

# UNIT I

## Income Tax Law & Accounts

### Introduction

In India, Income tax was introduced for the first time in **1860**, by **Sir James Wilson** in order to meet the losses sustained by the Government on account of the Military Mutiny of 1857. Thereafter; several amendments were made in it from time to time. In 1886, a separate Income tax act was passed. This act remained in force up to, with various amendments from time to time. In 1918, a new income tax was passed and again it was replaced by another new act which was passed in 1922. This Act remained in force up to the assessment year 1961-62 with numerous amendments. The Income Tax Act of 1922 had become very complicated on account of innumerable amendments. The Government of India therefore referred it to the law commission in 1956 with a view to simplify and prevent the evasion of tax. The law commission submitted its report in September 1958, but in the meantime the Government of India had appointed the Direct Taxes Administration Enquiry Committee submitted its report in 1956. In consultation with the Ministry of Law finally the **Income Tax Act, 1961** was passed. The Income Tax Act 1961 has been brought into force with 1 April 1962. It applies to the whole of India including Jammu and Kashmir.

Income-tax law in India The income tax law in India consists of the following components:

- Income tax Acts
- Income tax rules
- Finance Act
- Circulars, notifications etc.
- Legal decision of courts.

#### **Finance Act:**

Every year, the Finance Minister of the Government of India presents the Budget to the Parliament. Once the Finance Bill is approved by the Parliament and gets the assent of the President of India, it becomes the Finance Act.

#### **Income-tax Rules:**

The administration of direct taxes is looked after by the Central Board of Direct Taxes (CBDT). The CBDT is empowered to make rules for carrying out the purposes of the Act. For the proper administration of the Income-tax Act, the CBDT frames rules from time to time. These rules are collectively called Income-tax Rules, 1962.

Important Definitions

#### **Assessment Year: Section 2(9)**

“Assessment year” means the period starting from April 1 and ending on March 31 of the next year. E.g.: Assessment year 2022-23 this commences on April 1, 2022 and ends on March 31, 2023. Income of previous year of an assessee is taxed during the assessment year at the rates prescribed by the relevant Finance Act for tax rates.

Previous year: section 3 Income earned in a particular year is taxable in the next year. The year in which income is earned is known as previous year and the next year in which income is taxable is known as assessment year. In other words, previous year is the financial year immediately preceding the assessment year.

Exceptions to the general rule that previous year's income is taxable during the assessment year In the following situations income of an assessee is liable to be assessed to tax in the same year in which he earns the income:

- a. Income of non-residents from shipping;
- b. Income of persons leaving India either permanently or for a long period of time;
- c. Income of bodies formed for short duration;
- d. Income of a person trying to alienate his assets with a view to avoiding payment of tax;
- e. Income of a discontinued business.

Person: Section 2(31) The term "person" includes: 1. an individual; 2. a Hindu undivided family; 3. a company; 4. a firm; 5. an association of persons or a body of individuals, whether incorporated or not; 6. a local authority; and 7. every artificial juridical person not falling within any of the preceding categories.

### **Assessee: Section 2(7)**

Every person in respect of whom, any proceeding under the act has been taken for the assessment of his income or of the income of any other person in respect of which he is assessable or of the loss sustained by him or by such other person or the amount of refund due to him or to such other person may be called an assessee.

**Deemed Assessee:** A person who is deemed to be an assessee for some other person is called "Deemed Assessee".

**Assessee in Default:** When a person is responsible for doing any work under the Income Tax Act and he fails to do it, he is called an "Assessee in default".

### **Assessment [Section 2(8)]**

This is the procedure by which the income of an assessee is determined by the Assessing Officer.

### **Basis of Charge of Income Tax Sec: 4**

To know the procedure for charging tax on income, one should be familiar with the following:

1. Annual tax - Income-tax is an annual tax on income.
2. Tax rate of assessment year - Income of previous year is chargeable to tax in the next following assessment year at the tax rates applicable for the assessment year. This rule is, however, subject to some exceptions
3. Rates fixed by Finance Act - Tax rates are fixed by the annual Finance Act and not by the Income-tax Act. For instance, the Finance Act, 2022, fixes tax rates for the Assessment year 2022-23.
4. Tax on person - Tax is charged on every person

5. Tax on total income - Tax is levied on the “total income” of every assessee computed in accordance with the provisions of the Act.

### **INCOME: Section 2(24)**

The definition of the term “income” in section 2(24) is inclusive and not exhaustive. Therefore, the term “income” not only includes those things that are included in section 2(24) but also includes those things that the term signifies according to its general and natural meaning. Income, in general, means a periodic monetary return which accrues or is expected to accrue regularly from definite sources. However, under the Income-tax Act, 1961, even certain incomes which do not arise regularly are treated as income for tax purposes e.g. Winnings from lotteries, crossword puzzles.

### **Section 2(24) of the Act gives a statutory definition of income.**

At present, the following items of receipts are included in income:—

- Profits and gains.
- Dividends.
- Voluntary contributions received by a trust/institution created wholly or partly for charitable or religious purposes or by an association or institution
- The value of any perquisite or profit in lieu of salary taxable under section 17.
- Any special allowance or benefit other than the perquisite included above, specifically granted to the assessee to meet expenses wholly, necessarily and exclusively for the performance of the duties of an office or employment of profit.
- Any allowance granted to the assessee to meet his personal expenses at the place where the duties of his office or employment of profit are ordinarily performed by him or at a place where he ordinarily resides or to compensate him for the increased cost of living.
- The value of any benefit or perquisite whether convertible into money or not, obtained from a company either by a director or by a person who has a substantial interest in the company or by a relative of the director or such person and any sum paid by any such company in respect of any obligation which, but for such payment would have been payable by the director or other person aforesaid.
- The value of any benefit or perquisite, whether convertible into money or not, which is obtained by any representative assessee mentioned under section 160(1)(iii) and (iv), or by any beneficiary or any amount paid by the representative assessee for the benefit of the beneficiary which the beneficiary would have ordinarily been required to pay.
- Deemed profits chargeable to tax under section 41 or section 59.
- Profits and gains of business or profession chargeable to tax under section 28.
- Any capital gains chargeable under section 45.
- The profits and gains of any insurance business carried on by Mutual Insurance Company or by a cooperative society, computed in accordance with Section 44 or any surplus taken

to be such profits and gains by virtue of the provisions contained in the first Schedule to the Act.

- The profits and gains of any business of banking (including providing credit facilities) carried on by a co-operative society with its members.
- Any winnings from lotteries, cross-word puzzles, races including horse races, card games and other games of any sort or from gambling, or betting of any form or nature whatsoever.
- Any sum received by the assessee from his employees as contributions to any provident fund or superannuation fund or Employees State Insurance Fund (ESI) or any other fund for the welfare of such employees.
- Any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy will constitute income. “Keyman insurance policy” means a life insurance policy taken by a person on the life of another person where the latter is or was an employee or is or was connected in any manner what so ever with the former’s business.
- Any sum referred to clause (va) of Section 28. Thus, any sum, whether received or receivable in cash or kind, under an agreement for not carrying out any activity in relation to any business; or not sharing any know-how, patent, copy right, trade-mark, license, franchise, or any other business or commercial right of a similar nature, or information or technique likely to assist in the manufacture or processing of goods or provision of services, shall be chargeable to income tax under the head “profits and gains of business or profession”.
- Any sum of money or value of property referred to in section 56(2)(vii) or section 56(2)(viii).
- Any consideration received for issue of shares as exceeds the fair market value of shares referred to in section 56(2)(viib).

### **Gross Total Income Sec: 80b (5)**

As per section 14, the income of a person is computed under the following 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. If the income is not derived from any of the above sources, it is not taxable under the act. The aggregate income under these heads is termed as “gross total income”.

### **Total Income Sec: 2(45)**

Total income means the amount left after making the deductions under section 80C to 80U from the gross total income.

### **Casual Income**

Any receipt which is of a casual and non-recurring nature is called casual income. Casual income includes the following receipts:

1. Winning from lotteries,
2. Winning from crossword puzzles,
3. Winning from races (including horse races),
4. Winning from card games and other games of any sort
5. Winning from gambling or betting of any form or nature.

### **RATES OF INCOME TAX FOR THE ASSESSMENT YEAR 2023-24**

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

Individual:

Upto Rs.2,50,000 -----	Nil
Rs.500,001 to 10,00,000 -----	20%
Above Rs.10,00,000 -----	30%

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

Upto Rs.3,00,000 -----	Nil
Rs.3,00,001 to 5,00,000 -----	5%
Rs.5,00,001 to 10,00,000 -----	20%
Above Rs.10,00,000 -----	30%

Other individuals, (Above 80 years)

Upto Rs. 5,00,000 -----	Nil
Rs. 5,00,001 to 10,00,000 -----	20%
Above Rs. 10,00,000 -----	30%

Special Rates:

- On short term capital gains specified in Sec. 111A-----15%
- On long term capital gains -----20%
- On gains from listed shares without indexing the cost of acquisition-----10%
- On winnings from lottery, cross word puzzle, horse race, etc.-----30%
- Surcharge: Nil
- Education Cess: 3% on the amount of income tax.

### **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 as 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 includible 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]