

STUDY NOTE-16

WEALTH TAX

This Study Note includes

- Introduction
- Valuation of Assets
- Other Issues relating to Wealth Tax

16.1 Introduction

Wealth tax is not a very important or high revenue tax in view of various exemptions. Wealth tax is a socialistic tax. It is not on income but payable only because a person is wealthy.

Wealth tax is payable on net wealth on 'valuation date'. As per Section 2(q), valuation date is 31st March every year. It is payable by every individual, HUF and company. Tax rate is 1% on amount by which 'net wealth' exceeds Rs 15 lakhs. No surcharge or education cess is payable.

No wealth-tax is chargeable in respect of net wealth of any company registered under section 25 of the Companies Act, 1956; any co-operative society; any social club; any political party; and a Mutual fund specified under section 10(23D) of the Income-tax Act [section 45]

Net wealth = Value of assets [as defined in section 2(ea)] plus deemed assets (as defined in section 4) less exempted assets (as defined in section 5), less debt owed [as defined in section 2(m)].

Debt should have been incurred in relation to the assets which are included in net wealth of assessee. Only debt owed on date of valuation is deductible.

In case of residents of India, assets outside India (less corresponding debts) are also liable to wealth tax. In case of non-residents and foreign national, only assets located in India including deemed assets less corresponding debts are liable to wealth tax [section 6].

Net wealth in excess of Rs. 15,00,000 is chargeable to wealth-tax @ 1 per cent (on surcharge and education cess).

Assessment year - Assessment year means a period of 12 months commencing from the first day of April every year falling immediately after the valuation date [Section 2(d)].

16.1.1 Assets

Assets are defined in Section 2(ea) as follows.

Guest house, residential house or commercial building - The following are treated as “assets” - (a) Any building or land appurtenant thereto whether used for commercial or residential purposes or for the purpose of guest house (b) A farm house situated within 25 kilometers from the local limits of any municipality (whether known as a municipality, municipal corporation, or by any other name) or a cantonment board [Section 2(ea)(i)]

A residential house is not asset, if it is meant exclusively for residential purposes of employee who is in whole-time employment and the gross annual salary of such employee, officer or director is less than Rs. 5,00,000.

Any house (may be residential house or used for commercial purposes) which forms part of stock-in-trade of the assessee is not treated as “asset”.

Any house which the assessee may occupy for the purposes of any business or profession carried on by him is not treated as “asset”.

A residential property which is let out for a minimum period of 300 days in the previous year is not treated as an “asset”.

Any property in the nature of commercial establishments or complex is not treated as an “asset”.

Motor cars - Motor car is an “asset”, but not the following - (a) motor cars used by the assessee in the business of running them on hire (b) motor cars treated as stock-in-trade [Section 2(ea)(ii)]. In the case of a leasing company, motor car is an asset.

Jewellery, bullion, utensils of gold, silver, etc. [Section 2(ea)(iii)] - Jewellery, bullion, furniture, utensils and any other article made wholly or partly of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals are treated as “assets” [Section 2(ea)(ii)]

For this purpose, “jewellery” includes ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals, and also precious or semi-precious stones, whether or not set in any furniture, utensils or other article or worked or sewn into any wearing apparel.

Where any of the above assets (*i.e.*, jewellery, bullion, utensils of gold, etc.) is used by an assessee as stock-in-trade, then such asset is not treated as “assets” under section 2(ea)(iii).

Yachts, boats and aircrafts - Yachts, boats and aircrafts (other than those used by the assessee for commercial purposes) are treated as “assets” [Section 2(ea)(iv)]

Urban land - Urban land is an “asset” [Section 2(ea)(v)]

Urban land means land situated in the area which is comprised within the jurisdiction of a

municipality and which has a population of not less than 10,000 according to the last preceding census.

Land occupied by any building which has been constructed with the approval of the appropriate authority is not 'asset'.

Any unused land held by the assessee for industrial purposes for a period of 2 years from the date of its acquisition by him is not an asset. Any land held by the assessee as stock-in-trade for a period of 10 years from the date of its acquisition by him is also not an asset.

Cash in hand - In case of individual and HUF, cash in hand on the last moment of the valuation date in excess of Rs. 50,000 is an 'asset'. In case of companies, any amount not recorded in books of account is 'asset' [Section 2(ea)(vi)]

16.1.2 Deemed assets

Often, a person transfers his assets in name of others to reduce his liability of wealth tax. To stop such tax avoidance, provision of 'deemed asset' has been made. In computing the net wealth of an assessee, the following assets will be included as deemed assets u/s 4.

Assets transferred by one spouse to another - The asset is transferred by an individual after March 31, 1956 to his or her spouse, directly or indirectly, without adequate consideration or not in connection with an agreement to live apart will be 'deemed asset' [Section 4(1)(a)(i)]

If an asset is transferred by an individual to his/her spouse, under an agreement to live apart, the provisions of section 4(1)(a)(i) are not applicable. The expression "to live apart" is of wider connotation and even the voluntary agreements to live apart will fall within the exceptions of this sub-clause.

Assets held by minor child - In computing the net wealth of an individual, there shall be included the value of assets which on the valuation date are held by a minor child (including step child/ adopted child but not being a married daughter) of such individual [Section 4(1)(a)(ii)]

The net wealth of minor child will be included in the net wealth of that parent whose net wealth [excluding the assets of minor child so includible under section 4(1)] is greater.

Assets transferred to a person or an association of persons - An asset transferred by an individual after March 31, 1956 to a person or an association of person, directly or indirectly, for the benefit of the transferor, his or her spouse, otherwise than for adequate consideration, is 'deemed asset' of transferor [Section 4(1)(a)(iii)]

Assets transferred under revocable transfers - The asset is transferred by an individual to a person or an association of person after March 31, 1956, under a revocable transfer is 'deemed asset' of transferor [Section 4(1)(a)(iv)]

Assets transferred to son's wife [Section 4(1)(a)(v)] - The asset transferred by an individual after May 31, 1973, to son's wife, directly or indirectly, without adequate consideration will be 'deemed asset' of transferor [Section 4(1)(a)(iv)]

Assets transferred for the benefit of son's wife - If the asset is transferred by an individual after May 31, 1973, to a person or an association of the immediate or deferred benefit of son's wife, whether directly or indirectly, without adequate consideration, it will be treated as 'deemed asset' of the transferor [Section 4(1)(a)(vi)].

Interest of partner- Where the assessee (may or may not be an individual) is a partner in a firm or a member of an association of persons, the value of his interest in the assets of the firm or an association shall be included in the net wealth of the partner / member. For this purpose, interest of partner / member in the firm or association of persons should be determined in the manner laid down in Schedule III to the Wealth-tax Act [Section 4(1)(b)].

Admission of minor to benefits of the partnership firm - If a minor is admitted to the benefits of partnership in a firm, the value of his interest in the firm shall be included in the net wealth of parent of minor in accordance with the provisions of section 4(1)(a)(ii) [see para 546.2]. It will be determined in the manner specified in Schedule III.

Conversion by an individual of his self-acquired property into joint family property - If an individual is a member of a Hindu undivided family and he converts his separate property into property belonging to his Hindu undivided family, or if he transfers his separate property to his Hindu undivided family, directly or indirectly, without adequate consideration, the converted or transferred property shall be deemed to be the property of the individual and the value of such property is includible in his net wealth [Section 4(1A)]

If there was such transfer and if the converted or transferred property becomes the subject-matter of a total or a partial partition among the members of the family, the converted or transferred property or any part thereof, which is received by the spouse of the transferor, is deemed to be the asset of the transferor and is includible in his net wealth.

Gifts by book entries - Where a gift of money from one person to another is made by means of entries in the books of account maintained by the person making the gift, or by an individual, or a Hindu undivided family, or a firm or an association of persons, or a body of individuals with whom he has business connection, the value of such gift will be included in the net wealth of the person making the gifts, unless he proves to the satisfaction of the Wealth-tax Officer that the money had actually been delivered to the other person at the time the entries were made [Section 4(5A)]

Impartible estate - For the purpose of the Wealth-tax Act, the holder of an impartible estate shall be deemed to be the owner of all the properties comprised in the estate [Section 4(6)]

Property held by a member of a housing society - Where the assessee is a member of a co-operative housing society and a building or part thereof is allotted or leased to him, the assessee is deemed to be the owner of such building and the value of such building is includible in computing his net wealth. In determining the value of such building, any outstanding instalments, payable by the assessee to the society towards the costs of such house, are deductible as debt owed by the assessee. The above rules are also applicable if the assessee is a member of a company or an association of persons [Section 4(7)]



Property held by a person in part performance of a contract [Section 4(8)] - A person who is allowed to take or retain possession of any building or part thereof in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882. Similarly, a person can acquire any rights, excluding any rights by way of a lease from month to month or for a period not exceeding one year, in or with respect to any building or part thereof, by virtue of transaction as is referred to in section 269UA(f) of the Income-tax Act.

In above cases, the assets are taxable in the hands of beneficial owners, in the same manner in which they are taxed under the Income-tax Act :

16.1.3 Assets which are exempt from tax

The following assets are exempt from wealth-tax, as per section 5.

Property held under a trust - Any property held by an assessee under a trust or other legal obligation for any public purpose of charitable or religious nature in India is totally exempt from tax. [Section 5(i)].

Business assets held in trust, which are exempt - The following business assets held by an assessee under a trust for any public charitable / religious trust are exempt from tax - (a) where the business is carried on by a trust wholly for public religious purposes and the business consists of printing and publication of books or publication of books or the business is of a kind notified by the Central Government in this behalf in the Official Gazette (b) the business is carried on by an institution wholly for charitable purposes and the work in connection with the business is mainly carried on by the beneficiaries of the institution (c) the business is carried on by an institution, fund or trust specified in sections 10(23B) or 20(23C) of the Income-tax Act.

Any other business assets of a public charitable / religious trust is not exempt.

Coparcenary interest in a Hindu undivided family - If the assessee is a member of a Hindu undivided family, his interest in the family property is totally exempt from tax [Section 5(ii)].

Residential building of a former ruler - The value of any one building used for the residence by a former ruler of a princely State is totally exempt from tax [Section 5(iii)]

Former ruler's jewellery - Jewellery in possession of a former ruler of a princely State, not being his personal property which has been recognised as a heirloom is totally exempt from tax [Section 5(iv)]

The jewellery shall be permanently kept in India and shall not be removed outside India except for a purpose and period approved by the Board. Reasonable steps shall be taken for keeping that jewellery substantially in its original shape. Reasonable facilities shall be allowed to any officer of the Government, or authorised by the Board, to examine the jewellery as and when necessary.

Assets belonging to the Indian repatriates - Assets (as given below) belonging to assessee who is a person of Indian origin or a citizen of India, who was ordinarily residing in a foreign

country and who has returned to India with intention to permanently reside in India, is exempt. A person shall be deemed to be of Indian origin if he, or either of his parents or any of his grand-parents, was born in undivided India.

After his return to India, following shall not be chargeable to tax for seven successive assessment years - (a) moneys brought by him into India (b) value of asset brought by him into India (c) moneys standing to the credit of such person in a Non-resident (External) Account in any bank in India on the date of his return to India and (d) value of assets acquired by him out of money referred to in (a) and (c) above within one year prior to the date of his return and at any time thereafter [Section 5(v)]

One house or part of a house - In the case of an individual or a Hindu undivided family, a house or a part of house, or a plot of land not exceeding 500 sq. meters in area is exempt. A house is qualified for exemption, regardless of the fact whether the house is self-occupied or let out. In case a house is owned by more than one person, exemption is available to each co-owner of the house [Section 5(vi)]

16.2 VALUATION OF ASSETS

The value of an asset, other than cash, shall be its value as on the valuation date determined in the manner laid down in Schedule III.

Valuation of a building - Value of any building or land appurtenant thereto, or part thereof, is to be made in accordance with Part B of Schedule III to the Wealth-tax Act

The first step is to find out gross maintainable rent. Gross maintainable rent is (a) annual rent received / receivable by the owner or annual value of the property as assessed by local authority, whichever is higher (if the property is let out) or (b) annual rent assessed by the local authority or if the property is situated outside the jurisdiction of a local authority, the amount which the owner can reasonably be expected to receive as annual rent had such property been let (if the property is not let).

In the following cases “actual rent” shall be increased in the manner specified below : (a) Taxes borne by tenant (b) If property is rented, one-ninth of actual rent will be added, if expenditure on repairs in respect of the property is borne by the tenant (c) Interest @ 15% on deposit given by tenant or difference (d) Premium received as consideration for leasing of the property or any modification of the terms of the lease will be divided over the number of years of the period of the lease and will be added to ‘actual rent’ (d) If the derives any benefit or perquisite as consideration for leasing of the property or any modification of the terms of the lease), the value of such benefit or perquisite shall be added to actual rent.

Net maintainable rent is determined by deducting from the gross maintainable rent (a) the amount of taxes levied by any local authority in respect of property (deduction is available even if these are to be borne by the tenant) ; and (b) A sum equal to 15% of gross maintainable rent.



The net maintainable rent is finally capitalized to arrive as value of net asset.. This can be done by multiplying the net maintainable rent by 12.5. If the property is constructed on leasehold land, net maintainable rent is to be multiplied by 10 when the unexpired period of lease of such land is 50 years or more and multiplied by 8 where the unexpired period of lease of such land is less than 50 years).

If a property is acquired / constructed after March 31, 1974, then the value of the house property is determined as above. Original cost of construction / acquisition *plus* cost of improvement of the house property is calculated. The higher of the above is taken as capitalised value of net maintainable rent. This exception is applicable in respect one house property. The cost of acquisition / construction (*plus* cost of improvement) does not exceed Rs. 50 lakh, if the house is situated at Bombay, Calcutta, Delhi and Madras (Rs. 25 lakh at any other place).

If unbuilt area of the plot of land on which the property is built exceeds the specified area, premium is to be added to the capitalised value determined above.

Valuation of self-occupied property - If assessee owns a house (or a part of the house), being an independent residential unit and is used by the assessee exclusively for his residential purposes throughout 12 months ending on the valuation date, valuation will be as per provisions of section 7(2).

Assessee can either take value of the house as determined above on the valuation date relevant for the current assessment year or he take value of the house, as determined above, on the first valuation date next following the date on which he became the owner or the valuation relevant for the assessment year 1971-72, whichever is later. The choice is of the assessee.

Where the house has been constructed by the assessee, he shall be deemed to have become the owner thereof on the date on which the construction of such house was completed.

Valuation of assets of business - If the assessee is carrying on a business for which accounts are maintained by him regularly, the net value of the assets of the business as a whole, having regard to the balance sheet of such business on the valuation date, is taken as value of such assets [Part D, Schedule III].

- (A) The assets are valued as follows - **Depreciable assets** - Written down value, plus 20%, **Non-depreciable assets (other than stock-in-trade)** - Book value, plus 20%, **Closing stock** - Value adopted for the purpose of income-tax, plus 20%.
- (B) Then value of house property, life interest, jewellery and other assets is calculated as per other provisions of Wealth Tax Act.

Higher of A or B is taken as value of assets.

Value of interest in firm or association of persons - The net wealth of the firm on the valuation date is ascertained.. For determining the net wealth of the firm (or association), no account shall be taken of the exemptions given by section 5. The portion of the net wealth as is equal to the amount of the capital of the firm or association is allocated amongst the partners or the members in the proportion in which capital has been contributed by them.

The residue of the net wealth is allocated amongst the partners or the members in accordance with the agreement of the partnership or association of persons for the distribution of assets in the event of dissolution of the firm or association or in the absence of such agreement, in the proportion in which the partners (or members) are entitled to share profits [Part E, Schedule III]

Value of life interest - The value of life interest of an assessee shall be determined as per Part F, Schedule III. Average net annual income of the assessee derived from the life interest during 3 years ending on the valuation date is calculated. While computing net annual income, expenses incurred on the collection of such income (maximum of 5% of the average of annual gross income) shall be deducted. This is multiplied as per formula prescribed to arrive at value of asset.

Valuation of jewellery - The value of jewellery shall be estimated to be the price which it would fetch if sold in the open market on the valuation date (*i.e.*, fair market value). Where the value of jewellery does not exceed Rs. 5,00,000, a statement in Form No. O-8A is to be submitted. Where the value of the jewellery exceeds Rs. 5,00,000, a report of a registered valuer in Form No. O-8 should be submitted. The report is not binding on assessing officer (Valuation Officer) and he can determine fair market value of jewellery.

The value of jewellery determined by the Valuation Officer for any assessment year shall be taken to be the value of such jewellery for the subsequent four assessment years subject to the prescribed adjustments.

Valuation of any other asset - The value of any asset, other than cash (being an asset which is not covered in above paras) shall be estimated either by the Assessing Officer himself or by the Valuation Officer if reference is made to him under section 16A. In both these cases, the value shall be estimated to be the price which it would fetch if sold in the open market, on the valuation date. If the asset is not saleable in the open market, the value shall be determined in accordance with guidelines or principles specified by the Board from time to time by general or special order.

16.3 OTHER ISSUES RELATING TO WEALTH TAX

Charitable or religious trusts - A trust can forfeit exemption for any of the following reasons - (a) any part of the trust's property or any income of the trust, including income by way of voluntary contributions, is used for the benefit of the settlor, the trustee, their relatives etc.; or (b) any part of the income of the trust, created on or after April 1, 1962, including income by way of voluntary contributions, enures directly or indirectly, for the benefit of any of the persons referred to in section 13(3) of the Income-tax Act ; or (c) any funds of the trust are invested or deposited or any shares in a company are held by the trust in contravention of the investment pattern for trust funds laid down in section 11(5) of the Income-tax Act.

In such case, tax shall be leviable upon and recoverable from the trustee or manager in respect of the property held by him under trust at the rate of tax applicable to a resident in India.



These provisions are not applicable in the case of a scientific research association [Section 10(21) of the Income-tax Act] and in the case of any institution, fund or trust referred to in section 10(22), (22A), (22B) or (23C) of the Income-tax Act in specified situations [Section 21A]

Association of persons where shares of members are indeterminate/unknown - If assets chargeable to wealth-tax are held by an association of persons and the individual shares of the members in the income or assets of the association are indeterminate or unknown, wealth-tax is levied to the same extent as it would be leviable upon and recoverable from an individual who is citizen of India and resident in India [Section 21AA]

16.3.1 Return of wealth and assessment

Every person is required to file with the Wealth-tax Officer a return of net wealth in Form BA, if his net wealth or net wealth of any other person in respect of which he is assessable under the Act on the valuation date is of such an amount as to render him liable to wealth-tax. Return can be filed on or before the “due date” specified under section 139 of the Income-tax Act.

Return in response to a notice - In the case of any person who, in the opinion of Wealth-tax Officer, is assessable to tax, the Wealth-tax Officer may, before the end of the relevant assessment year, issue a notice requiring him to furnish, within 30 days from the date of service of such notice, a return of net wealth in the prescribed form.

Assessment - The assessee is required to pay the tax before filing of the return and such return is to be accompanied by the proof of such payment. Provisions of regular assessment, as applicable under Income Tax, will apply to wealth tax also.

Interest or penalty and prosecution - Interest @ 1% per month is payable for failure to pay wealth tax on due date. Penalty and prosecution provisions also apply.

QUESTION

Mr. A has the following assets on 31-3-2008:

Asset	Market value on 31-3-2008 Rs. lakhs	Loan outstanding On 31-3-2008 Rs. Lakhs (loans taken acquire the asset)	Security Given for Taking the Loan
Gold and silver	80	6	Shares
Shares	10	3	House B
Residential House A	50	4	Gold
Residential House B	42	38	Personal
Commercial House C(used for Carrying on own business)	95	5	Personal
Boat	8	12	Gold
Motor cars	11	1	Silver
Bank deposit	1	1	-----
Residential House D(let out throughout The financial year 2007-08)	55	40	House D
Commercial complex (having 20 offices)	190	100	Commercial Complex

A also took a bank loan of Rs. 75,000 against the security of his car for his friend's marriage. Out of the Rs. 12 lakh loan taken by him for purchasing the boat, he utilized Rs. 1 Lakh for his foreign visit. Compute the net wealth for assessment year 2008-09

Answer

	Assets (Rs. Lakh)	Debts owed Rs. Lakhs
	80	6
Shares- not an “asset” within the meaning of section 2(ea)	----	----
Residential House A[exempt under Section 5(vi)]		----
Residential House B	Gold and silver	38
Commercial House C(used for Carrying on own business- Therefore it is not an “asset” within the meaning of section 2(ea))	----	----
Boat	8	11
Motor cars	11	1
Bank deposit[not an asset within the meaning of section 2(ea)]	----	---
Residential House D(let out throughout the financial year 2005- 06) –Residential house not an “asset” if let out for 300 days or more in the previous year.	----	---
Commercial complex (having 20 offices) not an “asset” within the meaning of section 2(ea)	----	----
Total	141	56

Net wealth = Rs 141 lakhs *minus* Rs 56 Lakhs = Rs. 85 lakhs

Mr. A owns a commercial house property which is situated at Pune. The difference between unbuilt area and specified area is 22% of the aggregate area. The property was acquired on 31-5-1988 for Rs. 12,50,000. The property is built on freehold land. How will the property be valued for wealth-tax purposes?

As the difference between unbuilt area and specified area exceeds 20% of the aggregate area, value shall be estimated by the Assessing Officer himself or by the Valuation Officer under section 16A if the reference is made to him under section 16A. In either case, the value shall be estimated to be the price which it would fetch if sold in the open market, on the valuation date. If the property is not saleable in the open market, valuation shall be as per CBDT's guidelines specified from time to time.