

Income Tax Laws & Accounts

Paper Code: P-5

Unit- I

Introduction

Income tax in India was introduced for the first time in **1860** by **Sir James Wilson** to meet the financial losses caused by the **Military Mutiny of 1857**. Over the years, several amendments were made, and a separate **Income Tax Act was passed in 1886**. This was followed by new Acts in **1918** and **1922**, with the **Income Tax Act, 1922** remaining in force up to the **assessment year 1961–62**. Due to numerous amendments, the Act became complex, leading the Government to refer the matter to the **Law Commission in 1956** to simplify the law and prevent tax evasion. The Law Commission submitted its report in **September 1958**, and the **Direct Taxes Administration Enquiry Committee** also submitted its report in **1956**. After consultation with the Ministry of Law, the **Income Tax Act, 1961** was passed and came into force on **1 April 1962**, applying to the **whole of India, including Jammu and Kashmir**.

Components of Income Tax Law

Income tax law in India consists of:

- **Income-tax Act, 1961**
- **Income-tax Rules, 1962**
- **Finance Act**
- **Circulars and Notifications** issued by CBDT
- **Judicial decisions** of courts

Finance Act

- Presented every year by the **Finance Minister** in Parliament.
- After approval by Parliament and assent of the **President**, it becomes the **Finance Act**.
- It **fixes tax rates** for the relevant assessment year.

Income-tax Rules

- Administered by the **Central Board of Direct Taxes (CBDT)**.
- CBDT makes rules to implement the Income-tax Act.
- These are called **Income-tax Rules, 1962**.

Important Definitions

Assessment Year (AY) – Section 2(9)

- Period of **12 months from 1st April to 31st March**.

- Income of the **previous year** is taxed in the **assessment year**.
- Example:
 - **AY 2022–23** → 1 April 2022 to 31 March 2023

Previous Year – Section 3

- The year in which **income is earned**.
- It is the **financial year immediately before** the assessment year.

Exceptions: Income Taxable in Same Year

Income is taxed in the **same year** in the following cases:

1. Income of **non-residents from shipping**
2. Income of persons **leaving India permanently or for long period**
3. Income of **short-duration bodies**
4. Income of persons **trying to avoid tax by transferring assets**
5. Income of a **discontinued business**

Person – Section 2(31)

“Person” includes:

1. Individual
2. Hindu Undivided Family (HUF)
3. Company
4. Firm
5. Association of Persons (AOP) / Body of Individuals (BOI)
6. Local authority
7. Artificial juridical person

Assessee – Section 2(7)

- A person against whom **assessment proceedings** are taken.
- Includes persons liable for income, loss, or refund.

Deemed Assessee

- A person treated as assessee **for another person**.

Assessee in Default

- A person who **fails to perform duties** under the Income-tax Act.

Assessment – Section 2(8)

- Process of **determining taxable income** by the Assessing Officer.

Basis of Charge of Income Tax – Section 4

1. Income tax is an **annual tax**
2. Income of previous year is taxed in the **assessment year**
3. **Tax rates are fixed by Finance Act**
4. Tax is charged on **every person**
5. Tax is levied on **total income**

Income – Section 2(24)

- Definition is **inclusive**, not exhaustive.
- Income means **monetary return from a definite source**.
- Even **irregular income** can be taxable.

Items Included in Income

- Profits and gains
- Dividends
- Voluntary contributions to trusts
- Perquisites and profits in lieu of salary
- Allowances (special or personal)
- Benefits or perquisites from companies
- Deemed profits (Sections 41 & 59)
- Business and professional income (Section 28)
- Capital gains (Section 45)
- Insurance business profits
- Banking business income of co-operative societies
- Winnings from lotteries, games, gambling, betting
- Employees' contribution to PF, ESI, etc.
- Keyman insurance policy receipts
- Non-compete fees and similar receipts
- Gifts or property received (Section 56)
- Excess share premium (Section 56(2)(viib))

Heads of Income – Section 14

Income is classified under **five heads**:

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

5. Income from Other Sources

Gross Total Income – Section 80B(5)

- Total of income under **all five heads** before deductions.

Total Income – Section 2(45)

- **Gross Total Income minus deductions under Sections 80C to 80U.**

Casual Income

Casual income is **non-recurring and irregular** income such as:

1. Lottery winnings
2. Crossword puzzle winnings
3. Race winnings (including horse races)
4. Card games and other games
5. Gambling or betting income

RATES OF INCOME TAX FOR THE ASSESSMENT YEAR 2025-26

Old Tax Regime (Optional)

The old tax regime allows taxpayers to claim various deductions and exemptions (e.g., HRA, home loan interest, and investments under Section 80C, 80D, etc.). The basic exemption limit varies by age.

Individuals Below 60 Years / HUF / NRI

- Income up to ₹2,50,000 – No tax
- Income from ₹2,50,001 to ₹5,00,000 – 5% tax
- Income from ₹5,00,001 to ₹10,00,000 – 20% tax
- Income above ₹10,00,000 – 30% tax

Resident Senior Citizens (60 to 80 years)

- Income up to ₹3,00,000 – No tax
- Income from ₹3,00,001 to ₹5,00,000 – 5% tax
- Income from ₹5,00,001 to ₹10,00,000 – 20% tax
- Income above ₹10,00,000 – 30% tax

Resident Super Senior Citizens (Above 80 years)

- Income up to ₹5,00,000 – No tax
- Income from ₹5,00,001 to ₹10,00,000 – 20% tax
- Income above ₹10,00,000 – 30% tax

Note: A standard deduction of ₹50,000 is also available for salaried individuals under the old tax regime. Taxpayers with income up to ₹5 lakh can claim a full tax rebate under Section 87A, making their net tax liability zero.

New Tax Regime (Default) Slabs for FY 2024-25

The new tax regime is the default option for all individuals and HUFs. It features lower tax rates and simplified slabs but allows very few deductions and exemptions (e.g., no HRA, no Section 80C). A standard deduction of ₹50,000 for salaried individuals is available under this regime for FY 2024-25.

- Income up to **₹3,00,000 – No tax**
- Income from **₹3,00,001 to ₹7,00,000 – 5% tax**
- Income from **₹7,00,001 to ₹10,00,000 – 10% tax**
- Income from **₹10,00,001 to ₹12,00,000 – 15% tax**
- Income from **₹12,00,001 to ₹15,00,000 – 20% tax**
- Income **above ₹15,00,000 – 30% tax**

Note: A tax rebate under Section 87A makes income up to ₹7 lakh effectively tax-free in this regime.

Health & Education Cess

- Levied at **4%** on the **total income tax plus surcharge**
- Applicable under **both old and new tax regimes**

Surcharge

- Applicable when **total income exceeds ₹50 lakh**
- **New Tax Regime**
 - Maximum surcharge capped at **25%**
 - Applies for income **above ₹2 crore**
- **Old Tax Regime**
 - Surcharge can go up to **37%**
 - Applies for income **above ₹5 crore**

General Rates (Excluding short term capital gains specified in sec:111A, long term capital gains, winning from lottery, cross word puzzle, races, etc.):

➤ Short-Term Capital Gains (STCG)

- As per **Section 111A**, STCG continues to be taxed at **15%**.
- **Long-Term Capital Gains (LTCG)**
- Generally taxed at **20% with indexation benefit**.
- **LTCG on listed equity shares exceeding ₹1 lakh** is taxed at **10% without indexation**.
- **Winnings from Lottery, Crossword Puzzles, Horse Races, etc.**
- Taxed at a flat rate of **30%**.
- **Surcharge and Cess**
- Applicable as per the **latest Union Budget of India**.
- **Health and Education Cess** is levied at **4%** on the total income tax plus surcharge (earlier it was 3%).

Agriculture income

Agriculture income is exempt under the Indian Income Tax Act. This means that income earned from agricultural operations is not taxed. The reason for exemption of agriculture income from Central Taxation is that the Constitution gives exclusive power to make laws with respect to taxes on agricultural income to the State Legislature. However while computing tax on non-agricultural income agricultural income is also taken into consideration. As per Income Tax Act income earned from any of the under given three sources meant Agricultural Income;

- Any rent received from land which is used for agricultural purpose.
- Any income derived from such land by agricultural operations including processing of agricultural produce, raised or received as rent in kind so as to render it fit for the market, or sale of such produce.
- Income attributable to a farm house subject to the condition that building is situated on or in the immediate vicinity of the land and is used as a dwelling house, store house etc.

Now income earned from carrying nursery operations is also considered as agricultural income and hence exempt from income tax.

In order to consider an income as agricultural income certain points have to be kept in mind:

- There must be a land.
- The land is being used for agricultural operations.
- Agricultural operation means that efforts have been induced for the crop to sprout out of the land.
- If any rent is being received from the land then in order to assess that rental income as agricultural income there must be agricultural activities on the land.
- In order to assess income of farm house as agricultural income the farm house building must be situated on the land itself only and is used as a store house/dwelling house.

Certain income which is treated as Agriculture Income:

- (a) Income from sale of replanted trees.
- (b) Rent received for agricultural land.
- (c) Income from growing flowers and creepers.
- (d) Share of profit of a partner from a firm engaged in agricultural operations.

(e) Interest on capital received by a partner from a firm engaged in agricultural operations.

(f) Income derived from sale of seeds.

Certain income which is not treated as Agricultural Income:

(a) Income from poultry farming.

(b) Income from bee hiving.

(c) Income from sale of spontaneously grown trees.

(d) Income from dairy farming.

(e) Purchase of standing crop.

(f) Dividend paid by a company out of its agriculture income.

(g) Income of salt produced by flooding the land with sea water.

(h) Royalty income from mines.

(i) Income from butter and cheese making.

(j) Receipts from TV serial shooting in farm house are not agriculture income.

Partly agriculture income

Partly agricultural income consists of both the element of agriculture and business, so non-agricultural part of the income is taxed. Some examples for partly agricultural income are given below:

1. Profit of business other than Tea: This rule applicable to agricultural produce like cotton, tobacco, and sugarcane etc., here the market value of the agricultural produce raised by the Assessee for utilizing it as raw material for his business will be deducted out of the total profit of such Assessee while calculating tax on his income.
2. Profit from Tea manufacturing: If a person using his own tealeaves grown by him for his tea manufacturing business, then 60 % of his income will be treated as agricultural income and the remaining 40 % will be treated as business income. So he has to pay tax on that remaining 40% of income.
3. Income from the manufacturing of centrifuged latex or cenex: If a person manufacturing centrifuged latex by using his own made raw then, 65 % of the income derived from the sale of the same is treated as agricultural income so he has to pay tax remaining part of the income.
4. Income from the coffee manufacturing:
 - a) 75% of the income derived from the sale of coffee grown and cured by the seller in India is deemed to be agricultural income 25% is taken as business income.
 - b) 65% the income derived from the sale of coffee grown, cured, roasted and grounded by the seller in India is deemed to be agricultural income 40% is taken as business income.

Residential Status and Tax Incidence

Tax incidence on an assessee depends on his residential status. The residential status of an assessee is determined with reference to his residence in India during the previous year.

Therefore, the determination of the residential status of a person is very significant in order to find out his tax liability. Residence and citizenship are two different things. The incidence of tax has nothing to do with citizenship.

Residential Status of an Individual

As per section 6, an individual may be (a) resident and ordinarily resident in India, (b) resident but not ordinarily resident in India, or (c) non-resident in India. The following are the two sets of conditions for determining the residential status of an individual:

Basic conditions: He is in India in the previous year for a period of 182 days or more

OR

He is in India for a period of 60 days or more during the previous year and has been in India for a period of 365 days or more during 4 years immediately preceding the previous year.

Note: In the following two cases, an individual needs to be present in India for a minimum of 182 days or more in order to become resident in India:

- (a) An Indian citizen who leaves India during the previous year for the purpose of taking employment outside India or an Indian citizen leaving India during the previous year as a member of the crew of an Indian ship.
- (b) An Indian citizen or a person of Indian origin who comes on visit to India during the previous year (a person is said to be of Indian origin if either he or any of his parents or any of his grandparents was born in undivided India).

Additional Conditions:

- (i) He has been resident in India in at least 2 out of 10 previous years [according to basic condition noted above] immediately preceding the relevant previous year.

&

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

Resident

An individual is said to be resident in India if he satisfies any one of the basic conditions.

- Resident And Ordinarily Resident

An individual is said to be resident and ordinarily resident in India if he satisfies any one of the basic conditions and both of the additional conditions.

- Resident But Not Ordinarily Resident

An individual is said to be resident but not ordinarily resident in India if he satisfies any one of the basic conditions but not satisfies both of the additional conditions.

Non-Resident

An individual is a non-resident in India if he satisfies none of the basic conditions.

Residential Status of a Hindu Undivided Family

As per section 6(2), a Hindu undivided family (like an individual) is either resident in India or non-resident in India. A resident Hindu undivided family is either ordinarily resident or not ordinarily resident.

HUF: Resident or Non-Resident

A Hindu undivided family is said to be resident in India if control and management of its affairs is wholly or partly situated in India. A Hindu undivided family is non-resident in India if control and management of its affairs is wholly situated outside India.

A resident Hindu undivided family is an ordinarily resident in India if the karta or manager of the family (including successive kartas) satisfies the following two additional conditions as laid down by section 6(6)(b).

Additional condition (i) Karta has been resident in India in at least 2 out of 10 previous years [according to the basic condition mentioned in immediately preceding the relevant previous year] Additional condition (ii) Karta has been present in India for a period of 730 days or more during 7 years immediately preceding the previous year. If the Karta or manager of a resident Hindu undivided family does not satisfy the two additional conditions, the family is treated as resident but not ordinarily resident in India.

Residential Status of Firm and Association of Persons

As per section 6(2), a partnership firm and an association of persons are said to be resident in India if control and management of their affairs are wholly or partly situated within India during the relevant previous year. They are, however, treated as non-resident in India if control and management of their affairs are situated wholly outside India.

Residential Status of a Company

As per section 6(3), an Indian company is always resident in India. A foreign company is resident in India only if, during the previous year, control and management of its affairs is situated wholly in India. However, a foreign company is treated as non-resident if, during the previous year, control and management of its affairs is either wholly or partly situated out of India.

Scope of Total Income (Section 5):

Resident and ordinarily resident:

Total income of an assessee who is resident and ordinarily resident includes:

- (a) Any income received or deemed to be received in India during the previous year by or on behalf of the assessee; or
- (b) Any income accrues or arises or deemed to accrue or arise to him in India during the previous year; or
- (c) Any income accrues or arises to him outside India during such year.

Resident but not ordinarily resident:

- (a) Any income received or deemed to be received in India during the previous year by or on behalf of the assessee; or

(b) Any income accrues or arises or deemed to accrue or arise to him in India during the previous year; or

(c) Any income accrues or arises to him outside India from a business controlled in or a profession set up in India.

Non- resident:

(a) Any income received or deemed to be received in India during the previous year by or on behalf of the assessee; or any income accrues or arises or deemed to accrue or arise to him in India during the previous year.

Income Exempt from Income Tax

The following Income is exempt from Income tax:-

1. Agriculture Income [Sec. 10(1)]
2. Payments received from family income by a member of HUF [Sec. 10(2)]
3. Share of profit from a firm [Sec. 10(2A)]
4. Interest received by a nonresident from prescribed securities [Sec. 10(4)]
5. Interest received by a person who is resident outside India on amounts credited in the nonresident (External) account [Sec. 10(4)]
6. Leave travel concession provided by as employer to his Indian citizen employee, Sec. 10(5)]
7. Remuneration received by foreign diplomats of all categories [Sec. 10(6)]
8. Salary received by a foreign citizen as an employee of a foreign enterprise provided his stay in India does not exceed 90 days [Sec. 10(6)(vi)]
9. Salary received by a non-resident foreign citizen as a member of ship's crew provided his total stay in India does not exceed 90 days [Sec. 10(6)(vii)]
10. Remuneration received by an employee, being a foreign national, of a foreign government deputed in India for training in a Government establishment or public sector undertaking [Sec. 10(6)(xi)]
11. Tax paid on behalf of foreign companies [Sec. 10(6A)]
12. Tax paid by Government or an Indian concern in case of a non-resident / foreign company [Sec.10(6B)]
13. Income arising to notified foreign companies from services provided in or outside India in project connected with the security of India [Sec. 10(6C)]
14. Foreign allowance granted by the Government of India to its employees posted abroad [Sec. 10(7)]
15. Remuneration received from a foreign Government by an individual who is in India in connection with any sponsored co-operative technical assistance programme with a foreign Government and the income of the family members of such employee [Sec. 10(8)and(9)]
16. Remuneration / fee received by non-received consultants and their foreign employees [Sec. 10(8A),(8B) and (9)]
17. Death-cum-retirement gratuity [Sec. 10(10)]

18. Commuted value of pension and any payment received by way of commutation of pension by an individual out of annuity plan of LIC or any other insurer from a fund set up by that corporation or insurer [Sec. 10(10A)]
19. Leave salary [Sec. 10(10AA)]
20. Retrenchment compensation [Sec. 10(10B)]
21. Compensation received by victims of Bhopal gas leak disaster [Sec. 10(10BB)]
22. Compensation from the Central Government or a state Government or a local authority received by an individual or his legal heir on account of any disaster [Sec. 10(10BC)]
23. Compensation received from a public sector company at the time of voluntary retirement or separation [Sec. 10(10C)]
24. Tax on perquisite paid by employer [Sec. 10(10CC)]
25. Any sum (including bonus) on life insurance policy (not being a keyman insurance policy) [Sec. 10(10D)]
26. Any amount from provident fund paid to retiring employee [Sec. 10(11)]
27. Amount from an approved superannuation fund to legal heirs of the employee [Sec. 10(13)]
28. House rent allowance subject to certain limits [Sec. 10(13A)]
29. Special allowance granted to an employee [Sec. 10(14)]
30. Interest from certain exempted securities [Sec. 10(15)]
31. Payment made by an Indian company, engaged in the business of operation of an aircraft, to acquire an aircraft on lease from a foreign Government or foreign enterprise [Sec. 10(15A)]
32. Scholarship granted to meet the cost of education [Sec. 10(16)]
33. Daily allowance of a Member of Parliament or state Legislature (entire amount is exempt), any other allowance subject to certain conditions [Sec. 10(17)]
34. Rewards given by the central or state Government for literary, scientific or artistic work or attainment or for service for alleviating or for service for alleviating the distress of the poor, the weak and the ailing, or for proficiency in sports and games or gallantry awards approved by the Government [Sec. 10(17A)]
35. Pension and family pension of gallery award winners [Sec. 10(18)]
36. Family pension received by family members of armed forces [Sec. 10(19)]
37. National property income of any one place occupied by a former ruler [Sec. 10(19A)]
38. Income from local authorities [Sec. 10(20)]
39. Any income of housing boards constituted in India for planning, development or improvement of cities, town or villages [Sec. 10(20A)]
40. Any income of an approved scientific research association [Sec. 10(21)]
41. Income of specified non- agencies [Sec. 10(22B)]
42. Any income (other than interest on securities income from property income received for rendering any specific services and income by way of interest or dividends) of approved professional bodies [Sec. 10(23A)]

43. Any income received by any person on behalf of any regimental fund or nonpublic fund established by the armed forces of the union for the welfare of the past and present members of the such forces or their dependents [Sec. 10(23AA)]
44. Income of funds established for the welfare of employees [Sec. 10(23AAA)]
45. Any income of the pension fund set by LIC or any other insurer approved by the controller of insurance or insurance Regulatory and development authority [Sec. 10(23AAB)]
46. Any income (other than business income) of a trust or a society approved by Khadi and village industries commission [Sec. 10(23B)]
47. Income of an authority whether known as Khadi and village industries board or by any other name for the development of Khadi and village industries [Sec. 10(23BB)]
48. Income of the European Economic Community derived in India by way of, interest, dividends or capital gains in certain cases [Section 10(23BBB)]
49. Any income arising to anybody or authority established, constituted or appointed under any enactment for the administration of public religious or charitable trusts or endowments or societies for religious or charitable purposes [Section 10(23BBA)]
50. Income of SAARC Fund for Regional Projects set up by Colombo Declaration [Section 10(23BBC)]
51. Any income of Secretariat of Asian Organisation of Supreme Audit Institutions [Section 10(23BBD)]
52. Any income received by any person on behalf of specified national funds and approved public charitable trust or institution [Section 10(23C)]
53. Income of Mutual Fund set up by — a public sector bank or a public financial institution [Section 10(23D)]
54. Any income by way of dividend or long term capital gains of venture capital funds and venture capital companies [Section 10(23F)]
55. Income of a member of Scheduled Tribe, living in Nagaland, Manipur, Tripura, Arunachal Pradesh and Mizoram from any source arising by reason of his employment therein and income by way of dividend and interest on securities [Section 10(26)]
56. Any income accruing or arising to any resident of Ladakh from any source therein or out of India before the assessment year 1989-90, provided that such person was resident in Ladakh in the previous year relevant to the assessment year 1962-63 [Section 10(26A)]
57. Any income of a statutory Central or State corporation or of a body/institution, financed by the Government formed for promoting the interest of Scheduled Castes/Tribes [Section 10(26B)]
58. Income of co-operative society formed for promoting interests of members of Scheduled Castes/Scheduled Tribes [Section 10(27)]
59. Income by way of subsidy from Tea Board for replanting or replacement of tea bushes or for the purpose of rejuvenation or consolidation of areas used for cultivation of tea in India [Section 10(30)]
60. Subsidy received by planters of Rubber, Coffee, Cardamon [Section 10(31)]

61. Income of a minor child up to Rs. 1,500 in respect of each minor child whose income is includable under section 64(1A) [Section 10(32)]
62. Any income by way of Capital gains on transfer of US-64 units [Section 10(33)]
63. Dividend on or after April, 2003 from domestic companies [Section 10(34)]
64. Income on units of Mutual Funds on or after April 1, 2003 [Section 10(35)]
65. Long term Capital gains on transfer of listed Equity Shares purchased during 1-3-2003 to 29-2-2004 [Section 10(36)]
66. Capital gain to individual/HUF on compensation received on compulsory acquisition of urban agriculture land [Section 10(37)]
67. Long term capital gain in some cases [Section 10(38)]
68. Sum received without consideration from international sporting event held in India [Section 10(39)]
69. Income of Industrial Units situated in trade-free zones, specified technology parks etc. [Section 10A]
70. Income from specified 100% export oriented undertakings [Section 10B]
71. Income from property held for approved charitable or religious purposes [Section 11]
72. Specified Income of Registered political parties [Section 13A]