

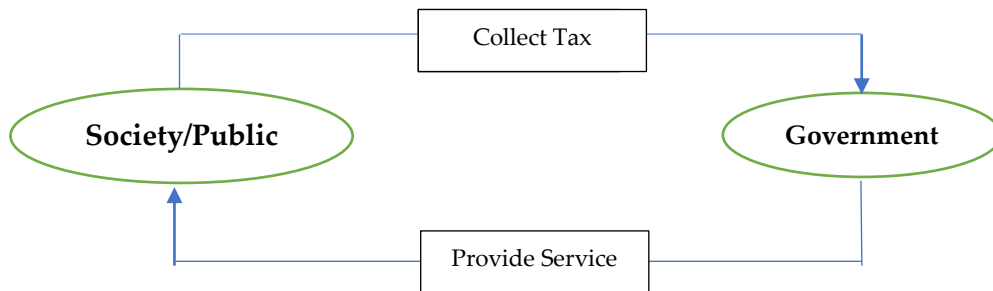
Chapter 1

Introduction to Income Tax

Syllabus:

Brief History of Indian Income Tax - Legal Frame Work – Types of Taxes - Cannons of Taxation – Important Definitions: Assessment, Assessment Year, Previous Year (including Exceptions), Assessee, Person, Income, Casual Income, Gross Total Income, Agricultural Income (including Scheme of Partial Integration – Theory Only) – Scheme of taxation. Meaning and classification of Capital & Revenue. Income tax authorities: Powers & functions of CBDT, CIT & A.O.

Introduction to Tax

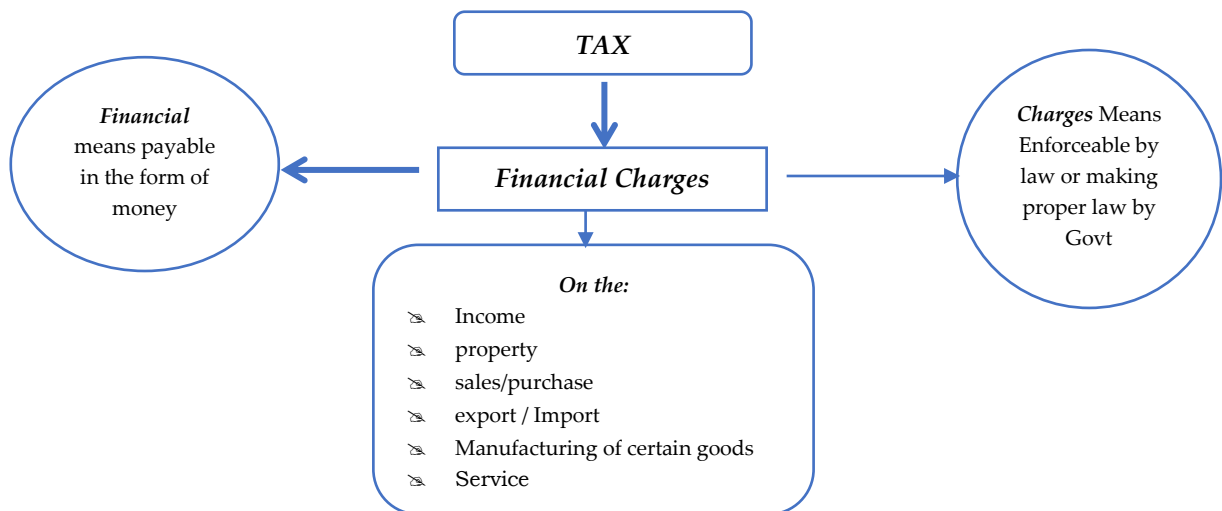


- Government collect funds from Society/public in the way of charging tax.
- Government provide public services Eg: Hospitals, roadways, Education, Dam construction Etc.,

Meaning of Tax

Tax is the mandatory financial charges or levy which is imposed upon a tax payer (Individual/entity) by the government in order to fund various public expenditure.

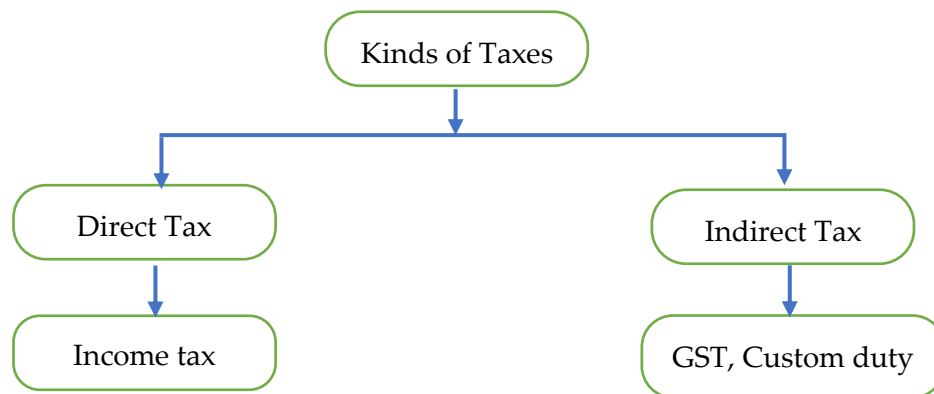
In other words, Tax refers to compulsory contribution made by citizens of the country to the government for the benefits obtained from government. In other words, tax means a financial charges or other levy upon a person (tax payers) by a state (government). *Tax is the Price we pay for living in a civilized society.*



According to Prof. Seligman “tax is a compulsory contribution from a person to the government to defray the expenses incurred in the common interest of all, without reference to special benefits conferred”.

The taxes are the basic source of revenue for the Government. Revenue raised from the taxes are utilized for meeting expense of Government like, provision for education, infrastructure facilities such as roads, dams etc. Taxes are broadly divided into two parts i.e. direct taxes and indirect taxes.

Country is run by the government. To run the country government needs funds and these funds are collected by government from various sources and one the main sources of revenue to the government is **Taxes**.



Direct Tax

Direct taxes are paid by the person (Tax payer) directly to the government. The person paying the taxes cannot shift its burden on some other person. In case of direct taxes **Impact** (*Immediate effect*) and **Incidence** (*Final burden*) are on same person. E.g. *Income Tax*

Indirect Tax

Indirect Taxes are those taxes which the tax payer pays indirectly. The person paying the taxes can recover it from another person. Therefore, in case of indirect tax **impact and incidence** are on two different persons. **Eg: Goods and Services Tax (GST), Customs and Excises (On selected items)**

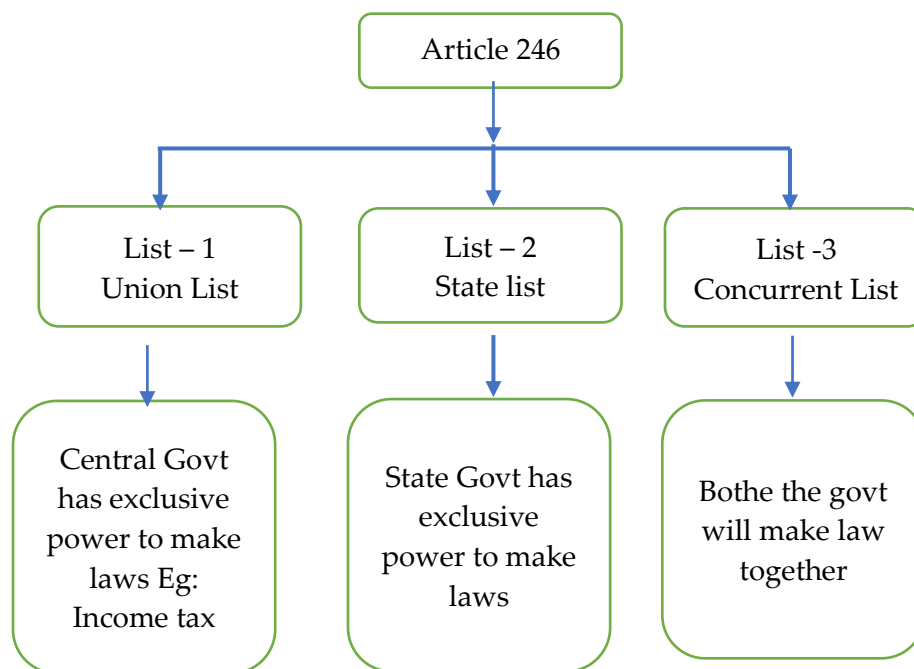
Important Points

1. The word **Tax** derived from **Latin** word which means “**assess**”.
2. The Tax are imposed by the government with legislative power.
3. It is an enforced payment.
4. Its evasion is punishable under law.

Constitution power to levy tax

1. Constitution of India is the parent law. Any law can be made in India provided; it is permitted by the constitution.
2. The Constitution of India, in *Article 265* lays down that *“No tax shall be levied or collected except by authority of law”*. Accordingly, for levy of any tax, a law needs to be framed by the government.
3. Constitution of India gives the power to levy and collect taxes, Whether direct or Indirect, to the central and state government. Article 246, of the constitution gives power to levy various kinds of tax.

Seventh schedule of Article 246 contains three lists which enumerate the matters under which the parliament and the state legislatures have the authority to make laws for the purpose of levy of taxes. Schedule VII gives power to collect taxes with the help of 3 lists.



Note: GST is levied now in place of Excise, VAT, Services tax etc., as per the article 246A of Constitution of India.

How laws are enacted by Central Government?

Central government laws are enacted through parliament and approval of president of India is must after that.

State government laws are enacted through state assembly and with the approval of president of state.

Since Income tax is central matter therefore central government has enacted Income tax Act, 1961 through parliament.



The concept of Income tax was introduced in India for the first time by James willson in the year 1860 in order to recover the expenditure incurred by the government on account of "SEPUY MUTINY" in the year 1857. From time to time numerous amendments were made especially from 1860 – 1886, in order to establish a possible system with which taxes could be imposed on a variety of services.

In the year 1886 a separate Income tax Act was passed with various amendments added from time to time. In 1918 another Act was passed, and it remained active but it was short lived and it was replaced by a new Act bought into force in 1922.

The Income Tax Act 1922 was to complicated because of numerous amendments. So, the Government of India referred to the law commission in 1956, Which submitted its report in September 1958. In the 1959, the "Direct Taxes Administration Enquiry Committee" appointed by government submitted its report and the Income Tax Act 1961 was passed in consultation with the Ministry of Law.

The Income Tax Act 1961 came into force with effect from 1st April 1962. The Income Tax Act, 1961 Applies to the whole of India including Jammu and Kashmir. Every year the union budget makes several amendments in the Income Tax (Finance Bill). The bill passes through both houses of parliament and finally receives the consent of the President of India to become the finance Act. This Act also has undergone several amendments from time to time.

Road Map of Income Tax Act

1860	Introduction of Tax by Sir James Wilson
1886	Separate Income Tax Act was Passed
1918	New Income Tax Act was passed
1922	Another Income tax Act was Passed
1956	Reference of Law Commission
1957	Submission of Report by Law commission
1958	Submission of report by DTAEC
1961	Farming of Income Tax Act 1961
1962	I.T Act 1961 was brought to force on 1 st April

Legal Frame work of Income Tax in India

Income Tax in India is governed and monitored by the following.

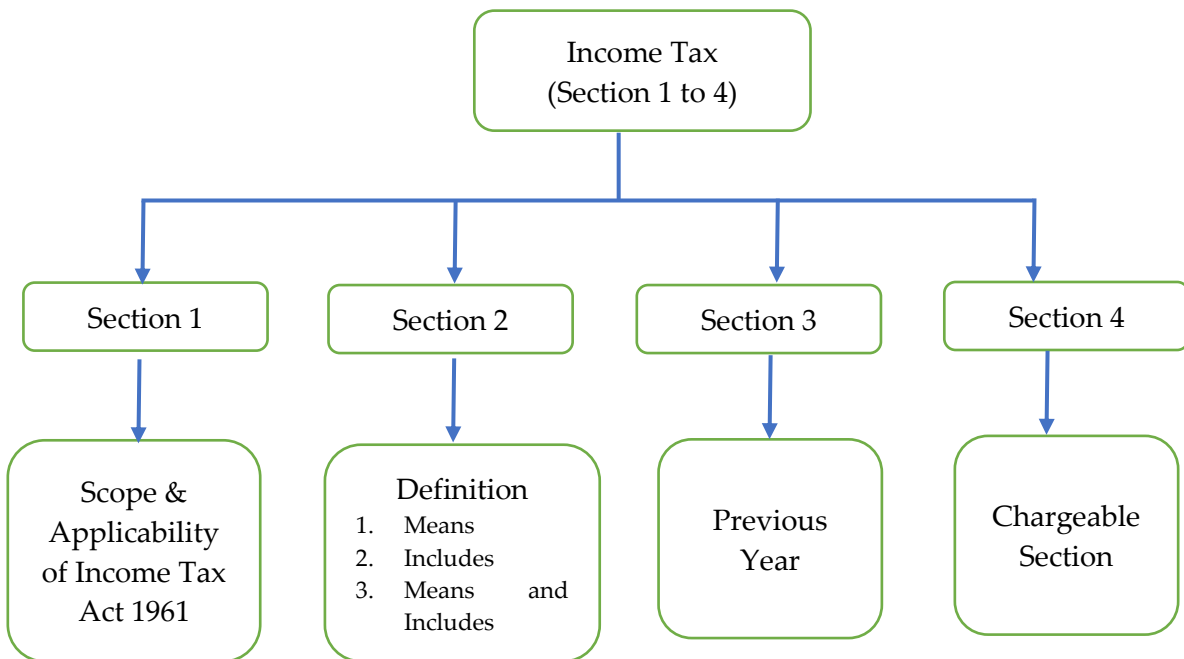
- Income Tax Act 1961 as amended time to time
- The Finance Act passed by the parliament every year
- The Income Tax rules 1962 framed and amended by the Central Board of Direct Tax (CBDT)
- The circular, Notification instruction given by the CBDT from time to time.
- Legal Decision of Courts.

Meaning of Income Tax

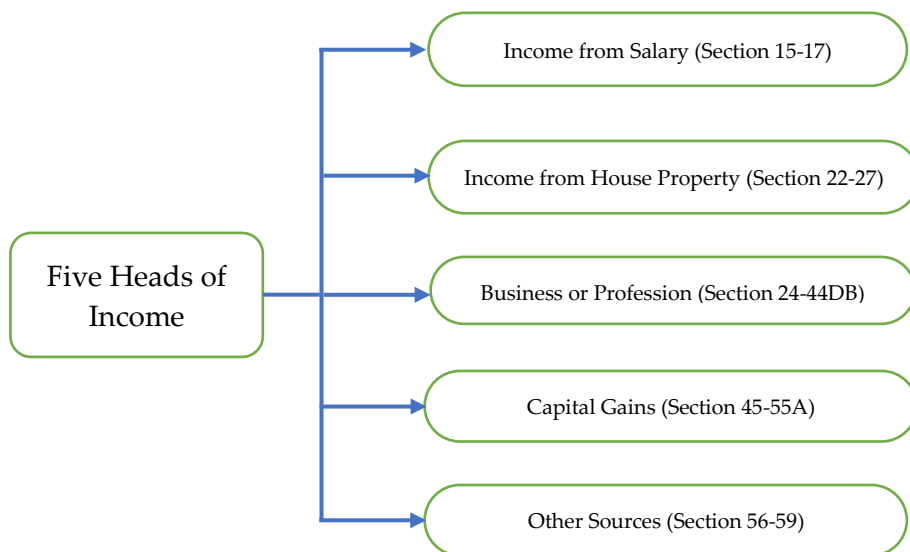
The tax that is levied directly on the income of a person is called direct tax. Income tax is one of form of direct taxes. The levy of income tax in India is governed by the Income Tax Act, 1961 and Income Tax Rules, 1962. It is charged on the Total Income. In other Words, Income Tax refers to tax on Income. There are five heads of Income under Income Tax.

It is the tax levied on Income earned by the assessee during the previous year and the tax is payable in the assessment year at the rate prescribed by the relevant Finance Act. It is the tax levied by the central government on the income earned by an assessee every year.

Income Tax Section 1 to 4



Heads of Income under Income Tax



Canons of Taxation

It refers to the principles of taxation. In other words, it refers to the basis on which the income is taxed. These principles are essential for a good taxation policy. The following are the important principles (canons) of taxation.

- ✘ **Canon of equality:** This is also known as “canon of equity”. This principle is mainly based on “justice”. i.e., all assesses should be treated equally. The burden of taxation must be distributed equally. The outcome of this principle is that the person who earns more income should pay more tax and the person who earn less income should pay lesser tax.
- ✘ **Canon of Certainty:** Under this principle, certainty regarding time of payment, manner of payment, amount to be paid, the authority to who the tax should be paid are discussed i.e., the tax amount to be paid should be certain and clear. The time and manner of payment should not be vague.
- ✘ **Canon of Economy:** This principle deals with cost of collection and it states that the cost of collection should be minimum. The basis of this principle is that imposing taxes which are widespread and difficult to administer will be of no use. Minimum expenditure and maximum collection principle should be followed.
- ✘ **Canon of Convenience:** This convenience principle concentrates on the tax payer (Assessee). This principle states that the assessee should feel convenient regarding the exact mode and timing of tax payment i.e., (submission of return of income). For example, a salaried employee should pay tax after collecting his income.
- ✘ **Canon of Productivity:** This is termed as fiscal adequacy. It states that the tax system will generate inflow of the treasury. i.e., it will bring revenue to the treasury. This principle also concentrates and implies that the tax system of generating revenue should not adversely affect production. Productive taxation makes it essential that it may not have any unfavourable effect on the saving potential of the people.
- ✘ **Canon of Simplicity:** The tax system should be made as simple as possible, in such a way that even a layman can understand it. The tax procedure, rules, regulation etc., are to be simple giving room for easy understanding.
- ✘ **Canon of diversity:** Under this principle, a multiple tax system should be followed. It suggests that the tax system should be of diverse nature. It is on the assumption that too much dependence on fewer sources of public revenue would lead to a lot of uncertainty to the treasury. A mixture of direct and indirect tax should be followed.
- ✘ **Canon of Expediency:** This principle states that tax determination and administrations should not give scope for any criticism.
- ✘ **Canon of Co-ordination:** This principle states that there should be co-ordination among the different taxes as and when they are imposed by the tax authorities.

Assessee Section 2(7)

The Assessee means a person by whom any tax or any other sum of money is payable under this Act. Any other sum includes fine, interest, penalty etc. There are three types of assessee.

- a) **Ordinary Assessee:** An ordinary assessee is one who has to pay any tax, penalty and interest to the income tax authority or who is eligible for any refund of tax from the tax authorities.
- b) **Deemed Assessee:** Deemed assessee is also known as representative assessee. This type of assessee is not only responsible for his income but also responsible for the income of the other person to whom he acts as a representative. For Example, if Mr. Kumar takes care of a minor, then Mr. Kumar is responsible for his income as well for the income of the minor.

Particular	Deemed Assessee
For a Minor	Guardian
For a Non- Resident	Agent
For deceased person (With Will)	Executor
For deceased person (without will)	Legal heir or the eldest in the family

- c) **Assessee in Default:** If any person fails to fulfil his duty or obligation, then he is termed as assessee in default. For Example, if a person who should submit a return of income fails to do so then he is assessee in default. If an employer who is supposed to deduct tax at source fails to do so then he will also be termed as an assessee in default.

Person Section 2(31)

Person includes the following:

1. Individual	Any natural human being created by god (Male, female, child, lunatic, idiot etc)
2. A Hindu Undivided Family	Which consists of all persons who are lineally descended from a common ancestor including wives, sons and unmarried daughters?
3. A Firm	As defined by the partnership Act.
4. An AOP or BOI	Trust
5. A Local authority	Municipal corporation
6. A Company	As defined by the partnership Act
7. Any artificial juridical person	Created by law not mentioned in the above categories – Similarly Universities, BAR councils will be assessed as artificial juridical person.

Assessment Year Section 2 (9)

Assessment year refers to the period of 12 months commencing from 1st April of each year and ending on the 31st March of following(next) year. It is a period during which assessment of assessee income of previous year will be made.

Assessment Year (AY) = 1st April 20__ to 31st March 20__

Previous Year Section 3

Previous year means the financial year immediately preceding the relevant assessment year is known as previous year. It is a period of 12 months or less than 12 months.

Note: In case of newly started business or profession or otherwise, previous year starts from the date of commencement of the business and ends on 31st March every year.

Previous Year (AY) = 1st April 20__ to 31st March 20__

Example 1: A new business is set up on 1 November 20__. The first previous year will consist of a period of 5 months, beginning on 1 November 20__ and ending on 31st March 20__.

Example 2: A new house property is purchased on 15th October 20__. The first previous year will begin on 15th October 20__ and will end on 31st March 20__.

Example 3: Mr J is appointed as Sales manager on 1st January 20__. The first previous year will begin on 1st January 20__ and will end on 31st March 20__.

Exception to the Rule of Previous Year:

1. Shipping business of Non-resident
2. Person Leaving India
3. Association of person or Body of Individuals or Artificial juridical person formed for a particular event or purpose
4. Income of a discontinued business
5. Income of a person likely to transfer property to avoid tax.

Income Section 2(24)

The Income tax does not define the term "Income". It has just specified certain things, which can be brought under the concept of Income. The Normal dictionary meaning (anything which brings benefit in the form of cash or kind) of income is taken into account for tax purpose. The following are some includes income:

1. Profits and Gains
2. Dividend
3. Voluntary Contribution to any trust created wholly or partly for charitable purposes.
4. Perquisites
5. Salary
6. Allowances Etc.,
- 7.

Gross Total Income Section 14

Gross total income is dealt under section 14 of the Income Tax Act 1961. Gross total income refers to sum total of various heads of incomes such as salary, house property, business or profession, capital gains and other sources. It should calculate as follows:

Particulars	Rs.
1. Income from salary	Xxx
2. Income from house property	Xxx
3. Income from business or profession	Xxx
4. Income from capital gains	Xxx
5. Income from other sources	Xxx
Gross Total Income	Xxx

Note: Any loss in the heads of income will be adjusted before calculating the Gross total income (GTI).

Agricultural Income

Agricultural income refers to

1. Any rent or revenue derived from land, which is situated in India and used for agricultural purpose.
2. Any income derived from such land, which is used for agricultural operations.
3. Any income from a farm house.
4. Any income derived from saplings or seedling grown in a nursery will be deemed as agricultural income.

Agricultural income is fully Exempted from Tax u/s 10(1).

Residential Status and Incidence of Tax

Syllabus:

Scope of Total Income/Incidence of Tax (Section 5)

Total Income of an assessee cannot be computed unless we know his residential status in India during the previous year. According to the residential status, the assessee can either be.

However, Individual and HUF cannot be simply called resident in India. If Individual is resident in India he will be either.

- a) Resident and Ordinarily resident in India
- Or
- b) Resident but not ordinarily resident in India

Incidence of Tax/Scope of Total Income Section 5

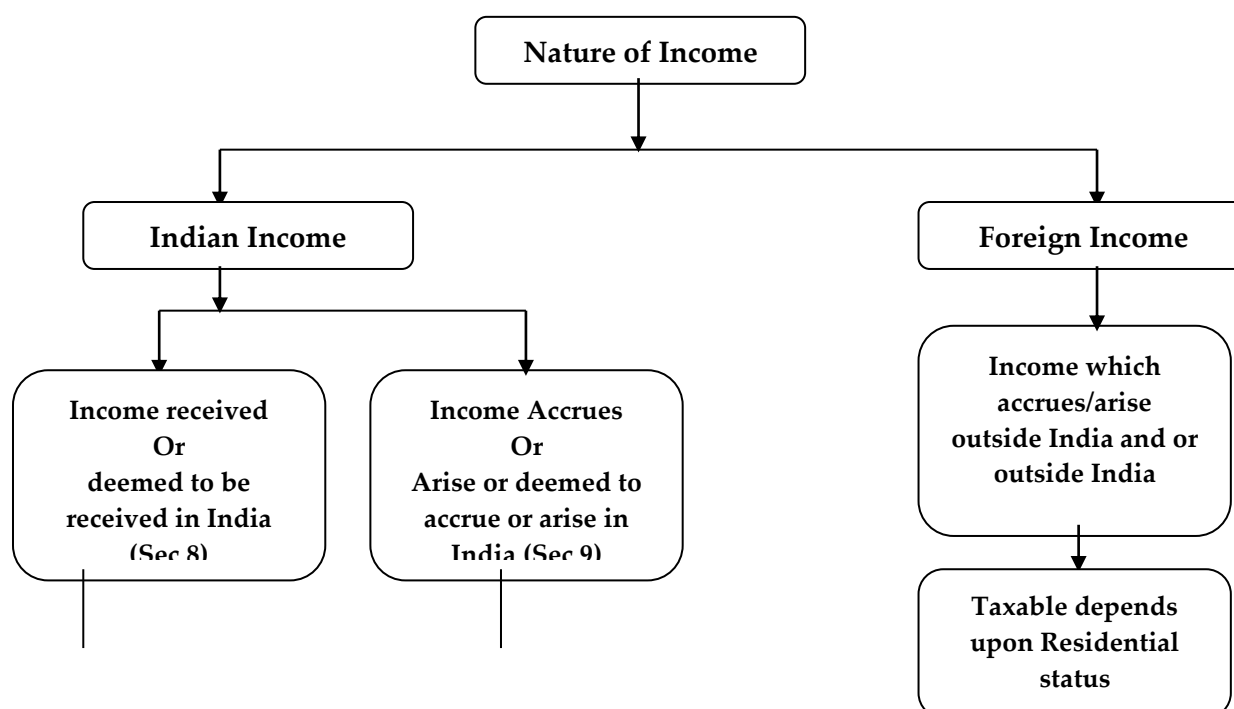
Introduction

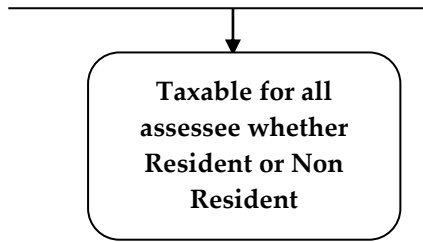
Section 5 deals with the scope of total income. The scope of total income depends on the residential status of a particular person. The total income liable to tax will vary according to the residential status a particular person gains in a particular previous year. The following table will show the tax incidence for different residential status.

Rules of Incidence Table

SL No	Type of Income	OR	NOR	NR
1	Any Income received or Deemed to receive in India, Whether accrued in India or Outside India.	Taxable	Taxable	Taxable
2	Any incomes accrue in India, Whether received in India or outside India.	Taxable	Taxable	Taxable
3	Income received outside India from a business or profession controlled from India	Taxable	Taxable	Not Taxable
4	Income received outside India from a business or profession controlled from outside India.	Taxable	Not Taxable	Not Taxable
5	Income received outside India from any other source apart from business	Taxable	Not Taxable	Not Taxable
6	Past untaxed Profit brought into India	Taxable	Not Taxable	Not Taxable
7	Income earned outside India in earlier years but later on remitted to India	Not Taxable	Not Taxable	Not Taxable

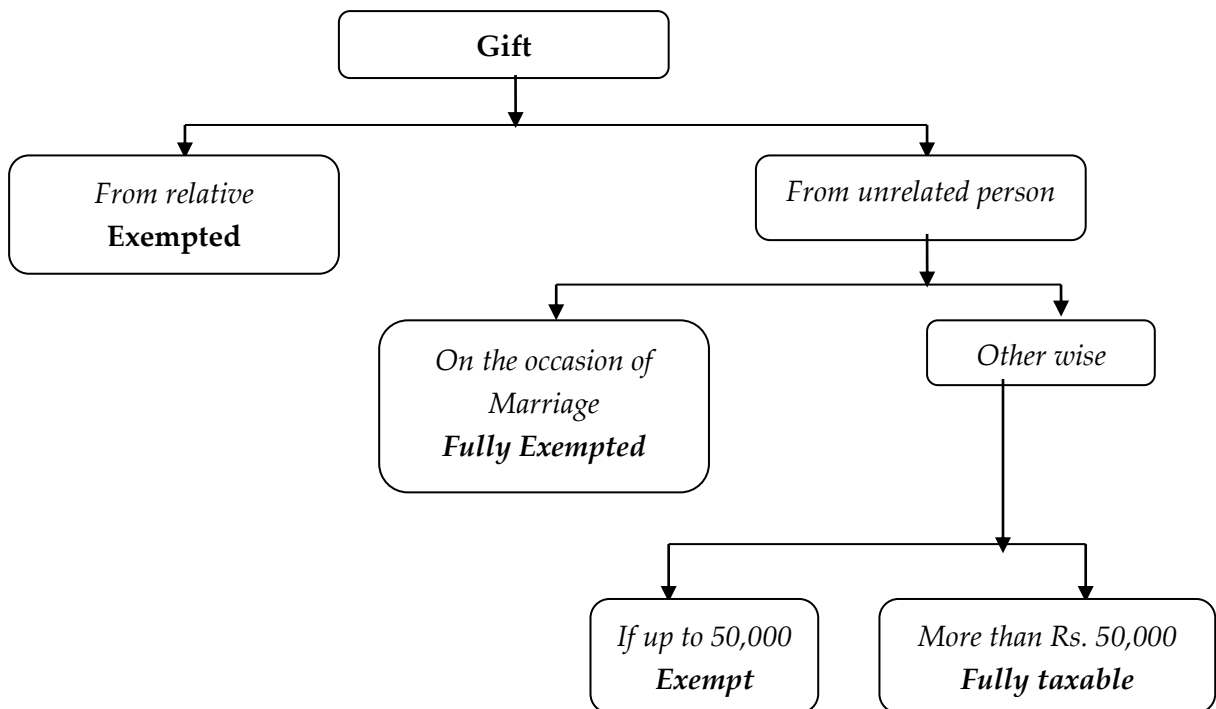
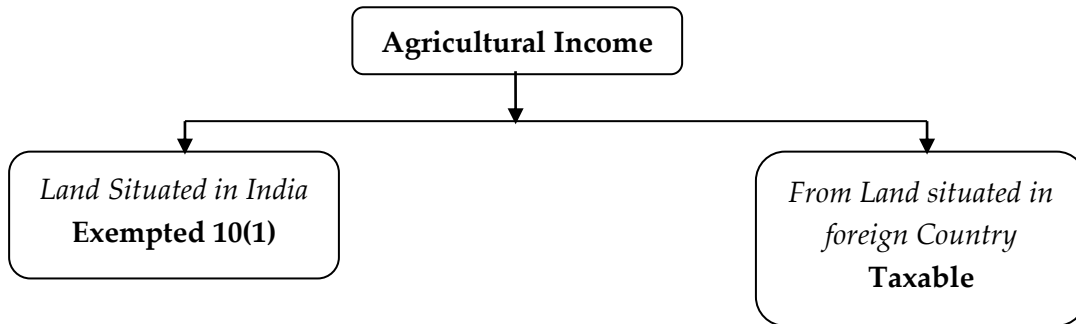
Liability to pay tax depends upon the nature of Income.





Note:

- 1. *If an income is taxed on an accrual basis then it will not be taxed again on receipt basis.*
- 2. *Exempt income is not to be included Eg: Agricultural income from land situated in India or Gift received from relatives etc.,*



- 3. *Income should relate to the previous year any other earlier previous year's income is not to be taken.*
- 4. *We tax Receipt of income not remittance of Income. Receipt means the first receipt.*

5. In the case of ROR, both Indians, as well as foreign incomes, are taxable in India.

Illustration 1

The following are the incomes of Mr. Ram for the previous year. Calculate his taxable income on the assumption that he is (a) ordinary resident (b) Not ordinary resident and (c) Non – Resident.

1. Profit from business carried from Hyderabad Rs. 50,000
2. Income accrued in India but received in Hongkong Rs. 75,000
3. The past untaxed income brought into India during this previous year Rs. 42,000.
4. Income from House property situated in Srilanka Rs. 48,000
5. Income from agriculture in the USA Rs. 1,00,000

Solution:**Calculation of Taxable Income of Mr. Ram**

SL No	Type of Income	OR	NOR	NR
1	Profit from business carried from Hyderabad	50,000	50,000	50,000
2	Income accrued in India but received in Hongkong	75,000	75,000	75,000
3	The past untaxed income brought into India during this previous year	-	-	-
4	Income from House property situated in Srilanka	48,000	-	-
5	Income from agriculture in USA	1,00,000	-	-
	Total Income	2,73,000	1,25,000	1,25,000

Illustration 2

From the following details calculate the total income of Ms. Mumtaj, is she is OR, NOR, and NR.

1. Dividend from Indian Company Rs. 1,00,000
2. Dividend from a foreign company Rs. 1,50,000, received in India.
3. Income from a business in Kanya but controlled from India Rs. 2,00,000.
4. Income from a business in Switzerland but controlled from Bangladesh Rs. 5,00,000.
5. Income accrued in Indonesia Rs. 2,50,000, 2/5th Received in India.

Solution:**Calculation of Taxable Income of Ms. Mumtaj**

SL No	Type of Income	OR	NOR	NR
1	Dividend from Indian Company	1,00,000	1,00,000	1,00,000
2	Dividend from a foreign company	1,50,000	1,50,000	1,50,000
3	Income from business in Kanya but controlled from India	2,00,000	2,00,000	-
4	Income from a business in Switzerland but controlled from Bangladesh	5,00,000	-	-
5	Income accrued in Indonesia			

	A. 2/5 TH received in India	1,00,000	1,00,000	1,00,000
	B. Balance 2/4 th received outside India	1,50,000	-	-
	Total Income	11,00,000	4,50,000	2,50,000

Illustration 3

Mr. Avinash furnishes the following information on income for the A.Y 2020-2021. Find out his total income if his residential status is: OR; NOR; NR.

1. Income from business from Mumbai Rs. 1,00,000
2. Profit from business in the USA controlled from India Rs. 50,000
3. Income from house property in Japan received there Rs. 50,000
4. Income from a business in India, but received in London Rs. 30,000
5. Salary Received in India for services rendered in USA Rs. 70,000
6. Profit from business in Malaysia controlled from India (1/3 received in India) Rs. 30,000.
7. The past untaxed income brought into India Rs. 8,000.
8. Dividend received from a domestic company Rs. 5,000.
9. Agricultural income earned in Nepal Rs. 25,000.
10. Interest received in Private company securities Rs. 25,000.
11. The gift in cash from father Rs. 30,000.

Calculation of Taxable Income of Ms. Mumtaj

SL No	Type of Income	OR	NOR	NR
1	Income from business from Mumbai			
2	Profit from business in the USA controlled from India			
3	Income from house property in Japan received there			
4	Income from a business in India			
5	Salary Received in India for services rendered in USA			
6	Profit from business in Malaysia controlled from India (1/3 received in India)			
7	The past untaxed income brought into India			
8	Dividend received from a domestic company			

9	Agricultural income earned in Nepal			
10	Interest received in Private company securities			
11	The gift in cash from father			
	Total Income			

Illustration 4

Sri Ram submits the following particulars of his income for the year 2020-2021.

1. Income from house property in Hasana received in Paris Rs. 6,50,000
2. Salary income from an Indian employer received in Newyork for two months Rs. 75,000 p.m
3. Income from a business in Mumbai received in Bangalore (40% remitted to Nepal) Rs. 12,50,000.
4. Dividend from the foreign company received in Chennai Rs. 1,80,000.
5. Income from a business in Hongkong and the business is controlled from Tumkur (25% received in Tumkur).
6. Interest in post office S.B A/c in Bangalore (Account is held in Joint names) Rs. 17,500.
7. Income from agricultural land in Srilanka (50% received in India) Rs. 2,05,000.
8. Share from HUF Rs. 60,000.
9. Royalty received in India for the service rendered in Japan Rs. 6,00,000.
10. Interest earned on U.S Government Bonds received in London Rs. 1,75,000.
11. Interest in SBI deposits received in Bhutan Rs. 7,080.
12. The past untaxed foreign income brought to India Rs. 6,10,000.
13. Interest on housing loan given to MR. X for construction of the house is Bangladesh received in Bangalore Rs. 65,020.

Calculate his gross total income for the A.Y 2020-2021 if he is

- a) *Ordinary Resident*
- b) *Not – Ordinary Resident*
- c) *Non- Resident*

Illustration 5

Mr. Krishna furnishes the following particulars of his income earned during the previous year 2019-2020.

1. Profit from business in Chennai Rs. 50,000.
2. Income from agriculture in Ceylon Rs. 1,90,000.
3. Income from the property in Mexico received there Rs. 2,00,000.
4. Interest in Singapore development bonds Rs. 1,50,000 (1/3 received in India).

5. Income from a business in Kuwait controlled from Mumbai Rs. 85,000 (Rs. 35,000 was received in India).
6. Dividend from domestic company Rs. 1,000.
7. Profit on sale of building in Bangalore received in Nepal Rs. 50,000.
8. Income from agriculture in Punjab Rs. 1,00,000.
9. Profit on sale of Plant at London Rs. 50,000(50% is received in India)
10. Rent from house property in Nepal received there Rs. 20,000.
11. Profit from business in Mysore received in Mandya Rs. 25,000.
12. Dividends from U.K based company received in U.K Rs. 27,000.

Compute his gross total income for the A.Y 2020-2021, if he is

- a) Ordinary resident*
- b) Not Ordinary resident*
- c) Non – resident*

Illustration 6

Mr. Akshay furnishes the following particulars of his income for the previous year 2019-2020. Determine his taxable income for the A.Y 2020-2021. If his residential status is: OR; NOR; NR.

1. Income from a business in Hubli Rs. 1,00,000.
2. Profit from business in the UK controlled from India Rs. 60,000.
3. Income from house property in Japan received there Rs. 50,000
4. Income from a business in India received in Pakistan Rs. 30,000.
5. Salary received in India for service rendered in USA Rs. 70,000.
6. Interest on deposits with SBI in Mysore Rs. 20,000.
7. Profit from business in Singapore controlled from India (1/3rd Received in India) Rs. 30,000.
8. The past untaxed foreign income brought into India Rs. 8,000.
9. Dividend received from a domestic company Rs. 5,000.
10. Agricultural income earned in Nepal Rs. 25,000
11. The commission received in India for service given in Japan Rs. 10,000.
12. Income from the profession in India but received in France Rs. 10,000.

Illustration 7

The following are the income of Mr. Vishnu for the previous year 2019-2020.

1. Received Rs. 20,000 in India, which accrued in England.
2. Rs. 10,000 earned in India but received in England.
3. Rs. 5,000 were earned and received in Africa but brought to India.
4. Rs. 10,000 were earned and received in Japan from a business that was controlled and managed in Japan.
5. Rs. 16,000 was untaxed foreign income of some earlier year, which was brought to India in the previous year.
6. Interest on fixed deposit state bank of Mysore, Bangalore Rs. 1,200.
7. Income from agriculture is Africa Rs. 10,000.

8. Dividends received in the U.K from an American Company Rs. 10,000.
9. Salary income for three months for working in the Indian Embassy's office in Australia and Salary received there Rs. 72,000.
10. Income from house property in Mumbai Rs. 1,00,000.

Compute his gross total income for the A.Y 2020-2021, if he is

- a) Ordinary resident*
- b) Not Ordinary resident*
- c) Non – resident*

Illustration 8

From the following particulars of Mr. Harish calculate total income if he is OR, NOR, and NR.

- a. Income from profession set-up in India but the amount received in Afghanistan Rs. 1,25,000.
- b. Income accrued in Bhopal but received in Uttaranchal Rs. 29,000.
- c. Income from a business in Uganda, Controlled from Trichy (25,000 received in Trichy) Rs. 50,000.
- d. Royalty received from the government of India Rs. 75,000.
- e. Past untaxed profit of 2017-18 brought into India during the current previous year Rs. 85,000.
- f. A gift in foreign currency from a friend received in India Rs. 56,000.
- g. Salary from an India company received in London Rs. 5,00,000 (Rs. 2,00,000 is paid for service rendered in India).

Illustration 10

MR. Jagan discloses the following particulars of his receipts during the financial year 2020-2021.

1. Salary income earned at Delhi but received in Paris Rs. 1,50,000.
2. Profit earned from a business in Paris which is controlled in India, half of the profits being received in India Rs. 1,20,000.
3. Income from property, situated in England, and received there Rs. 25,000
4. Income from agriculture in Nepal and Brought to India Rs. 48,000.
5. Dividend paid by an India Company but received in London on 15th May 2019 Rs. 22,000.
6. Interest in USA development Bonds and one half of which was received in India Rs. 24,000.
7. The past foreign untaxed income brought to India Rs. 40,000.
8. Capital gain from land in Delhi, consideration received in Ceylon Rs. 50,000.
9. Loss from foreign business, controlled from India, Sales being received in India Rs. (-2,00,000).

Determine his taxable income for the previous year 2019-2020. If he is OR; NOR: NR.

Income from House Property

(Section 22 to 27)

Syllabus

Basis of Charge – Deemed Owners – Exempted Incomes from House Property –Composite Rent - Annual Value – Determination of Annual Value – Treatment of Unrealized Rent – Loss due to Vacancy – Deductions from Annual Value – Problems on Income from House Property.

Section 22	Charging Section
Section 23	Annual Value
Section 24	Deductions
Section 25	Recovery of Unrealised Rent/Arrears of Rent
Section 26	Co- Ownership
Section 27	Deemed Ownership

Introduction:

In the process of making assessment, the next step is to compute taxable income under each 'head of income'. This chapter explains computation of taxable income under the second head – "Income from House Property".