

Clubbing Of Income under the Income Tax Act, 1961 (Section 60 to Section 64)

Introduction – Generally an assessee is taxed in respect of his own income. But sometimes in some exceptional circumstances this basic principle is deviated and the assessee may be taxed in respect of income which legally belongs to somebody else. Earlier the taxpayers made an attempt to reduce their tax liability by transferring their assets in favour of their family members or by arranging their sources of income in such a way that tax incidence falls on others, whereas benefits of income is derived by them. So to counteract such practices of tax avoidance, necessary provisions have been incorporated in sections 60 to 64 of the Income Tax Act. Hence, a person is liable to pay tax on his own income as well as income belonging to others on fulfillment of certain conditions.

Inclusion of others' incomes in the income of the assessee is called Clubbing of Income and the income which is so included is called Deemed Income. It is as per the provisions contained in Sections 60 to 64 of the Income Tax Act.

Main concern for clubbing:-

- Circumstances when income of some other person is included in the income of Assessee
- Provisions when these sections will be applicable
- Under what head and in whose income it will be included.

Cases of Clubbing

Under the following circumstances, the income of other person is included in the income of the assessee. We will be discussing each one of them in the pages to follow.

A. Transfer of Income without Transfer of Asset (Sec. 60)

Section 60 is applicable if the following conditions are satisfied:

- The taxpayer owns an asset
- The ownership of asset is not transferred by him.
- The income from the asset is transferred to any person under a settlement, or agreement.

If the above conditions are satisfied, the income from the asset would be taxable in the hands of the transferor.

Example: Mr. A owns Debentures worth Rs 2,000,000 of ABC Ltd., (annual) interest being Rs. 200,000. On April 1, 2012, he transfers interest income to Mr. S., his friend without transferring the ownership of these debentures. Although during 2012-13, interest of Rs. 100,000 is received by Mr. S, it is taxable in the hands of Mr. A as per Section 60.

B. Revocable Transfer of Assets (Sec 61)

If the following conditions are satisfied section 61 will become applicable.

- An asset is transferred under a “revocable transfer”,
- The transfer for this purpose includes any settlement, or agreement

Then any income from such an asset is taxable in the hands of the transferor and not the transferee (owner).

Note:-In the case of irrevocable transfer of asset, the income from such assets will be deemed to be the income of the transferee (To whom the asset has been transferred), provided that the transfer is not for the benefit of the spouse of the transferor.

‘Revocable transfer, means the transferor of asset assumes a right to re-acquire asset or income from such an asset, either whole or in parts at any time in future, during the lifetime of transferee. It also includes a transfer which gives a right to re-assume power of the income from asset or asset during the lifetime of transferee.

C. Income of Spouse

The following incomes of the spouse of an individual shall be included in the total income of the individual:

(i) Remuneration from A Concern In Which Spouse Has Substantial Interest [Sec 64 (1) (ii)]

Concern - Concern could be any form of business or professional concern. It could be a sole proprietor, partnership, company, etc.

Substantial interest – An individual is deemed to have substantial interest, if he /she (individually or along with his relatives) beneficially holds equity shares carrying not less than 20 per cent voting power in the case of a company or is entitled to not less than 20 percent of the profits in the case of a concern other than a company at any time during the previous year.

If the following conditions are fulfilled this section becomes applicable.

- If spouse of an individual gets any salary, commission, fees etc. (remuneration) from a concern
- The individual has a substantial interest in such a concern
- The remuneration paid to the spouse is not due to technical or professional knowledge of the spouse.

Then such salary, commission, fees, etc. shall be considered as income of the individual and not of the spouse.

Example: - X has a substantial interest in A Ltd. and Mrs. X is employed by A Ltd. without any technical or professional qualification to justify the remuneration. In this case, salary income of Mrs. X shall be taxable in the hands of X.

When both husband and wife have substantial interest

Where both the husband and wife have a substantial interest in a concern and both are in receipt of the remuneration from such concern both the remunerations will be included in the total income of husband or wife whose total income, excluding such remuneration, is greater.

(ii) Income From Assets Transferred To Spouse [SEC. 64(1) (iv)]

Income from assets transferred to spouse becomes taxable under provisions of section 64 (1) (iv) as per following conditions:-

- The taxpayer is an individual
- He/she has transferred an asset (other than a house property) The asset is transferred to his/her spouse
- The asset is transferred without adequate consideration. Moreover there is no agreement to live apart.

If the above conditions are satisfied, any income from such asset shall be deemed to be the income of the taxpayer who has transferred the asset.

Example – X transfers 700 debentures to his wife without adequate consideration. Interest income on these debentures will be included in the income of X.

When Section 64(i) (iv) is not applicable

On this basis of the aforesaid discussion and judicial pronouncements, section 64 is not applicable in the following cases:

- If assets are transferred before marriage.
- If assets are transferred for adequate consideration.
- If assets are transferred in connection with an agreement to live apart.
- If on the date of accrual of income, transferee is not spouse of the transferor.
- If property is acquired by the spouse out of pin money (i.e. an allowance given to the wife by her husband for her dress and usual household expenses).

In the aforesaid five cases, income arising from the transferred asset cannot be clubbed in the hands of the transferor.

D. Income From Assets Transferred To Son's Wife [SEC. 64 (1) (VI)]

Income from assets transferred to son,s wife attract the provisions of section 64 (1) (vi) as per conditions below:-

- The taxpayer is an individual.
- He/she has transferred an asset after May 31, 1973. The asset is transferred to son's wife.
- The asset is transferred without adequate consideration.

In the case of such individuals, the income from the asset is included in the income of the taxpayer who has transferred the asset.

E. Income from Assets Transferred To A Person For The Benefit Of Spouse [SEC. 64(1) (VII)]

Income from assets transferred to a person for the benefit of spouse attract the provisions of section 64 (1) (vii) on clubbing of income. If:

- The taxpayer is an individual.
- He/she has transferred an asset to a person or an association of persons. Asset is transferred for the benefit of spouse.
- The transfer of asset is without adequate consideration.

In case of such individuals income from such an asset is taxable in the hands of the taxpayer who has transferred the asset.

F. Income from Assets Transferred To A Person For The Benefit Of Son's Wife [Sec. 64 (1) (VIII)]

Income from assets transferred to a person for the benefit of son's wife attract the provisions of section 64 (1) (vii) on clubbing of income. If,

- The taxpayer is an individual.
- He/she has transferred an asset after May 31, 1973.
- The asset is transferred to any person or an association of persons. The asset is transferred for the benefit of son's wife.
- The asset is transferred without adequate consideration.

In case of such individual, the income from the asset is included in the income of the person who has transferred the asset.

G. Income of Minor Child (SEC. 64 (1A))

All income which arises or accrues to the minor child shall be clubbed in the income of his parent (Sec. 64(1A), whose total income (excluding Minor's income) is greater. However, in case parents are separated, the income of minor will be included in the income of that parent who maintains the minor child in the relevant previous year.

Exemption to parent [Sec 10(32)]

An individual shall be entitled to exemption of Rs. 1,500 per annum(p.a.) in respect of each minor child if the income of such minor as included under section 64 (1A) exceeds that amount. However if the income of any minor child is less than Rs. 1,500 p.a. the aforesaid exemption shall be restricted to the income so included in the total income of the individual.

When Section 64(1A) is not applicable

In case of income of minor child from following sources, the income of minor child is not clubbed with the income of his parent.

- Income of minor child on account of any manual work.
- Income of minor child on account of any activity involving application of his skill, talent or specialized knowledge and experience.
- Income of minor child (from all sources) suffering from any disability of the nature specified in sec 80U.

Other Points for Clubbing

Can negative income be clubbed?

- If clubbing provisions are applicable and income from such a source is negative it will still be clubbed in the income of assessee.

Head of income under which an income belonging to somebody else would be clubbed?

- The other person's income is taxable under the head under which it would have been taxable if it is the income of the assessee himself.

For example Mr. X gifts Mrs. X Rs 1 lakhs from which she starts a business. Now as per clubbing provisions whatever is the profit from this business it will be taxable in the hands of Mr. X. Since it is an income taxable under the head 'Profits & gains of Business & profession, that is why it will be taxable under the same head and income will be calculated as if it is the business of Mr. X.