MAA OMWATI DEGREE COLLEGE HASSANPUR (PALWAL)

SYLLABI

FOR INCOME TAX

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SESSION: 2026- 2027

Unit I Basic concepts of Income Tax: Person, assessee, tax year, income, gross total income, total income, casual income, role of PAN and Aadhar number in income tax, tax evasion, tax avoidance, tax planning and tax management, agricultural income, residential status, scope of total income on the basis of residential status.

Unit II Computation of income from Salaries (including retirement benefits); Income from House Property

Unit III Computation of income from Business or Profession (including Depreciation); Income from Capital Gains

Unit IV Income from other sources; Clubbing and aggregation of income; Set-off and carry forward of losses; Exempted income.

Short question

Unit I – Basic Concepts of Income Tax

1. Who is a **person** under the Income Tax Act?
2. Who is an **assessee**?
3. What is meant by a **tax year**?
4. What is **agricultural income**?
5. What is the difference between **tax evasion and tax avoidance**?

Unit II – Income from Salaries & House Property

6. What is meant by **salary income**?
7. What are **retirement benefits**?
8. What is **gratuity**?
9. What is meant by **annual value of a house property**?
10. What is **deduction under Section 24** for house property?

Unit III – Business/Profession & Capital Gains

11. What is meant by **income from business or profession**?

12. What is **depreciation**?
13. What are **capital gains**?
14. What is the difference between **short-term and long-term capital gains**?
15. What is meant by **cost of acquisition**?

Unit IV – Other Sources, Clubbing, Losses & Exempt Income

16. What is meant by **income from other sources**?
17. What is **clubbing of income**?
18. What is meant by **set-off of losses**?
19. What is **carry forward of losses**?
20. What is **exempted income**?

Additional 5 Questions – Important Revision

21. What is the role of **PAN** in income tax?
22. What is the role of **Aadhaar** in income tax?
23. What is **residential status**?
24. What is **gross total income**?
25. What is **total income**?

Answer of short question

Unit I – Basic Concepts of Income Tax

1. Who is a person under the Income Tax Act?
Answer: A person includes an **individual, Hindu Undivided Family (HUF), company, firm, association of persons, body of individuals, local authority, and artificial juridical person**.

2. Who is an assessee?
Answer: An assessee is a **person who is liable to pay tax or any other amount under the Income Tax law**.

3. What is meant by a tax year?
Answer: A tax year is the **12-month period beginning on 1 April**, for which income is calculated and tax liability is determined. Under the new Income-tax Act, 2025, this terminology applies from **Tax Year 2026–27**.

4. What is agricultural income?
Answer: Agricultural income is income earned from **agricultural land and agricultural activities**, such as cultivation of crops, subject to the conditions prescribed by tax law.

5. What is the difference between tax evasion and tax avoidance?
Answer:

- **Tax evasion:** Illegal method of reducing or avoiding tax.
- **Tax avoidance:** Using legal arrangements to reduce tax liability, though some arrangements may be challenged if they are abusive.

Unit II – Income from Salaries & House Property

6. What is meant by salary income?
Answer: Salary income is income received by an employee from an employer, including **salary, wages, bonus, commission, allowances, pension and certain benefits**.

7. What are retirement benefits?
Answer: Retirement benefits are amounts received by an employee on or after retirement, such as **gratuity, pension, leave encashment and provident fund benefits**.

8. What is gratuity?
Answer: Gratuity is a **lump-sum amount paid by an employer to an employee**, generally in recognition of long-term service.

9. What is meant by annual value of a house property?
Answer: Annual value is the **value of the house property considered for calculating taxable income from house property**, generally based on its expected or actual rental value as applicable.

10. What is deduction under Section 24 for house property?
Answer: Section 24 provides deductions from income from house property, mainly for **30% of annual value** and **interest on borrowed capital**, subject to applicable conditions and limits.

Unit III – Business/Profession & Capital Gains

11. What is meant by income from business or profession?
Answer: It is income earned from **carrying on a business, trade, commerce, manufacture or profession**.

12. What is depreciation?
Answer: Depreciation is the **decrease in the value of an asset due to use, wear and tear or obsolescence**. A prescribed depreciation deduction may be allowed for eligible business/professional assets.

13. What are capital gains?
Answer: Capital gains are the **profits or gains arising from the transfer of a capital asset**, such as land, building or shares.

14. What is the difference between short-term and long-term capital gains?
Answer:

- **Short-term capital gain:** Gain from the transfer of an asset held for a relatively shorter period as prescribed by law.
- **Long-term capital gain:** Gain from the transfer of an asset held for the prescribed longer period.

15. What is meant by cost of acquisition?
Answer: Cost of acquisition means the **amount paid to acquire a capital asset**, including certain expenses directly related to its acquisition.

Unit IV – Other Sources, Clubbing, Losses & Exempt Income

16. What is meant by income from other sources?
Answer: It is income that **does not fall under salary, house property, business/profession or capital gains**. Examples include certain interest and dividend income.

17. What is clubbing of income?
Answer: Clubbing of income means **including another person's income in the taxpayer's total income** when the law specifically requires it, such as in certain cases involving a spouse or minor child.

18. What is meant by set-off of losses?
Answer: Set-off of losses means **adjusting a loss against income** according to the rules of income-tax law.

19. What is carry forward of losses?
Answer: Carry forward of losses means **taking an eligible loss to a future tax year** and setting it off against income in accordance with prescribed conditions.

20. What is exempted income?
Answer: Exempted income is income that is **not included in taxable total income**, because it is specifically exempt under the tax law.

Additional 5 Questions – Important Revision

21. What is the role of PAN in income tax?
Answer: PAN (Permanent Account Number) is a unique identification number used for **tax filing, tax payments, financial transactions and communication with the Income Tax Department**.

22. What is the role of Aadhaar in income tax?
Answer: Aadhaar helps in **identity verification, e-verification of returns and certain tax-related services**. PAN-Aadhaar linking is also important for maintaining an operative PAN in applicable cases.

23. What is residential status?
Answer: Residential status determines whether a person is **Resident, Resident but Not Ordinarily Resident (where applicable), or Non-Resident** for tax purposes. It helps determine the **scope of taxable income**.

24. What is gross total income?
Answer: Gross Total Income (GTI) is the **total income calculated under the applicable heads of income before allowing deductions under Chapter VI-A**.

25. What is total income?
Answer: Total income is the **taxable income after making allowable deductions from Gross Total Income**. Tax is generally calculated on this amount.

Long Question

Unit I – Basic Concepts of Income Tax

1. **Explain the meaning of Person, Assessee, Income, Gross Total Income and Total Income under the Income Tax law. Discuss their important features.**
2. **Explain the role and importance of PAN and Aadhaar in income tax. Also discuss the difference between Tax Evasion, Tax Avoidance, Tax Planning and Tax Management.**
3. **What is Agricultural Income? Explain its meaning, different types and the tax treatment of agricultural income under the Income Tax law.**
4. **What is Residential Status? Explain the rules for determining the residential status of an individual and discuss its importance in determining tax liability.**
5. **Explain the scope of total income on the basis of residential status. Discuss the taxability of income in India in the case of Resident, Resident but Not Ordinarily Resident and Non-Resident.**

Unit II – Income from Salaries & House Property

6. **Explain the meaning of Salary under the Income Tax law. Discuss the various components of salary income, including basic salary, allowances, perquisites, bonus and commission.**
7. **Explain the computation of taxable income from salary. Discuss the various deductions and exemptions available from salary income with suitable examples.**
8. **What are retirement benefits? Explain the tax treatment of Gratuity, Pension, Leave Encashment and Provident Fund received by an employee.**
9. **Explain the meaning of Income from House Property. Discuss the method of computation of taxable income from a let-out house property with suitable examples.**
10. **Explain the concept of Annual Value of house property. Discuss the deductions available under Section 24, including the standard deduction and interest on borrowed capital.**

Unit III – Business/Profession & Capital Gains

11. **Explain the meaning of Profits and Gains of Business or Profession. Discuss the various expenses that are allowed and disallowed while computing taxable business income.**
12. **What is depreciation? Explain the concept of depreciation under Income Tax law. Discuss the conditions for claiming depreciation and the method of its computation.**
13. **Explain the meaning of Capital Gain and Capital Asset. Discuss the difference between Short-Term Capital Gain and Long-Term Capital Gain with suitable examples.**
14. **Explain the method of computation of taxable Capital Gains. Discuss Cost of Acquisition, Cost of Improvement and expenses incurred in connection with the transfer of a capital asset.**
15. **What are the exemptions available from Capital Gains? Explain the important provisions relating to exemption from capital gains with suitable examples.**

Unit IV – Other Sources, Clubbing, Losses & Exempt Income

16. **Explain the meaning of Income from Other Sources. Discuss the various types of income taxable under this head and explain the method of computation.**
17. **What is Clubbing of Income? Explain the provisions relating to clubbing of income of spouse, minor child and other persons with suitable examples.**
18. **Explain the provisions relating to Set-off and Carry Forward of Losses. Discuss the rules for intra-head and inter-head adjustment of losses with suitable examples.**
19. **What is Exempt Income? Explain the meaning and importance of exempt income and discuss important examples of income that are exempt from tax.**
20. **Explain the provisions relating to aggregation of income, clubbing of income, set-off and carry forward of losses. Discuss how these provisions affect the computation of total income.**

Answer of long Question

UNIT I – BASIC CONCEPTS OF INCOME TAX

Q. 1. Explain the meaning of Person, Assessee, Income, Gross Total Income and Total Income under the Income Tax law. Discuss their important features.

Ans. Introduction

Income tax is a direct tax imposed by the Government on the income of a person. For understanding income tax, it is important to understand basic terms such as **Person, Assessee, Income, Gross Total Income and Total Income**. These terms form the foundation for computation of tax liability.

1. Meaning of Person

Under income-tax law, the term **Person** has a wide meaning. It does not mean only an individual.

A person generally includes:

1. **Individual** – A human being, such as a salaried employee or businessman.
2. **Hindu Undivided Family (HUF)** – A family recognized as a separate taxable unit.
3. **Company** – A company incorporated under the applicable law.
4. **Firm/LLP** – A partnership firm or eligible limited liability partnership.
5. **Association of Persons (AOP)** – Two or more persons joining together for a common purpose.
6. **Body of Individuals (BOI)** – A group of individuals associated for a common purpose.
7. **Local Authority** – Certain municipal or local governmental bodies.
8. **Artificial Juridical Person** – A legal entity recognized by law but not falling in the above categories.

Thus, the concept of person covers different types of taxpayers.

2. Meaning of Assessee

An **assessee** is a person who is liable to pay tax or any other amount under income-tax law.

An assessee may include:

- A person whose income is taxable.
- A person against whom income-tax proceedings are taken.
- A person who is required to pay tax, interest or penalty.
- A person who is treated as an assessee under the provisions of law.

Example:
If Rahul earns taxable salary income, Rahul is an assessee for income-tax purposes.

3. Meaning of Income

Income means any amount or benefit that is taxable under income-tax law. Income may arise from different sources.

Important sources of income include:

- Salary
- House property
- Business or profession
- Capital gains
- Other sources

Income may be received in **cash or kind**, depending on the nature of the income and the applicable provisions.

4. Gross Total Income

Gross Total Income (GTI) means the aggregate income computed under the different heads of income **before allowing eligible deductions**.

The major heads of income are:

1. Income from Salary
2. Income from House Property
3. Profits and Gains of Business or Profession
4. Capital Gains
5. Income from Other Sources

The income under these heads is calculated according to the relevant provisions. After considering permissible adjustments and set-off of eligible losses, the resulting amount is generally referred to as Gross Total Income before deductions.

5. Total Income

Total Income means the taxable income after allowing the deductions permitted under the applicable provisions from Gross Total Income.

A simple formula is:

Gross Total Income
− Allowable deductions
= Total Income

Tax is calculated on the **Total Income**, subject to the applicable tax rates, rebates, exemptions and other provisions.

Difference between Gross Total Income and Total Income

Basis	Gross Total Income	Total Income
Meaning	Income before eligible deductions	Income after eligible deductions
Deductions	Not deducted	Deducted as permitted
Use	Intermediate stage	Basis for tax computation
Formula	Aggregate income after applicable adjustments	GTI − allowable deductions

Importance of these concepts

These terms are important because:

- They identify the taxpayer.
- They determine what income is taxable.
- They help in calculating taxable income.
- They determine the final tax liability.
- They provide a systematic method of income-tax computation.

Example

Suppose a taxpayer has:

- Salary income = ₹6,00,000
- House property income = ₹1,00,000
- Other income = ₹50,000

If the applicable computation gives a Gross Total Income of ₹7,50,000 and eligible deductions are ₹1,00,000:

GTI = ₹7,50,000
Less: Deductions = ₹1,00,000
Total Income = ₹6,50,000

Conclusion

Thus, **Person and Assessee** identify the taxpayer, while **Income, Gross Total Income and Total Income** help in determining taxable income. A proper understanding of these concepts is essential for calculating the tax liability of a taxpayer.

Q. 2. Explain the role and importance of PAN and Aadhaar in income tax. Also discuss the difference between Tax Evasion, Tax Avoidance, Tax Planning and Tax Management.

Ans. Introduction

PAN and Aadhaar are important identification tools in India's tax system. They help in identification, verification and compliance. At the same time, taxpayers use lawful tax planning and management to reduce or properly manage their tax liability. These should be clearly distinguished from illegal tax evasion.

A. PAN

PAN means Permanent Account Number. It is a unique identification number used by the Income Tax Department to identify taxpayers and track tax-related transactions.

Importance of PAN

1. **Identification of taxpayer**
   PAN provides a unique identity to a taxpayer.
2. **Income-tax return filing**
   PAN is used in filing income-tax returns and carrying out various tax-related activities.
3. **Tax payments**
   PAN helps link tax payments with the correct taxpayer.
4. **Financial transactions**
   PAN is required or quoted for various specified financial transactions.
5. **Communication with Income Tax Department**
   It helps the department maintain and access taxpayer records.
6. **Prevention of tax evasion**
   PAN helps the department track transactions and compare information reported by different sources.

B. Aadhaar

Aadhaar is a unique identity number issued by the Unique Identification Authority of India (UIDAI).

Aadhaar is useful in income-tax compliance for:

- Identity verification.
- E-verification of certain tax-related processes.
- Linking with PAN where applicable.
- Digital authentication and taxpayer services.

The Income Tax Department currently provides a PAN-Aadhaar linking facility. For applicable taxpayers, failure to link can result in PAN becoming inoperative, subject to applicable exemptions and rules.

Importance of linking PAN and Aadhaar

PAN-Aadhaar linking helps:

- Verify the identity of taxpayers.
- Reduce duplicate or false identities.
- Improve transparency.
- Facilitate electronic tax services.
- Strengthen tax administration.

C. Tax Evasion

Tax evasion means illegally avoiding payment of tax.

Examples include:

- Concealing income.
- Maintaining false accounts.
- Showing false expenses.
- Hiding taxable transactions.
- Giving incorrect information to tax authorities.

Tax evasion is **illegal** and may result in interest, penalties and prosecution as applicable.

D. Tax Avoidance

Tax avoidance generally means arranging financial affairs to reduce tax liability by using legal provisions or gaps in the law.

However, aggressive or abusive arrangements designed mainly to obtain an improper tax benefit may be challenged under anti-avoidance provisions.

Example

If a taxpayer uses a deduction specifically permitted by law, it is generally legitimate tax planning. Creating a sham transaction merely to obtain a tax benefit can be challenged.

E. Tax Planning

Tax planning means arranging one's financial affairs in a lawful manner to reduce or defer tax liability while complying with the law.

Examples include:

- Making eligible investments for deductions.
- Selecting an appropriate tax regime where applicable.
- Planning the timing of income and expenses within legal provisions.
- Using available exemptions and deductions.

Features of tax planning

- It is lawful.
- It uses available provisions of tax law.
- It helps reduce tax liability.
- It should be based on genuine transactions.

F. Tax Management

Tax management means properly complying with tax laws and completing tax-related responsibilities on time.

It includes:

- Maintaining proper records.
- Filing tax returns on time.
- Paying taxes on time.
- Maintaining documents.
- Responding to tax notices.
- Correctly deducting and depositing applicable TDS.
- Keeping PAN and other tax information updated.

Difference between the Four Concepts

Basis	Tax Evasion	Tax Avoidance	Tax Planning	Tax Management
Nature	Illegal	Uses legal arrangements but may involve aggressive arrangements	Legal	Legal compliance
Main objective	Illegally reduce tax	Reduce tax through arrangements	Lawfully minimize tax	Properly manage tax obligations
False information	Often involved	Not necessarily	No	No
Risk	Penalty/prosecution	May be challenged if abusive	Generally low when properly done	Low
Example	Hiding income	Artificial arrangement to exploit a loophole	Claiming eligible deduction	Filing return on time

Conclusion

PAN and Aadhaar play an important role in taxpayer identification and digital tax compliance. A responsible taxpayer should follow **tax planning and tax management**, while avoiding illegal **tax evasion** and abusive tax arrangements.

Q. 3. What is Agricultural Income? Explain its meaning, different types and the tax treatment of agricultural income under the Income Tax law.

Ans. Introduction

Agriculture is an important sector of the Indian economy. Income arising from agricultural activities receives special treatment under income-tax law. However, not every income connected with agriculture automatically qualifies as agricultural income.

Meaning of Agricultural Income

Agricultural income generally refers to income derived from **agricultural land situated in India** and from specified agricultural activities connected with such land.

The important requirements are:

1. There must generally be **land situated in India**.
2. The land must be used for **agricultural purposes**.
3. Income must arise from agricultural operations or activities covered by the law.

Types of Agricultural Income

1. Rent or Revenue from Agricultural Land

Income received as rent or revenue from agricultural land situated in India may qualify as agricultural income, subject to the prescribed conditions.

Example:
A farmer leases agricultural land and receives rent from it. Such rent may qualify as agricultural income if the statutory conditions are satisfied.

2. Income from Agricultural Operations

Income earned from cultivation of agricultural land may be agricultural income.

Agricultural operations may include activities such as:

- Preparing the land.
- Sowing seeds.
- Irrigation.
- Growing crops.
- Harvesting.

Example:
Income earned by a farmer from growing and selling wheat, rice or vegetables may qualify as agricultural income, subject to the applicable provisions.

3. Income from Farm Buildings

Income from certain buildings connected with agricultural land may be treated as agricultural income when the statutory conditions relating to the building and its use are satisfied.

4. Income from Nursery Operations

Income from certain nursery activities can receive agricultural-income treatment where the prescribed conditions are satisfied.

Conditions for Agricultural Income

For income to qualify as agricultural income, the following factors are important:

- The land should generally be situated in India.
- The land should be used for agricultural purposes.
- There should be a connection between the income and agricultural operations or the agricultural land.
- The activity must fall within the definition provided by income-tax law.

Tax Treatment of Agricultural Income

Agricultural income is generally **exempt from central income tax** when it qualifies as agricultural income under the applicable provisions.

However, this does not mean that agricultural income is completely irrelevant for all tax purposes.

Partial Integration

In certain cases, agricultural income is considered for determining the applicable rate of tax on non-agricultural income. This process is commonly called **partial integration of agricultural income with non-agricultural income**.

It is subject to prescribed conditions relating to the amount of agricultural and non-agricultural income.

Example

Suppose a taxpayer has:

- Non-agricultural income = ₹8,00,000
- Agricultural income = ₹2,00,000

The agricultural income may not itself be directly taxed as ordinary taxable income, but where the conditions for partial integration are satisfied, it can affect the rate applied to the taxable non-agricultural income.

Agricultural Income and Non-Agricultural Income

Agricultural Income	Non-Agricultural Income
Arises from qualifying agricultural activities	Arises from other sources
Generally exempt subject to law	Generally taxable subject to exemptions/deductions

Agricultural Income	Non-Agricultural Income
May influence tax rate through partial integration	Forms part of taxable income
Must satisfy statutory conditions	Does not require agricultural connection

Examples

Agricultural income

- Sale proceeds from crops grown on agricultural land.
- Rent from qualifying agricultural land.
- Certain income from qualifying farm buildings.
- Certain qualifying nursery income.

Non-agricultural income

- Salary received by an employee.
- Interest from a bank.
- Income from a non-agricultural business.
- Capital gains from sale of shares.

Importance of Agricultural Income

Agricultural-income provisions are important because:

1. They provide special tax treatment to genuine agricultural income.
2. They recognize the importance of agriculture.
3. They distinguish agricultural income from other taxable income.
4. They may affect the tax rate through partial integration.
5. They help prevent misuse of the agricultural-income exemption by requiring statutory conditions to be satisfied.

Conclusion

Agricultural income is income arising from qualifying agricultural land and agricultural activities. It generally enjoys exemption from central income tax, but it can influence the tax rate on other income in cases where partial integration applies. Therefore, it is important to correctly identify whether an income actually qualifies as agricultural income under the law.

Q. 4. What is Residential Status? Explain the rules for determining the residential status of an individual and discuss its importance in determining tax liability.

Ans. Introduction

Residential status is an important concept in income tax because the taxability of a person's income depends largely on whether the person is **Resident, Resident but Not Ordinarily Resident (RNOR), or Non-Resident**.

Residential status is determined separately for each tax year. The Income Tax Department confirms that the residential-status rules under the Income-tax Act, 2025 apply to tax years beginning on or after **1 April 2026**, while earlier years continue under the 1961 Act.

Meaning of Residential Status

Residential status does **not** simply depend on citizenship.

A person may be an Indian citizen but a non-resident for income-tax purposes. Similarly, residential status is primarily determined according to the person's **physical stay in India and other statutory conditions**.

Categories of Residential Status

For an individual, the main categories are:

1. **Resident**
2. **Resident and Ordinarily Resident (ROR)**
3. **Resident but Not Ordinarily Resident (RNOR)**
4. **Non-Resident (NR)**

Basic Test for Residence

For tax years beginning on or after 1 April 2026, an individual is generally treated as resident if the prescribed stay conditions are satisfied.

The basic stay test includes:

- Stay in India for **182 days or more** during the relevant tax year; or
- Stay in India for **60 days or more** during the relevant tax year and **365 days or more** during the preceding four tax years,

subject to the special rules and exceptions provided by law.

Special Rules

Certain special rules apply to Indian citizens and persons of Indian origin visiting India, and to Indian citizens meeting specified income and tax-residency conditions.

The purpose of these provisions is to prevent situations where a person may otherwise avoid tax residence despite having substantial economic connections with India.

Resident but Not Ordinarily Resident

A person who is resident may be classified as **RNOR** if the prescribed conditions relating to residence in earlier years or stay in India in earlier years are satisfied.

Under the current law, the Income Tax Department states that the relevant continuity tests include being non-resident in **9 out of the 10 preceding years** or having stayed in India for **729 days or less during the preceding 7 years**.

Non-Resident

An individual who does not satisfy the conditions for being resident is generally treated as a **Non-Resident**.

Importance of Residential Status

Residential status is important because it determines the **scope of income that may be taxable in India**.

1. Resident and Ordinarily Resident

A resident ordinarily resident is generally taxable in India on:

- Income received or deemed to be received in India.
- Income accruing or arising or deemed to accrue or arise in India.
- Income accruing or arising outside India.

Thus, the global income of an ROR is generally within the Indian tax net, subject to the applicable provisions.

2. Resident but Not Ordinarily Resident

RNOR enjoys a more limited scope of taxation.

Generally, foreign income is not taxable in India merely because it is foreign income, unless it is derived from a business controlled in or a profession set up in India, or falls within another taxable category.

3. Non-Resident

A non-resident is generally taxable in India on income:

- Received or deemed to be received in India; or
- Accruing or arising or deemed to accrue or arise in India.

Foreign income that has no taxable connection with India is generally outside the Indian tax scope.

Example

Suppose:

- A = Resident and Ordinarily Resident
- B = RNOR
- C = Non-Resident

If all three receive ₹5 lakh from an Indian source, that Indian income may be taxable in India according to the applicable provisions.

If they receive ₹5 lakh from a foreign source, the tax treatment can differ significantly depending on their residential status.

Difference between Residential Categories

Basis	ROR	RNOR	NR
Indian income	Generally taxable	Generally taxable	Generally taxable
Foreign income	Generally taxable	Limited taxation	Generally not taxable merely because it is foreign income
Importance	Global income generally considered	Intermediate category	Source/receipt in India becomes important

Conclusion

Residential status is one of the most important concepts in income tax. It determines the extent to which a person's income falls within the Indian tax system. Therefore, every taxpayer should correctly determine residential status for each tax year before calculating taxable income.

Q. 5. Explain the scope of total income on the basis of residential status. Discuss the taxability of income in India in the case of Resident, Resident but Not Ordinarily Resident and Non-Resident.

Ans. Introduction

The term **scope of total income** refers to the extent of income that is considered taxable in India. The scope mainly depends on the residential status of the taxpayer.

The three important categories are:

1. **Resident and Ordinarily Resident (ROR)**
2. **Resident but Not Ordinarily Resident (RNOR)**
3. **Non-Resident (NR)**

Residential status therefore plays a major role in determining tax liability.

1. Resident and Ordinarily Resident

An ROR is generally taxable in India on a **global basis**.

This means the following types of income are generally considered:

- Income received in India.
- Income accruing or arising in India.
- Income deemed to accrue or arise in India.
- Income accruing or arising outside India.

Example

Suppose an ROR has:

- Indian salary = ₹6,00,000
- Indian bank interest = ₹50,000
- Foreign business income = ₹3,00,000

The foreign business income is generally also included in the Indian tax computation, subject to the applicable law and relief provisions.

Thus, **ROR → Global income generally taxable.**

2. Resident but Not Ordinarily Resident

RNOR occupies an intermediate position between ROR and NR.

An RNOR is generally taxable on:

1. Income received or deemed to be received in India.
2. Income accruing or arising or deemed to accrue or arise in India.
3. Certain foreign income from a business controlled in India or a profession set up in India.

Other foreign income is generally outside the Indian tax scope.

Example

Suppose an RNOR receives:

- Indian salary = ₹5,00,000
- Indian interest = ₹50,000
- Foreign investment income = ₹2,00,000

The Indian income is generally taxable in India. The foreign investment income may not be taxable in India merely because the person is RNOR, subject to the applicable provisions.

Thus:

RNOR → Indian income + specified foreign income.

3. Non-Resident

A Non-Resident is generally taxed only on income that has the required connection with India.

The important categories include:

Income received in India

If income is received or deemed to be received in India, it may be taxable in India.

Income accruing in India

Income that accrues or arises in India may be taxable.

Income deemed to accrue or arise in India

Certain types of foreign-source income are specifically treated by law as accruing or arising in India.

Foreign income

Foreign income with no taxable connection with India is generally not taxable in India in the hands of a non-resident.

Thus:

NR → Mainly Indian-source/India-connected income.

Scope of Total Income – Comparison

Particulars	ROR	RNOR	NR
Income received in India	Taxable	Taxable	Taxable
Income accruing in India	Taxable	Taxable	Taxable
Income deemed to accrue in India	Taxable	Taxable	Taxable
Foreign income	Generally taxable	Generally not taxable, subject to specified exceptions	Generally not taxable if no Indian connection
Business controlled from India	Taxable	Specified foreign income may be taxable	Generally depends on Indian tax connection
Global income	Generally taxable	Limited	Generally not taxable

Importance of Residential Status

Residential status is important because two persons having exactly the same amount of income may have different tax liabilities due to different residential statuses.

Example

Suppose Rahul and Amit each earn:

- Indian income = ₹7 lakh
- Foreign income = ₹3 lakh

If Rahul is an ROR, his foreign income will generally also be considered for Indian tax purposes.

If Amit is an NR, the foreign income may generally remain outside Indian taxation if it has no taxable connection with India.

Therefore, residential status can significantly affect tax liability.

Important Points

1. Citizenship is different from residential status

Being an Indian citizen does not automatically make a person a resident for income-tax purposes.

2. Residential status is determined every year

A person's residential status can change from one tax year to another depending on the circumstances and statutory tests.

3. Source of income is important

For an NR, the place where income is received or where it accrues/arises is particularly important.

4. Foreign income is important for residents

An ROR generally has the widest tax scope because foreign income may also be included.

5. Double taxation relief

Where foreign income is taxable in India as well as in another country, relief may be available under applicable tax treaties or domestic provisions, subject to the relevant conditions.

Simple Illustration

Suppose a taxpayer earns:

Source	Income
Salary in India	₹6,00,000
Bank interest in India	₹1,00,000
Foreign income	₹3,00,000
Total	**₹10,00,000**

If taxpayer is ROR

Generally, the full ₹10,00,000 is considered for Indian taxation, subject to applicable provisions.

If taxpayer is RNOR

Indian income is generally taxable, while foreign income is considered only where the applicable conditions make it taxable.

If taxpayer is NR

The ₹7,00,000 Indian income is generally taxable, while the foreign income is generally outside Indian taxation if it has no taxable connection with India.

Conclusion

The scope of total income is closely connected with residential status. **ROR has the widest scope of taxation, RNOR has an intermediate scope, and NR has the most limited scope**, generally focusing on income received, accruing or deemed to accrue in India. Correct determination of residential status is therefore essential for calculating the correct tax liability.

Unit :- 2

Q. 6. Explain the meaning of Salary under the Income Tax law. Discuss the various components of salary income, including basic salary, allowances, perquisites, bonus and commission.

Ans. Introduction

Salary is one of the five major heads of income under the Income-tax Act. Income received by an employee from an employer for services rendered is generally taxable under the head **"Salaries."**

For an amount to be taxable under the head Salaries, there must generally be an **employer–employee relationship**.

Salary income includes not only basic salary but also allowances, perquisites, bonus, commission, pension and certain other payments.

Meaning of Salary

Salary means remuneration received by an employee from an employer in return for services rendered.

It may be received in:

- Cash
- Kind
- Regular payments
- Lump-sum payments
- Benefits or facilities

Salary is generally taxable on the basis of the **due or receipt rule**, subject to the provisions of the law.

Important Components of Salary

1. Basic Salary

Basic salary is the fixed amount paid to an employee according to the terms of employment.

For example:

Basic salary = ₹40,000 per month

Annual basic salary:

₹40,000 × 12 = ₹4,80,000

Basic salary is fully taxable.

It is also important because several allowances and retirement benefits may be calculated with reference to basic salary.

2. Dearness Allowance

Dearness Allowance (DA) is paid to compensate employees for the effect of inflation.

The tax treatment depends on the applicable provisions and, in some cases, whether it forms part of salary for specific purposes such as retirement benefits.

Example:

Basic salary = ₹4,80,000
DA = ₹60,000

Both may form part of taxable salary, subject to the applicable rules.

3. Allowances

An allowance is a fixed amount paid by an employer to an employee for a particular purpose or to meet certain expenses.

Allowances may be:

1. Fully taxable
2. Partly exempt
3. Fully exempt, where specifically provided

Examples of allowances

- House Rent Allowance (HRA)
- Transport-related allowances

- Children Education Allowance
- Leave Travel Allowance
- Entertainment Allowance
- City Compensatory Allowance
- Special Allowance

4. House Rent Allowance

HRA is paid to an employee to meet the cost of rented accommodation.

For eligible employees, exemption is available subject to prescribed conditions and limits.

Under the old regime, exemption under Section 10(13A) is generally the least of:

1. Actual HRA received
2. Rent paid minus 10% of salary
3. 50% of salary for specified metropolitan cities or 40% for other cities

The remaining amount is taxable.

5. Perquisites

A **perquisite** is a benefit or facility provided by an employer to an employee in addition to salary.

Examples include:

- Rent-free accommodation
- Concessional accommodation
- Motor car facility
- Free or concessional education
- Interest-free or concessional loans
- Domestic servants
- Certain employer-provided benefits

The taxability of a perquisite depends upon the nature of the benefit and the applicable rules.

6. Bonus

Bonus is an additional payment made by an employer to an employee.

It may be paid:

- Annually
- On achieving targets
- As a performance bonus
- As a festival bonus

Bonus is generally taxable as salary according to the applicable tax rules.

Example:

Basic salary = ₹5,00,000
Bonus = ₹50,000

Taxable salary includes the bonus, subject to applicable provisions.

7. Commission

Commission is an amount paid to an employee based on sales, performance or business generated.

For example, a salesperson may receive:

Basic salary = ₹3,60,000
Commission = ₹60,000

The commission forms part of salary income.

Commission can also be relevant in calculating certain exemptions or deductions where the law specifically uses salary as a base.

8. Pension

Pension received from an employer after retirement may be taxable under the head Salaries, subject to applicable exemptions and rules.

Pension may be:

- Commuted pension
- Uncommuted pension

Their tax treatment is different.

9. Leave Encashment

Leave encashment means receiving money in place of accumulated leave.

Its tax treatment depends on whether the employee is:

- A government employee
- A non-government employee
- Receiving the amount during service
- Receiving it at retirement

General Structure of Salary

A simple structure can be shown as:

Basic Salary

- **Dearness Allowance**
- **Bonus**
- **Commission**

- **Taxable Allowances**
- **Taxable Perquisites**
- **Retirement Benefits, where taxable**
  = Gross Salary

Then applicable deductions/exemptions are considered to determine taxable salary.

Example

Suppose an employee receives:

Particular	Amount
Basic Salary	₹5,00,000
DA	₹60,000
Bonus	₹50,000
Commission	₹30,000
Taxable Allowances	₹40,000
Taxable Perquisites	₹20,000
Gross Salary	**₹7,00,000**

Thus, the employee's gross salary is **₹7,00,000**, before considering applicable exemptions and deductions.

Conclusion

Salary income includes much more than basic pay. It may consist of **basic salary, DA, allowances, perquisites, bonus, commission, pension and other employment-related payments**. Proper classification of each component is necessary to calculate the employee's taxable income correctly.

Q. 7. Explain the computation of taxable income from salary. Discuss the various deductions and exemptions available from salary income with suitable examples.

Ans. Introduction

Salary income is calculated by identifying all taxable components of salary and then allowing the exemptions and deductions available under the Income-tax Act.

The computation generally follows a systematic process.

Steps for Computation of Taxable Salary

Step 1: Calculate Basic Salary

Basic salary received or due during the relevant period is considered.

Step 2: Add taxable allowances

Examples include:

- Fully taxable special allowance
- Taxable portion of HRA
- Taxable portion of other allowances

Step 3: Add taxable perquisites

Taxable perquisites provided by the employer are included.

Step 4: Add bonus and commission

Bonus, commission and other taxable employment-related payments are added.

Step 5: Add taxable retirement benefits

Taxable portions of gratuity, pension, leave encashment, etc., are included where applicable.

This gives **Gross Salary**.

Formula

Gross Salary = Basic Salary + Allowances + Perquisites + Bonus + Commission + Taxable Retirement Benefits

Then:

Gross Salary
− Exemptions
− Deductions under Section 16
= Income Chargeable under Salaries

Major Exemptions from Salary

1. House Rent Allowance

HRA exemption is available to eligible employees subject to prescribed conditions.

Under the old tax regime, the exemption is generally the least of:

- Actual HRA received
- Rent paid minus 10% of salary

- 50% of salary for specified metropolitan cities or 40% for other cities

The balance is taxable.

Example

Suppose:

HRA received = ₹1,20,000
Rent paid = ₹1,50,000
Salary for HRA purposes = ₹4,00,000

Rent minus 10% salary:

₹1,50,000 − ₹40,000 = **₹1,10,000**

The exemption would be determined by comparing the prescribed alternatives.

Deductions from Salary

1. Standard Deduction

A standard deduction is available to eligible salaried taxpayers subject to the applicable tax regime and prescribed amount.

It is allowed without requiring the taxpayer to submit individual expense bills for the deduction.

2. Entertainment Allowance

Entertainment allowance deduction is available under the old regime to certain government employees, subject to prescribed conditions and limits.

The deduction is not generally available to private-sector employees.

3. Professional Tax

Professional tax paid by an employee is deductible from salary income subject to the applicable provisions.

Example of Salary Computation

Suppose an employee has:

Particular	Amount
Basic Salary	₹6,00,000
DA	₹60,000

Particular	Amount
Bonus	₹50,000
HRA	₹1,20,000
Taxable Perquisites	₹20,000
Gross Salary	**₹8,50,000**

Suppose eligible HRA exemption = ₹80,000.

Then:

Gross Salary = ₹8,50,000
Less: HRA exemption = ₹80,000
Balance = ₹7,70,000

Suppose applicable standard deduction = ₹50,000.

Then:

Taxable Salary = ₹7,20,000

The exact deduction amount depends on the applicable tax regime and tax year.

Importance of Correct Computation

Correct salary computation is important because:

1. It determines taxable income.
2. It prevents excess payment of tax.
3. It helps the employee claim legitimate exemptions.
4. It ensures compliance with income-tax law.
5. It helps in filing an accurate income-tax return.

Conclusion

Taxable salary is calculated by first determining **gross salary**, then deducting applicable exemptions and deductions. Important components include basic salary, allowances, perquisites, bonus, commission and retirement benefits. Proper application of exemptions and deductions is essential for arriving at the correct taxable salary.

Q. 8. What are retirement benefits? Explain the tax treatment of Gratuity, Pension, Leave Encashment and Provident Fund received by an employee.

Ans. Introduction

Retirement benefits are payments and benefits received by an employee on retirement, resignation, termination or after completion of service.

Important retirement benefits include:

1. Gratuity
2. Pension
3. Leave Encashment
4. Provident Fund

Their tax treatment depends on the nature of employment, type of benefit and applicable provisions.

1. Gratuity

Gratuity is a lump-sum payment made by an employer to an employee in recognition of past services.

It is commonly received:

- At retirement
- On resignation
- On termination
- On death, subject to applicable rules

Tax Treatment

The exemption depends on the category of employee and applicable conditions.

Government employees

Gratuity received by specified government employees is generally exempt subject to the applicable provisions.

Employees covered by the Payment of Gratuity Act

Exemption is available subject to the prescribed formula and statutory maximum.

Other employees

Exemption is available subject to prescribed conditions and limits.

The excess over the exempt amount is taxable.

2. Pension

Pension is a periodic payment received after retirement.

There are two important forms:

A. Uncommuted Pension

This is regular pension received periodically.

It is generally taxable as salary.

B. Commuted Pension

Under commutation, a portion of future pension is received as a lump sum.

The tax treatment depends on whether the employee is a government employee and whether gratuity is received, subject to the applicable exemption rules.

3. Leave Encashment

Leave encashment means receiving payment for accumulated leave.

It may be received:

- During service
- At retirement
- At resignation

During service

Leave encashment received during employment is generally taxable.

At retirement

For government employees, the applicable exemption is generally broader.

For non-government employees, exemption is subject to prescribed conditions and limits.

The taxable portion is included in salary income.

4. Provident Fund

Provident Fund is a retirement savings arrangement under which contributions are made by the employee and, in eligible cases, by the employer.

Important types include:

1. Statutory Provident Fund

2. Recognised Provident Fund
3. Unrecognised Provident Fund
4. Public Provident Fund

Their tax treatment differs.

Statutory Provident Fund

Subject to applicable conditions, contributions and interest may receive favorable tax treatment.

Recognised Provident Fund

Tax treatment depends on prescribed limits and conditions concerning:

- Employee contribution
- Employer contribution
- Interest
- Final withdrawal

Unrecognised Provident Fund

Tax treatment is different and depends upon the components of the amount received.

Public Provident Fund

PPF enjoys tax benefits under the applicable provisions, subject to the statutory rules.

Summary Table

Retirement Benefit	General Tax Treatment
Gratuity	Exemption available subject to employee category and limits
Uncommuted pension	Generally taxable
Commuted pension	Fully/partly exempt depending on applicable conditions
Leave encashment	Exemption subject to employee category and limits
Provident Fund	Depends on type of PF and applicable conditions

Example

Suppose an employee receives:

- Gratuity = ₹8,00,000
- Pension = ₹2,40,000
- Leave encashment = ₹5,00,000
- Provident Fund = ₹10,00,000

The entire amounts cannot simply be treated as taxable. Each benefit must be examined separately under the applicable exemption and tax rules.

For example, the taxable pension may be determined after considering the applicable treatment of commuted/uncommuted pension, while gratuity and leave encashment require examination of the employee's category and applicable limits.

Conclusion

Retirement benefits provide financial security to employees after retirement. However, their tax treatment differs significantly. Therefore, **gratuity, pension, leave encashment and provident fund should be examined separately** before calculating taxable salary.

Q. 9. Explain the meaning of Income from House Property. Discuss the method of computation of taxable income from a let-out house property with suitable examples.

Ans. Introduction

Income-tax law provides a separate head called **"Income from House Property."**

Income from a building or land attached to a building may be taxable under this head when the statutory conditions are satisfied.

The person must generally be the **owner or deemed owner** of the property.

Meaning of House Property

House property generally includes:

- Residential buildings
- Commercial buildings
- Flats
- Shops
- Offices
- Buildings with attached land

Income from such property may be taxable under the head "Income from House Property."

Conditions for Taxability

Generally, three conditions are important:

1. There must be a building or land appurtenant to it

The property should be a building or land attached to a building.

2. The taxpayer should be the owner/deemed owner

Income is generally taxable in the hands of the owner or deemed owner.

3. The property should not be occupied by the owner for business/profession

Where a property is used by the owner for the purposes of a business or profession whose income is chargeable to tax, different treatment applies.

Types of House Property

House property may generally be:

1. Let-out property
2. Self-occupied property
3. Deemed let-out property in applicable cases

This question relates specifically to **let-out property**.

Computation of Income from Let-Out House Property

The general format is:

Gross Annual Value (GAV)
− **Municipal Taxes actually paid by owner**
= **Net Annual Value (NAV)**
− **Standard Deduction under Section 24(a)**
− **Interest on Borrowed Capital under Section 24(b)**
= **Income from House Property**

Step 1: Determine Gross Annual Value

For a let-out property, annual value is determined according to the prescribed rules, taking into account factors such as:

- Expected rent
- Actual rent
- Vacancy
- Unrealised rent, where applicable

Step 2: Deduct Municipal Taxes

Municipal taxes are deductible if:

- They are borne by the owner; and
- They are actually paid during the relevant year.

The amount after deduction is called **Net Annual Value**.

Formula

NAV = GAV − Municipal Taxes Actually Paid

Step 3: Standard Deduction

Under Section 24(a), a standard deduction of **30% of Net Annual Value** is allowed.

It is allowed irrespective of the actual amount spent on repairs and maintenance.

Step 4: Interest on Borrowed Capital

Interest payable on borrowed capital used for acquisition, construction, repair, renewal or reconstruction of the property may be deductible subject to the applicable provisions and limits.

For a let-out property, the interest deduction is generally available subject to the applicable rules.

Example

Suppose:

- Expected rent = ₹3,60,000
- Actual rent = ₹4,00,000
- Municipal taxes paid = ₹40,000
- Interest on housing loan = ₹1,00,000

Assume that after applying the relevant annual-value rules:

Gross Annual Value = ₹4,00,000

Less: Municipal taxes = ₹40,000

Net Annual Value

₹4,00,000 − ₹40,000 = **₹3,60,000**

Standard Deduction

30% of ₹3,60,000:

₹1,08,000

Interest

Interest = **₹1,00,000**

Income from House Property

₹3,60,000
− ₹1,08,000

− ₹1,00,000
= **₹1,52,000**

Therefore:

Taxable Income from House Property = ₹1,52,000

Importance of House Property Computation

The rules are important because:

- Rental income is systematically calculated.
- Municipal taxes are given appropriate treatment.
- A standard deduction is allowed for maintenance.
- Interest on borrowed capital may be deducted.
- The correct taxable income can be determined.

Conclusion

Income from a let-out house property is calculated by determining the **Gross Annual Value**, deducting eligible municipal taxes to arrive at **Net Annual Value**, and then allowing the standard deduction and eligible interest deduction. This systematic method ensures correct computation of taxable house-property income.

Q. 10. Explain the concept of Annual Value of house property. Discuss the deductions available under Section 24, including the standard deduction and interest on borrowed capital.

Ans. Introduction

Annual Value is one of the most important concepts in the computation of income from house property.

The annual value represents the amount for which a property may reasonably be expected to be let out, subject to the specific rules applicable to the property.

Meaning of Annual Value

Annual value is the amount used to determine taxable income from a house property.

For a let-out property, determination of annual value involves consideration of:

- Expected rent
- Actual rent
- Vacancy
- Unrealised rent
- Municipal taxes

Determination of Annual Value

The computation can be understood through the following steps.

1. Expected Rent

Expected rent is generally determined with reference to the reasonable rent that the property could fetch, subject to the applicable rules.

Factors may include:

- Municipal valuation
- Fair rent
- Standard rent, where applicable

2. Actual Rent

Actual rent means the rent actually received or receivable by the owner.

If actual rent is higher than expected rent, the applicable rules determine the Gross Annual Value.

3. Vacancy

If a property remains vacant for part of the year and the conditions prescribed by law are satisfied, the vacancy may affect the determination of annual value.

4. Unrealised Rent

Unrealised rent means rent that the owner could not recover from the tenant.

Subject to prescribed conditions, unrealised rent may be excluded while determining actual rent for annual-value purposes.

Gross Annual Value

After applying the applicable rules, the amount determined is the **Gross Annual Value (GAV)**.

Then:

GAV − Municipal Taxes Actually Paid = Net Annual Value (NAV)

Deductions under Section 24

Section 24 provides two important deductions:

Section 24(a) – Standard Deduction

A standard deduction of **30% of Net Annual Value** is allowed.

Section 24(b) – Interest on Borrowed Capital

Interest payable on borrowed capital used for acquisition, construction, repair, renewal or reconstruction of the property is deductible subject to applicable conditions.

1. Standard Deduction – Section 24(a)

The standard deduction is:

30% of Net Annual Value

The actual amount spent on:

- Repairs
- Maintenance
- Painting
- Renovation

does not determine the amount of the standard deduction.

Example

If:

Net Annual Value = ₹5,00,000

Then:

30% of ₹5,00,000 = **₹1,50,000**

Therefore, standard deduction = **₹1,50,000**.

2. Interest on Borrowed Capital – Section 24(b)

Interest paid or payable on borrowed capital used for the acquisition, construction, repair, renewal or reconstruction of a property may be deductible under Section 24(b), subject to applicable conditions.

The treatment differs depending on whether the property is:

- Let out
- Self-occupied
- Used for specified purposes

For a let-out property, the interest deduction is generally allowed subject to the applicable provisions.

Example of Complete Computation

Suppose:

- Gross Annual Value = ₹6,00,000
- Municipal taxes paid = ₹60,000
- Interest on housing loan = ₹1,50,000

Step 1: Net Annual Value

GAV = ₹6,00,000

Less: Municipal taxes = ₹60,000

NAV = ₹5,40,000

Step 2: Standard Deduction

30% of ₹5,40,000:

₹1,62,000

Step 3: Interest

Interest = **₹1,50,000**

Step 4: Income from House Property

₹5,40,000
− ₹1,62,000
− ₹1,50,000
= **₹2,28,000**

Therefore:

Income from House Property = ₹2,28,000

Importance of Section 24

Section 24 is important because it provides deductions that recognize:

1. General maintenance of the property through the standard deduction.
2. Financing costs through interest on borrowed capital.
3. A systematic method of calculating taxable house-property income.

Summary Table

Particular	Amount

Particular	Amount
Gross Annual Value	₹6,00,000
Less: Municipal Taxes	₹60,000
Net Annual Value	₹5,40,000
Less: Standard Deduction @ 30%	₹1,62,000
Less: Interest on Borrowed Capital	₹1,50,000
Income from House Property	**₹2,28,000**

Unit :- 3

Q. 11. Explain the meaning of Profits and Gains of Business or Profession. Discuss the various expenses that are allowed and disallowed while computing taxable business income.

Ans. Introduction

Income earned from carrying on a business or profession is taxable under the head **"Profits and Gains of Business or Profession" (PGBP)**.

The purpose of computing business income is to determine the **real taxable profit** of a business after allowing expenses that are permitted under income-tax law and disallowing expenses that are not permitted.

Meaning of Business

The term **business** includes activities such as:

- Trade
- Commerce
- Manufacture
- Buying and selling of goods
- Providing business services
- Other commercial activities

A business may be carried on by an individual, firm, company, HUF or other eligible person.

Example

If Ravi purchases goods for ₹5,00,000 and sells them for ₹7,00,000, the business profit before other expenses is:

₹7,00,000 − ₹5,00,000 = ₹2,00,000

Meaning of Profession

A profession generally involves an occupation requiring specialized knowledge, skill or training.

Examples include:

- Doctor
- Lawyer
- Chartered Accountant
- Architect
- Engineer
- Consultant

Income earned from professional activities is also taxable under PGBP.

Computation of Business Income

Business income is generally calculated as:

Net Profit as per Profit & Loss Account

Add: Expenses debited but not allowable

Less: Income credited but taxable under another head / expenses allowable but not debited, as applicable

= Taxable Business Income

Expenses Allowed While Computing Business Income

An expense is generally allowable when it is incurred **wholly and exclusively for the purposes of the business or profession**, subject to specific provisions.

1. Salary and Wages

Salary and wages paid to employees for business purposes are generally deductible.

Example:

Salary paid to employees = ₹3,00,000

This can generally be claimed as a business expense, subject to applicable provisions.

2. Rent

Rent paid for business premises is generally deductible.

For example:

Shop rent = ₹2,40,000 per year

The rent may be allowed as a business expense if the relevant conditions are satisfied.

3. Repairs and Maintenance

Expenses incurred for repairs and maintenance of business premises, machinery and other business assets may be deductible, subject to the applicable rules.

4. Electricity and Telephone Expenses

Expenses relating to electricity, telephone, internet and other utilities used for business purposes are generally deductible.

If an expense has both personal and business use, the personal portion is not allowable.

5. Insurance

Insurance premiums relating to business assets and business risks may be deductible.

Examples:

- Insurance of factory building
- Insurance of machinery
- Insurance of business stock

6. Interest on Business Loans

Interest paid on money borrowed for business purposes is generally deductible, subject to applicable provisions.

Example:

Interest on business loan = ₹80,000

It may be allowed as a business expense if the borrowing and use satisfy the applicable requirements.

7. Depreciation

Depreciation on eligible business assets is allowed according to the prescribed rules.

Examples:

- Machinery
- Furniture
- Buildings
- Computers
- Vehicles used for business

8. Advertisement Expenses

Expenses incurred on genuine business advertising and promotion are generally deductible, subject to applicable restrictions.

9. Travelling Expenses

Business-related travelling expenses may be allowed.

However, personal travelling expenses are not deductible.

10. Professional and Legal Expenses

Fees paid to lawyers, accountants, consultants and other professionals for business purposes may be deductible.

Expenses Disallowed

Certain expenses are not allowed while computing taxable business income.

1. Personal Expenses

Expenses incurred for personal purposes are not deductible.

Example:

A businessman spends ₹50,000 on a family vacation.

This is a personal expense and cannot be claimed as a business expense merely because the person owns a business.

2. Capital Expenditure

Capital expenditure is generally not deducted as an ordinary revenue expense.

For example:

- Purchase of a building
- Purchase of machinery
- Purchase of furniture

Instead, depreciation may be available where permitted.

3. Income Tax

Income tax paid by a taxpayer on business income is generally not allowed as a business expense.

4. Penalties and Fines for Violation of Law

Penalties or fines for an offence or for violation of law are generally not deductible.

However, legitimate business expenditure that is not penal in nature may be treated differently depending on the applicable provisions.

5. Excessive or Unreasonable Payments

Certain payments to related persons may be disallowed to the extent they are considered excessive or unreasonable under the applicable provisions.

6. Expenses Relating to Exempt Income

Certain expenses relating to income that does not form part of total income may be disallowed according to the applicable provisions.

7. Certain Cash Payments

Expenses paid in cash beyond the prescribed limits may be disallowed, subject to the exceptions provided by law.

8. Unpaid Statutory Liabilities

Certain statutory liabilities are deductible only when the conditions relating to actual payment are satisfied.

Difference Between Allowed and Disallowed Expenses

Allowed Expenses	Disallowed Expenses
Business salary	Personal expenses
Business rent	Income tax
Business electricity	Capital expenditure as ordinary expense
Business insurance	Certain penalties/fines
Business interest	Certain excessive related-party payments
Business advertising	Certain prohibited cash payments
Business depreciation	Certain expenses relating to exempt income

Example of Computation

Suppose a business has:

Net Profit as per P&L = ₹8,00,000

Expenses included in P&L:

- Income tax = ₹50,000
- Personal expenses = ₹30,000
- Depreciation as per books = ₹40,000

Tax depreciation allowable = ₹60,000.

Computation

Net Profit = ₹8,00,000

Add:

Income tax = ₹50,000
Personal expenses = ₹30,000
Book depreciation = ₹40,000

Subtotal:

₹9,20,000

Less:

Tax depreciation allowable = ₹60,000

Taxable Business Income = ₹8,60,000

This is a simplified illustration; actual computation requires applying all relevant provisions.

Conclusion

Profits and Gains of Business or Profession represent income earned from business or professional activities. To calculate taxable business income, genuine business expenses are allowed while personal, capital, prohibited or otherwise specifically disallowed expenses are excluded. Proper classification of expenses is therefore essential for correct tax computation.

12. What is depreciation? Explain the concept of depreciation under Income Tax law. Discuss the conditions for claiming depreciation and the method of its computation.

Introduction

Depreciation means the reduction in the value of an asset due to **wear and tear, use, obsolescence or passage of time**.

Business assets lose their value as they are used. Income-tax law therefore allows depreciation on eligible assets used for business or profession, subject to prescribed conditions.

Meaning of Depreciation

Depreciation is an allowance representing the decline in the value of an eligible asset used for business or professional purposes.

Examples of depreciable assets include:

- Buildings
- Machinery
- Plant
- Furniture
- Computers
- Certain other eligible assets

Importance of Depreciation

Depreciation is important because:

1. It recognizes the reduction in value of business assets.
2. It provides a deduction while computing business income.
3. It helps determine the correct taxable profit.
4. It encourages businesses to invest in productive assets.
5. It spreads the cost of an asset over its useful period according to tax rules.

Conditions for Claiming Depreciation

1. Ownership

The taxpayer should generally own the asset, wholly or partly, subject to the specific provisions applicable to certain situations.

2. Asset Must Be Eligible

The asset must fall within the category of assets on which depreciation is allowed.

Examples:

- Building
- Machinery
- Plant
- Furniture
- Certain intangible assets under the applicable provisions

3. Use for Business or Profession

The asset should be used for the purposes of business or profession.

If an asset is partly used for business and partly for personal purposes, depreciation may be restricted to the business-use portion.

4. Actual Use

The asset must be put to use during the relevant period for depreciation to be available according to the applicable rules.

Where an asset is acquired and put to use for less than the prescribed period during the year, special rules may apply to the amount of depreciation.

Block of Assets

One of the important concepts in tax depreciation is the **block of assets**.

A block generally consists of assets falling within the same prescribed class and carrying the same depreciation rate.

For example, assets of the same prescribed category and rate may form one block.

Depreciation is calculated on the **written-down value (WDV) of the block**, subject to the applicable provisions.

Written Down Value

The basic idea can be expressed as:

Opening WDV

- **Cost of eligible additions**
  − Sale consideration of assets sold from the block, subject to the rules
  = Adjusted WDV

Depreciation is then calculated at the prescribed rate.

Example of Depreciation

Suppose:

Opening WDV of block = ₹5,00,000

New machinery purchased = ₹1,00,000

Assume the applicable depreciation rate is 15% and the full amount qualifies for the relevant depreciation treatment.

Adjusted value:

₹5,00,000 + ₹1,00,000

= **₹6,00,000**

Depreciation:

15% of ₹6,00,000

= **₹90,000**

Closing WDV:

₹6,00,000 − ₹90,000

= **₹5,10,000**

This is a simplified illustration; the actual computation depends on the applicable rules regarding additions, disposals and period of use.

Half Depreciation Rule

Under the traditional provisions of the Income-tax Act, 1961, where an asset is acquired during the year and is put to use for **less than 180 days**, depreciation is generally restricted to **50% of the normal depreciation**.

Example

Cost of machinery = ₹2,00,000

Normal depreciation rate = 10%

Normal depreciation:

₹2,00,000 × 10% = ₹20,000

If the less-than-180-days rule applies:

₹20,000 × 50% = **₹10,000**

Therefore, depreciation allowed would be ₹10,000.

Depreciation on Intangible Assets

Under the 1961 Act, depreciation may also be available for specified intangible assets such as:

- Know-how
- Patents
- Copyrights
- Trademarks
- Licences
- Franchises

Goodwill is subject to specific statutory treatment and is not treated as a depreciable intangible asset under the current 1961 Act provisions.

Book Depreciation vs Tax Depreciation

Depreciation calculated in the financial accounts may differ from depreciation allowed under income-tax law.

Therefore, while calculating taxable business income, the taxpayer generally makes appropriate adjustments to arrive at **tax depreciation**.

Conclusion

Depreciation is an important deduction in computing business or professional income. It recognizes the reduction in value of eligible business assets. Under the Income-tax Act, depreciation is generally calculated according to the **block-of-assets and written-down-value system**, subject to conditions and prescribed rates.

Q. 13. Explain the meaning of Capital Gain and Capital Asset. Discuss the difference between Short-Term Capital Gain and Long-Term Capital Gain with suitable examples.

Ans. Introduction

Capital gains are profits arising from the transfer of a capital asset. They are taxable under the head **"Capital Gains."**

Examples of capital assets include:

- Land
- Building
- Shares
- Securities
- Jewellery
- Certain other investments

Meaning of Capital Asset

A **capital asset** generally means property of any kind held by an assessee, whether or not connected with business or profession, subject to statutory exclusions.

Capital assets may include:

- Land
- House
- Gold
- Shares
- Mutual fund units
- Securities
- Jewellery

Certain items are excluded by law, such as specified stock-in-trade and certain personal effects, subject to statutory definitions.

Meaning of Capital Gain

Capital gain means the **profit or gain arising from the transfer of a capital asset**.

The basic formula is:

Full Value of Consideration

− **Transfer Expenses**

− **Cost of Acquisition**

− **Cost of Improvement**

= **Capital Gain**

For long-term assets, applicable indexation or other statutory adjustments must be considered according to the relevant tax year and asset type.

Types of Capital Gains

There are two major types:

1. **Short-Term Capital Gain (STCG)**
2. **Long-Term Capital Gain (LTCG)**

The classification depends on the **period for which the asset is held**, and the holding period varies according to the type of asset.

Short-Term Capital Gain

A gain is generally short-term when the capital asset is held for a period **not exceeding the prescribed holding period** applicable to that asset.

The holding-period rules differ depending on the type of capital asset.

Example

Suppose a person purchases shares for:

₹2,00,000

and sells them after a period that makes them a short-term capital asset for:

₹2,80,000.

Capital gain:

₹2,80,000 – ₹2,00,000

= **₹80,000**, before considering applicable transfer expenses and other adjustments.

Long-Term Capital Gain

A gain is generally long-term when the capital asset is held for **more than the prescribed holding period** applicable to that type of asset.

Example

A person purchases a long-term capital asset for ₹5,00,000 and later sells it for ₹9,00,000.

Ignoring other adjustments:

Capital gain =

₹9,00,000 – ₹5,00,000

= **₹4,00,000**

The actual taxable LTCG depends on the applicable rules for the asset and tax year.

Difference Between STCG and LTCG

Basis	STCG	LTCG
Meaning	Gain from short-term capital asset	Gain from long-term capital asset
Holding period	Within prescribed short-term period	Beyond prescribed long-term period
Tax treatment	Depends on nature of asset	Depends on nature of asset
Cost adjustment	As prescribed	As prescribed; indexation may apply in eligible cases
Exemptions	Certain exemptions may apply	Several specific exemptions may apply

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Holding Period

The holding period is important because it determines whether the gain is short-term or long-term.

The period differs according to the asset.

For example, under the current 1961 Act framework, certain listed securities have a different holding-period rule from immovable property and other assets.

Therefore, students should always check the holding-period rule applicable to the particular asset.

Special Rate for Certain Securities

Certain short-term and long-term capital gains from specified securities may be subject to special tax rates.

For example, listed equity shares and certain equity-oriented investments have specific provisions.

Therefore, not every STCG or LTCG is taxed at the same rate.

Example

Suppose a person purchases an asset for ₹3,00,000 and sells it for ₹5,00,000.

Selling expenses = ₹20,000.

Capital gain:

₹5,00,000
− ₹20,000
− ₹3,00,000
= **₹1,80,000**

Whether this ₹1,80,000 is STCG or LTCG depends upon the holding period and nature of the asset.

Conclusion

Capital gain is the profit arising from the transfer of a capital asset. Correct determination of the **nature of the asset and its holding period** is essential because it determines whether the gain is short-term or long-term and which tax provisions and exemptions apply.

Q. 14. Explain the method of computation of taxable Capital Gains. Discuss Cost of Acquisition, Cost of Improvement and expenses incurred in connection with the transfer of a capital asset.

Ans. Introduction

Capital gain is calculated by deducting certain allowable costs and expenses from the consideration received on the transfer of a capital asset.

The calculation differs depending upon whether the gain is **short-term or long-term**.

Basic Formula

For a simple capital-gain computation:

Full Value of Consideration

Less: Expenses incurred wholly and exclusively in connection with transfer

Less: Cost of Acquisition

Less: Cost of Improvement

= Capital Gain

For eligible long-term assets, the applicable cost-indexation or other statutory rules must also be considered for the relevant tax year.

1. Full Value of Consideration

Full value of consideration means the amount received or receivable as a result of the transfer.

Example

Sale price of land = ₹10,00,000

The full value of consideration is generally ₹10,00,000, subject to special deeming provisions where applicable.

2. Expenses on Transfer

Expenses incurred **wholly and exclusively in connection with the transfer** may be deductible.

Examples include:

- Brokerage
- Commission
- Legal fees directly related to transfer
- Transfer-related professional charges
- Certain registration-related transfer expenses

Example

Sale price = ₹10,00,000

Brokerage paid = ₹20,000

Amount after transfer expenses:

₹10,00,000 − ₹20,000 = ₹9,80,000

3. Cost of Acquisition

Cost of acquisition is the amount paid to acquire the capital asset, subject to specific statutory adjustments.

It may include:

- Purchase price
- Certain acquisition-related expenses
- Other amounts included under the applicable provisions

Example

Purchase price of land = ₹4,00,000

Legal expenses directly related to acquisition = ₹20,000

Cost of acquisition may therefore be:

₹4,20,000

subject to the applicable provisions.

4. Cost of Improvement

Cost of improvement refers to capital expenditure incurred to improve the capital asset.

Examples:

- Major structural improvement
- Construction of an additional floor
- Permanent improvement to a building
- Other qualifying capital improvements

Routine repairs and maintenance are not automatically treated as cost of improvement.

Example

Purchase price = ₹5,00,000

Capital improvement = ₹1,00,000

Cost of acquisition = ₹5,00,000

Cost of improvement = ₹1,00,000

Total relevant cost = ₹6,00,000, subject to applicable rules.

5. Indexed Cost

For eligible long-term capital assets, indexation has historically been an important concept under the 1961 Act. However, the availability of indexation depends on the **asset, date of transfer and applicable current provisions**.

Therefore, students should use the indexation rules prescribed for the relevant assessment year rather than assuming that indexation applies to every LTCG.

Example of Capital Gain Computation

Suppose:

Sale consideration = ₹12,00,000

Transfer expenses = ₹30,000

Cost of acquisition = ₹6,00,000

Cost of improvement = ₹1,00,000

Computation

Sale consideration = ₹12,00,000

Less: Transfer expenses = ₹30,000

Balance = ₹11,70,000

Less: Cost of acquisition = ₹6,00,000

Less: Cost of improvement = ₹1,00,000

Capital Gain = ₹4,70,000

This is a simplified example and does not include any special deeming provisions, exemption or applicable indexation adjustment.

Important Points

Cost of Acquisition

It represents the cost incurred to acquire the asset.

Cost of Improvement

It represents qualifying capital expenditure incurred to improve the asset.

Transfer Expenses

They must generally be incurred wholly and exclusively in connection with the transfer.

Personal Expenses

Personal expenses are not deductible merely because they are incurred around the time of sale.

Computation of Long-Term Capital Gain

The general structure is:

Full Value of Consideration

− **Transfer Expenses**

− **Applicable Cost of Acquisition**

− **Applicable Cost of Improvement**

− **Other statutory adjustments, where applicable**

= **Long-Term Capital Gain**

Then:

Long-Term Capital Gain

− **Eligible Exemptions**

= **Taxable Long-Term Capital Gain**

Computation of Short-Term Capital Gain

Generally:

Full Value of Consideration

− **Transfer Expenses**

− **Cost of Acquisition**

− **Cost of Improvement**

= **Short-Term Capital Gain**

Then applicable exemptions, if any, are considered.

Conclusion

The correct computation of capital gains requires careful determination of **sale consideration, transfer expenses, cost of acquisition and cost of improvement**. The taxpayer must also consider the applicable rules for the nature of the asset, holding period, special provisions and exemptions.

Q. 15. What are the exemptions available from Capital Gains? Explain the important provisions relating to exemption from capital gains with suitable examples.

Introduction

The Income-tax Act provides certain exemptions from capital gains where the taxpayer reinvests the sale proceeds or capital gain in specified assets or uses them for specified purposes.

The important exemptions under the **Income-tax Act, 1961** include:

- Section 54
- Section 54B
- Section 54D
- Section 54EC
- Section 54F
- Section 54G
- Section 54GA
- Section 54GB

The availability of each exemption depends on specific conditions.

1. Section 54 – Sale of Residential House

Section 54 provides exemption to an eligible **individual or HUF** where a long-term residential house is transferred and the capital gain is reinvested in another residential house in India, subject to the prescribed conditions.

Conditions

Generally:

- The original asset should be a long-term residential house.
- The assessee should be an individual or HUF.
- The new residential house should be purchased or constructed within the prescribed time.
- The prescribed conditions regarding number and timing of residential properties must be satisfied.

Example

Long-term capital gain = ₹6,00,000

Amount invested in eligible new residential house = ₹5,00,000

Subject to the applicable conditions, exemption may be available to the extent permitted.

2. Section 54B – Transfer of Agricultural Land

Section 54B provides relief in specified cases where an individual or HUF transfers agricultural land used for agricultural purposes and invests in another agricultural land within the prescribed period.

Example

Capital gain from agricultural land = ₹4,00,000

Amount invested in eligible agricultural land = ₹3,00,000

Subject to the statutory conditions, exemption may be available to the eligible extent.

3. Section 54EC – Investment in Specified Bonds

Section 54EC provides an exemption from eligible long-term capital gains arising from transfer of land or building or both where the capital gain is invested in specified bonds within the prescribed period.

The exemption is subject to:

- Specified bonds
- Time limit for investment
- Maximum investment limit
- Lock-in period
- Other statutory conditions

Example

Eligible long-term capital gain = ₹8,00,000

Eligible investment in specified bonds = ₹8,00,000

Subject to the applicable limits and conditions, the eligible capital gain may qualify for exemption.

4. Section 54F – Transfer of Capital Asset Other Than Residential House

Section 54F provides relief to an individual or HUF where a **long-term capital asset other than a residential house** is transferred and the net consideration is invested in a residential house in India, subject to prescribed conditions.

The exemption is generally proportionate to the amount invested where the entire net consideration is not invested.

Basic idea

Exemption = Capital Gain × Amount invested / Net consideration

subject to the statutory conditions and limits.

Example

Long-term capital gain = ₹5,00,000

Net sale consideration = ₹10,00,000

Amount invested in eligible residential house = ₹8,00,000

Illustratively:

₹5,00,000 × ₹8,00,000 / ₹10,00,000

= **₹4,00,000 exemption**

The remaining ₹1,00,000 would be taxable, subject to the actual provisions.

5. Section 54G – Shifting of Industrial Undertaking

Section 54G provides relief in specified cases where an industrial undertaking is shifted from an urban area to a non-urban area and the taxpayer invests in specified assets for the new undertaking.

The purpose is to encourage industrial development outside specified urban areas.

6. Section 54GA – Shifting to Special Economic Zone

Section 54GA provides relief in specified cases where an industrial undertaking is shifted from an urban area to a Special Economic Zone, subject to prescribed conditions.

7. Section 54GB – Investment in Eligible Company/Start-up

Section 54GB provides relief in specified cases where an individual or HUF transfers a long-term residential property and invests the required amount in an eligible company or specified eligible investment, subject to the conditions of the provision.

Capital Gains Account Scheme

The **Capital Gains Account Scheme (CGAS)** is important where the taxpayer has not utilized the capital gain for the eligible purpose before the due date for filing the return.

Subject to the applicable provisions, the taxpayer may deposit the amount in the specified Capital Gains Account Scheme to claim the relevant exemption, provided the statutory conditions are satisfied.

Summary of Important Exemptions

Section	Main Exemption
54	Investment in residential house after transfer of eligible residential house
54B	Investment in agricultural land
54D	Certain compulsory acquisition cases involving industrial undertaking
54EC	Investment in specified bonds
54F	Investment in residential house after transfer of eligible long-term capital asset other than residential house
54G	Shifting industrial undertaking from urban area
54GA	Shifting industrial undertaking to SEZ
54GB	Investment in eligible company/start-up subject to conditions

Important Conditions for Capital-Gain Exemptions

A taxpayer should carefully check:

1. Nature of original asset

The exemption may be available only for a specified type of capital asset.

2. Nature of new investment

The amount must generally be invested in the specific asset prescribed by the relevant section.

3. Time limit

Purchase or construction/investment must be completed within the prescribed period.

4. Eligible taxpayer

Some exemptions are available only to:

- Individual
- HUF

while others have different eligibility requirements.

5. Amount of exemption

The exemption may be:

- Full
- Partial
- Proportionate

depending upon the particular provision.

Example of Section 54

Suppose:

Sale of old residential house = ₹15,00,000

Cost and other adjustments = ₹9,00,000

Long-term capital gain = ₹6,00,000

The taxpayer purchases an eligible new residential house for ₹7,00,000 within the prescribed period.

Subject to all statutory conditions, the eligible capital gain may qualify for exemption under Section 54.

Therefore, the taxable capital gain may be reduced substantially or potentially become nil depending on the amount eligible for exemption.

Importance of Capital-Gain Exemptions

These exemptions are important because they:

1. Encourage investment.
2. Promote purchase of residential houses.
3. Encourage investment in agricultural land.
4. Encourage investment in specified bonds.
5. Support industrial development.
6. Help taxpayers reinvest capital gains instead of immediately paying tax.-

Unit :- 4

Q. 16. Income from Other Sources: Meaning, Types and Method of Computation

Ans. Introduction

Under the Income-tax Act, 1961, income is classified under different heads for the purpose of computing the taxable income of an assessee. The main heads of income are:

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

The head **"Income from Other Sources"** is a **residuary head of income**. It covers those incomes which are taxable but do not fall under any of the other specific heads of income.

Meaning of Income from Other Sources

Section 56 of the Income-tax Act provides for taxation of income under the head **"Income from Other Sources."**

In simple words, if an income is taxable under the Income-tax Act but cannot be classified as salary income, house property income, business/professional income or capital gains, it is generally taxed under the head **Income from Other Sources**.

Thus, this head acts as a **residuary category**.

Example

Suppose Mr. A earns:

- Salary – ₹6,00,000
- Rent from house property – ₹2,00,000
- Interest on bank deposits – ₹50,000

Salary will be taxed under "Salaries," rent under "Income from House Property," and bank interest, if not otherwise taxable as business income, will generally be taxed under **Income from Other Sources**.

Types of Income Taxable under Income from Other Sources

Several types of income may be taxable under this head.

1. Interest Income

Interest received from investments and deposits is generally taxable under this head where it is not taxable as business income.

Examples include:

- Interest on bank fixed deposits
- Interest on savings bank accounts
- Interest on recurring deposits
- Interest on loans given to others
- Interest on securities, where applicable

Example

Mr. X receives ₹80,000 as interest from fixed deposits.

Income from Other Sources = ₹80,000

The applicable deduction, if any, is considered according to the relevant provisions.

2. Dividend Income

Dividend income is generally taxable in the hands of the shareholder, subject to the provisions applicable for the relevant assessment year.

For example, if an assessee receives dividend of ₹1,20,000, it may be taxable under **Income from Other Sources**, subject to applicable deductions and restrictions.

3. Family Pension

Family pension received by the legal heir of a deceased employee is taxable under the head **Income from Other Sources**, and not under Salaries.

A specified deduction is available from family pension subject to the applicable statutory limit.

Example

Suppose a widow receives family pension of ₹3,00,000.

The taxable amount is calculated after allowing the deduction prescribed under the Income-tax Act.

4. Winnings from Lotteries, Crossword Puzzles, Races, Gambling, etc.

Winnings from:

- Lotteries
- Crossword puzzles
- Card games
- Gambling
- Betting
- Horse races
- Certain online games
- Other specified games

are generally taxable under this head, subject to the special tax provisions applicable to such winnings.

Such winnings are generally taxed at **special rates**, rather than ordinary slab rates.

Example

If an individual wins ₹1,00,000 from a lottery, the amount is taxable subject to the special provisions relating to lottery winnings.

5. Gifts

Certain gifts received without consideration or for inadequate consideration may become taxable under Section 56(2)(x), subject to specified exceptions.

For example, money received without consideration may be taxable if the aggregate amount exceeds the prescribed threshold.

However, gifts received from specified relatives and certain gifts received on specified occasions or in specified circumstances may be exempt.

Example

Mr. A receives ₹3,00,000 in cash from a person who is not his relative, without consideration. If the statutory conditions are satisfied, the amount may become taxable under Income from Other Sources.

6. Rent from Machinery, Plant or Furniture

Where an assessee earns rent from machinery, plant or furniture and such income is not taxable as business income, it may be taxable under Income from Other Sources.

Example

Mr. X lets out machinery and receives ₹2,00,000 as rent. If the letting does not constitute his business, the income may be taxable under this head after allowing permissible deductions.

7. Composite Rent

Where an assessee lets out buildings along with machinery, plant or furniture and the letting of the building is inseparable from the letting of the other assets, the income may be taxable under Income from Other Sources if it is not taxable as business income.

8. Income from Letting of Plant, Machinery or Furniture

Income earned from letting plant, machinery or furniture is specifically covered by the provisions of Section 56 in circumstances where it does not fall under business income.

9. Compensation or Certain Other Receipts

Certain compensation or other receipts that do not fall under another specific head may also be taxable under Income from Other Sources depending on the nature of the receipt and applicable provisions.

Deductions from Income from Other Sources

Section 57 provides for deductions from income taxable under this head, subject to specific conditions.

Important deductions include:

1. Expenses incurred for earning income

Any expenditure laid out or expended wholly and exclusively for the purpose of making or earning such income may be allowed, subject to the statutory conditions.

Example

Mr. A earns interest of ₹1,00,000 and incurs ₹10,000 of allowable expenditure exclusively for earning that interest.

Taxable income:

₹1,00,000 – ₹10,000 = ₹90,000

2. Family Pension Deduction

A prescribed deduction is available from family pension subject to the statutory limit.

3. Interest on Compensation

In certain cases, 50% of interest received on compensation or enhanced compensation may be allowed as a deduction under the applicable provisions.

Expenses Not Deductible

Section 58 places restrictions on certain deductions.

For example, expenses relating to winnings from lotteries, crossword puzzles, races, gambling, betting and specified games are generally not deductible against such winnings.

Therefore, if a person spends money on purchasing lottery tickets and subsequently wins a lottery, the expenditure is generally not allowed to be deducted from the lottery winnings.

Method of Computation

The general method can be represented as:

Gross Income from Other Sources

Add:

- Interest income
- Dividend income
- Taxable gifts

- Family pension
- Rent from machinery/plant/furniture
- Other taxable residual income

Less:

- Permissible deductions under Section 57
- Other deductions specifically permitted by law

= **Income chargeable under the head "Income from Other Sources"**

Illustrative Example

Suppose Mr. A has:

Particulars	Amount
Bank interest	₹80,000
Dividend	₹40,000
Family pension	₹2,00,000
Rent from machinery	₹1,50,000
Allowable expenditure	₹20,000

The gross income is:

₹80,000 + ₹40,000 + ₹2,00,000 + ₹1,50,000
= **₹4,70,000**

Less allowable expenditure:

₹4,70,000 – ₹20,000
= **₹4,50,000**

The final taxable income under this head would then be determined after considering the specific deduction applicable to family pension and any other relevant statutory provisions.

Conclusion

Income from Other Sources is a **residuary head of income**. It ensures that taxable receipts which do not fall under the other four heads do not escape taxation. Interest, dividends, family pension, certain gifts, winnings and income from letting machinery or furniture are important examples. The income is computed by adding taxable receipts and deducting only those expenses and deductions specifically permitted by law.

Q. 17. Clubbing of Income: Meaning and Provisions Relating to Spouse, Minor Child and Other Persons

Introduction

Normally, every person is taxed on the income earned by him or her. However, the Income-tax Act contains certain provisions under which the income of another person is **included in the total income of the assessee**.

These provisions are known as the **clubbing provisions**.

The main purpose is to prevent taxpayers from reducing their tax liability by transferring assets or income to their spouse, minor children or other related persons without genuine economic substance.

Meaning of Clubbing of Income

Clubbing of income means including the income of another person in the total income of the assessee under specific provisions of the Income-tax Act.

The person whose income is included is sometimes called the **transferor**, while the person whose income is transferred or whose income is included is the **transferee**.

Example

Mr. A transfers ₹10,00,000 to his wife without adequate consideration. His wife earns ₹80,000 interest from that amount.

Subject to the statutory conditions, the ₹80,000 may be included in Mr. A's total income.

Thus, although the interest was actually received by the wife, it is taxable in the hands of the husband under the clubbing provisions.

Clubbing of Income of Spouse

The Income-tax Act provides for clubbing of certain income of a spouse.

1. Transfer of Assets to Spouse

Where an individual transfers an asset to his or her spouse:

- directly or indirectly,
- otherwise than for adequate consideration, and
- not in connection with an agreement to live apart,

the income arising from such asset may be included in the total income of the transferor.

Example

Mr. A gifts ₹5,00,000 to his wife.

His wife invests the money in a fixed deposit and earns ₹40,000 interest.

The interest of ₹40,000 may be clubbed with Mr. A's income, subject to the conditions of the Act.

2. Remuneration to Spouse from a Concern

Where a spouse receives salary, commission, fees or remuneration from a concern in which the other spouse has a substantial interest, such remuneration may be clubbed with the income of the spouse having substantial interest.

However, there is an important exception where the spouse possesses **technical or professional qualifications** and the income is solely attributable to the application of such knowledge and experience.

Example

Mr. A has a substantial interest in a company. His wife receives ₹3,00,000 salary from that company, but she does not possess the required technical/professional qualification and the statutory conditions for clubbing are satisfied.

The salary may be included in Mr. A's total income.

If, however, she is professionally qualified and the income is solely attributable to her professional knowledge and experience, the clubbing provision may not apply.

Clubbing of Income of Minor Child

Income of a minor child is generally clubbed with the income of the parent whose total income is higher, subject to the statutory provisions.

Example

Mr. A's minor son earns ₹1,00,000 interest income.

If Mr. A has higher total income than his wife and the income does not fall under an exception, the minor child's income may be included in Mr. A's total income.

Exceptions to Minor Child Clubbing

The income of a minor child is generally not clubbed where it is:

1. Income arising from the minor's manual work; or
2. Income arising from the minor's activity involving application of his skill, talent, specialised knowledge or experience; or
3. Income of a minor child suffering from specified disability under the applicable law.

Example

A 15-year-old child is a talented singer and earns ₹2,00,000 from singing performances.

Since the income arises from the application of the child's talent, it may not be clubbed with the parent's income.

Deduction in Respect of Minor Child's Income

Where minor child's income is included in the income of a parent, the Act provides a specified deduction, subject to conditions and limits, in respect of each minor child whose income is so included.

The exact statutory amount should be applied according to the relevant assessment year.

Clubbing of Income from Transferred Assets

The clubbing provisions are not limited only to spouses. Certain transfers of assets may result in income being included in the transferor's income under specified circumstances.

Example

A transfers an income-generating asset to B without adequate consideration.

If the statutory clubbing provisions apply, the income generated from that asset may be included in A's taxable income.

Transfer of Assets for the Benefit of Spouse

If an asset is transferred to another person or an arrangement is created for the benefit of the spouse, and the statutory conditions are satisfied, the resulting income may be clubbed with the transferor's income.

Revocable Transfer of Assets

Where a person transfers an asset under circumstances where the transfer can be revoked, the income from such asset may be taxable in the hands of the transferor.

This provision prevents a taxpayer from escaping taxation by making temporary or revocable transfers.

Example

A transfers an income-generating investment to B but retains the right to take back the asset under the terms of the arrangement.

The income arising from that asset may continue to be taxable in A's hands.

Important Principle Regarding Income from Clubbed Income

A useful distinction should be remembered between:

- **Income from the transferred asset**, and
- **Income from reinvestment of that income**.

For example:

Mr. A transfers ₹10 lakh to his wife. His wife earns ₹1 lakh interest.

The ₹1 lakh interest may be clubbed with Mr. A's income.

Suppose the wife invests that ₹1 lakh and earns another ₹10,000.

The treatment of the ₹10,000 has to be examined under the statutory rules concerning income arising from income and not merely assumed to be automatically clubbed.

Purpose of Clubbing Provisions

The major objectives are:

1. To prevent tax avoidance through artificial transfers.
2. To discourage taxpayers from transferring assets to family members solely to reduce tax.
3. To ensure that tax liability reflects the economic ownership of income-producing assets.
4. To prevent misuse of lower tax rates through splitting of income among family members.

Conclusion

Clubbing provisions are anti-avoidance provisions under the Income-tax Act. They make certain income taxable in the hands of a person other than the person who actually receives it. Important provisions concern transfers to spouses, remuneration of spouses, income of minor children, revocable transfers and transfers made for the benefit of specified persons. These provisions ensure that merely transferring assets or income to family members does not automatically reduce the overall tax liability.

Q. 18. Set-off and Carry Forward of Losses: Intra-head and Inter-head Adjustment

Introduction

During a financial year, an assessee may earn income from several sources but may also incur losses from one or more sources. The Income-tax Act provides rules for adjusting such losses against income.

Two important concepts are:

1. **Set-off of losses**
2. **Carry forward of losses**

The purpose is to provide a systematic method for determining taxable income after considering permissible losses.

Meaning of Set-off

Set-off means adjustment of a loss against income.

For example:

- Business profit = ₹5,00,000
- Loss from another eligible business = ₹2,00,000

If adjustment is legally permitted, the net income becomes:

₹5,00,000 – ₹2,00,000 = **₹3,00,000**

Types of Set-off

There are two major types:

1. Intra-head adjustment

Adjustment of loss from one source against income from another source **under the same head**.

2. Inter-head adjustment

Adjustment of loss under one head against income under **another head**.

A. Intra-head Adjustment

Intra-head adjustment means that a loss from one source is adjusted against income from another source under the same head.

Example

An assessee has:

- Business A profit = ₹5,00,000
- Business B loss = ₹2,00,000

Both are under the head "Profits and Gains of Business or Profession."

Therefore:

₹5,00,000 – ₹2,00,000 = **₹3,00,000**

The loss of Business B is set off against the profit of Business A, subject to applicable restrictions.

Restrictions on Intra-head Set-off

The law imposes certain restrictions.

1. Speculation Loss

Speculation loss generally cannot be set off against non-speculative business income.

Example

- Speculative business loss = ₹1,00,000
- Normal business profit = ₹3,00,000

The speculative loss cannot ordinarily be adjusted against normal business profit.

It is carried forward subject to the special rules governing speculative losses.

2. Long-term Capital Loss

Long-term capital loss can generally be set off only against **long-term capital gains**.

It cannot ordinarily be set off against short-term capital gains.

3. Short-term Capital Loss

Short-term capital loss is generally permitted to be set off against:

- Short-term capital gains, and
- Long-term capital gains,

subject to the applicable provisions.

4. Loss from Certain Specified Activities

Losses from certain specified activities, such as specified businesses, may be subject to special restrictions.

B. Inter-head Adjustment

If a loss remains after intra-head adjustment, it may, subject to the Act, be adjusted against income under another head.

This is known as **inter-head set-off**.

Example

Suppose:

- Business loss = ₹2,00,000
- Salary income = ₹6,00,000

Subject to statutory restrictions, business loss may be eligible for adjustment against income from another head in the manner permitted by law.

However, several important restrictions apply.

Important Restrictions on Inter-head Set-off

1. Business Loss Against Salary

A normal business loss cannot generally be set off against salary income.

Therefore, if:

- Business loss = ₹2,00,000
- Salary income = ₹7,00,000

the business loss cannot simply be deducted from salary income.

2. Capital Loss

Capital loss cannot generally be set off against income under other heads.

For example, a capital loss cannot normally be adjusted against salary income.

3. House Property Loss

House property loss is subject to specific restrictions when adjusted against other heads of income.

Under the general regime, the amount of house property loss that can be set off against income from other heads in the same year is subject to the statutory ceiling, with the balance eligible for carry forward subject to the applicable conditions.

4. Loss from Speculation Business

Speculation loss cannot be set off against ordinary business income or other heads in the manner of an ordinary business loss.

Carry Forward of Losses

When a loss cannot be fully set off in the same year, it may be carried forward to subsequent assessment years, subject to conditions.

The carried-forward loss can then be set off against future eligible income.

Important Types of Carry Forward

Type of Loss	General period/rule
House property loss	Up to 8 assessment years
Normal business loss	Up to 8 assessment years

Type of Loss	General period/rule
Speculation business loss	Up to 4 assessment years
Short-term capital loss	Up to 8 assessment years
Long-term capital loss	Up to 8 assessment years
Certain specified business losses	Special rules may apply

The exact conditions should always be checked for the relevant assessment year.

Conditions for Carry Forward

One of the most important conditions is timely filing of the return.

For certain losses, particularly business losses, speculation losses and capital losses, the return must generally be filed within the prescribed due date in order to carry forward the loss.

House property loss has special treatment under the law.

Example of Set-off and Carry Forward

Suppose an assessee has:

Current year:

- Salary income = ₹6,00,000
- Business loss = ₹3,00,000
- House property loss = ₹2,00,000

The house property loss can be subject to the prescribed inter-head set-off limit. Business loss cannot generally be set off against salary income.

Any eligible unadjusted loss may be carried forward subject to the applicable rules.

Difference Between Set-off and Carry Forward

Basis	Set-off	Carry Forward
Meaning	Adjustment in the same year	Adjustment in future years
Time	Current assessment year	Subsequent assessment years
Purpose	Reduce current year's taxable income	Preserve eligible loss for future adjustment
Types	Intra-head and inter-head	Depends on type of loss

Basis	Set-off	Carry Forward
Conditions	Subject to applicable restrictions	Subject to additional statutory conditions

Conclusion

The provisions relating to set-off and carry forward of losses are important for determining the correct taxable income. First, eligible losses are adjusted through **intra-head set-off**. If a loss remains, **inter-head set-off** may be available subject to restrictions. Any remaining eligible loss can be **carried forward** for adjustment against future income. These provisions prevent unfair taxation of an assessee who has genuine losses while also preventing misuse of losses for tax avoidance.

Q. 19. Exempt Income: Meaning, Importance and Important Examples

Introduction

Not every receipt or income earned by a person is taxable. The Income-tax Act provides exemptions for certain types of income. Such income is generally referred to as **exempt income**.

Exempt income plays an important role in determining the total taxable income of an assessee.

Meaning of Exempt Income

Exempt income means income which, under a specific provision of the Income-tax Act, is not included in taxable income, either fully or to the extent specified by the law.

In simple words:

Exempt income is income which is not chargeable to tax because the Income-tax Act specifically provides an exemption.

Difference Between Exempt Income and Non-taxable Receipt

It is important to understand that every receipt which is not taxed is not necessarily "exempt income."

For example:

- A capital receipt may not be taxable because of its nature.
- A receipt may be outside the scope of income.
- An income may be specifically exempt under a particular section.

Therefore, the reason for non-taxability must be examined.

Importance of Exempt Income

1. Reduces Taxable Income

Exempt income is not included in taxable income to the extent of exemption.

2. Encourages Certain Activities

The government uses exemptions to encourage:

- Agricultural activities
- Certain savings and investments
- Charitable activities
- Social welfare
- Retirement benefits
- Certain employee benefits

3. Provides Relief to Taxpayers

Exemptions prevent certain socially or economically important receipts from becoming taxable.

4. Helps in Tax Planning

Understanding exempt income helps an assessee determine the actual taxable income and plan financial affairs within the law.

mportant Examples of Exempt Income

1. Agricultural Income

Agricultural income, as defined under the Income-tax Act, is generally exempt from central income tax.

However, agricultural income may be considered for **rate purposes** under the concept of partial integration in cases where the statutory conditions are satisfied.

Example

A farmer earns ₹4,00,000 from qualifying agricultural operations.

Such agricultural income is generally exempt from central income tax, subject to the statutory definition and conditions.

2. Share of Profit from a Partnership Firm

A partner's share of profit from a partnership firm is generally exempt in the hands of the partner under the applicable provisions because the firm's income has already been subjected to tax according to the relevant tax regime.

However, salary, bonus, commission or interest received by the partner may be taxable subject to applicable provisions.

3. Certain Scholarships

Scholarships granted to meet the cost of education are generally exempt under the Income-tax Act, subject to the applicable conditions.

4. Certain Receipts by Members of HUF

Income received by a member from the Hindu Undivided Family may be exempt subject to the applicable provisions.

5. Certain Life Insurance Receipts

Certain sums received under life insurance policies may be exempt subject to statutory conditions.

The exemption is not universal; policy type, premium conditions, issue date and other statutory requirements can affect taxability.

6. Certain Agricultural Receipts

Various receipts falling within the statutory definition of agricultural income may be exempt, provided they satisfy the legal conditions.

7. Certain Government Allowances and Benefits

Certain allowances or benefits may be exempt to the extent and under the conditions specified in the Income-tax Act.

8. Certain Retirement Benefits

Some retirement-related receipts, such as qualifying gratuity, commuted pension and other specified retirement benefits, may be fully or partially exempt depending on the employee's category and statutory conditions.

9. Leave Encashment

Leave encashment received at retirement may be fully or partially exempt depending upon the nature of employment and the applicable statutory provisions.

For government employees, the exemption rules may differ from those applicable to other employees.

10. Certain Dividends or Income Specifically Exempt under Law

Where the Act specifically grants exemption to a particular income, the amount is not included in taxable income subject to the conditions of the relevant provision.

Exempt Income and Deductions

A major distinction should be made between **exemption** and **deduction**.

Exemption

Income itself is excluded from taxable income.

Deduction

Income is first included in gross total income and then a specified amount is deducted under the relevant provisions.

Example

If salary = ₹8,00,000 and an exempt allowance = ₹50,000:

Taxable salary may be computed after excluding the exempt amount, subject to the applicable conditions.

A deduction, on the other hand, operates at a later stage in the computation.

Exempt Income and Total Income

The broad computation process can be shown as:

Income under five heads

Less:

Exempt income

= Gross Total Income

Then:

Less: Eligible deductions under Chapter VI-A

= Total Income

However, the exact treatment depends on the nature of the receipt and the applicable statutory provisions.

Conclusion

Exempt income is an important part of the Indian income-tax system. It includes income which the law specifically excludes from taxation, either fully or subject to prescribed conditions. Agricultural income, qualifying scholarships, certain retirement benefits, certain life-insurance receipts and a partner's share of profit from a firm are important examples. A proper understanding of exempt income is necessary for correctly calculating gross total income and total income.

Q. 20. Aggregation of Income, Clubbing of Income, Set-off and Carry Forward of Losses

Introduction

The computation of total income under the Income-tax Act is not limited to simply adding all receipts earned by an assessee. The Act prescribes a systematic procedure involving:

1. Computation of income under different heads
2. Aggregation of income
3. Clubbing of income
4. Set-off of losses
5. Carry forward of unadjusted losses
6. Deduction of eligible amounts
7. Determination of total income

These provisions ensure that the correct amount of taxable income is determined.

1. Aggregation of Income

Meaning

Aggregation means combining taxable income from different sources and different heads after applying the relevant rules.

For example, an assessee may have:

- Salary income
- House property income
- Business income
- Capital gains
- Income from other sources

These incomes are computed separately first and are then aggregated according to the provisions of the Act.

Example

Suppose:

Head	Income
Salary	₹6,00,000
House Property	₹2,00,000

Head	Income
Business	₹3,00,000
Capital Gains	₹1,00,000
Other Sources	₹50,000

Total before considering applicable losses, exemptions and deductions:

₹6,00,000 + ₹2,00,000 + ₹3,00,000 + ₹1,00,000 + ₹50,000

= **₹12,50,000**

This is not necessarily the final taxable income because further adjustments may be required.

2. Clubbing of Income

As discussed earlier, certain income belonging to another person is required to be included in the assessee's income.

This is done under the clubbing provisions.

Example

Mr. A transfers ₹10,00,000 to his wife without adequate consideration.

The wife earns ₹1,00,000 interest.

If the statutory conditions are satisfied, the ₹1,00,000 may be included in Mr. A's income.

Thus:

Mr. A's own income = ₹8,00,000
Clubbing income = ₹1,00,000

Adjusted income = ₹9,00,000

3. Set-off of Losses

After computing income from different sources, eligible losses are adjusted.

There are two forms:

Intra-head set-off

Loss from one source is adjusted against income from another source under the same head.

Inter-head set-off

After intra-head adjustment, eligible remaining loss may be adjusted against income under another head, subject to restrictions.

. Carry Forward of Losses

If a loss cannot be fully adjusted in the current year, it may be carried forward to subsequent years where the law permits.

For example:

Current year:

Business loss = ₹5,00,000

Current-year eligible set-off = ₹2,00,000

Balance:

₹5,00,000 – ₹2,00,000 = **₹3,00,000**

The remaining ₹3,00,000 may be carried forward subject to the relevant conditions.

. Effect on Computation of Total Income

These provisions significantly affect the final taxable income.

The broad process is:

Step 1: Compute income under each head

Income is separately calculated under:

- Salaries
- House Property
- Business/Profession
- Capital Gains
- Other Sources

Step 2: Apply exemptions

Income specifically exempt under the Act is excluded according to the relevant provisions.

Step 3: Apply clubbing provisions

Income required to be clubbed is added to the income of the appropriate assessee.

Step 4: Aggregate income

The adjusted income under different heads is combined.

Step 5: Set off losses

Eligible losses are adjusted against eligible income through intra-head and inter-head set-off.

Step 6: Carry forward remaining losses

Losses that cannot be adjusted in the current year may be carried forward subject to statutory conditions.

Step 7: Determine Gross Total Income

After the appropriate adjustments, the Gross Total Income is determined.

Step 8: Deduct eligible deductions

Deductions under the relevant provisions, including applicable Chapter VI-A deductions, are then considered.

Step 9: Determine Total Income

The amount remaining after permitted deductions is the **Total Income** on which tax is calculated according to the applicable tax regime and rates.

Comprehensive Illustration

Suppose Mr. X has the following income:

Particulars	Amount
Salary income	₹7,00,000
House property income	₹1,50,000
Business income	₹3,00,000
Capital gains	₹1,00,000
Interest income	₹50,000

Step 1: Aggregate income

₹7,00,000 + ₹1,50,000 + ₹3,00,000 + ₹1,00,000 + ₹50,000

= **₹13,00,000**

Suppose Mr. X also has eligible house property loss of ₹1,00,000 from another property.

The loss is adjusted according to the rules applicable to house property losses.

Suppose further that ₹50,000 of income is required to be clubbed with Mr. X's income under the applicable provisions.

Then the computation will take into account:

- Income under each head
- Clubbed income
- Permissible loss adjustment
- Carry-forward provisions, if any
- Eligible deductions

Thus, the final taxable income may be significantly different from the simple total of all receipts.

Relationship Between the Four Concepts

These four concepts are closely connected.

Aggregation

Brings together taxable income from different sources and heads.

Clubbing

Adds certain income of another person to the assessee's income where the Act requires it.

Set-off

Allows eligible losses to reduce taxable income in the same year.

Carry Forward

Allows eligible unadjusted losses to be used in future years.

They work together to determine the assessee's final taxable income.

Importance of These Provisions

1. Correct determination of tax liability

They ensure that the tax is calculated on the correct amount of income.

2. Prevention of tax avoidance

Clubbing provisions prevent artificial diversion of income to family members.

3. Relief for genuine losses

Set-off and carry-forward provisions recognize genuine economic losses.

4. Proper classification

Aggregation ensures that income from different heads is considered according to the correct statutory rules.

5. Fairness in taxation

The provisions help ensure that taxpayers are taxed on their actual taxable income rather than merely on gross receipts.

Difference Between Aggregation, Clubbing, Set-off and Carry Forward

Basis	Aggregation	Clubbing	Set-off	Carry Forward
Meaning	Combining taxable incomes	Including another person's specified income	Adjusting loss against income	Taking unadjusted loss to future years
Purpose	Determine combined income	Prevent tax avoidance	Reduce current taxable income	Use loss in later years
Time	Current computation	Current computation	Generally current year	Future years
Example	Salary + business income	Spouse's specified income	Business loss vs eligible business profit	Unabsorbed business loss

Overall Computation of Total Income

A simplified structure can be represented as:

Income under Salaries

- **Income from House Property**
- **Business/Professional Income**
- **Capital Gains**
- **Income from Other Sources**
  = Income before relevant adjustments

Then:

+ Income required to be clubbed
– Exempt income, where applicable
– Eligible set-off of losses
= Gross Total Income

Then:

Less: Eligible deductions

= **Total Income**

Tax is then calculated on the total income according to the applicable provisions, rates and tax regime.

Conclusion

The provisions relating to **aggregation of income, clubbing of income, set-off and carry forward of losses** form an essential part of the process of computing total income. First, income is calculated under each head. Exempt income is excluded according to the relevant provisions, specified income of other persons may be clubbed, and eligible losses are set off. Losses that remain unadjusted may be carried forward subject to statutory conditions. Finally, eligible deductions are allowed and the resulting amount is known as the **Total Income**.

These provisions ensure that the income-tax system takes into account the assessee's complete taxable income, genuine losses and specified anti-avoidance rules while arriving at the correct tax liability.