LESSON 1
BASIC CONCEPTS

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STRUCTURE

1.0 INTRODUCTION

Before one can embark on a study of the law of income-tax, it is absolutely vital to understand some of the expressions found under the Income-tax Act, 1961. The purpose of this Chapter is to enable the students to comprehend basic expressions. Therefore, all such basic terms are explained and suitable illustrations are provided to define their meaning and scope.

1.1 OBJECTIVES

After going through this lesson you should be able to understand:

- Concept of assessment year and previous year
- Meaning of person and assessee
- How to charge tax on income
- What is regarded as income under the Income-tax Act
- What is gross total income
- Income-tax rates

1.2 ASSESSMENT YEAR

"Assessment year" means the period starting from April 1 and ending on March 31 of the next year.

Example- Assessment year 2006-07 which will commence on April 1, 2006, will end on March 31, 2007.

Income of previous year of an assessee is taxed during the next following assessment year at the rates prescribed by the relevant Finance Act [for tax rates, *see* Para 1.9].

Check Your Progress

Activity A: Every financial year is an assessment year. Comment.

1.3 PREVIOUS YEAR

Income earned in a 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.

Illustration 1.1 - For the assessment year 2006-07, the immediately preceding financial year (*i.e.,* 2005-06) is the previous year.

Income earned by an individual during the previous year 2005-06 is taxable in the immediately following assessment year 2006-07 at the rates applicable for the assessment year 2006-07.

Similarly, income earned during the previous year 2006-07 by a company will be taxable in the assessment year 2007-08 at the rates applicable for the assessment year 2007-08.

This rule is applicable in all cases [*see*, however, Para 1.3.1 for exception to this rule].

Check Your Progress

Activity B: Previous year is a financial year immediately preceding the assessment year. Comment.

1.3.1 WHEN INCOME OF PREVIOUS YEAR IS NOT TAXABLE IN THE IMMEDIATELY FOLLOWING ASSESSMENT YEAR

The rule that the income of the previous year is taxable as the income of the immediately following assessment year has certain exceptions. These are:

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; and

e. Income of a discontinued business.

In these cases, income of a previous year may be taxed as the income of the assessment year immediately proceeding the normal assessment year.

These exceptions have been incorporated in order to ensure smooth collection of income tax from the aforesaid taxpayers who may not be traceable if tax assessment procedure is postponed till the commencement of the normal assessment.

1.3.2 A FINANCIAL YEAR HAS A DOUBLE ROLE TO PLAY - IT IS A PREVIOUS YEAR AS WELL AS AN ASSESSMENT YEAR

On the basis of the aforesaid discussion, it can be said that a financial year plays a double role—it is a previous year as well as an assessment year.

1.4 PERSON

The term "person" includes:

a. an individual;

b. a Hindu undivided family;

c. a company;

d. a firm;

e. an association of persons or a body of individuals, whether incorporated or not;

f. a local authority; and

g. every artificial juridical person not falling within any of the preceding categories.

These are seven categories of persons chargeable to tax under the Act. The aforesaid definition is inclusive and not exhaustive. Therefore, any person, not falling in the above-mentioned seven categories, may still fall in the four corners of the term "person" and accordingly may be liable to tax.

Check Your Progress

Activity C: Indicate whether the following statements are true or false-

1. X is a partner of a firm. He is assessable as an "individual".

2. Y is a managing director of A Ltd; Y is assessable as an "individual".

1.5 ASSESSEE

"Assessee" means a person by whom income tax or any other sum of money is payable under the Act. It includes every person in respect of whom any proceeding under the Act has been taken for the assessment of his income or loss or the amount of refund due to him. It also includes a person who is assessable in respect of income or loss of another person or who is deemed to be an assessee, or an assessee in default under any provision of the Act.

1.6 HOW TO CHARGE TAX ON INCOME

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 [*see* Para 1.3.1].

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, 2006, fixes tax rates for the assessment year 2006-07.

4 ***Tax on person* -** Tax is charged on every person [*see* Para 1.4].

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

1.7 MEANING OF INCOME

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.

1.8 GROSS TOTAL INCOME

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.

The aggregate income under these heads is termed as "gross total income". In other words, gross total income means total income computed in accordance with the provisions of the Act before making any deduction under sections 80C to 80U.

1.9 INCOME TAX RATES

Rates for the assessment year 2006-07 are as follows—

1. For **individual, every HUF/AOP/BOI/artificial juridical person**, the tax rates are as under:

- For resident woman (who is below 65 years at any time during the previous year) –

Net income range	*Income-tax rates [*see *also Para 0.6]*	*Surcharge [*see *Note 1]*	*Education cess [*see *Note 2]*
Up to Rs. 1,35,000	*Nil*	*Nil*	*Nil*
Rs. 1,35,000 – Rs. 1,50,000	10% of (total income *minus* Rs. 1,35,000)	*Nil*	2% of income-tax
Rs. 1,50,000 – Rs. 2,50,000	Rs. 1,500 + 20% of (total income *minus* Rs. 1,50,000)	*Nil*	2% of income-tax
Rs. 2,50,000 – Rs. 10,00,000	Rs. 21,500 + 30% of (total income *minus* Rs. 2,50,000)	*Nil*	2% of income-tax
Above Rs. 10,00,000	Rs. 2,46,500 + 30% of (total income *minus* Rs. 10,00,000)	10% of income-tax	2% of income-tax and surcharge

- For resident senior citizen (who is 65 years or more at any time during the previous year) –

Net income range	*Income-tax rates*	*Surcharge [see Note 1]*	*Education cess [see Note 2]*
Up to Rs. 1,85,000	*Nil*	*Nil*	*Nil*
Rs. 1,85,000 – Rs. 2,50,000	20% of (total income *minus* Rs. 1,85,000)	*Nil*	2% of income-tax
Rs. 2,50,000 – Rs. 10,00,000	Rs. 13,000 + 30% of (total income *minus* Rs. 2,50,000)	*Nil*	2% of income-tax
Above Rs. 10,00,000	Rs. 2,38,000 + 30% of (total income *minus* Rs. 10,00,000)	10% of income-tax	2% of income-tax and surcharge

- For any other individual, every HUF/AOP/BOI/artificial juridical person –

Net income range	*Income-tax rates*	*Surcharge [see Note 1]*	*Education cess [see Note 2]*
Up to Rs. 1,00,000	*Nil*	*Nil*	*Nil*
Rs. 1, 00,000 – Rs. 1,50,000	10% of (total income *minus* Rs. 1,00,000)	*Nil*	2% of income-tax
Rs. 1, 50,000 – Rs. 2,50,000	Rs. 5,000 + 20% of (total income *minus* Rs. 1,50,000)	*Nil*	2% of income-tax
Rs. 2, 50,000 – Rs. 10,00,000	Rs. 25,000 + 30% of (total income *minus* Rs. 2,50,000)	*Nil*	2% of income-tax
Above Rs. 10,00,000	Rs. 2,50,000 + 30% of (total income *minus* Rs. 10,00,000)	10% of income-tax	2% of income-tax and surcharge

Notes:

1. Surcharge for the assessment year 2006-07 - Surcharge is 10 per cent of income-tax if net income of an individual, Hindu undivided family, association of persons, or body of individuals, exceeds Rs. 10, 00,000. In the case of artificial juridical person, the surcharge is 10 percent of income-tax.

2. Education cess for the assessment year 2006-07 - It is 2 per cent of income-tax and surcharge.

2. *Firms* - A firm is taxable at the rate of 30 per cent for the assessment year 2006-07.

Surcharge for the assessment year 2006-07: 10 per cent of income-tax for the assessment year 2006-07.

Education cess for the assessment year 2006-07 - It is 2 per cent of income-tax and surcharge.

3 Companies - For the assessment year 2006-07, the following rates of income-tax are applicable:

Company	*Rate of income-tax (per cent)*
In the case of a domestic company	30
In the case of a foreign company	40

Surcharge - Surcharge is applicable at the rates given below-

	Assessment year 2006-07
Domestic company	10%
Non-domestic company	2.5%

Education cess - It is 2 per cent of income-tax and surcharge for the assessment year 2006-07.

Activity D: Find out the tax liability in the following cases:

1. Mrs. X (age: 66 years) for the assessment year 2006-07 if her income is Rs. 11, 20,000.

2. X (age: 28 years) for the assessment year 2006-07 if his income is Rs. 5, 56,000.

3. Y (date of birth: April 2, 1940) for the assessment year 2006-07 is his income is Rs. 8, 86,000.

4. Z (date of birth: January 31, 1952) for the assessment year 2006-07 if his income is Rs. 15, 10,000.

1.10 LET US SUM UP

The lesson discusses in detail the meaning of various terms relevant for the purpose of studying income-tax in India. These terms are: assessment year, previous, person, assessee and income. In addition, the income-tax rates for the various categories of assess as are applicable to the assessment year 2006-07 is also enlisted in a tabular manner.

1.11 GLOSSARY

Financial year: Period of 12 months beginning on April 1 every year and ending on immediately following March 31.
Finance Act: The finance bill is commonly referred to as budget and is presented generally on the last day of February every year. The finance bill when signed by the President becomes the Finance Act.

1.12 SELF ASSESSMENT EXERCISES

1. Income of a previous year is chargeable tax in the immediately following assessment year. Is there any exception to this rule? Discuss.
2. Define the term "person".
3. How would you calculate income-tax for the assessment year 2006-07 in the case of different assesses?
4. Explain how surcharge on income-tax and education cess to applicable for the assessment year 2006-07?
5. X starts his business on April 26, 2005. Determine the previous year to the assessment year 2006-07?
6. Every financial year is a previous year as well as an assessment year. Discuss.

1.13 FURTHER READINGS AND SOURCES

Income-tax Act, 1961, Taxmann Publications Pvt. Ltd., New Delhi (latest edition).

Singhania, Vinod. K. and Monica Singhania, *Students Guide to Income-tax,* Taxmann Publications Pvt. Ltd., New Delhi (latest edition).