

INCOME FROM OTHER SOURCES

Some Key Points : Recent Amendments

Transfer of property without consideration [Section 56(2)(vii)(b)]

Any immovable property received by an individual or HUF on or after 01.10.2009 **without any consideration** it is chargeable to tax as income under the head 'other sources' if the stamp duty value of such property exceeds Rs.50,000.

Transfer of immovable property for inadequate consideration is not liable to tax in the hands of the transferee (which was the case as per the amendment made by the Finance (No.2) Act, 2009, which was subsequently reversed in the Finance Act, 2010 on retrospective basis).

Meaning of the term 'property'

The Finance Act, 2010 has amended clause (d) of the Explanation to section 56(2)(vii) dealing with the term 'property'.

"Property" means the following **capital asset of the assessee** namely:–

- (a) Immovable property being land or building or both;
- (b) Shares and securities;
- (c) Jewellery
- (d) Archaeological collections;
- (e) Drawings
- (f) Paintings;
- (g) Sculptures;
- (h) Any work of art; or
- (i) Bullion

Transfer of shares to firm and company liable to tax [Section 56(2)(viiia)]

Where a firm or company (not being a company in which public are substantially interested) receives, in any previous year, from any person or persons, on or after 01.06.2010, any property, being shares of the company not being a company in which public are substantially interested –

- (a) **Without consideration**, the aggregate fair market value of which exceeds Rs.50,000, the whole of the aggregate fair market value is taxable;
- (b) **For a consideration**, which is less than the aggregate fair market value by an amount exceeding Rs.50,000, the aggregate fair market value of such property as exceeds the consideration.

Direct Tax Laws

Exception : The abovesaid provisions for shares received without consideration or for inadequate consideration will not apply in respect of any transactions covered by section 47(via) or section 47(vic) or section 47(vicb) or section 47(vid) or section 47(vii).

Question 1

Mr. Ganesh received the following gifts during the P.Y.2010-11 from his friend Mr. Sundar, -

- (1) Cash gift of Rs.51,000 on his birthday, 19th June, 2010.
- (2) 50 shares of Beta Ltd., the fair market value of which was Rs.60,000, on his birthday, 19th June, 2010.
- (3) 100 shares of Alpha Ltd., the fair market value of which was Rs.70,000 on the date of transfer. This gift was received on the occasion of Diwali. Mr. Sundar had originally purchased the shares on 10-8-2010 at a cost of Rs.50,000.

Further, on 20th November, 2010, Mr. Ganesh purchased land from his sister's mother-in-law for Rs.5,00,000. The stamp value of land was Rs.7,00,000.

On 15th February, 2011, he sold the 100 shares of Alpha Ltd. for Rs.1 lakh.

Compute the income of Mr. Ganesh chargeable under the head "Income from other sources" and "Capital Gains" for A.Y.2011-12.

Answer

Computation of "Income from other sources" of Mr.Ganesh for the A.Y.2011-12

Particulars	Rs.
(1) Cash gift received on 19.06.2010 is taxable under section 56(2)(vii)	51,000
(2) Value of shares of Beta Ltd. gifted by Mr.Sundar on 19 th June, 2010 is taxable	60,000
(3) Fair market value of shares of Alpha Ltd. is taxable	70,000
(4) Purchase of land for inadequate consideration on 20.11.2010 would not attract the provisions of section 56(2)(vii), since there is consideration and only where the consideration is fully absent, it is chargeable to tax.	Nil

Income from Other Sources 1,81,000

Computation of "Capital Gains" of Mr. Ganesh for the A.Y.2011-12

Sale Consideration (15.02.2011)	1,00,000
Less: Cost of acquisition [deemed to be the fair market value charged to tax under section 56(2)(vii)]	70,000
Short-term capital gains	30,000

Question 2

Mrs. Harini Rao, who draws a salary of Rs.12,000 p.m. received the following gifts during the previous year 2010-11 -

- (i) *Gift of Rs.1,50,000 on 15-5-2010 from her close friend.*
- (ii) *Gift of jewellery worth Rs.3,00,000 on 1-8-2010 from her fiancée.*
- (iii) *Gifts of Rs.51,000 each received from her two friends on the occasion of her marriage on 30-10-2010.*
- (iv) *Gift of Rs.51,000 on 1-11-2010 from her father's sister.*
- (v) *Gift of Rs.21,000 from her husband's friend on 1-1-2011.*
- (vi) *Gift of Rs.25,000 on 12-1-2011 from her family friend.*
- (vii) *Gift of Rs.11,000 on 12-2-2011 from her brother's mother-in-law.*
- (viii) *Gift of Rs.75,000 from her sister-in-law.*

Compute her gross total income for the assessment year 2011-12.

Answer

Computation of gross total income of Mrs. Harini Rao for the A.Y.2011-12

Particulars	Rs.	Rs.
Salary		
Salary 12,000 x 12		1,44,000
Income from other sources		
(i) Gift from close friend is taxable	1,50,000	
(ii) Gift of jewellery is exempt as it is in kind	3,00,000	
(iii) Gifts received from her two friends are exempt as they have been received on the occasion of her marriage	-	
(iv) Gift from her father's sister is exempt as the donor is covered in the definition of 'relative'	-	
(vi) Gift from her husband's friend is taxable	21,000	
(vii) Gift from her family friend is taxable	25,000	
(viii) Gift from her brother's mother-in-law is taxable as the donor is not covered in the definition of 'relative'	11,000	
(ix) Gift from her sister-in-law (husband's sister) is exempt as the donor is covered in the definition of 'relative'	-	
	5,07,000	
Gross Total Income		6,51,000

Question 3

Explain in the context of provisions of the Act, whether the income derived during the year ended on 31.03.2011 in each of the following case shall be subject to tax in the A.Y. 2011-12:

Chitra received gifts of Rs.1,00,000 from her father-in-law and of Rs.11,000 each from her 10 friends at the time of her marriage on 11.03.11.

Answer

The cash gifts received by Chitra at the time of her marriage shall not be subject to tax by virtue of clause (b) of the second proviso to section 56(2)(vii). Therefore, gifts of Rs.1 lakh received from her father-in-law and Rs.1.10 lakh received @ Rs.11,000 each from her 10 friends shall not be taxable as all such gifts were received by her on the occasion of her marriage.

Question 4

MNO Ltd. is a company in which the public are not substantially interested. K is a shareholder of the company holding 15% of the equity shares. The accumulated profits of the company as on 31.3.2010 amounted to Rs.10,00,000. The company lent Rs.1,00,000 to K by an account payee bank draft on 1.10.2010. The loan was not connected with the business of the company. K repaid the loan to the company by an account payee bank draft on 30.3.2011. Examine the effect of the borrowal and repayment of the loan by K on the computation of his total income for the assessment year 2011-12.

Answer

As per section 2(22)(e), any payment by a company, in which the public are not substantially interested, by way of advance or loan to a shareholder, being a person who is the beneficial owner of shares holding not less than 10% of the voting power, shall be treated as dividend to the extent to which the company possesses accumulated profits.

In the instant case, MNO Ltd. is a company in which the public are not substantially interested. The company has accumulated profits of Rs.10,00,000 on 31.3.2010. The loan given by the company to K was not in the course of its business. K holds more than 10% of the equity shares in the company. Therefore, assuming that K has voting power equivalent to his shareholding, section 2(22)(e) comes into play and the sum of Rs.1,00,000, representing the amount lent by the company to K, is includible as dividend in the total income of K for the assessment year 2011-12.

Under section 2(22)(e), the liability arises the moment the loan is borrowed by the shareholder and it is immaterial whether the loan is repaid before the end of the accounting year or not. Therefore, the repayment of loan by K to the company on 30.3.2011 will not affect the taxability of the sum of Rs.1,00,000 as dividend in his hands.

Question 5

Discuss the taxability or otherwise of the following gifts received by M, an individual, during the financial year 2010-11:

- (i) Rs.24,000 each from his four friends on the occasion of his birthday.

- (ii) Wrist watch valued at Rs.60,000 from his friend.
- (iii) Acquired a vacant site from a friend (non-relative). The stamp duty value of the land was Rs.5 lakhs but the consideration paid and agreed was Rs.3 lakhs.
- (iv) Received a gift of vacant land from grandfather's younger brother, the stamp duty value of the land being Rs.1,50,000

Answer

- (i) Section 56(2)(vii) provides that where any sum of money is received without consideration by an individual or a Hindu undivided family from any person or persons exceeding Rs.50,000 in aggregate in any previous year, the whole of the aggregate value of such sum will be liable to tax. In the instant case, M has received Rs.24,000 from each of his four friends. The aggregate amount of gifts received works out to Rs.96,000. As such, the entire amount of Rs.96,000 is taxable under the head "Income from other sources".
- (ii) Section 56(2)(vii) brings within its scope, in addition to any sum of money, the value of property received without consideration. For this purpose, "property" means immovable property being land and building or both, shares and securities, jewellery, archaeological collections, drawings, paintings, sculptures or any work of art. Therefore, the gift of wrist watch valued at Rs.60,000 received by M from his friend is not covered by the term 'property'. Accordingly, it is not chargeable to tax.
- (iii) The Finance Act, 2010 has substituted sub-clause (b) of section 56(2)(vii) with retrospective effect from 01.10.2009. After the amendment, where any immovable property is obtained without consideration and if the stamp duty value of the property exceeds Rs.50,000, the stamp duty value of such property is chargeable to tax as income. In this case, there was some consideration but it was less than the stamp duty value. Only in the absence of consideration, is a transaction in respect of immovable property received from a non-relative chargeable to tax. Therefore, the difference between stamp duty value and actual consideration is not chargeable to tax in the hands of the vendee.
- (iv) There is no consideration on receipt of gift of land from the younger brother of grandfather. Since the younger brother of grandfather is not a 'relative' as per Explanation to section 56(2)(vii), the stamp duty value is chargeable to tax as income under the head 'income from other sources'.

Question 6

The Assessing Officer found, during the course of assessment of a firm, that it had paid rent in respect of its business premises amounting to Rs.60,000, which was not debited in the books of account for the year ending 31.3.2010. The firm did not explain the source for payment of rent. The Assessing Officer proposes to make an addition of Rs.60,000 in the hands of the firm for the assessment year 2010-11. The firm claims that even if the addition is made, the sum of Rs.60,000 should be allowed as deduction while computing its business income since it has been expended for purposes of its business. Examine the claim of the firm.

Answer

The claim of the firm for deduction of the sum of Rs.60,000 in computing its business income is not tenable. The action of the Assessing Officer in making the addition of Rs.60,000, being the payment of rent not debited in the books of account (for which the firm failed to explain the source of payment) is correct in law since the same is an unexplained expenditure under section 69C. The proviso to section 69C states that such unexplained expenditure, which is deemed to be the income of the assessee, shall not be allowed as a deduction under any head of income. Therefore, the claim of the firm is not tenable.

Question 7

D, a lady, received the following gifts during the year ending 31.3.2011:

- (i) *Rs.30,000 from her elder sister.*
- (ii) *Rs.1,25,000 from various friends on the occasion of her marriage.*
- (iii) *Rs.50,000 from the daughter of her elder sister.*

Discuss the taxability or otherwise of these gifts in the hands of D

Answer

- (i). Section 56(2)(vii) provides for taxation of gifts exceeding Rs.50,000, received by an individual from any person other than those specified, under the head "Income from other sources". The proviso states that gifts received from any relative would not be so taxed. *Explanation* to section 56(2)(vii) defines the term "relative". Sister of the individual is included in the said definition. Therefore, gift of Rs.30,000 received by D from her elder sister is not taxable.
- (ii) The proviso to section 56(2)(vii) stipulates that gifts received by an individual on the occasion of the marriage of the individual, is not taxable. Therefore, gifts amounting to Rs.1,25,000 received by D from her friends on the occasion of her marriage are not taxable.
- (iii) Daughter of the elder sister of an individual is not a "relative" within the definition of the term as contained in *Explanation* to section 56(2)(vii). Since the amount received from the daughter of her elder sister is exactly Rs.50,000 and the gifts received in (i) and (ii) above are not chargeable, the whole of the amount gifted shall not be included in D's total income. Therefore, the entire sum of Rs.50,000 is not taxable in the hands of D.

Question 8

M, an individual, is 70 years of age. He is a sitting member of the State Assembly of Karnataka and for the financial year 2010-11 received the following amounts from the Assembly Secretariat :

- | | |
|------------------------------------|--|
| (i) <i>Basic pay</i> | <i>Rs.16,000 p.m.</i> |
| (ii) <i>Constituency allowance</i> | <i>Rs.8,000 p.m.</i> |
| (iii) <i>Telephone allowance</i> | <i>Rs.4,000 p.m.</i> |
| (iv) <i>Electricity allowance</i> | <i>Rs.3,000 p.m. [from June, 2010 onwards]</i> |

Income from Other Sources

He owns a house in Delhi which has been let out at Rs.15,000 p.m. He received rent for 10 months only, the house having remained vacant for two months. Municipal taxes of Rs.12,000 were paid by the tenant. Interest of Rs.50,000 was paid by M on the amount borrowed by him to buy the house.

Compute his total income for the assessment year 2011-12.

Answer

Computation of total income of Mr. M for A.Y.2011-12

Particulars	Rs.	Rs.
<i>Income from house property</i>		
Gross Annual Value (GAV) [See Note 1 below]	1,50,000	
Municipal taxes (not allowed since it is borne by tenant)	-	
Net annual value (NAV)	1,50,000	
Less: Deduction u/s 24		
(a) 30% of NAV	45,000	
(b) Interest on borrowed capital	50,000	
	95,000	55,000
<i>Income from Other Sources [See Note 2 below]</i>		
Basic Pay	1,92,000	
Constituency allowance (Rs.8,000 x 12)	96,000	
Electricity allowance (Rs.3,000 x 10)	30,000	
Telephone allowance (Rs.4,000 x 12)	48,000	
	1,74,000	
Less: Exempt u/s 10(17)[Rs.8000 p.m.]	96,000	78,000
Total Income		3,25,000

Note – 1. In the absence of other information, rent received has been taken as the Gross Annual Value.

2. The pay and allowances of a member of the State Assembly would be taxable under the head "Income from other sources", since there is no employer-employee relationship in this case.

Question 9

V.G. had placed to deposit of Rs.10 lakhs in a bank on which he received interest of Rs.80,000. He had also borrowed Rs.5 lakhs from the same bank on the security of the deposit and was liable to pay Rs.50,000 by way of interest to the bank. He therefore offered the difference between two amounts of Rs.30,000 as income from other sources. Is this correct?

Answer

The interest income from deposit in the bank is assessable under the head "Income from Other Sources". The deduction admissible against this income is any expenditure (not being in the nature of capital expenditure) laid out or expended wholly and exclusively for the purpose of making or earning such income. However, the interest paid on the borrowing of Rs.5 lakhs does not fall in this category. This has been held by the Supreme Court in *CIT v. Dr. V. Gopinathan (2001) 248 ITR 449*. In that case, the Supreme Court observed that the interest received by the assessee from the bank on a fixed deposit is income in his hands and there could be no deduction there from unless there is a law permitting such deduction. The interest on a loan taken by the assessee on the security of the fixed deposit would not go to reduce the income by way of interest on the fixed deposit as there is no provision for deduction of such interest on the loan.

Therefore, in this case, the full sum of Rs.80,000 will be liable to tax under the head "Income from Other Sources".

Note: In case the assessee had deposited business funds and availed loan against such deposit for business use of such loan, the interest on loan against deposit is eligible for deduction.

Question 10

Parimal, Managing Director of Heavens Engg. Pvt. Ltd. holds 70% of its paid up capital of Rs.20 lakhs. The balance as at 31-03-10 in General Reserve was Rs.6 lakhs. The company on 1-07-10 gave an interest-free loan of Rs.5 lakhs to its Supervisor having salary of Rs.4,000 p.m., who in turn on 15-8-10 advanced the said amount of loan so taken from the company to Shri Parimal. The Assessing Officer had taxed the amount of advance in the hands of Parimal. Is the action of Assessing Officer correct?

Answer

The company had advanced a loan to an employee who in turn had advanced the same to the Managing Director of the company holding 70% of its capital. By virtue of the provisions of section 2(22)(e), the same shall be treated as the payment by a company in which public are not substantially interested, on behalf of, or for individual benefit of any such share holder (who holds not less than 10% of the voting power), to the extent to which the company possesses accumulated profits.

In this case, the company has reserves of Rs.6 lakhs on 31st March of the preceding year and the amount of loan advanced on 1st July is Rs.5 lakhs. Therefore, the payment is to be treated as deemed dividend. The amount of interest-free loan of Rs.5 lakhs given by the company to the supervisor who in turn had given the same to Mr.Parimal, shall be construed as the amount given for the benefit of Mr. Parimal and is treated as deemed dividend chargeable to tax in the hands of Mr. Parimal. This has been held by the Supreme Court in the case of *L.Alagusundaram Chettiar v. CIT (2001) 252 ITR 813/(2002) 121 Taxman 587*.

Income from Other Sources

Question 11

An enterprise engaged in manufacturing of steel balls discontinued its activities and decided to lease out its factory building, plant and machinery and furniture from 1.4.2010 on a consolidated lease rent of Rs.50,000 per month. Compute the income for Assessment Year 2011-12 of the assessee from following information:

	Rs.
(i) Interest received on deposits	1,00,000
(ii) Brokerage paid on hundi loan taken	2,000
(iii) Interest paid on hundi and other loans which were given as deposits on interest to others	75,000
(iv) Expenses incurred on repairs of building, plant and machinery.	15,000
(v) Fire insurance premium of plant and machinery and furniture.	12,000
(vi) Depreciation for the year	1,47,500
(vii) Legal fees paid to an advocate for drafting and registering the lease agreement	1,500
(viii) Factory licence fees paid for the year	1,000
(ix) There is unabsorbed depreciation of Rs.2,75,000 of the Assessment Years 2005-06 and 2006-07.	
(x) Interest paid includes an amount of Rs.25,000 remitted outside India on which TDS was not deducted at source.	

Answer

The income derived from leased assets shall be chargeable to tax as 'Income from other sources' under section 56(2)(iii) of the Act but the computation thereof shall be made after allowing deductions specified under sections 30, 31 and 32 subject to section 38 of the Act. This is as per the provisions of section 57(ii) and 57(iii) of the Act.

Income from other sources

	Amount (Rs.)	Amount (Rs.)
(A) Lease Rent for 12 months @ Rs.50,000 p.m.		6,00,000
Less: Expenses and deductions allowable under section 57(ii) & 57(iii) of the Act:		
Repairs	15,000	
Fire Insurance Business	12,000	
Legal expenses for drafting of lease agreement	1,500	
Factory Licence fee	1,000	
Depreciation for the year	1,47,500	
Unabsorbed depreciation of earlier assessment years – eligible for deduction	<u>2,75,000</u>	<u>4,52,000</u>
		1,48,000

Direct Tax Laws

(B) Interest on Deposits		1,00,000	
Less: Expenses allowable U/s.57(i)			
Brokerage	2,000		
Interest on hundi loans (Note 2)	<u>50,000</u>	<u>52,000</u>	
			<u>48,000</u>
Total Income			<u>1,96,000</u>

Note:

1. Depreciation of Rs.2,75,000 pertains to earlier assessment years. The unabsorbed depreciation shall form part of the current year depreciation and can be set off against any other head of income. Accordingly, the amount of Rs 2,75,000 is adjustable / allowed to be set off against 'Income from other sources'.
2. Interest paid to non-resident is not eligible for deduction as the tax has not been deducted at source.

Question 12

Shyam was contributing amount to unrecognized provident fund. On 15th March, 2011, he had finally drawn the deposited amount along with interest. He seeks your advice as to how it has to be dealt, in his computation for assessment year 2011-12.

Answer

Shyam's own contribution to the unrecognized provident fund will not attract any tax liability on its return to him. However, any payment received from an employer or former employer from an unrecognized provident fund to the extent to which it does not consist of contribution by him or interest on such contribution will constitute profits in lieu of salary under section 17(3)(ii) and will thus be chargeable to tax on receipt.

Hence, Shyam will be advised to include in his return of income the amounts withdrawn by him from the unrecognized provident fund to the extent it constitutes the contribution by the employer and interest thereon.

Interest on own contribution to unrecognized provident fund however is taxable under the head "income from other sources".