fact that a coparcener has rendered some service would not change the character of the receipt. But if, on the other hand, it is essentially a remuneration for the services rendered by the coparcener, the circumstances that his services were availed of because of the reason that he was a member of the family which had invested funds in that business or that he had obtained the qualification shares from out of the family funds would not make the receipt the income of the HUF. [Raj Kumar Singh HukamChandji v. CIT (1970) 78 ITR 33].

The Supreme Court's decision supra in the case of Raj Kumar Singh HukamChandji v. Commissioner of Income-tax has come to stay as one of the most followed/applied case laws. This decision had been followed by Patna (Full Bench), Allahabad, Bombay and Gujarat High Courts, applied by Andhra Pradesh, Madras, Kerala, Delhi, and Supreme Court itself. It would suffice to refer to the Supreme Court's decision in the case of Y.L. Aggarwalla and others v. Commissioner of Income-tax (1978, 114 ITR 471) holding that the share income was a return made to the family because of the investments of the family funds in the business and the share income was not the individual income of minor sons but was the income of the Hindu undivided family and had to be assessed in the hands of the family.

(iii) Where a member of a HUF is a partner in a firm on behalf of the family and on partition of the property of the family, the share in the firm is allotted to such a member, subsequent to such allotment when the firm settles its accounts the whole income for that year would be the income of the individual member and no part of the income would be added to the income of the family. [CIT v. Ashok Bhai Chiman Bhai (1965) 56, ITR, 42 (S.C.)].

(iv) The personal earning, including income from self-acquired property of a member of the HUF, even though he has sons, would not be included in the income of the family. Such income shall be assessed as income of that individual. [KalyanjiVithal Das v. CIT (1937) 5 ITR 90 (PC)].

(v) Any sum paid by an H.U.F to a member of the family out of its income is not deductible in computing the income of the family. However, such amount will not be included in the income of such individual whether the family had paid tax on its income or not [Section 10(2)].

(vi) If any remuneration is paid by the Hindu Undivided family to the karta or any other member for services rendered by him in conducting family's business, the remuneration is deductible if remuneration is (a) paid under a valid and bona fide agreement; (b) in the interest of, and expedient for, the business of family; and (c) genuine and not excessive. Jugal Kishore BaldeoSahai v. CIT [1967] 63 ITR 238 (SC).

(vii) If salary is paid by the Hindu undivided family to its karta for looking after its interest in firms in which it is partner through said karta, such salary is allowable as deduction - CIT v. Prakash Chand Agarwal [1982] 11 Taxman 55 (MP).

(viii) Income from 'stridhan' is not includible in the income of the family. Property derived by a woman from her father or brother or husband or any other relative either before or after her marriage is known as 'stridhan'.

(ix) If a member has converted or transferred without adequate consideration after December 31, 1969 his self-acquired property into joint family property, income from such property is not taxable in the hands of the family.

(x) Income from impartible estate is taxable in the hands of the holder of the estate and not in the hands of the Hindu undivided family. Though, the impartible estate belongs to the family, income arising therefrom belongs to the holder of the estate who is the senior most male member of the family. Income from impartible estate is taxable in the hands of the holder of the estate.

(xi) Personal income of the members cannot be treated as income of Hindu undivided family.

(xii) Under the Dayabhaga School of law, as stated in a preceding page, no son has any right in the ancestral property during the lifetime of his father. If, therefore, the father does not have any brother as a coparcener, income arising from ancestral property is taxable as his individual income.

List of deductions out of Gross total Income available to HUF

Deductions in respect of certain payments

- (i) Notified savings and investments u/s 80 C
- (ii) Payment of medical insurance premium u/s 80 D
- (iii) Maintenance including medical treatment of handicapped dependent u/s 80 DD
- (iv) Expenditure for medical treatment of specified disease or ailment u/s 80 DDB
- (v) Donations to certain funds or charitable institutions u/s 80 G
- (vi) Donation for scientific research or rural development u/s 80 GGA
- (vii) Contribution to political parties u/s 80 GGC

Deductions in respect of certain incomes.

- (i) Profits and gains from industrial undertakings engaged in infrastructure development u/s 80 IA

- (ii) Profits and gains from industrial undertakings engaged in development of special economic zones u/s 80 IAB
- (iii) Profits and gains from certain industrial undertakings from certain business u/s 80 IB
- (iv) Profit and gains from the business of hotel and convention centre in specified areas u/s 80 ID
- (v) Profits and gains from housing project [Section 80 IBA]
- (vi) Profits of certain undertakings in north eastern states u/s 80 IE
- (vii) Profits and gains from business of collecting and processing of bio- degradable waste u/s 80 JJA
- (viii) Deduction in respect of employment of new employees [Section 80 JJAA]
- (ix) Deduction in respect of wages paid to additional workmen
- (x) Interest on deposits in certain saving accounts u/s 80 TTA

Assessment of HUF – Certain important points

The hindu undivided family is a separate unit of assessment and is taxable through its manager or karta. A single person, male or female , does not constitute a family. The following rules are to be observed while making the assessment of hindu undivided family.

1. The share of income received by a member of HUF from the income of family is not be included in his individual income being exempted in the hands of the coparcener of HUF even though the family may not have paid the tax on such income . [Section 10 (2)]
2. The income received by a member from an asset which was previously owned by him but has been put into common pool of HUF shall remain as his individual income
3. Salary paid out of the fund of HUF to a member is allowed as the legitimate expenditure of the HUF , if the member has rendered some service to the HUF

4. A member can carry on any business in his own name and the income from such business shall be included in his individual total income. It is immaterial that the funds were provided by HUF.
5. Jain , sikh , Buddhist families are also treated as HUF.
6. A Gift of property to the wife out of the family property is a bonafide transfer and as such income from such property shall belong to the wife.
7. On the death of manager, the succeeding manager- not the member of family or wife, shall be his legal representative.
8. In case any HUF holds share in a company and any loan is advanced to members of HUF, it will not be deemed as dividend u/s 2 (22) (e) Because individual members are not shareholders of that company.

3.13 PARTITION OF A HINDU UNDIVIDED FAMILY (Section 171)

‘Partition’ signifies division of property. In the cases of property capable of physical division, share of each member is determined by making physical division thereof. It must be noted that a division of income without physical division of property does not amount to partition. Where, however, the property is not capable of physical division, partition implies such division as the property may admit.

- ***Who is entitled to share on partition***

Though only coparceners can demand partition, once the partition takes effect, the following persons are entitled to a share:

- (a) All coparceners;
- (b) A son in the womb of his mother at the time of partition;
- (c) Mother, who gets an equal share if the partition takes place among her sons after the death of her husband; and
- (d) Wife, who gets a share equal to that of a son at the time of a partition between father and sons.

- ***Assessment after partition (Section 171)***

A joint family, once assessed as a HUF, continues to be assessed as such till one or more coparceners claim partition. Such claim must be made by the coparceners before the assessment of the income of the HUF for the relevant assessment year is completed. On the receipt of such a claim, the Assessing Officer must make an inquiry after giving due notice to the members and record a finding whether there has been a partition and, if so, the date of the partition. The income of the family from the first day of the previous year to the date of partition is assessed as income of the HUF and from the next date of the partition to the date of close of the previous year, as the individual income of the recipient-members. If the recipient member forms another HUF along with his wife and son(s), the income of the property which was subject to partition is chargeable to tax in the hands of the new H.U.F.

- ***A partition of the HUF can be both total and partial***

Where the entire joint family property is divided among all coparceners and the family ceases to exist as an undivided family, the partition is total. A partial partition may be as regards: (a) the persons constituting the joint family, or (b) the properties belonging to the joint family, or (c) both. The device of partial partition has been used as a medium for reduction of proper tax liability. To curb such a practice, the Finance (No. 2) Act, 1980 inserted Sub-section 9 in Section 171 which lays down that partial partitions of HUFs effected after 31st Dec., 1978 will not be recognised for tax purposes.

The provisions made by Sub-section (9) in Section 171 are as follows:

(i) In a case where a partial partition of a HUF has taken place after 31.12.1978, no claim of such partition will be enquired into and the Assessing Officer will not record a finding as to whether there has been a partition of the family property. Further, any finding regarding partial partition recorded under Section 171(3) will be null and void and of no legal effect.

(ii) Such family will continue to be assessed as if no such partial partition has taken place, i.e., the property or source of income will be deemed to continue to belong to the Hindu undivided family and no member will be deemed to have separated from the family.

(iii) Each member or group of members of such family will be jointly and severally liable for any tax, interest, penalty, fine or other sum payable under the Act by the family, whether before or after such partition. The several liability of any member or group of members of such family will be computed according to the portion of the joint family property allotted to him on such partial partition. This amendment has come into force with effect from April 1, 1980 and has, accordingly, been applicable with effect from assessment year 1980-81 and onwards.

Residence of HUF

Resident [Section 6 (2)]: A hindu undivided family shall be resident in India in a previous year in all cases except when control and management of its affairs is wholly situated outside India. In other words, if even a small part of control of management is situated in India it will be a resident Hindu undivided family

Non – Resident [Section 2 (30)]: A HUF is said to be non- resident of India for any previous year if it is not a resident as per section 6 (2). In other words, if the control and management of the affairs of a HUF is situated wholly outside India it is non- resident Hindu Undivided Family.

Not Ordinary Resident: A hindu undivided family can claim the status of ‘Not ordinary resident’ if the karta (Manager) of HUF can prove that:

- (a) He was not a resident of India for 9 out of 10 Previous years exceeding the relevant previous year or
- (b) He was not in India for a period totaling 730 days or more during 7 previous years preceding the relevant previous year.

Applicability of alternate minimum tax (AMT) On HUF [W.E.F A.Y 2013-14][Section 115JC TO JF]

The finance act, 2011 , introduced the concept of alternate minimum tax on limited liability partnership. However, the finance act, 2012 has extended the system of alternate minimum tax on all persons other than a company subject to certain conditions. Thus, w.e.f assessment year 2013-14, alternate minimum tax is applicable on HUF's also.

HUF's covered under AMT [section 115 JEE (1)]

The provisions of alternate minimum tax shall apply to a HUF:

1. Which has claimed any deductions Under:
 - (a) u/s 35 AD or
 - (b) any deductions other than section 80P included in chapter VI-A under the heading C- Deductions in respect of certain incomes[i.e., u/s 80 IA to Section 80 RRB] or
 - (c) Section 10 AA(SEZ); and
2. Whose adjusted total income exceeds Rs 20 lakhs.

HUF's not covered under AMT

The provisions of alternate minimum tax shall not apply to a HUF whose Adjusted total income does not exceed Rs 20 Lakh.

Scheme of AMT

Where the regular income tax payable by HUF for a particular previous year is less than the alternate minimum tax payable for such previous year, the adjusted total income shall be deemed to be the total income of such HUF for such previous year and it shall be liable to pay income tax on such total income @ 18.5%.

Thus, AMT is an alternate amount of tax which a hindu undivided family has to pay if the regular income tax for any previous year is less than 18.5 % of its adjusted total income as defined for this purpose. Section 115 JC is an overriding section and provides a specific tax rate on a specific figure for certain HUF's. It provides a new concept of Adjusted total income for HUF's which is to be treated as total income of the HUF and On this total income, tax is required to be calculated @ 18.5 % . This tax is called Alternate minimum tax . AMT has brought into tax net those HUF's which were earning profits but were not paying any income tax due to various deductions or exemptions available to them under the income tax act, 1961

Ultimate Tax liability of HUF.

- (i) Regular income tax payable as per normal provisions of IT act, or

- (ii) Tax @ 18.5 % on adjusted total income.

Whichever is higher.

Note: In the case of a unit located in an international financial service centre (IFSC) Which derives its income solely in convertible foreign exchange, AMT shall be charged at a concessional rate of 9 % [w.e.f. A.Y. 2019-20]

Surcharge: Surcharge on AMT for A.Y 2019-20 Shall be as under:

- (i) If adjusted total income does not exceed Rs 50 lakhs.
- (ii) If adjusted total income exceeds Rs 50 lakhs but does not exceed Rs 1 crore.
- (iii) If adjusted total income exceeds Rs 1 Crore.

Meaning of Regular income tax [Section 115 JF (d)]

It means the income tax payable for a previous year by a hindu undivided family on its total income in accordance with provisions of IT act, 1961 Other than the provisions of this chapter XIIB.

Meaning of Adjusted Total Income [Section 115 JC (2)]

Adjusted total income means the total income before giving effect to this newly inserted chapter XII BA as increased by:

- (i) Deductions claimed under any sections included in chapter VI-A Under the heading C – Deduction in respect of certain incomes except section 80 P and
- (ii) Deduction claimed , if any, u/s 10 AA.
- (iii) Deduction claimed u/s 35 AD less depreciation allowable u/s 32 on the cost of that asset.

3.14 SUMMARY

An income tax is a tax imposed on individuals or entities (taxpayers) that varies with the income or profits (taxable income) of the taxpayer. Details vary widely by jurisdiction. Many jurisdictions refer to income tax on business entities as companies tax or corporate tax. Income tax generally is computed as the product of a tax rate times taxable income.

The tax rate may increase as taxable income increases (referred to as graduated rates). Taxation rates may vary by type or characteristics of the taxpayer. Capital gains may be taxed at different rates than other income. Credits of various sorts may be allowed that reduce tax. Some jurisdictions impose the higher of an income tax or a tax on an alternative base or measure of income.

Individual income tax is a subject matter of central govt. If an individual want to assess his/her income tax then he/she should have knowledge of individual income tax structure. Individuals after calculating their total income for a particular financial year can assess their income tax after deduction of saving and doing other adjustments. By doing so they can plan in advance about their savings and income tax.

Income tax is levied on an assessee's total income. Such total income has to be computed as per the provisions contained in the Income-tax Act, 1961. The procedure of computation of total income for the for the purpose of levy of income tax starts with the determination of residential status of Individual. The residential status of a person has to be determined to ascertain which income is to be included followed by the classification of income under various heads. The Act prescribes five heads of income. These heads of income exhaust all possible types of income that can accrue to or be received by an individual. An individual has to classify the income earned by him under the relevant head of income then exclusion of exempted income takes place as there are certain incomes which are wholly exempt from income tax e.g., income from mutual fund. These incomes have to be excluded and will not form part of GTI. The balance income over and above the prescribed limits would enter computation of total income and have to be classified under the relevant head of income. After the calculation of GTI under each head, net income under each head is computed and then incomes are clubbed and if there is some losses which are to be setoff and forwarded are accordingly dealt with. After following all these steps we compute Gross Total Income, deduction from Gross Total Income and the finally computation of total income takes place.

A joint family or undivided family is an extended family arrangement prevalent throughout the Indian subcontinent, particularly in India, consisting of many generations living in the same household, all bound by the common relationship.

Historically, for generations India had a prevailing tradition of the joint family system or undivided family. The system is an extended family arrangement prevalent throughout the Indian subcontinent, particularly in India, consisting of many generations living in the same home, all bound by the common relationship. A patrilineal joint family consists of an older man and his wife, his sons and daughters and his grandchildren from his sons and daughters.

The family is headed by a senior person called a karta, usually the oldest male, who makes decisions on economic and social matters on behalf of the entire family. The patriarch's wife generally exerts control over the household and minor religious practices and often wields considerable influence in domestic matters. Family income flows into a common pool, from which resources are drawn to meet the needs of all members, which are regulated by the heads of the family. However, with urbanisation and economic development, India has witnessed a break up of traditional joint family into more nuclear-like families, and the traditional joint family in India accounted for a small number of Indian households

A Hindu undivided family or HUF is a legal term related to the Hindu Marriage Act. The female members are also given the right of share to the property in the HUF. The term finds reference in the provisions of the Income Tax Act, but the expression is not defined in the act. There are various aspects of Hindu law relevant for the purpose assessment of income and wealth in the status of HUF, as well as the impact of the provisions of Hindu Succession Act 1956 as amended by Hindu Succession (Amendment) Act 2005 relevant for the purpose of assessment of income and wealth in the status of HUF under the Income Tax Act 1961.

In the case of Surjit lal Chhabra 101 ITR 776 SC, joint family and undivided family are synonymous: "A joint Hindu family consists of persons lineally descended from a common ancestor and includes their wives and unmarried daughters. The daughter, on marriage, ceases to be a member of her father's family and becomes a member of her husband's family."

In 2016, a judgment of the Delhi High Court ruled that the eldest female member of a Hindu Undivided Family can be its "karta" (manager)

ILLUSTRATION 1

A HUF with more than one coparcener entitled to claim partition, owns a property which is let out at Rs. 600 per month per unit. The property consists of ten identical residential

units. Following deductions are claimed by the HUF including the expenses on tenant's amenities.

Municipal rental Value for ten units(annual)	60,000
Municipal taxes	4200
Lift Maintenance	2000
Water pump expenses	800
Actual expenses on repairs	8000
Renovation to the property during the year	50,000
Edu. Cess levied by the state Govt.	2000
Rent collectors salary per month	200
Interest on loan taken against mortgage of the property but The money was actually used in the business of the HUF	5000
The income from business for the assessment year 2019-20	2,10,000

(After charging interest on loan)

A lottery ticket of 100 Rs. Was purchased out of family funds on the name of HUF and it won a prize of Rs. 100000. The Karta has acquired a shop out of his own savings which he gifted to his wife. Shop has an annual income of Rs 24000.

Compute the HUF's total income and tax payable for the assessment year 2019-20.

SOLUTION 1

Computation of total income of HUF

Income from House Property	Rs	Rs
Rental value of 10 units for 12 months	72,000	
Less: Cost of facilities borne by the owner:		
Lift maintenance	2000	

Water pump expenses	800	2,800
Annual Rent		69,200
Or		
Municipal Rental Value		60,000
Whichever is higher is ARV		69,200
Less: Municipal taxes		4,200
Net Annual Value		65,000
Ded. u/s 24		19,500
Standard deduction= 30% of NAV		45,500
Profits and gains: Business Profit		2,10,000
Other Sources: Lottery		1,00,000
GTI as Total Income		3,55,500
Computation of tax:		
Tax on lottery income (30% of 1,00,000)		30,000
Tax on other income(3,55,500 - 1,00,000)= 2,55,500		
On 2,50,000		Nil
On 5,500 @ 5%	275	275
Tax		30,275
Add: Health and Edu. Cess @2 4% of Tax		1,211
Total Tax		31,486
Total tax rounded off Rs. 31,490		

ILLUSTRATION 2

The following particulars have been submitted by ram Lal in the capacity of Karta of a HUF for assessment purposes:

- a) Profit from families' business, Rs. 25000 after charging an amount of Rs. 60,000 given as salary to Karta's brother who has been actively participating in it.
- b) Salary income of Kartas another brother who is manager in a cooperative bank Rs. 11000 p.m.
- c) Directors fees received by Karta Rs. 5000(HUF holds 20% shares in this company).
- d) Bank interest on fixed deposits 24000.
- e) Long term capital gain from the transfer of building 28000.
- f) Long term capital gain from the transfer of investment 40000.
- g) Donation to a college which is an approved institution 40000.
- h) Rental value of the property let 36000.
 - Municipal taxes paid in respect of the house 4500.
 - Interest on loan taken for repair of house 12000.

You are required to calculate total income and tax liability of the family for the assessment year 2019-20.

SOLUTION 2:

Computation of income of HUF managed by Karta Ram Lal.

I. Income from house property:	Rs.	Rs.
Annual rental Value	36000	
Less: Municipal taxes	4500	
N.A.V	31500	
<i>Less: Ded. U/s 24:</i>		
30% of NAV	9450	

Interest on loan	12000	21,450
		10,050
II. Profits and gains of business and profession:		
Profit from family business		250,000
III. Capital Gain: Long Term		
Transfer of building	28000	
Transfer of other assets	40000	68,000
IV. Income from other sources:		
Bank interest (fixed deposit)	24000	
Directors remuneration (assumed as HUF income)	5000	29000
Gross Total Income		3,57,050
Ded. U/s 80:		
80G: Donation 40000: Q.A restricted to 10% of G.T.I		
[357050-68000=289050]		
Q.A 28905 Rate 50%		14453
Total Income		342,597
Rounded off to Rs. 342600		
Tax Liability:		
Total Income = 342600		
Tax on long term capital gain (68000@ 20%)		13600
On balance income (342600-68000) = 274600		
Tax on Rs. 250000	Nil	
On balance Rs. 24600 @ 5%	1230	1230
Tax		14830

Tax Payable**15,423**

Tax payable rounded off Rs. 15,420

ILLUSTRATION 3

Mr. K. Ramanna is Karta of HUF consisting of Himself and his two brothers. He furnishes the following particulars of Income.

- (i) Mr. V. Ramanna, Karta younger brother, is manager of M/s steel ltd. And he received Rs 120,000 as salary.
- (ii) The family business profit was Rs 444,000. Mr. K. Ramanna is member of an AOP in the representative capacity and his $\frac{1}{2}$ share of profits received from such AOP is Rs 4,000. Mr. D. Ramanna, 3rd brother, is a lawyer and his professional income is Rs 10,000.
- (iii) The family has an ancestral house whose rental value is Rs 21,000 p.a. Another house, which was bought in the name of Mr. D Ramanna out of family funds has annual letting value of Rs 9,000. Taxes Paid in the respect of these houses are Rs 2,100 and Rs 900 respectively.
- (iv) Rs 60,000, 8% Debentures of a company Purchased by Mr. V. Ramanna out of his salary savings and Rs 9,000 received as net interest on debentures (Listed) of a company which were purchased out of family funds.
- (v) Dividend of Rs 5,000 Received by Mr. K. Ramanna out of her stridhan and interest on Govt. securities Rs 4,000 and securities were purchased out of family funds.

Calculate the total income of the HUF for A.Y 2019-20

Solution 3**Income from house property**

Let out Annual Rental Value	9,000	
Less: Municipal taxes	900	
NAV	<u>8,100</u>	
Standard deduction : 30 % of NAV	<u>2,430</u>	
Income from let out house	<u>5,670</u>	
Self occupied house		
NAV	Nil	5,670
Profit and Gains of business or profession		
Profits from family business		444,000
Income from other sources:		
Interest on Govt. securities	4,000	
Interest on debentures – Listed Net 9,000		
Gross (9,000 X 100 / 90)	<u>10,000</u>	14,000
Gross total income		<u>463,670</u>
Less: Deductions u/s 80		<u>Nil</u>
Total income		<u>463,670</u>

ILLUSTRATION 4

Sanjay chopra , his two brothers and major son constitute an HUF and the following statement of income has been submitted by them for assessment purposes:

- (1) Profits from business carried on by the karta in the account and on behalf of HUF Rs 180,000 after deducting Rs 6,000 paid to vijay a member of the HUF for working as travelling salesman and Rs 20,000 paid to sanjay chopra for managing the affairs of the business
- (2) The family owns a house with the rental value of RS 10,000 , Local charges in respect of this being Rs 500 . It is used for Residence of the family. Mr. chopra has created a charge on this house for payment of Rs 5,000 P.a to his sister. Fire insurance premium paid is Rs 100 and theft insurance Rs 200
- (3) The HUF sold another house for Rs 11,50,000 on 10th april, 2018 (Cost inflation index in 2018-19 was 280) which was acquired in 1955. Its fair market value on 1st april, 2001 was Rs 420,000 [CII for 2001-02 was 100]

- (4) Loss of stock in trade occasioned by enemy action Rs 5,000 not charged earlier.
- (5) Sanjay chopra wins a prize of Rs 50,000 in rajasthan state lottery and claims it as his personal winnings. It is on record that the ticket was brought in his name though the rupee has been spent from the cash box of the business
- (6) Dividend on units of mutual fund Rs 5,000 (Gross) . Interest credited in saving bank a/c Rs 15,000 and interest on debentures Rs 10,000 and interest on govt. securities held by family was Rs 9,000

Compute total income of the family for the assessment year 2019-20 giving sufficient explanation for each item.

Solution V

Computation of total income

Income from house property		
Self occupied house		
NAV		Nil
Profits and gains		
Profit from family business	Nil	
Less: loss of stock in trade due to enemy action		175,000
Capital gains	180,000	
Sale of long term residential house	<u>5,000</u>	
Less: Indexed cost [420,000 x 280/100]		26,000
Long term capital loss to be C/F	11,50,000	
Income from other sources	<u>11,76,000</u>	
Dividend on units of mutual funds – exempted		
Interest on debentures		
Bank interest- savings	Nil	
Interest on govt. securities	10,000	34,000
Gross total income	15,000	<u>209,000</u>
Less: Deduction u/s 80 TTA	<u>9,000</u>	<u>10,000</u>
Total income		<u>199,000</u>

3.15 GLOSSARY

- Individual includes both male and female assesseees. The total income has to be computed as per the provisions of the Income-tax Act, 1961. In addition to individuals own income, income of other persons received by him in some other capacity or received by other persons is to be clubbed with individual assesseees income. Following steps are considered for computing total income and to charge tax.
- The term ‘Hindu undivided family’ has not been defined in the Income-tax Act. However, in general parlance it means an undivided family of Hindus. Creation of a HUF is a God-gifted phenomenon. As soon as a married Hindu gets a child, a new HUF comes into existence. It is not at all necessary that every HUF must have joint property or family income.
- A Hindu Joint Family consists of Coparceners & members.
- The gross total income of the family for the relevant previous year shall be computed under the relevant heads (as per the provisions of the Income-tax Act) as it is computed for other assesseees.
- ‘Partition’ signifies division of property. In the cases of property capable of physical division, share of each member is determined by making physical division thereof. It must be noted that a division of income without physical division of property does not amount to partition.
- Income tax has to be paid by every individual person, Hindu Undivided Family (HUF), Association of Persons (AOP), Body of Individuals (BOI), corporate firms, companies, local authorities and all other artificial juridical persons that generate income.
- Coparceners: The lineal male descendants of a person upto the third generation of such person are known as coparceners. The coparceners acquire, on birth, ownership in the ancestral properties of such ascendant and have a right to claim partition of such property at any time.
- Hindu Succession Act, 1956: This Act came into force on and from 17th June, 1956. It lays down a uniform and comprehensive system of inheritance and applies

to persons governed by the Mitakshara as well as the Dayabhaga Schools, superseding and abrogating all previous law or customs or usage having the force of law.

- **Karta:** Property of the family is ordinarily managed by the father or other senior member for the time being of the family. He is called Karta. However, the senior member may give up his right of management and a junior member may be appointed as Karta with the consent of all other members. [Narendra Kumar J. Modi v. CIT (1976) 105, ITR, 109 (S.C.)].
- Where a member of a HUF is a partner in a firm on behalf of the family and on partition of the property of the family, the share in the firm is allotted to such a member, subsequent to such allotment when the firm settles its accounts the whole income for that year would be the income of the individual member and no part of the income would be added to the income of the family

3.16 SELF-ASSESSMENT QUESTIONS

1. Discuss the concept of Individual assessee?

2. Discuss the meaning of Hindu Undivided Family?

3. Explain the need and importance of Assessment?

4. List the steps to be followed while computing Total income of the assessee?

5. What are the steps to be considered for computing total income and to charge tax?

6. What do you mean by Partition of a Hindu undivided family? Who is entitled to share on partition?

7. List the Income of other persons to be included in the total income of an individual?

8. What is Karta?

9. Explain the various steps to be followed while computing the taxable income of Hindu Undivided Family?

3.17 BOOKS RECOMMENDED

1. Dr. V.K. Singhania: Students Guide to Income-tax; Taxmann Publications Pvt. Ltd., New Delhi.
2. Girish Ahuja and Ravi Gupta: Systematic Approach to Income-tax and Sales-tax; Bharat Law House, New Delhi.
3. Dr. H.C Meharotra and Dr S. P Goyal: Income Tax Law and Accounts; Sahitya Bhavan Publications.
4. V. P Gaur & D. B Narang: Income Tax Law & Practice; Kalyani Publishers.
5. V. K Singhania & Kapil Singhania: Direct Taxes Law & Practices; Taxman Publications.
6. Mahesh Chandra, D. C Shukla, K. A Mahajan & M. A Shah: Income Tax Law & Practices; pragati Publication, New Delhi.
7. Arvind Tuli & Dr. Neeru Chadda: Conceptual Clarity on Income Tax and Wealth Tax; Kalyani Publication, New Delhi.

**ASSESSMENT OF FIRMS AND ASSOCIATION OF PERSONS
INCLUDING COMPUTATION OF TAX LIABILITY**

STRUCTURE:

- 4.1 Introduction
- 4.2 Objective
- 4.3 Taxation of Firms
- 4.4 Scheme of taxation of a firm and its partners
- 4.5 Change in Constitution of a Firm (Section 187)
- 4.6 Losses of Registered Firms (Section 75)
- 4.7 Succession of one firm by another firm (Section 188)
- 4.8 Computation of income on estimated basis in case, taxpayers are engaged in certain business
- 4.9 Other Provisions relating to Limited Liability Partnership
- 4.10 Alternate Minimum Tax (AMT) (Section 115JC)
- 4.11 Association of Persons
- 4.12 Formation of an Association of Persons
- 4.13 Tax Liability of Association of Persons

4.14 Method of Computing Share of a Member of Association of Persons, etc. (Section 67A)

4.15 Tax on Income of association of persons, etc. which is indeterminate or unknown.

4.16 Share of a member of association etc. (Section 86)

4.17 Summary

4.18 Glossary

4.19 Self-Assessment Questions

4.20 Books Recommended

4.1 INTRODUCTION

Assessment is the act of judging or deciding the amount, value, quality, or importance of something, or the judgment or decision that is made. It is a procedure used by government assessors to determine the value of a property, or the income of a person or entity, in order to charge taxes or to levy on the orders of a court. In other words it is a value calculated as the basis for determining the amounts to be paid or assessed for tax or insurance purposes. A tax assessor is responsible for preparing and maintaining the assessment roll, the tax roll and collecting the tax levies in accordance with the quality standards.

The core service responsibilities include:

- Preparing annual market value assessments for all properties.
- Preparing the business assessment valuations for all business premises.
- Maintaining accurate property information and ownership on all realty accounts.
- Maintaining accurate business information and ownership on all business accounts.
- Defending assessments before municipal and provincial assessment tribunals.
- Responding to inquiries and requests for information related to assessment and taxation.
- Producing and mailing annual assessment and tax notices to tax payers.
- Reporting assessment rolls and meeting annual audits.

A partnership firm is a separate entity in the eyes of income tax department. It is so because the definition of the term 'person' given under section 2(31) also includes 'firm'. Though the income earned by firm is the joint income of the partners yet such income is taxable as the income of the firm. A firm is liable to pay tax at a flat rate (on normal income as well as on certain special incomes) without any basic exemption limit (as is there in case of individual and Hindu Undivided Family).

In this lesson the Income Tax Treatment with relation to Firms and Associations of Persons is being discussed. The tax implications, rates of tax and other issues relating to the above persons have been discussed elaborately. With regard to firms the focus is on partnership firms or Limited liability partnerships.

4.2 OBJECTIVE

At the end of this lesson, you will learn

- What is partnership firm
- What are the tax implications in the hands of partners and firm
- What are admissible expenses/inadmissible expenses while calculating the book profit of the firm.
- What are the provisions of Alternate Minimum Tax
- What do you mean by Association of Person.
- How Association of persons is formed
- What is the method of computation of share of a member of AOP?

4.3 TAXATION OF FIRMS

Under Section 2(23) of the Income-tax Act, the terms "firm", "partner", and "partnership" have the meanings respectively assigned to them in the Indian Partnership Act, 1932 and Limited Liability Partnership Act, 2008.

The expression "partner" also includes a minor who has been admitted to the benefits of partnership and a partner of a Limited Liability Partnership Act 2008. However

a minor cannot validly enter into any partnership as a 'full partner' with other persons but he can be admitted to the benefits of partnership only.

A joint Hindu family as such cannot be a partner in a firm. However, through its Karta it may enter into a valid partnership with a third person or with a member of the undivided family in his individual capacity. In such a case, the Karta occupies a dual position. On the partnership he functions in his individual capacity; on the relations to other members of the Hindu undivided family, in his representative capacity.

An incorporated company being a legal person may form a partnership with an individual or with another company. In considering the maximum number of partners comprising a firm, the company will be considered as one person only.

A partnership firm as such is not entitled to enter into a partnership with another firm, H.U.F., individual, or a company. However, its partners in their individual capacity can enter into another partnership.

A partnership firm including LLP is a separate entity in the eyes of income tax department. It is so because the definition of the term ' person ' given u/s 2 (31) also includes ' firm ' including LLP. Though the income earned by firm/ LLP is the joint income of the partners yet such income is taxable as the income of the firm/LLP . A firm/LLP is liable to pay tax at the flat rate on normal income as well as on certain special income without any basic exemption limit as there in case of individual and HUF.

Partnership [Section 2 (23) (iii)] Partnership shall have the meaning assigned to it in the Indian Partnership Act, 1932 and shall include a limited liability partnership as defined in the LLP act, 2008.

Meaning of partnership , Partner and Firm under Indian Partnership Act , 1932

Section 4 of the Indian Partnership Act has defined the word ' Partnership ' as " the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all " .

From this definition , the following points emerge:-

- That partnership is an association of two or more persons.

- There must be an agreement entered into by all persons.
- The agreement is to carry on some business or profession.
- The business to be carried on by all or by any one of them acting on behalf of all and for the benefit of all.
- The agreement is to share the profits and losses of business or profession.

The term 'partner' is defined as any person who has entered into partnership . Partners entering into a contract with one another are called individually as partners and collectively a firm and the name under which their business is carried on is called the firm's name. The word ' partner ' shall also include any person who being a minor has been admitted to the benefits of partnership.

The term firm means the entity which comes into existence as a result of partnership agreement.

Limited Liability Partnership [LLP]

'Limited Liability Partnership' (LLP) is a corporate form of partnership having separate legal entity which is distinct from its partners and carries limited liability for them. It is a new form of business organization brought into existence by the limited liability partnership act, 2008, which is applicable in the whole of India.

Features of Limited Liability Partnership [LLP]

- 1- LLP is a body corporate under the LLP act, 2008.
- 2- LLP has a separate legal entity.
- 3- LLP shall have perpetual succession.
- 4- LLP is not covered by the Indian partnership act, 1932.
- 5- LLP is incorporated by the registration of ' incorporation document ' with the registrar of the state in which the registered office of the LLP is to be situated.
- 6- The liability of the partners of LLP is limited.

Necessity of have separate PAN:

A Partnership firm/LLP is required to have its own separate 'Permanent Account Number' (PAN) which will be different from the permanent account number of the partner (s) if any. The PAN of firm/LLP bears its name and is used for filing return of income of the firm. It is important to note that the individual income of the partner (s) shall not be clubbed with the income of the firm/LLP.

The share of income received by partners from the firm is exempt in the hands of partners and hence is not included in their individual income. Under Income Tax act, a partnership firm can be of following two types:

A) A Firm/LLP which fulfills conditions prescribed u/s 184

- (i) It has submitted its partnership deed (Instrument of Partnership).
- (ii) Such deed must show the respective share of each partner.
- (iii) It is duly signed by all partners except a minor partner.
- (iv) It is submitted along with its return for the assessment year 1993-94. In case of firms coming into existence after 1-4-1993 it is to be submitted along with their first return.
- (v) In case there is any change in the profit sharing ratio a revised deed must be submitted.
- (vi) The firm should not have been assessed to tax u/s 144 i.e., best judgement assessment.

B) A firm /LLP which does not fulfill the conditions prescribed u/s 184

As given above or it is firm which fulfills conditions given u/s 184 but has been assessed to tax u/s 144

Instrument of partnership

It is the written partnership agreement entered into by partners. It has to be signed and certified by all the existing partners except minors. In case firm has been dissolved before filing or return of income, it should be signed by all those persons who were partners in the firm immediately before its dissolution and in case partner has died the instrument must be signed by his legal representatives immediately before its dissolution as in case partner has died the instrument must be signed by his legal representative. For a limited liability partnership the instrument of partnership is known as incorporation document filed with the registrar.

When instrument of partnership is to be submitted ?

The section 184 (2) of the act provides that a certified copy of the instrument of partnership must accompany the return of the income of the firm of the previous year relevant to the assessment year 1993-94 or the assessment year in respect of which assessment as a firm is first sought.

Effect of best judgment assessment

Where in respect of an assessment year there is on the part of a firm any such failure as is mentioned in section 144 and such firm is subjected to best judgement assessment, the firm shall be assessed in the same manner as given below for firms which fails to fulfill conditions prescribed u/s 184 [Section 184 (5)].

Treatment if conditions prescribed u/s 184 are not fulfilled [section 185]

In case a firm does not comply with the provisions of section 184 for any assessment year, the firm shall be assessed in the same manner as given above but

- (a) It shall not be allowed to deduct remuneration as allowed u/s 40 (b)
- (b) Full amount of interest on capital paid to partners is disallowed.
- (c) The amount of remuneration and interest shall not be added in the individual income of partners.
- (d) The firm shall pay tax in the same manner as in case of firm, which fulfils conditions prescribed u/s 184.

Firm dissolved or business discontinued.

Where any firm is dissolved or business is discontinued, the firm shall be assessed by the assessing officer on its total income as if no such discontinuance or dissolution had taken place. The notices may be issued in the name of the dissolved firm and the assessment be made in the name of the discontinued firm [section 189 (1)].

In case during the proceedings before assessing officer, or the commissioner (Appeals) the firm is found guilty of any acts as given u/s 271 to 275 , the penalty can be imposed on such firms [section 189 (2)].

Every person who at the time of such discontinuance or dissolutions was a partner of the firm or the legal representative of any such person who is deceased , shall be jointly and severally liable for the amount of tax, penalty and any other sum payable under the provisions of this act. [Section 189 (3)

Where such discontinuance or dissolution takes place after any proceedings in respect of an assessment year have commenced the proceedings may be continued for the persons referred above from the stage at which they stood at the time of such dissolution or discontinuance [Section 189 (4)]

4.4 SCHEME OF TAXATION OF A FIRM AND ITS PARTNERS

Assessment as a Firm (Section 184)

Computation of Firm's business income:

Adjustment of net profit as per profit and loss account of the firm:

- (a) While calculating firm's business profit, the provisions as given u/s 28 to 44 are applicable.
- (b) Section 40 (b) lays down following rules regarding payment of salary , commission or remuneration to working partners and interest on capital on all partners. These rules are as follows:
 - (i) Any payment of salary , commission or remuneration paid to a partner who is not a working partner, is disallowed.

- (ii) Any remuneration paid to a working partner, who is not authorized by or which is not in accordance with terms of partnership deed (Instrument of partnership) is disallowed.
- (iii) Any interest paid to partners according to terms of partnership deed is allowed provided rate of interest does not exceed 12 % . Excess is disallowed.
- (iv) Any interest paid to partner , who is not authorized by or is not in accordance with partnership deed is disallowed.
- (v) In case interest or remuneration is paid to a partner and is authorized by partnership deed but relates to the period prior to the date of such deed and it was also not authorized by any earlier deed, it shall be disallowed.

In case any payment for remuneration is made to one or more working partners during the previous year, it is allowed up to limits given below. Excess is diallowed.

Limits on payment of remuneration to working partners.

<i>Finance Act, 2009 provides for uniform limits for both professional firms and non-professional firms:</i>	
<i>I. On the first Rs. 3,00,000 of the book-profit or in case of a loss</i>	<i>Rs. 1,50,000 or 90% of the book-profit, whichever is more</i>
<i>II. On the balance of the book-profit</i>	

Meaning of Book Profit [Explanation 3 to section 40(b)]

Book-profit” means the net profit, as shown in the profit and loss account and make the additions and deductions as per section 28 to 44D explained under the head income from Business and Profession increased by the aggregate amount of the remuneration paid or payable to all the partners of the firm if such amount has been deducted while computing the net profit. Interest paid/payable to partners in excess of 12% shall also be disallowed as per section 40(b).

Certain explanations

1. In case an individual is partner in a representative capacity for the benefit of another person, such partner is called partner in representative capacity and the other person is called person so represented.
2. Any interest paid to partner in representative capacity shall be subject to aforesaid limits but any interest paid to him in his individual capacity (As creditor) Shall not be subject to above mentioned limits.
3. Any interest paid to an individual (Who is neither partner in representative capacity nor in personal capacity) and he on behalf of or for the benefit of any other person receives such interest, it shall not be subject to the aforesaid limits.
4. The term book profit means the net profits as shown in the P/L a/c for the relevant previous year computed according to provisions given u/s 28 to 44 D of the act and after adding back the full amount of remuneration given to partners.
5. The term working partner means an individual who is actively engaged in conducting the affairs of the business or profession of the firm of which he is a partner.

Allowable remuneration to working partners in case of loss to a firm

In case there is a loss to a firm or book profit is less and actual remuneration given to working partners is more than Rs 150,000 , then a maximum of Rs 150,000 shall be allowed to be deducted out of book profit.

4.5 CHANGE IN CONSTITUTION OF A FIRM (Section 187)

Change in constitution.

When a firm is assessed as firm for any assessment year it shall be assumed in same capacity for every subsequent year unless there is change in the constitution of firm or in the share of partners as evidenced by the instrument of partnership submitted along with the return for first assessment. [section 184 (3)]

In case any change has been taken place during the previous year the firm shall furnish a certified copy for the previous year in which such change takes place. In such case the firm will continue to be assessed as firm. [Section 184 (4)]

Meaning of change in constitution [Section 187]

In following , two circumstances a change can occur in the constitution of firm:

1. If one or more of the partners cease to be partners one or more partners quit or retire from the firm or one or more new partners are admitted but one or more of the old partners are still continuing with the firm after the change.
2. Where all the partners continue with a change in their respective shares or in the shares or in the share of some of the firm.

In other words, if during the previous year one or more persons but not all have retired or one or more partners have joined the partnership firm or there is a change in the profit sharing ratio of the partners, it amounts to a change in the constitution of the firm.

Computation of total income of a firm/ LLP

1. Income is computed headwise. Firm cannot have salary income.
2. It cannot have self occupied house, income from let out house property is computed in same manner as already studied under the head ‘ house property’.
3. Profits and gains income computed as per rules
4. Income under the head capital gains is computed in same manner with no exemption u/s 54, 54 B , 54 F
5. Income from other sources is computed in same manner.
6. Carry forward and set off of losses is done in the same manner.
7. Deductions out of gross total income ; A firm can claim following deductions.

u/s 80 G

For donations

u/s 80 GGA

For contribution to certain funds

u/s 80 GGC	For donation to political parties.
u/s 80 IA	For infrastructure projects.
u/s 80 IAB	For setting up special economic zones.
u/s 80 IB	For new industrial undertaking.
u/s 80 IBA	For profits and gains from housing projects.
u/s 80 IC	For setting up industry in backward states
u/s 80 ID	For setting up hotel or convention centre
u/s 80IE	For undertakings in north –eastern state
u/s80JJA	For use of bio waste
u/s 80 JJAA	For employment of new employees

Tax rates applicable to firm including LLP for assessment year 2019-20

- (1) It Pays tax at flat rate of 30 % with no exemption limit.
- (2) On LTCG – Rate of tax is 20%
- (3) On LTCG- sale of shares (STT Paid) As per section 112 A
- (4) On STCG- on securities covered under STT – Rate of tax is 15 %
- (5) On winnings from lotteries, crossword puzzle, races, card games, gambling and betting- rate of tax is 30 %.
- (6) Tax so calculated shall be increased by surcharge @12 % of tax if total income of the firm/ LLP exceeds Rs 1 crore.
- (7) It is further increased by health and education cess @4 % plus surcharge, if any.

Treatment of share of income from firm/ LLP

It is fully exempted from tax u/s 10 (2A) and as such is not added in individual income of partners.

Treatment of remuneration and interest received from firm/LLP

Following amounts shall be added in the individual income of partners under the head profits and gains:

- (a) Interest paid by firm to partners shall not be added in the individual income of partners if it has been disallowed to firm as it was paid without its being mentioned in deed. Interest paid by firm to partners shall be fully added in individual income of partners if it has been fully allowed to firm and it was paid as it was mentioned in deed and rate of interest was up to 12 %. Interest paid by firm to partners shall be added in individual income of partners up to 12 % P.a. If it has been allowed to firm ! 12 % P.a. if mentioned in deed.

This means that if partnership deed allows interest to partners @ 12 % or less, then it is allowed to be debited to P/L A/c of the firm and while calculating individual income of the partners it is added in the individual income of partners. So by debiting this amount of the interest to P/L a/c, the profit of the firm is reduced whereas the same amount of interest is added in the individual income of the partners and thus, partners would pay tax on such interest. In case , partnership deed allows interest which is more than 12 % , then only 12 % is allowed and excess will be added back in the profit of the firm if already debited to the P/L a/c. This simply means that only 12 % is allowed to be debited to P/L a/c of the firm and only the same amount is treated as individual income of partners.

- (b) Remuneration paid to partners and allowed to firm shall be added in individual income of partners in following manner.

- (i) If it is fully allowed it shall be fully added in partner's individual income.
- (ii) If it was allowed up to restricted amount as per above, amount to be added shall be

Restricted remuneration = Actual remuneration of a partner/ total remuneration of all partners.

4.6 LOSSES OF REGISTERED FIRMS (Section 75)

Carry forward and set off of losses in case of change in constitution of firm or on succession [Section 78(1)] Where a change has occurred in the constitution of a firm on account of death or retirement, the firm is not entitled to carry forward and set off so much of the loss proportionate to the share of a retired or deceased partner as exceeds his share of profits, if any, in the firm in respect of the previous year.

Method of computation of amount not to be allowed to be carried forward

Step 1: In the year of change first ascertain the share of outgoing partner in the profit or loss of the firm.

Step 2: Compute share of loss of the outgoing partner for each of the preceding years from which the loss is carried forward.

Step 3: Amount not allowed to be carried forward: (i) Sum of [Amounts computed in Steps (1) and (2) where there is loss in the year of change]. (ii) Difference of [Amounts computed in Steps (1) and (2) in case of profit in the year of change].

ASSESSMENT OF PARTNERS

As per Section 10(2A) of the Act, any person who is a partner of a firm which is assessed as such, his share in the total income of the firm will not be included in computing his total income. Partner includes a minor admitted to the benefits of partnership as per Section 2(23) of the Act.

Further, the explanation to Sub-clause (2A) provides that the share of a partner in the total income of the firm assessed as a firm shall be an amount which bears to the total income of the firm the same proportion as the amount of his share in the profits of the firm (in accordance with the partnership deed) bears to such profits.

In terms of a formula, the amount exempt would be:

Partners share in the profit of the firm =

As shown in the partnership deed

Total income of the firm

Total Profits of the firm

Any interest, salary, bonus, commission or remuneration by whatever name called which is due to or received by a partner of a firm from the firm will be chargeable to tax in the hands of the partner under the head “profits and gains of business or profession”. However, if such salary, interest, bonus, commission or remuneration (or any part thereof) has not been allowed as deduction as per Section 40(b) in the hands of the firm, the amount not allowed as deduction shall not be charged to tax in the hands of partners.

Further, deductions under Sections 32 to 37 can be claimed by a partner from any income where any expenditure was incurred to earn such income.

4.7 SUCCESSION OF ONE FIRM BY ANOTHER FIRM (Section 188)

When all the partners in the predecessor firm are replaced by new partners in the successor firm, it is known as succession of one firm by another firm. If a firm is dissolved and some of the partners take over the firm’s business or carry on a similar business with or without new partners, it would be a case of succession by a new firm (62 I.T.R. 75).

In CIT v. K.H. Chambers (1965) 55 ITR 674, the Supreme Court laid down the following requisites of succession:

- (i) There is a change of ownership.
- (ii) The whole business is transferred.
- (iii) Substantially the identity and the continuity of the business are preserved.

Where the partnership deed does not provide specifically for continuance of the firm on the death of a partner, there would be no change in constitution of the firm but it would be a case of succession. [*Addl. CIT v. Thyagasundaramudaliar*(1981) 127 ITR 520].

Where a firm is succeeded by another firm, separate assessments are made on the predecessor and successor firms respectively in accordance with the provisions of Section 170 which provides that the predecessor shall be assessed in respect of the income of the previous year in which the succession took place up to the date of succession and the successor shall be assessed in respect of the income of the previous year after the date of succession. If the predecessor cannot be found, or the tax assessed on the predecessor cannot be recovered from him for the previous year (in which the succession took place)

and the previous year immediately preceding such previous year, the unrealised tax payable by the predecessor shall be recovered from the successor.

However, the successor firm is entitled to recover from the predecessor firm any tax paid by it on behalf of the former. If any tax is due against any partner of the predecessor firm, it cannot be recovered from the successor firm.

Joint and several liability of partners for tax payable by firm (Section 188A)

As per this section every person who was, during the previous year, a partner of a firm, and the legal representative of any such person who is deceased, shall be jointly and severally liable along with the firm for the amount of tax, penalty or other sum payable by the firm for the assessment year to which such previous year is relevant, and all the provisions of Income-tax Act, so far as may be, shall apply to the assessment of such tax or imposition or levy of such penalty or other sum.

Firm Dissolved or Business Discontinued (Section 189)

Where any business or profession carried on by a firm has been discontinued or where a firm is dissolved, the assessment of the total income of the firm shall be made as if no such discontinuance or dissolution had taken place and all the provisions of the Act, including the provisions relating to penalty or any other sum (interest, fine) chargeable under the Act, shall apply. Consequently, every person who was a partner of the firm at the time of discontinuance of business or dissolution of the firm and legal representative of the deceased partner shall be jointly and severally liable to the amount of tax penalty and any other sum. Where the dissolution or discontinuance of business takes place after any proceedings in respect of an assessment year have commenced, the proceedings may be continued against the partners or legal representative of a deceased partner from the stage at which the proceedings stood at the time of such dissolution or discontinuance.

Thus, every partner of the firm and the legal representative of the deceased partner is liable to pay the tax which is already due or may have become due after the dissolution, irrespective of his interest in the firm. However, if there was any irrecoverable amount at the time of dissolution or discontinuance of business and later on it was recovered by the partners, the partners shall personally pay the tax on their share so recovered.

4.8 COMPUTATION OF INCOME ON ESTIMATED BASIS IN CASE TAX PAYERS ARE ENGAGED IN CERTAIN BUSINESS (Section 44AD)

An assessee being an individual, a resident HUF or a partnership firm (not being a LLP), who has not claimed any deduction under Sections 10A, 10AA, 10B, 10BA, 80HH to 80RRB in the relevant assessment year is eligible to pay tax on estimated basis.

Further, the assessee should be engaged in any business (whether it is retail trading or wholesale trading or civil construction or any other business). The turnover/gross receipt of the eligible business should not exceed ₹ 1 crore during the previous year.

The following persons are not eligible to avail benefit under Section 44AD:

- (a) a person carrying on profession as referred to in Section 44AA(1) or*
- (b) a person earning income in the nature of commission or brokerage or*
- (c) a person carrying on any agency business or*
- (d) a person who is in the business of plying, hiring or leasing goods carriages.*

If the above conditions are satisfied, the income from eligible business is estimated @ 8% of gross receipt or total turnover. Further, it is assumed that all the deductions have been allowed and no other deduction is allowed.

However, in case of firm, the normal deduction in respect of salary and interest to partners under Section 40(b) shall be allowed.

4.9 OTHER PROVISIONS RELATING TO LIMITED LIABILITY PARTNERSHIP:

(1) Transfer of capital asset or intangible asset by a private Limited company or a non-listed company to Limited Liability Partnership and correspondingly any transfer of a share or shares held in a company by a shareholder shall not be treated as transfer:

Any transfer of a capital asset or intangible asset by a private company or unlisted public company (hereafter in this clause referred to as the company) to a limited liability partnership or any transfer of a share or shares held in the company by a shareholder as a result of

conversion of the company into a limited liability partnership in accordance with the provisions of section 56 or section 57 of the Limited Liability Partnership Act, 2008 shall not be treated as transfer for the purpose of capital gain under section 45 subject to the following conditions:

- (a) all the assets and liabilities of the company immediately before the conversion become the assets and liabilities of the limited liability partnership;
- (b) all the shareholders of the company immediately before the conversion become the partners of the limited liability partnership and their capital contribution and profit sharing ratio in the limited liability partnership are in the same proportion as their shareholding in the company on the date of conversion;
- (c) the shareholders of the company do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of share in profit and capital contribution in the limited liability partnership;
- (d) the aggregate of the profit sharing ratio of the shareholders of the company in the limited liability partnership shall not be less than fifty per cent at any time during the period of five years from the date of conversion;
- (e) the total sales, turnover or gross receipts in the business of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed sixty lakh rupees; and
- (f) no amount is paid, either directly or indirectly, to any partner out of balance of accumulated profit standing in the accounts of the company on the date of conversion for a period of three years from the date of conversion.

(2) Consequential amendments due to conversion of a private limited company or a non-listed company into LLP:

(i) Allowability of depreciation: Aggregate deduction, in respect of depreciation of buildings, machinery, plant or furniture, being tangible assets or know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature, being intangible assets allowable to the predecessor and the successor in the case of succession of company into LLP, shall not exceed in any

previous year the deduction calculated at the prescribed rates as if the succession, had not taken place.

(ii) Successor LLP will be allowed deduction of payment under Voluntary Retirement Scheme for the unexpired period: Where a private company or unlisted public company is succeeded by a limited liability partnership fulfilling the conditions laid down in the proviso to clause (xiiib) of section 47, the provisions of this section shall, as far as may be, apply to the successor limited liability partnership, as they would have applied to the said company, if reorganisation of business had not taken place.]

(iii) Cost of Acquisition of the asset in case the predecessor company has claimed deduction under section 35AD shall be taken to be nil in the hands of LLP.

(iv) Actual cost of the block of the asset in the hand of successor LLP: Where in any previous year, any block of assets is transferred by a private company or unlisted public company to a limited liability partnership and the conditions specified in the proviso to clause (xiiib) of section 47 are satisfied, then, notwithstanding anything contained in clause (1), the actual cost of the block of assets in the case of the limited liability partnership shall be the written down value of the block of assets as in the case of the said company on the date of conversion of the company into the limited liability partnership.

(v) Carry Forward and set off of losses (Section 72A(6A): Where there has been reorganisation of business whereby a private company or unlisted public company is succeeded by a limited liability partnership fulfilling the conditions laid down in the proviso to clause (xiiib) of section 47, then, notwithstanding anything contained in any other provision of this Act, the accumulated loss and the unabsorbed depreciation of the predecessor company, shall be deemed to be the loss or allowance for depreciation of the successor limited liability partnership for the purpose of the previous year in which business reorganisation was effected and other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly.

However, if any of the conditions laid down in the proviso to clause (xiiib) of section 47 are not complied with, the set off of loss or allowance of depreciation made in any

previous year in the hands of the successor limited liability partnership, shall be deemed to be the income of the limited liability partnership chargeable to tax in the year in which such conditions are not complied with.

“Accumulated loss” means so much of the loss of the predecessor firm or the proprietary concern or the private company or unlisted public company before conversion into limited liability partnership or the amalgamating company or the demerged company, as the case may be, under the head “Profits and gains of business or profession” (not being a loss sustained in a speculation business) which such predecessor firm or the proprietary concern or the company or amalgamating company or demerged company, would have been entitled to carry forward and set off under the provisions of section 72 if the reorganisation of business or conversion or amalgamation or demerger had not taken place.

“Unabsorbed depreciation” means so much of the allowance for depreciation of the predecessor firm or the proprietary concern or the private company or unlisted public company before conversion into limited liability partnership or the amalgamating company or the demerged company, as the case may be, which remains to be allowed and which would have been allowed to the predecessor firm or the proprietary concern or the company or amalgamating company or demerged company, as the case may be, under the provisions of this Act, if the reorganisation of business or conversion or amalgamation or demerger had not taken place.

(vi) MAT credit of the predecessor company will lapse.

4.10 ALTERNATE MINIMUM TAX (AMT) (Section 115JC TO JF)

Applicability :

- (i) The scheme of alternate minimum tax (AMT) is applicable on a limited liability partnership as defined in section 2 (1) (n) of the limited liability partnership act, 2008.

According to section 2 (1)(n) of LLP act, 2008 , LLP means a partnership formed and registered under this act i.e., LLP Act, 2008.

Thus, alternate minimum tax is applicable to a limited liability partnership formed and registered in India under LLP act , 2008. It is not applicable to a foreign LLP i.e., a LLP formed, registered or incorporated outside India and having a place of business within India.

- (ii) With effect from assessment year 2013-14, the scheme of AMT is also applicable on partnership firms governed by the partnership act, 1932.

Where the regular income tax payable for a previous year by a person other than a company is less than the alternate minimum tax payable for such previous year then the adjusted total income shall deemed to be the total income of that person for such previous year and it shall be liable to pay income tax on such adjusted total income @ 18.5% plus Health and education cess @ 4%.

Up to Assessment Year 2012-13, Alternate Minimum Tax (AMT) is levied on limited liability partnerships (LLPs). However, no such tax is levied on the other form of business organisations such as partnership firms, sole proprietorship, association of persons, etc.

In order to widen the tax base vis-à-vis profit linked deductions, the provisions regarding AMT has been broaden to cover all persons other than a company, who has claimed deduction under any section (other than section 80P) included in Chapter VI-A under the heading “C – Deductions in respect of certain incomes” or under section 10AA, shall be liable to pay AMT.

Accordingly, where the regular income-tax payable for a previous year by a person (other than a company) is less than the alternate minimum tax payable for such previous year, the adjusted total income shall be deemed to be the total income of such person and he shall be liable to pay income-tax on such total income at the rate of eighteen and one-half per cent.

For the purpose of the above,

(i) “adjusted total income” shall be the total income before giving effect to provisions of Chapter XII-BA as increased by the deductions claimed under any section (other than section 80P) included in Chapter VI-A under the heading “C – Deductions in respect of certain incomes” and deduction claimed under section 10AA;

(ii) “alternate minimum tax:” shall be the amount of tax computed on adjusted total income at a rate of eighteen and one half per cent; and

(iii) “regular income-tax” shall be the income-tax payable for a previous year by a person other than a company on his total income in accordance with the provisions of the Act other than the provisions of Chapter XII-BA.

Meaning of Adjusted Total Income

Adjusted total income means the total income before giving effect to this newly inserted chapter XII BA as increased by:

- (i) Deductions claimed under any sections other than 80 P included in chapter VI- A Under the heading “C – i.e., Deduction in respect of certain incomes and
- (ii) Deduction claimed , if any, u/s 10 AA
- (iii) Deduction claimed u/s 35 AD less Depreciation allowable u/s 32 on cost of that asset.

It is important to note that Part C of chapter VI-A covers various deductions u/s 80 in respect of certain incomes. These deductions for LLP /Firms are as follows:

u/s 80 IA	For infrastructure projects.
u/s 80 I-AB	For setting up special economic zones.
u/s 80 IB	For new industrial undertaking.
u/s 80 IBA	For profits and gains from housing projects.
u/s 80 IC	For setting up industry in backward states
u/s 80 ID	For setting up hotel or convention centre
u/s 80IE	For undertakings in north –eastern state
u/s 80JA	For use of bio waste
u/s 80 JJAA	For employment of new employees

In other words, adjusted total income for the purposes of section 115 JC (1) shall be calculated as follows:

Total income as per normal provisions of IT act		xxxx
Add: deductions in respect of certain incomes [section 80 IA to 80 LA]		xx
Add: Deduction u/s 10AA		xx
Add: Deduction allowable u/s 35 AD	xx	
Less: Depreciable allowable u/s 32	<u>xx</u>	xxx
Adjusted total income		<u>xxxxxxx</u>

Meaning of regular income tax [Section 115 JF (d)]

It means the income tax payable for a previous year by a limited liability partnership /Firm on its total income in accordance with provisions of IT act, 1961 other than the provisions of this chapter XIIB.

Furnishing of report obtained from charatered accountant [Section 115 JC (3)]

Every LLP/Firm covered u/s 115 JC shall obtain a report , in prescribed form an accountant [as defined in section 288 (2)] certifying that the adjusted total income and the alternate minimum tax have been computed in accordance with the provisions of this chapter. Such report shall be furnished to income tax department on or before the due date of filling of return under section 139 (1).

Tax credit for alternate minimum tax [section 115 JD]

1. The credit for tax paid by a limited liability partnership /Firm under section 115 JC shall be allowed to it in accordance with the provisions of this section [Section 115 JD (1)]
2. Computation of amount of tax credit [Section 115 JD (2)] The tax credit of an assessment year shall be the excess of alternate minimum tax paid over the regular income tax payable for that year . In other words,

Amount of tax credit= alternate minimum tax - tax payable on total income computed as per normal provisions of income tax act

3. Time limit to carry forward tax credit [Section 115 JD (4)]. The tax credit for any assessment year immediately succeeding the assessment year for which tax credit becomes allowable u/s 115 JC (1).
4. Set off of tax credit [Section 115 JD (5)]. Tax credit shall be allowed in any assessment year, in which the regular income tax exceeds the alternate minimum tax. Such set off shall be allowed to the extent of the excess of regular income tax over the alternate minimum tax and the balance of the tax credit, if any, shall be carried forward.

Increase/ Decrease of tax credit [Section 115 JD (6)]

If the amount of regular income tax or the alternate minimum tax is reduced or increased as a result of any order passed under this act, the amount of tax credit allowed under this section shall also be adjusted / Varied accordingly.

Application of other provisions of this act [Section 115 JE]

Same as otherwise provided in this chapter, all other provisions of this act shall apply to a limited liability partnership / Firm referred to in this chapter.

PROBLEMS

A) PARTNERSHIP FIRM/LLP ASSESSED U/S 184.

ILLUSTRATION 1

A and B are active partners and C and D are sleeping partners in a firm. A profit and loss account, drawn for the year ending 31-3-2019 shows a profit of Rs. 25000. The Profit has been arrived at after allowing salary and interest to partners as follows:

	A	B	C	D
Salary	25000	23000	—	—
Interest @ 9%	2000	4000	6000	3000

Further the long term capital gains of the firm are Rs. 40000. Partners share the profit and loss equally. Compute the total income of the firm and its tax liability. Interest to all the partners and salary to working partners has been paid as per deed.

SOLUTION 1:

	Rs.	Rs.
Net profit as per profit and loss A/C		25000
Add: Disallowed deductions:		
Salary to partners		
A	25000	
B	23000	
Interest to partners is less than 12% & hence allowed	—	48000
Book Profit		73000
Less: allowable remuneration to partner's u/s 40(b)		
Since salary etc. given to all partners is less than		
Rs. 150000 hence allowed in full		48000
Business profit		25000
Capital gain:		
Long term capital gain		40000
G.T.I & Total Income		65000
Tax liability of the firm		
On long term capital gain of Rs 40000 @ 20%		8000
On balance income (65000-40000 = 25000) @ 30%		7500

Tax	15,500
Add: Health and Education cess @ 4% of tax	620
Tax Payable	16,120

ILLUSTRATION 2

Profit and Loss Account of ABC and Co. (a firm of chartered accountants) for the year ending 31-3-2019 is as follows:

	Rs.		Rs.
Expenses	10000	Receipts from clients	135000
Depreciation	75000	Bank interest	25000
Remuneration to working partners	80000	Net Loss	42500
Interest on capital to partners @ 20%	37500		
	202500		202500

Other information:

- i) Out of expenses of Rs. 10000, Rs. 6400 is not deductible by virtue of section 36 and 37.
- ii) Depreciation as per section 32 is Rs. 27500.

Find out the amount of net income of the firm for the assessment year 2019-20. The remuneration and interest on capital to partners have been paid according to partnership deed which has been submitted along with return.

SOLUTION 2:

Computation of Firms Total Income	Rs.	Rs.
Professional receipts		135000
Less: Professional expenses		
Allowable Expenses (10000-6400)	3600	
Allowable depreciation	27500	

Interest on capital (37500x 12/20)	22500
53600	
Book Profit	81400
Less: Allowable remuneration u/s 40(b)	
Actual Remuneration	80000
Or	
90% of Book Profit of Rs. 81400	73260
Whichever is more is allowed	80000
Taxable Business profit	1400
Add: Income from other sources	
Bank Interest	25000
Firms total Income	26400

ILLUSTRATION 3

The doctors Dr. Ahalya and Somnath are running a nursing home under a partnership firm profits and losses equally and showed Rs. 16600 as profit for the previous year 2018-19 after charging the following:

<i>Operation charges to Dr. Somnath(100 per operation)</i>	
<i>1500</i>	
<i>Remuneration to Dr. Ahalya</i>	<i>6200</i>
<i>Honorarium to Dr. Somnath</i>	<i>3000</i>
<i>Bonus to Each Doctor</i>	<i>2000</i>
<i>Donation to shelter for Hindus</i>	<i>3750</i>
<i>Interest on Capital to each Doctor@9%</i>	<i>2000</i>
<i>Purchase of surgical equipment</i>	<i>12500</i>

<i>House property rent</i>	9600
<i>Bank Interest</i>	4000

Compute firms' total income and find out the income of partners taxable under the head profit and gains. Firm's deed provides for payment of operation charges, remuneration, bonus, honorarium and interest on capital.

SOLUTION 3

Computation of Firms Professional Gain	Rs
Rs	
Net profit as per P&L A/C	16600
<i>Add: Disallowed expenses</i>	
Operation charges to Dr. Somnath	1500
Remuneration to Dr. Ahalya	6200
Honorarium to Dr. Somnath	3000
Bonus to each doctor	4000
Donation to shelter for Hindus	3750
Cost of surgical equipment	12500
30950	
	47550
<i>Less: Allowable expenses</i>	
Depreciation (12500 @ 15%)	1875
	45675
<i>Less: Income not taxable under this head</i>	
Rent from House property	9600
Bank interest	4000
	13600

Book Profit		32075
<i>Less: Allowable remuneration/s 40(b)</i>		
Operation charges to Dr. Somnath	1500	
Honorarium to Dr. Somnath	3000	
Remuneration to Dr. Ahalya	6200	
Bonus to each Doctor(2000)		4000
14700		
Professional gain		17375

Computation of Firms Total Income

<i>House Property: ARV</i>	9600	
Less: M.Taxes	Nil	
N.A.V	9600	
	Standard deduction: 30% of NAV	2880
6270		
<i>Other sources: Bank interest</i>		4000
Total Income		28095

Rounded off to Rs. 28100

Firms Tax: 30% of 28100=Rs. 8430 + Health and Edu. cess@4 % i.e. Rs.337= Rs 8767, rounded off to 8770

Partners Professional Income

1. Dr Ahalya:	Remuneration	6200
	Bonus	2000
	Interest on Capital	2000
		10200

2. Dr Somnath: Operation Charges	1500
Honorarium	3000
Interest on Capital	2000
Bonus	2000
	8500

Notes: 1.share of income from Firm is fully exempted u/s 10(2A) in the hands of partners.

2.Operating charges, remuneration, honorarium and bonus paid to partners are fully allowed as they are within limits.

B) ASSESSMENT OF FIRM/LLP U/S 185.

ILLUSTRATION 1

Asim, John and Rahim are partners in a firm assessed as u/s 185 sharing profits and losses in the ratio of 5:3:2. Profit and loss account for the year ending on 31-3-2019 was as follows:

<i>Profit & Loss</i>			
To rent and taxes	6000	By Gross Profit	40000
To salaries	9000	By Interest on securities	3000
To electric charges	1200		
To interest on capital			
Asim	2000		
John	1500		
Rahim	1000		
To Depreciation	2500		
To Reserve for bad debts	500		

To interest on loan from John	300	
To commission to Rahim	1000	
To Balance:		
Asim	9000	
John	5400	
Rahim	3600	
	43000	43000

Note: 1. Salary includes Rs. 2000 paid to Rahim

2. Depreciation allowable amount to Rs. 2400

Compute the Business Income for Firm as AOP and U/s 185.

SOLUTION 1

Computation of business income of the firm assessed u/s 185

	Rs	Rs
Profit as per P/L A/c		18000
Add: expenses charged but not allowed:		
Interest on capital		
Asim	2000	
John	1500	
Rahim	1000	4500
		22500
Depreciation	2500	
Reserve for Bad debts	500	
Interest on loan from John	300	

Commission to Rahim	1000	
Salary to Rahim	2000	<u>6300</u>
		28800
Less: Income credited but to be treated under a separate head:		
Income from other sources: Interest on Securities		3000
		<u>25800</u>
Less: Allowable business expenses		
Depreciation		<u>2400</u>
Business Income of Firm		<u>23400</u>

ILLUSTRATION 2

PQR and Co. A partnership firm with three partners P, Q and R sharing profits and losses in the ratio of 3:2:1, gives the following particulars of its profit and loss account for the year ending on 31st March 2019:

- a) Profit as per profit and loss account, Rs 50000
- b) Drawings debited to profit and loss account Rs. 40000
- c) Depreciation debited 75000. actually admissible 90000.
- d) Entertainment expenses 10000
- e) Bad debts recovered and credited to P/L A/c-15000. This is recovery out of a debt of 40000 written off as bad in 2017-18 of which only Rs 30000 was allowed in the relevant assessment.
- f) Salaries paid to Q. Rs 12000
- g) Commission paid to R. Rs 20000

Compute the total income of the firm as u/s 18. Each item of information above should be fully dealt with in your answer.

SOLUTION 2

Computation of Firms Total Income assessed u/s 185

	Rs	Rs
Profit as per P/L A/c		50000
Add: Disallowed items		
Drawings	40000	
Depreciation	75000	
Salaries to Q	12000	
Commission to R	<u>20000</u>	<u>147000</u>
		197000
Less: Incomes not taxable under the head		
Bad debts recovered—Disallowed earlier (40000-30000=10000) being exempted		<u>10000</u>
		187000
Less: Expenses allowed but not debited		
Depreciation		<u>90000</u>
Firms Total Income		

4.11 ASSOCIATION OF PERSONS

‘Association of persons’ or a body of individuals is a separate person under the income tax 1961. An AOP or BOI is a combination of persons (Individuals, HUF, Firms OR companies) formed with the object of earning income. An AOP may have individuals, HUF, Firms or companies as its members whereas a BOI may have only Individuals as its members. An AOP or BOI is such a combination which is neither a HUF nor a firm nor a company and nor a local authority. The persons must combine together to earn income

which may either be received by the AOP or BOI or by any member thereof. A family other than HUF carrying on a joint business shall be treated as an AOP.

4.12 FORMATION OF AN ASSOCIATION OF PERSONS

For the formation of an AOP the association need not necessarily be on the basis of a contract, consent and understanding may be presumed [Shanmugham & Co. v. CIT (1971) 81 ITR 310 (S.C.)].

Applying the ratio laid down by the Supreme Court in the case of N. V. Shanmugham & Co. v. Commissioner of Income-tax (1971, 81 ITR 310) the Calcutta High Court held in the case of Gopal Chand Sen v. Income-tax Officer and others (1977, 109 ITR 820) that an assessment of business income has to be done in the hands of receivers and in such an assessment, the receivers are never assessed as independent earners of income. The income in the hands of the receiver is assessable in the like manner and to the same extent as it would have been assessed on the real owners.

However, co-owners, co-heirs or co-legatees do not constitute an AOP in respect of the income of the joint or common asset by reason only of their jural relationship. But if they write themselves with the objective of earning income they constitute an AOP for assessment purposes. [Estate of Mohamed Rowther v. CIT (1963, 49 ITR 39)]. Section 26 of the Income-tax Act provides that where property consisting of building or buildings and lands appurtenant thereto is owned by two or more persons in definite and ascertainable shares, such persons shall not, in respect of such property be assessed as an AOP, but on their respective share of income therefrom.

In order to constitute an association of persons, there must be joining together in a common purpose or in a common action, the object of which is to produce income, profits and gains. Though a body of individuals is not identical with an association of persons, they have some similarities. An association of persons may consist of non-individuals also but a body of individuals has to consist only of human beings. The word 'body' would require an association for some common purpose or for a common cause or there must be unity under some common tie or occupation. A mere collection of individuals without a common tie or common aid cannot be taken to be a body of individuals falling under Section 2(31) of the Income-tax Act, 1961. [See CIT v. Deghamwala Estates (1980, 121 ITR 684)].

4.13 TAX LIABILITY OF ASSOCIATION OF PERSONS

With effect from assessment year 1989-90, the following provisions are applicable to assessees other than companies, co-operative societies and societies registered under the Societies Registration Act, 1860 or any law corresponding to that Act in force in any part of India.

(1) Interest paid by the AOP to a member will not be allowed as a deduction from the income of the Association of Persons [Section 40(ba)]. In cases where interest is paid by the AOP to any member, who has also paid interest to the AOP, the net amount of interest that will be disallowed is the amount of interest paid by the AOP to the member less the amount of interest paid to the AOP by the member [Explanation 1 to Section 40(ba)].

(2) In cases where an individual is a member of an AOP in a representative capacity, any interest paid by the AOP to such individual or by such individual to the AOP, otherwise than in a representative capacity will not be subject to disallowance under explanation 2(i) to Section 40(ba).

(3) In the cases of interest paid by AOP to such individual or by such individual to the AOP in a representative capacity any interest paid by the AOP to the person represented by such person or vice versa, will not be allowed under Section 40(ba) [Explanation 2(ii) to Section 40(ba)].

(4) Explanation 3 to Section 40(ba) further provides that where an individual is a member of the AOP otherwise than as member in a representative capacity, any interest paid by the AOP to such individual will not be disallowed if the interest is received by him on behalf of any other person.

(5) Any salary, bonus, commission or remuneration (by whatever name called) paid by the AOP to a member will not be allowed as a deduction.

Section 167B makes the following provisions as regards the incidence of charge of tax on the association of persons.

A. Where shares of members are determinate

1. In case total income excluding share from AOP of any member of AOP does not exceed the exempted limit i.e., Rs 250,000 for individuals both males and females, Rs 300,000 for resident senior citizens of 60 years or more but less than 80 years, Rs 500,000 for resident super senior citizens of 80 years or more the total income of such AOP shall be assessed to tax at same rates as are applicable to an individual.
2. In case total income of any member of AOP exceeds the exempted limit- the total income of such AOP shall be assessed at MMR.
3. In case AOP has any member whose total income in case of foreign companies only is taxable at a higher than MMR, the total income of such AOP shall be split up in two parts.
 - (i) The share of income of the member whose income is assessable at a higher than MMR, this part of total income of AOP shall be taxable at such higher rate.

And balance total income of AOP/BOI shall be assessed to tax at MMR

B. Where the shares of the members are indeterminate

1. In case AOP (excluding a company, a co- operative society or a society registered under societies act, 1860) where shares of its members are not known or are indeterminate and it does not have any such member whose income is taxable at a rate higher than MMR – the total income of such AOP shall be taxable at MMR i.e. 30 %
2. In the above case , If AOP has any member such as company or Firm whose individuals income is taxable at a rate higher than MMR an amount equal to the share of income of such member shall be taxable at such higher rate and balance total income of AOP/ BOI shall be taxable at MMR.

Computation of AOP Total Income

1. Income of AOP is calculated head wise. It cannot have any income under the head salaries.

2. In case of house property rules given under the head income from house property are applicable. It cannot have self occupied house.
3. Profits and gains of business or profession are to be computed in the same manner as given under the head profits and gains of business or profession.
4. Income under the head capital gains is to be computed in the same manner as per provisions of capital gains but exemptions u/s 54, 54 B and 54 F are not allowed.
5. Set off and carry forward of losses is to be done as per provisions of section 70 to 74 of the act.
6. Deductions out of gross total income: AOP can claim the following deductions.

u/s 80 G	For donations
u/s 80 GGC	For donation to political parties.
u/s 80 IA	For infrastructure projects.
u/s 80 IAB	For setting up special economic zones.
u/s 80 IB	For new industrial undertaking.
u/s 80 IBA	Profits and gains from housing projects.
u/s 80 IC	For setting up industry in backward states
u/s 80 ID	For setting up hotel or convention centre
u/s 80IE	For undertakings in north –eastern state
u/s 80JJA	For use of bio waste
u/s 80 JJAA	For employment of new employees

4.14 METHOD OF COMPUTING SHARE OF A MEMBER OF ASSOCIATION OF PERSONS, ETC. (Section 67A)

Section 67A seeks to provide for the method of computing a member's share in the income of an association of persons or a body of individuals, wherein the shares of the

members are determinate, in the same manner as provided for in Sub-sections (1) to (3) of Section 67 for computing a partner's share in a firm. This section lays down the following methods of computing the member's share:

(a) Any interest, salary, bonus, commission or remuneration, by whatever name called, paid to any member in respect of the previous year shall be deducted from the total income of the association or body and the balance ascertained and apportioned among the members in the proportion in which they are entitled to share the income of the association or body.

(b) Where the amount apportioned to a member under (a) hereinabove is a profit, any interest, salary, bonus, commission or remuneration paid to the member by the AOP in respect of the previous year shall be added to that amount - the result shall constitute the member's share in the income of the association or body.

(c) Where the amount apportioned to a member under (a) is a loss, any interest, salary, bonus, commission or remuneration aforesaid paid to the member by the association or body in respect of the previous year shall be adjusted against that amount, the result shall be adjusted against that amount, and the result shall be treated as the member's share in the income of the association or body.

See also explanatory notes on the provision of DTL (Amendment) Act, 1987 Board circular No. 551 dated 23.1.1990 [(1990, 183 ITR 1 (SC)].

4.15 TAX ON INCOME OF ASSOCIATION OF PERSONS, ETC. WHICH IS INDETERMINATE OR UNKNOWN (New Section 167B)

Section 167B seeks to provide that where the individual shares of the members of an association or body in the whole or any part of the income of such association or body are indeterminate or unknown, tax shall be charged on the total income of the association or body at the maximum marginal rate. However, where the total income of any member of such association or body is chargeable to tax at a rate which is higher than the maximum marginal rate, tax shall be charged on the total income of the association or body at such higher rate. Also, where the total income of any member of an association of persons or body of individuals as above for the previous year (excluding his share from such association or body) exceeds the maximum amount which is not chargeable to tax in the case of that

member, tax shall be charged on the total income of the association or body at the maximum marginal rate. However, where any member or members of such association or body of individuals is or are chargeable to tax for the previous year at a rate or rates which is or are higher than the maximum marginal rate, tax shall be charged on that portion or portions of the total income of the association or body of individuals which is or are relatable to the share or shares of such member or members at such higher rate or rates, as the case may be, and the balance of the total income the association or body shall be taxed at the maximum marginal rate.

In the explanation to the above provisions, it is provided that the shares of the members of an association or body in the whole or any part of the income of such association or body shall be deemed to be indeterminate or unknown if such shares (in relation to the whole or any part of such income) are indeterminate or unknown on the date of formation of such association or body or any time thereafter.

4.16 SHARE OF MEMBER OF ASSOCIATION ETC.(Section 86)

Section 86 relates to shares of members of an association of persons or a body of individuals in the income of the association or body. This section provides that if the assessee is a member of an association of persons or a body of individuals (other than a company or a Co-operative society or a Society registered under the Societies Registration Act, 1860, or any law corresponding to that Act in force in any part of India), his share in the income of the association or body, computed in the manner provided in Section 67A shall not be liable to tax. Further, where the association or body is chargeable to tax on its total income at the maximum marginal rate or any higher rate, under any of the provisions of the Income-tax Act, his share computed in the manner stated above shall not be included in his total income. But, in other cases and in cases where no income-tax is chargeable on the total income of the association or body, the member's share shall be chargeable to tax as part of his total income and Section 86 shall not be applicable to such case.

The charge of tax on the member's share in AOP will depend on the following factors:

- (i) Income-tax is not payable by the member in respect of his share in the income of the AOP, computed in the manner provided in Section 67A.
- (ii) His share in the income of the AOP is includible in his total income for rate purposes.

(iii) Where the AOP is chargeable to tax on its total income at the 'maximum marginal rate' or at any higher rate, the share of the member will not be includible in his total income. In this case, the member's share in the income of the AOP will not be included in his income even for rate purposes.

(iv) In any other case, the member's share will form part of his total income.

(v) Where no income-tax is chargeable on the total income of the AOP, the share of the member will be chargeable to tax part of his total income. Section 86 will not be applicable to such cases.

Assessment in case of Dissolution of an Association of Persons (Section 177) Where any business or profession carried on by an AOP has been discontinued or an AOP is dissolved, the Assessing Officer shall make an assessment of the total income of the AOP as if no such discontinuance or dissolution had taken place, and all provisions of this Act, including the provisions relating to the levy of penalty or any other sum chargeable under any provisions of the Income-tax Act shall apply.

Every person who was at the time of such discontinuance or dissolution a member of the AOP and the legal representative of any such person who is deceased, shall jointly and severally be liable for the amount of tax, penalty or other sum payable.

Where such discontinuance or dissolution takes place after any proceeding in respect of an assessment year have commenced, the proceedings may be continued against the members from the stage at which the proceedings stood at the time of such discontinuance or dissolution.

4.17 SUMMARY

Assessment is a procedure used by government assessors to determine the value of a property, or the income of a person or entity, in order to charge taxes or to levy on the orders of a court. In other words it is a value calculated as the basis for determining the amounts to be paid or assessed for tax or insurance purposes. A tax assessor is responsible for preparing and maintaining the assessment roll, the tax roll and collecting the tax levies in accordance with the quality standards.

Under Section 2(23) of the Income-tax Act, the terms “firm”, “partner”, and “partnership” have the meanings respectively assigned to them in the Indian Partnership Act, 1932 and Limited Liability Partnership Act, 2008.

The expression “partner” also includes a minor who has been admitted to the benefits of partnership and a partner of a Limited Liability Partnership Act 2008. However a minor cannot validly enter into any partnership as a ‘full partner’ with other persons but he can be admitted to the benefits of partnership only.

A joint Hindu family as such cannot be a partner in a firm. However, through its Karta it may enter into a valid partnership with a third person or with a member of the undivided family in his individual capacity. In such a case, the Karta occupies a dual position. On the partnership he functions in his individual capacity; on the relations to other members of the Hindu undivided family, in his representative capacity.

An incorporated company being a legal person may form a partnership with an individual or with another company. In considering the maximum number of partners comprising a firm, the company will be considered as one person only.

“Association of persons” means an association in which two or more persons join in for a common purpose or common action to produce income, profits or gains”. An association of persons may consist of non-individuals (Companies, firms joint families) [Ipoth v. CIT (1968) 67 ITR 106 (S.C.)]. A minor can join an AOP if his lawful guardian gives his consent. [Murugesan & Bros. v. CIT (1973) 88 ITR 432 (SC)]. Applying the ratio laid down by the Supreme Court in the case of G. Murugesan and Bros. v. Commissioner of Income-tax (1973, 88 ITR 432), the Kerala High Court held in the case of Commissioner of Income-tax v. Goel C. Dalal and Perin C. Dalal (1990, 184 ITR 248) that in order to acquire the status of an association of persons, the persons must join in a common purpose or action and the object of the association must be to produce income. It is not enough that the persons receive the income jointly.

Section 67A seeks to provide for the method of computing a member’s share in the income of an association of persons or a body of individuals, wherein the shares of the members are determinate, in the same manner as provided for in Sub-sections (1) to (3) of Section 67 for computing a partner’s share in a firm. This section lays down the following methods of computing the member’s share:

(a) Any interest, salary, bonus, commission or remuneration, by whatever name called, paid to any member in respect of the previous year shall be deducted from the total income of the association or body and the balance ascertained and apportioned among the members in the proportion in which they are entitled to share the income of the association or body.

(b) Where the amount apportioned to a member under (a) hereinabove is a profit, any interest, salary, bonus, commission or remuneration paid to the member by the AOP in respect of the previous year shall be added to that amount - the result shall constitute the member's share in the income of the association or body.

(c) Where the amount apportioned to a member under (a) is a loss, any interest, salary, bonus, commission or remuneration aforesaid paid to the member by the association or body in respect of the previous year shall be adjusted against that amount, the result shall be adjusted against that amount, and the result shall be treated as the member's share in the income of the association or body.

PROBLEMS

ILLUSTRATION 1

The total income of a AOP in which A, B & C are members share profits and losses in the ratio of 1:2:2 was assessed at Rs. 16000. In computing the total income of Rs. 16000 the Income Tax Officer has made the necessary adjustments in respect of the following sums:

Salaries of Rs. 12000 and 8000 to A and B respectively.

Interest of Rs. 1000, Rs. 6000 and 25000 to A, B and C respectively.

Commission of Rs. 2000, 5000 and Rs. 7000 to A, B and C respectively.

C has borrowed capital for his investment in the firm and had paid interest of Rs. 15000 separately to the lender. Compute the share of the respective partners for their individual assessment.

SOLUTION 1 :

Allocation of Firms income amongst members

C	A	B
Income		
Salary	12000	8000
		Nil
Interest	1000	6000
25000		
Commission	<u>2000</u>	<u>5000</u>
<u>7000</u>		
Total	15000	19000
32000		
Share of Income [16000-(15000+19000=32000)]	<u>-10000</u>	<u>-20000</u>
<u>-20000</u>		
Net share	+5000	+1000
+12000		
Interest on loan taken by C		-
15000		
BalanceShare		3000

B and C cannot adjust their share of loss from their individual income. A's share shall be added in his individual income.

ILLUSTRATION 2

Arun and Barun were members of an AOP whose accounting year ends on 31st March every year. On 1st April 2018 Shanti (Barun's wife) joined the firm as a member and thereafter all the three members are entitled to share profits and losses equally. Shanti invested a sum of Rs. 200000 as her capital in the firm, the source of such investment being the gift received from her father. The other two members have no capital in the firm. Shanti is actively engaged in the business.

For the assessment year 2019-20, the firms total income has been determined by the income tax officer at Rs. 45000 after making due adjustments in respect of the following items:

1) *Salary:*

<i>Arun</i>	<i>15000</i>	
<i>Barun</i>	<i>10000</i>	
<i>Shanti</i>	<i>10000</i>	<i>35000</i>

2) *Interest on Capital*

<i>Shanti</i>	<i>28000</i>
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3) *Brokerage:*

<i>Arun</i>	<i>12000</i>	
<i>Shanti</i>	<i>12000</i>	<i>24000</i>

4) *Rent*

<i>Barun(for the office premises owned by him)</i>	<i>9000</i>
----------------------------------------------------	-------------

Arun won a prize of Rs. 10000 in west Bengal State Lottery and a sum of Rs. 3000 was deducted at source out of the same. Shanti holds 10000 equity shares of a company in which a dividend of 95 paise per share was declared by the company in its Annual General Meeting held on 28 March 2019. Apart from the above, no partner has any other income whatsoever.

SOLUTION 2 :

Allocation of Firms income against partners

	Arun	Barun	Shanti
Income			
Salary	15000	10000	10000
Interest			28000

Brokerage	<u>12000</u>	<u>Nil</u>	<u>12000</u>
Total	27000	10000	50000
Share of Income			
[45000-(27000+10000+50000)]=42000 Ratio equal	<u>-14000</u>	<u>-14000</u>	<u>-14000</u>
Net Share	<u>+13000</u>	<u>-4000</u>	<u>+36000</u>

Individual Income of members:

<i>House Property: For Barun[rent 9000 less 30%]</i>	Nil	6300	Nil
<i>Profits and gains: Share from AOP</i>	13000	Nil	36000
<i>Income from other sources:</i>			
<i>Lottery prize for Arun</i>	10000	Nil	Nil
<i>Dividend from Indian Co. for Shanti-exempted</i>	<u>Nil</u>	<u>Nil</u>	<u>Nil</u>
<i>Total income of each member</i>	<u>23000</u>	<u>6300</u>	<u>36000</u>

Barun cannot set off his share of loss from AOP out of his individual Income

ILLUSTRATION 3

Mr. K, Mrs. L and Mr. M are members of an AOP sharing profits and losses equally. During the year ending 31-3-2019 total income of AOP was 338,000. The details of individual income of its members are given below:

Mr. K

Rent from house property:	60,000
Interest on deposits with HUDCO	36,000
Bank interest	50,000
Short-term capital gain on sale of jewelry	56,000

Mrs. L

House property income (computed)	80,000
Bank interest on fixed deposits:	54,000
Interest on post office fixed deposit	12,000
Interest on debentures (gross)	96,000

Mr. M (Age 81 Years)

Pension from Govt.	336,000
Interest accrued on NSC VIII issue	12,600
Interest on Govt. securities	15,000

Compute tax liability of AOP and its members.

SOLUTION 3

Computation of tax liability of AOP

AOP shall pay tax at the rates applicable to an individual as total income of each (or all) of its members without adding share from AOP as calculated below does not exceed the exempted limit.

Tax on 338,000	Rs.
Rs.	
On 2,50,000	Nil
Tax on balance Rs. 88,000 @ 5%	4400
Add: Health and Education Cess @ 4% of tax	176
Total tax payable	4,576
Tax payable rounded off to Rs. 4580	

Computation of total income and tax liability of members of AOP

Mr. K

Income from house property: ARV	60,000
Less: Municipal tax	Nil
Annual Value	60,000
Standard Deduction 30%	18,000
Income	42,000
Capital gain: Short term capital gain on sale of jewellery	56,000
Income from other sources: Interest on deposits (HUDCO)	36,000
Bank Interest	50,000
	86,000
Gross Total Income	1,84,000
Deduction u/s 80C to 80U:	Nil
Total Income	1,84,000
Add: 1/3 rd share from AOP: 1/3 of 338,000	112,667
	296,667

Tax Liability:

On 2,50,000:	Nil
On 46,670@ 5%	2334
Tax	2334
Less: Rebate u/s 87A	2334
Tax Payable	Nil

Mrs. L

House property income (computed)	80,000
----------------------------------	--------

Income from other sources: Bank Interest	54,000
Interest on post office deposits	12,000
Interest on debentures	96,000
Gross Total Income	242,000
Deduction u/s 80C to 80U	Nil
Total Income	2,42,000
Add: 1/3 rd share from AOP	112,667
	3,54,667

Tax Liability:

On Rs. 250000	Nil
On balance Rs. 66000 @ 5%	5234
Tax	5234
Less: Rebate u/s 87A	Nil
Tax	5234
Add: Surcharge @ 3%	209
	5443
Less rebate u/s 86 at average rate	<u>1729</u>
[5443 X 100/354,670 =]	
Tax payable	<u>3714</u>

Tax payable rounded off Rs. 3710

Mr. M (Age 81 Years)

Income from salary: Govt Pension (336,000 -40,000)	2,96,000
Income from other sources: Intrest accrued (NSC)	12600

Interest (Govt. securities)	15000	27,600
Gross Total Income		3,23,600
Deduction u/s 80C: Interest acc. on NSC		12,600
Total Income		3,11,000
Add: 1/3 rd share from AOP		112,667
		423,667

Tax liability = Nil as total income does not exceed Rs 500,000 as he is super senior citizen

Tax payable = Nil

4.18 GLOSSARY

- **Partnership Firm:** Under Section 2(23) of the Income-tax Act, the terms “firm”, “partner”, and “partnership” have the meanings respectively assigned to them in the Indian Partnership Act, 1932 and Limited Liability Partnership Act, 2008.
- As per the scheme, a partnership firm shall be assessed as a firm if the following conditions are satisfied:
 - The partnership is evidenced by an instrument i.e. partnership deed.
 - The individual shares of the partners are specified in that instrument.
 - A copy of the partnership deed certified by all the partners in writing (other than the minors) is submitted along with the return of income in respect of which assessment as a firm is first sought.
- As per Section 10(2A) of the Act, any person who is a partner of a firm which is assessed as such, his share in the total income of the firm will not be included in computing his total income. Partner includes a minor admitted to the benefits of partnership as per Section 2(23) of the Act.
- When all the partners in the predecessor firm are replaced by new partners in the successor firm, it is known as succession of one firm by another firm. If a firm is dissolved and some of the partners take over the firm’s business or carry on a

similar business with or without new partners, it would be a case of succession by a new firm.

- Where a change has occurred in the constitution of a firm on account of death or retirement, the firm is not entitled to carry forward and set off so much of the loss proportionate to the share of a retired or deceased partner as exceeds his share of profits, if any, in the firm in respect of the previous year.
- Alternate Minimum Tax: From the assessment year 2012-13 onwards, where the regular income tax payable for a previous year by a person other than a company is less than the alternate minimum tax payable for such previous year then the adjusted total income shall be deemed to be the total income of such person for such previous year and it shall be liable to pay income tax on such adjusted total income @ 18.5% plus education & SHEC @ 3%.
- Association of persons: “Association of persons” means an association in which two or more persons join in a common purpose or common action to produce income, profits or gains.
- For the formation of an AOP the association need not necessarily be on the basis of a contract, consent and understanding may be presumed.
- Section 167B makes the following provisions as regards the incidence of charge of tax on the association of persons.
 - Where shares of members are determinate In this case, tax is chargeable on the income of the association of persons at the same rate as applicable to an individual. However, where the total income of any member of the association of persons for the previous year (excluding his share of income from the association of persons) exceeds the maximum amount not chargeable to tax in the case of an individual, tax will be charged on the total income of the AOP at the maximum marginal rate of 30%, i.e. the highest slab applicable to an individual.
 - Where the shares of the members are indeterminate In these cases, tax will be charged on the total income of the AOP at the maximum marginal rate, that is, the rate of tax as well as surcharge, if any, applicable to the highest slab of income in the case of an individual as specified in the Finance Act of the relevant year

- Section 67A seeks to provide for the method of computing a member's share in the income of an association of persons or a body of individuals, wherein the shares of the members are determinate, in the same manner as provided for in Sub-sections (1) to (3) of Section 67 for computing a partner's share in a firm.

4.19 SELFASSESSMENT QUESTIONS

1. What do you mean by Firm?

2. What is the New Scheme of Taxation of a firm?

3. Explain in brief the condition for allowability of deduction of interest to a partner?

4. Explain the difference between the change in constitution and succession of a firm. Illustrate.

5. What is meant by Association of Persons? How is it formed?

6. Discuss tax liability of an Association of Persons?

7. Discuss tax liability of the members of Association of Persons. State the circumstances, if any, under which their share of income from an association of persons is not chargeable to tax?

8. Explain Alternate Minimum Tax (AMT)?

9. Explain Scheme of taxation of a firm and its partners?

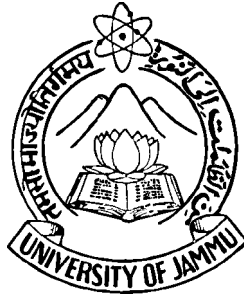
4.20 BOOKS RECOMMENDED

1. Dr. V.K. Singhanian: Students Guide to Income-tax; Taxmann Publications Pvt. Ltd., New Delhi.
2. Girish Ahuja and Ravi Gupta: Systematic Approach to Income-tax and Sales-tax; Bharat Law House, New Delhi.
3. Dr. H.C Meharotra and Dr S. P Goyal: Income Tax Law and Accounts; SahityaBhavan Publications.
4. V. P Gaur & D. B Narang: Income Tax Law & Practice; Kalyani Publishers.
5. V. K Singhanian & Kapil Singhanian: Direct Taxes Law & Practices; Taxman Publications.
6. Mahesh Chandra, D. C Shukla, K. A Mahajan & M. A Shah: Income Tax Law & Practices; pragati Publication, New Delhi.
7. Arvind Tuli & Dr. Neeru Chadda: Conceptual Clarity on Income Tax and Wealth Tax; Kalyani Publication, New Delhi.

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Printed and Published on behalf of the Directorate of Distance Education, University of Jammu, Jammu by the Director, DDE, University of Jammu, Jammu.

INCOME TAX LAW AND PRACTICE-II

Course Review
Gurcharan Singh

Edited by
Rohini Gupta Suri

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