OUTLINE: -

Why Tax Is?

What Tax Is?

How Tax Is?

Types of Tax.

What Income Is?

How to find whether Income is Taxable or Not?

Capital and Revenue Receipt.

Who is Chargeable to Tax?

Period of Which Income is Taxable?

Residential Status.

Income Classification – Indian or Foreign?

Specific Indian Incomes – Sec 7 & 9.

Taxability on the Basis of Residential Status

Accounting Method and Applicability of AS.

With Best Wishes
Vivek Mehta (CA, CS, MBA)
Ph: +91-9413118508
E-mail: - vivekmehta@icai.org, cavivekmehta@gmail.com

WHY TAX IS?

The first and very foremost question that arises to each and every one's mind is that why and how do government levy taxes, it forms law for better administration that is ok....but why these taxes on so much masses that to so much in amount…who has authorized it to levy tax…why are we duty bound to pay taxes to government…so the answer to all this is that we the peoples of India have got certain Fundamental Rights which we all know and we always plead and ask upon…and fight for, that has been conferred to us by the CONSTITUTION OF INDIA...in such similar manner we have also got certain duties and we have given certain powers to the government and hence the power to levy taxes is given to the legislature bodies by CONSTITUTION OF INDIA, wherein the list of subject matters over which the state or the centre on which they can make laws and levy taxes is listed in schedule 7th.

But now one may be surprised that government has so many powers so then they can do anything what they want at their desire and can levy taxes on anything. But it's not so as per the ruling of Apex Court in one of the case law it was held that a Law must not be a colourable use of or a fraud upon the legislative power to tax, i.e. a tax proposed must be within the legislative competency of legislature.

And for levying the taxes over income other than agriculture income Entry 82 of List I of Schedule – 7 empowers state, and hence the Income Tax Act, 1961 was enacted.

WHAT TAX IS?

Now before we start up with the Study to further topics we are required to go into the details of the subject matter and we should be very clear with a thought that what is meant by a tax; by hearing and reading this thing mind each and every one is reminded of with the Income tax, Sales Tax(VAT), Service Tax, Excise Duty and all such things which Government levies and collects form a person or a class of person with a view to take the things and revert back to the society in more beneficial manner than what they take it off.

It has been rightly said in ***Raghuvansham Mahakavyam "For the sake of welfare of the Subject, he received taxes from them just as the sun extracts water in order to render it back a thousand fold"***

From above words of The Literary Epic it is clear that Taxes is not just levied by the Government but it is any charge on a transaction or a group of transaction or any such thing which an authority levies on, with an authoritative power. Hence the Government Bodies and Income Tax Department and various such other department levies on with an authoritative power conferred on to them given by the respective act which in turn has been enacted by the Government who derives its power from constitution of India.

HOW TAX IS?

So why the tax is and from where the tax is? The answer to these questions has been answered off in the above Para's but now a matter arises how the tax is? The answer to this question lies in economics and it says that where the person does not get the utility of the expenditure he make he is not happy and not in favour to incur such expenditure, but since the liability has been enacted and we are duty bound to follow and act accordingly hence we are having no chance of escaping from the same. Hence in this head we shall discuss on to the matter of the Structure of Tax or the Regime of Taxation, System of Taxation: -

- Progressive System (Eg. Taxes on Individual, HUF's)
- Regressive System (Eg. VAT)
- Usually the old system was in existence with only two types but with the passage of time the other type also evolved and that system is Constant System of taxation (Eg. Wealth Tax, Corporate Tax)

TYPES OF TAXES

Now further with the nexus of burden, taxes can broadly be classified into two categories: -

- **Direct Taxes:** Direct Tax means a tax on property in respect of ownership, possession, or enjoyment of property. Direct Taxes are those which the taxpayers pays directly from his income/wealth etc.
- **Indirect Taxes:** It is a tax on goods and services, the incidence of which is borne by the consumers who ultimately consume the goods and services.

SOURCES OF INCOME TAX LAWS

Income Tax Act, 1961

- The provision of income tax extend to the whole of India and became effective from 1/4/1962 (sec.1). The Act contain provisions for
  - determination of taxable income
  - determination of tax liability
  - procedure for assessment, appeals, penalties and prosecutions
  - powers and duties of Income tax authorities

Income Tax Rule, 1962

- As per Sec.295, the Board may, subject to the control of the Central Government, make rules for the whole or any part of India for carrying out the purposes of the Act.

Finance Act

- Amendment in Income tax Act is made through Union Budget. Every year a Finance Bill is presented before the Parliament by the Finance Minister. When the finance bill is approved by both the Houses of Parliament and receives the assent of the President, it becomes the Finance Act.
- *Imp: If on the 1st day of April of the A.Y., the new Finance Act not been enacted, the provisions in force in the preceding A.Y. or the provisions proposed in the Finance Bill before the Parliament, whichever is more beneficial to the assessee, will apply until the new provisions become effective*

Circulars and Clarifications by CBDT

- U/s 119, the CBDT may issue certain circulars and clarifications from time to time, which have to be followed and applied by the Income tax authorities.
- circulars or clarifications are binding upon the Income tax authorities, but the same are not binding on the assessee. However, assessee can claim benefit under such circulars
- circulars are not binding on the Income Tax Appellate Tribunal or Courts

Judicial decision

- **Principle given by the Supreme Court :** shall be applicable as law till there is any change in law by the Parliament. These are binding on all.
- **Contradiction in the decisions of the Supreme Court:** The decision of larger bench, whether earlier or later, shall always prevail. In case where decisions are given by benches having equal number of judges, the decision of the recent case shall be applicable
- **Decisions given by a High Court or ITAT(Income Tax Appellate Tribunal) :** binding on all assesses and Income tax authorities, which fall under the jurisdiction, unless it is over ruled by a higher authority.

WHAT INCOME IS?

In general the Income means excess of receipt over expenditure. But here it is important to understand that how act defines and says the things.

But before one looks and tries to understand with the act, one should clearly understand some following terms which are very helpful and beneficial in understanding the act, viz: -

(a.) **<u>"MEANS"</u>**: When a definition uses a term "means", then the definition is self explanatory and exhaustive. It implies that the term so defined means only what is defined therein and nothing beyond that. For e.g.: Definition of "Assessment Year".

(b.) **<u>"INCLUDES"</u>**: When an exhaustive definition is not possible or Legislature wants to widen the scope of the definition, it uses the term "includes", in order to give an inclusive definition or an illustrative definition. For e.g.: Definition of "Income" or definition of "Person".

(c.) **<u>"MEANS AND INCLUDES"</u>**: When Legislature intends to define a term and also include certain items, it includes both the terms "means and includes". For e.g.: definition of "Assessee".

Quoting out the Income as defined under the Act

As per Section 2 (*24*)

"income" ***<u>includes</u>***—

(*i*) profits and gains;

(*ii*) dividend;

(*iia*) voluntary contributions received by a trust created wholly or partly for charitable or religious purposes or by an institution established wholly or partly for such purposes or by an association or institution referred to in clause (*21*) or clause (*23*), or by a fund or trust or institution referred to in sub-clause (*iv*) or sub-clause (*v*) or by any university or other educational institution referred to in sub-clause (*iiiad*) or sub-clause (*vi*) or by any hospital or other institution referred to in sub-clause (*iiiae*) or sub-clause (*via*)] of clause (*23C*) of section 10 or by an electoral trust.

Explanation.—For the purposes of this sub-clause, "trust" includes any other legal obligation;

(*iii*) the value of any perquisite or profit in lieu of salary taxable under clauses (*2*) and (*3*) of section 17;

(*iiia*) any special allowance or benefit, other than perquisite included under sub-clause (*iii*), specifically granted to the assessee to meet expenses wholly, necessarily and exclusively for the performance of the duties of an office or employment of profit;

(*iiib*) any allowance granted to the assessee either to meet his personal expenses at the place where the duties of his office or employment of profit are ordinarily performed by him or at a place where he ordinarily resides or to compensate him for the increased cost of living;

(*iv*) the value of any benefit or perquisite, whether convertible into money or not, obtained from a company either by a director or by a person who has a substantial interest in the company, or by a relative of the director or such person, and any sum paid by any such company in respect of any obligation which, but for such payment, would have been payable by the director or other person aforesaid;

(*iva*) the value of any benefit or perquisite, whether convertible into money or not, obtained by any representative assessee mentioned in clause (*iii*) or clause (*iv*) of sub-section (1) of section 160 or by any person on whose behalf or for whose benefit any income is receivable by the representative assessee (such person being hereafter in this sub-clause referred to as the "beneficiary") and any sum paid by the representative assessee in respect of any obligation which, but for such payment, would have been payable by the beneficiary;

(*v*) any sum chargeable to income-tax under clauses (*ii*) and (*iii*) of section 28 or section 41 or section 59;

(*va*) any sum chargeable to income-tax under clause (*iiia*) of section 28;

(*vb*) any sum chargeable to income-tax under clause (*iiib*) of section 28;

(*vc*) any sum chargeable to income-tax under clause (*iiic*) of section 28;

(*vd*) the value of any benefit or perquisite taxable under clause (*iv*) of section 28;

(*ve*) any sum chargeable to income-tax under clause (*v*) of section 28;

(*vi*) ***<u>any capital gains</u> chargeable under section 45***;

(*vii*) the profits and gains of any business of insurance carried on by a mutual insurance company or by a co-operative society, computed in accordance with section 44 or any surplus taken to be such profits and gains by virtue of provisions contained in the First Schedule;

(*viia*) the profits and gains of any business of banking (including providing credit facilities) carried on by a co-operative society with its members;

(*ix*) any winnings from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever.

Explanation.—For the purposes of this sub-clause,—

(*i*) "lottery" includes winnings from prizes awarded to any person by draw of lots or by chance or in any other manner whatsoever, under any scheme or arrangement by whatever name called;

(*ii*) "card game and other game of any sort" includes any game show, an entertainment programme on television or electronic mode, in which people compete to win prizes or any other similar game;

(*x*) any sum received by the assessee from his employees as contributions to any provident fund or superannuation fund or any fund set up under the provisions of the Employees' State Insurance Act, 1948 (34 of 1948), or any other fund for the welfare of such employees;

(*xi*) any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.

Explanation.—For the purposes of this clause, the expression "Keyman insurance policy" shall have the meaning assigned to it in the *Explanation* to clause (*10D*) of section 10;

(*xii*) any sum referred to in clause (*va*) of section 28;

(*xiii*) any sum referred to in clause (*v*) of sub-section (2) of section 56;

(xiv) any sum referred to in clause (vi) of sub-section (2) of section 56;

(*xv*) any sum of money or value of property referred to in clause (*vii*) or clause (*viia*) of sub-section (2) of section 56;

Understanding the concept of Income from the above clause is not so easy and moreover the given sub-section is not exhaustive and complete in itself, it's just an illustrative list by the help of which act has tried to define the Income. And hence over and above the times the matter has drawn judicial attention as to which all forms income as per Income as per the act.

In general we all know that there are two types of income: -

- Revenue Income
- Capital Income

As per act also if you study the income is classified in this two type of income only but it has a peculiarity about chargeability which can be summarised as bellow: -

Revenue Income → It is always and always chargeable to tax unless specifically exempt under section 10.

Capital Income → It is chargeable to tax only and only if it satisfies section 45(1)

HEADS OF INCOME

Classification of the Taxable Income: - The Act has from the point of administration and taxability has divided the income into 5 head under **section 14**:

Heads of income.

Sec. 14: Save as otherwise provided by this Act, ***all income shall***, for the purposes of charge of income-tax and computation of total income, ***be classified under the following heads of income*** :

A.—Salaries.

B.— [***]

C.—Income from house property.

D.—Profits and gains of business or profession.

E.—Capital gains.

F.—Income from other sources.

PROVISION AS APPLICABLE FOR COMPUTING INCOME

Rule	Purpose	Effect of amendment
Rule one	For computing income	• Rule one is applicable only for computing total income. • Total income is computed in accordance with the provisions, as stand on the *first day of the assessment year*. • If an amendment is made w.e.f. April 2 or any other date, it is irrelevant for computing income for that assessment year.
Rule two	For other purpose	If an amendment is made (which has no effect on computation of total income), then it is applicable from the date of amendment. (Eg. procedural amendment or change in rate of interest for non-payment, late payment of tax, etc.)

GENERAL PRINCIPLE REGARDING INCOME

Diversion of income and Application of income Diversion of income

- **Diversion of income**
  - Where income or portion of income is diverted at the source by an overriding title before it reaches the assessee, it is a diversion of income and not taxable.
  - It must be noted that the charge or obligation is *on source of income and not on the receiver.*
  - Income is taxable in the hands of person to whom income is diverted by overriding title and not in the hands of person who first receive it.
- **Application of income**
  - After earning the income, if it is required to be applied to discharge an obligation, it is merely an "application of income and chargeable to tax".
  - In order to decide whether a particular income is a diversion of income or application of income, it has to be determined whether the amount sought to be diverted reaches the assessee's hands *as his own income or not.*

INCOME OR SURPLUS FROM MUTUAL ACTIVITY

- A person cannot make income / profit from a transaction with himself. Income must, therefore come from outside.

With Best Wishes
Vivek Mehta (CA, CS, MBA)
Ph: +91-9413118508
E-mail: - vivekmehta@icai.org, cavivekmehta@gmail.com

- A surplus arising to a mutual concern cannot be regarded as income chargeable to tax.
    - **Conditions: -** For income from mutual activity to be exempted from tax, the following conditions should be satisfied.
        - The arrangement between the concern and its members should be non-trading in character.
        - There should be complete identity of the contributors to the fund and the participants of benefits and surplus of the fund.
        - The contributors do not derive profit from the contributions made by themselves. The surplus should only be either expended or refunded to them.
    - **Exception: -** In the following cases, income from a mutual activity is taxable.
        - Profits and gains of any insurance business carried on by a mutual insurance company / co-operative society.
        - Income of a trade, professional or similar association from specific services rendered to its members.

INCOME SHOULD BE REAL AND NOT FICTIONAL

- Income means real income and not fictional income.
- In *Sir Kikabhai Premchand case*, Supreme Court held that a person cannot make a profit by trading with himself or out of transfer of funds / assets from one pocket to another pocket.
- **Example**
    - Income does not arise in a transaction between head office and branch office even if goods are invoiced at a price higher than the cost price.
    - Income does not accrue or arise at the time of revaluation of assets.

REVENUE RECEIPT VS. CAPITAL RECEIPT

The distinction between capital and revenue receipts is vital because –

- Capital receipts are not taxable unless they are expressly taxable in the Act (e.g. capital gain taxable u/s. 45).
- Revenue receipts are always taxable; unless they are expressly exempt from tax (e.g. income exempted u/s. 10).
- As such no strait-jacket set of principles has been enshrined or laid in the Act for drawing a distinction between a capital and revenue receipt, although this has been in most of the cases the issue of conflict between revenue and the assessee but by studying in the depth by taking the help of the verdict of apex court and various other benches of the state high court you'll find that in all there was some or the other basis

taken for to give the judgment, but if we summarise the most apt judgments and laying out broad frame work for the same we may find a solution to the same viz named as Test of Source, Further it can be stated that: -

- Nature of receipt in the hands of recipient is material. The source from which payment is made has no relevance.
- Receipt *in lieu of source of income* is a capital receipt (e.g. compensation for loss of employment, where as a receipt *in the lieu of income* is a revenue receipt (e.g. compensation for temporary disablement).
- The motive of the payer is not relevant.
- The fact that payment is lump sum / large / periodic is not relevant.

- Now it's important to determine that how can u classify Income as Revenue or Capital: - Well basically for this one needs to look after the nature of receipt, because if the nature of receipt is revenue than the Income so getting generated shall be Revenue only and if the nature of receipt is capital than it will be a capital Income.
- Now going into the detailed discussion on the topic together with the help of the various case laws we'll try to find and establish and understand the relationship of various principles laid down by the various benches and their verdicts, and then we shall summarise the same.
- In the absence of transfer of a capital asset, to ascertain whether the receipt is on account of loss of income or source of income. It is a trite law that any receipt in the nature of compensation, costs damage, etc. by whatever name called ***towards loss of income is a revenue receipt***. However any receipt ***to compensate or the loss of source of income is a capital receipt*** (so now again you'll find that the word source has been used and the same thinking has been adopted): -
  - **Oberoi Hotel (P) Ltd. Us. CIT (1999) 152 CRT 474 (SC):** In that case, the assessee-company was operating, managing and administering many hotels belonging to others for a fee at several places. The company agreed to operate the Hotel Oberoi Imperial for which it was to receive a certain fee. The agreement was to run for an initial period of ten years. The agreement also gave the assessee a right to exercise the option of purchasing the hotel in case its owners desired to transfer the same during the period of the agreement. On a further agreement with the receiver, the right to exercise the option was given up by the assessee. It was agreed that the receiver would be at liberty to sell or otherwise dispose of the said property at such price and on such terms as he may deem fit and was not under any obligation requiring the purchaser to enter into any agreement with the assessee for the purpose of operating and managing the hotel or otherwise and in its return the assessee received compensation of Rs.29,47,500. ***The said amount was claimed as a capital receipt***. The ITO rejected. The claim but the CIT(A) and the Tribunal upheld (supported) it. The Higher Court held it to be a revenue receipt. Reversing the decision of the High Court, ***the Hon'ble Supreme Court*** held that the amount received by the assessee was the consideration for ***giving up its right*** to purchase and/or to operate the property or for getting it on leaser before it was transferred or let out to other persons and ***it was not for settlement of rights***

under a trading contract, but the injury was inflicted (imposed) on the capital asset on the assessee and giving up the contractual right on the basis of the principal agreement had ***resulted in the loss of source*** of the assessee's income. The receipt was held to be a capital receipt.

- **CIT vs. Bombay Burmah Trading Corporation Ltd. (1986) 58 CTR 144 (SC): (1986) 161 ITR 386 (SC):** It was held that the compensation received for *immobilization, sterilization, destruction or loss total or partial, of a capital asset would be a capital receipt but if a sum represented profit in a new form, then that would be revenue receipt but where the agreement relates to the structure of the assessee's profit-making apparatus and affects the conduct of the business, the sums received for cancellation or variation of such agreement would be capital receipt.*
- From the above discussion it can be easily noticed that if the receipt is to make good actual or prospective loss in a particular trading transaction or set of transactions, it is a revenue receipt liable to tax. However, any receipt towards loss of source of income is a capital receipt. Loss of Source of income does not necessarily mean that it must absolutely extinguish. If the source of income has been severely beaten thereby causing serious damage to the income-earning apparatus itself, it will also be construed as the loss of source of income. Such indentation to the source can be caused in different ways. One of such ways may be maligning the name of the business, resulting in tarnishing the reputation and causing damage to the goodwill of business. So if goodwill of the business is damaged and later on some compensation is awarded in lieu of that, it will also fall in the same category of loss to the source of income and consequently such a receipt will also qualify to be characterized as a capital receipt. It is imperative that the receipt should be, in fact, towards loss of goodwill in general and no part of it should relate to make good the loss in a particular trading transaction or set of transactions. If such a receipt cannot be identified with the loss in a particular transaction(s) but to make good the injury caused to the reputation of business which had the effect of impairing the source of income, it will be a capital receipt.

- ***<u>Incentive And Subsidy Whether Capital Or Revenue</u>***
  - Hon'ble Allahabad High Court has decided that the incentive received to the assessee by way of additional quota for free-sale of sugar which is directly connected with the business activities of the assessee shall form the part of the business receipt and hence the matter was adjudged in favour of the Revenue in the case of **CIT v. Kisan Sahkari Chini Mills Ltd. [2006] 284 ITR 418.**
  - The Hon'ble court considered a number of decisions, including that of the Hon'ble Supreme Court in the case of **Sahney Steel and Press Works Ltd. V. CIT [1997] 228 ITR 253 and CIT v. Rajaram Maize Products [2001] 251ITR**

427, in which it was held that the amount o subsidy received as incentive for production or running of an industry was of revenue nature.

- ***Damages Whether Capital Or Revenue***
    - **CIT VS Saushatra Cement Ltd. [2010] 325 ITR 422 (SC): -** A question arose whether the amount of liquidation charges paid because of delay in supply of a capital asset received by the assessee as damages was a capital or a revenue receipt? The Tribunal relying on the ratio of the decisions of this court in **CIT v. Rai Bahadur Jairam Valji [1959] 35 ITR 148 (SC)** and **Kettlewell Bullen and co. Ltd. V. CIT [1964] 54 ITR 261: AIR 1965 SC 65,** it came to conclusion that the said amount could not be treated as a revenue receipt. According to the Tribunal, the payment of liquidated damages to the assessee by the supplier was intimately linked with the supply of machinery, i.e., a fixed asset on capital account, which could be said to be connected with the **source of income** or profit making apparatus rather than a receipt in course of profit earning process and, therefore, it could not be treated as part of receipt relating to a normal business activity of the assessee. The Tribunal also observed that the said receipt had no connection with loss or profit because the very source of income, viz., the machinery was yet to be installed. Accordingly, the Tribunal allowed the appeal and deleted the addition made on this account. **High Court Held that it is in nature of capital receipt in appeal to SC the held that** "We have considered the matter in the light of the aforenoted broad principle. It is clear that the liquidated damages were to be calculated at 0.5 percent of the price of the respective machinery and equipment to which the items were delivered late, for each month of delay in delivery completion, without proof of the actual damages the assessee would have suffered on account of the delay. The delay in supply could be of the whole plant or a part thereof but the determination of damages was not based upon the calculation made in respect of loss of profit on account of supply of a particular part of the plant. It is evident that the damages to the assessee was directly and intimately linked with the procurement of a capital asset, i.e., the cement plant, which would obviously lead to delay in coming into existence of the profit-making apparatus, rather than a receipt in the course of profit earning process. Compensation paid for the delay in procurement of capital asset amounted to sterilization of the capital asset of the assessee as supplier had failed to supply the plant within time as stipulated in the agreement. The aforesaid amount received by the assessee towards compensation for **sterilization of the profit earning source**, not in the ordinary course of their business, in our opinion, **was a capital receipt** in the hands of the assessee. We are, therefore, in agreement with the opinion recorded by the High Court and hold that the amount received by the assessee from the suppliers of the plant was in the nature of a capital receipt."

- ***Loss Of Agency – Compensation Received***
  - In **Guffic Chem P. Ltd. VS CIT [2011] 17 ITCD 131 (SC), [2011] 332 ITR 602 (SC)** two questions arose for determination, namely, whether the amounts received by the appellant for **loss of agency** was in normal course of business and therefore whether they constituted revenue receipt? The **second question** which arose before this Court was whether the amount received by the assessee **(compensation) on the condition not to carry on a competitive business** was in the nature of capital receipt? It was held that the compensation received by the assessee for loss of agency was a revenue receipt whereas compensation received for refraining from carrying on competitive business was a capital receipt. This dichotomy has not been appreciated by the High Court in its impugned judgment. In the present case, the Department has not impugned the genuineness of the transaction. In present case the view of High Court was erroneous in interring with the concurrent findings of fact recorded by the CIT (Appeals) and the Tribunal. One more aspect needs to be highlighted, payment received as non-competition fee under a negative covenant was always treated as a capital receipt till the assessment year 2003-04, It is only vide Finance Act, 2002 with effect from 1.4.2003 that the said capital receipt is now made taxable as revenue receipt under Business and Profession Head [See: Section 28(va)]. The Finance Act, 2002 itself indicates that during the relevant assessment year compensation received by the assessee under noncompetition agreement was a capital receipt, not taxable under the 1961 Act. It became taxable only with effect from 1.4.2003. **It is well settled** that a liability cannot be created retrospectively. Hence in present case, compensation received under Non-Competition Agreement is a capital receipt and not a revenue receipt by specified legislative mandate, vide Section 28(va) and that took with effect from 1.4.2003. Hence, the said Section 28(va) is amendatory and not clarificatory. Lastly, in **Commissioner of Income-Tax, Nagpur v. Rai Bahadur Jairam Valji reported in 35 ITR 148** it was held by this Court that if a contract is entered into in the ordinary course of business, any compensation received for its termination (loss of agency) would be a revenue receipt.

- ***Amount Received For Loss Of Reputation And Goodwill***
  - Whether the compensation awarded to the assessee against the **loss of reputation and goodwill** can be considered as revenue or capital receipt. It is a common law that every receipt by the assessee is not chargeable to tax. Therefore, it follows that unless the receipt represents income chargeable to tax, the question of attracting taxability on such receipt does not arise. Sub-Section 24 of section 2 defines "income' includes (i) profits and gains …" Thus,

this definition includes various items as mentioned in clause. (i) to (xiv). If any other item of receipt is or contains the element of income in common parlance that would still be included within the scope of the definition of 'income' under this provision notwithstanding the fact that there is no specific inclusion of such item in the definition. The word 'income' has to be understood in the generic sense. If a receipt bears the trails of income as per the plain and natural meaning, the same will still be included within the scope of Section 2(24) even if there is no specific mention of such item in the definition clause. It is more aptly demonstrated from the scheme of the Act itself by which the receipt by way of rent from property, although not included under sub-Section 24 of Section 2 is income as specifically included in Chapter IV-C of the Act.

- In the case of **C.R. Karthikeyan,** the assessee was having income from various sources including salary and business. He participated in the All India Highway Motor Rally and was awarded the first prize of Rs.20,000 by the Indian Oil Corporation and another sum of Rs.2,000 by the All India Highway Motor Rally. The said sum was claimed as not chargeable to tax. The ITO negated the assessee's view and included the sum of Rs.22,000 in the income of the assessee. The Assessee held that as the rally was not a race the amount received could not be treated as income. The Tribunal approved the view by holding that the rally was not a race but it was predominantly a test of skill and endurance. The High Court also approved the view taken by the Tribunal. However, when the matter came up before the Hon'ble Supreme court it held that the assessee entered the contest to win it and what he got was a "return for his skill And endurance'. Overturning the view taken by the High Court the Hon'ble Supreme court held that the amount in question was income under section 2(24) even if no specific clause in this regard was contained in the provision. It held that "even if a receipt does not fall within the ambit of any of the sub-clauses in Section 2(24)," it may still be income if it partakes of the nature of the income. The idea behind providing inclusive definition in Section 2(24) is not to limits meaning but to widen its net. This Court has repeatedly said that the word 'income' is of widest amplitude and that it must be given its natural and grammatical meaning". Similar view has been reiterated recently by the Hon'ble Madras High Court in the case of **CIT vs. K. Thangamani (2009) 221 CTR (Mad) 742: (2009) 18 DTR (Mad) 6: (2009) 309 ITR 15 (Mad)** by holding that "Section 2(24) gives an inclusive definition to the word 'income'. The expression 'income' is very wide and the object of the IT Act being one to tax income it has to be given an extended meaning. From these judicial pronouncements, it is evident that even if a particular item of income is not specified in Section 2(24), the same can also be included. in the definition of 'income'. What the assessee received in the case of G.R. Karthikeyan was the return for his skill and endurance which has been held to be includible in the definition of income under Section 2(24). At the same time it is since qua non that the receipt must be in the nature of income. It is not so, then it will not be held as income. For example, the receipt of a gift by a person from another cannot be subjected to tax because even though it is a receipt, but it is devoid of the traits of income and, hence, such an amount cannot be held to be liable to tax.

- ***Club Membership Fee Is Capital Receipt*: -** Receipt on account of entrance fees and life membership fees received by the assessee from its members is not a revenue or trading receipt and therefore, cannot be included in the assessable income.

  Case Law

  1. **CIT VS. DINESS BUSIENSS SERVICE P. LTD. (2003) ITR 1 (BOM)**
  2. **CIT VS. WIAA CLUB LTD. (1982) 136 ITR 569 (BOM)**
  3. **ACIT VS. KARNVATICLUB LTD. (2010) 4 ITR 174 (TRIB) (A'BAD)**

- ***Premature Termination Of Lease And Licence Agreement:*** - On account of premature termination of the lease and licenses agreement forfeiture of Security deposit received from the licensee is not taxable as revenue receipt as the deposit was in the nature of 100 and in the capital filed **– ACIT VS. DAS & CO. (2010) 133 TTJ 542 (TAT-MUM)**
- Now with the ignited minds when you all will look upon the issue again and will try to give your own reasoning with the issue in the broader outlook, you'll find that the main test that you all are applying and that you all can think of are many but in true sense all the test given in the various case laws above are in some or the other manner revolving around the Basic and Foremost thing of Source, whether the receipt is from source or against/ for source.

Hence it is important to note that income if accrues of arises be it incidental it shall be chargeable to tax if it falls within the ambit of sec 2(24) i.e. income shall be taxable irrespective of the fact whether it is earned with a profit motive or not.

Certain special provisions which are not the income of the current but then also the same is deemed to be Income of the current year in which they are tracked.

Cash credits.

Sec. 68: Where **<u>any sum</u>** is found **<u>credited in the books</u>** of an assessee maintained for any previous year, and the assessee offers no explanation about the nature and source thereof or the **<u>explanation</u>** offered by him **<u>is not</u>**, in the opinion of the Assessing Officer, **<u>satisfactory</u>, <u>the sum so credited may be charged to income-tax as the income</u>** of the assessee of that previous year.

Unexplained investments.

Sec. 69: Where in the financial year immediately preceding the assessment year the assessee has made investments which are not recorded in the books of account, if any, maintained by him for any source of income, and the assessee offers **no explanation about the nature and source of the investments** or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the value of the investments may be deemed to be the income of the assessee of such financial year.

Unexplained money, etc.

Sec. 69A: Where in any financial year the assessee is found to be the **owner of any money, bullion, jewellery or other valuable article and such money, bullion, jewellery or valuable article** is **not recorded in the books** of account, if any, maintained by him for any source of income, and the assessee offers no explanation about the nature and source of acquisition of the money, bullion, jewellery or other valuable article, or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the money and the value of the bullion, jewellery or other valuable article may be deemed to be the income of the assessee for such financial year.

Amount of investments, etc., not fully disclosed in books of account.

Sec. 69B: Where in any financial year the assessee has made investments or is found to be the owner of any bullion, jewellery or other valuable article, and the Assessing Officer finds that the **amount** expended on making such investments or in acquiring such bullion, jewellery or other valuable article **exceeds the amount recorded in** this behalf in the **books of account** maintained by the assessee for any source of income, and the assessee offers no explanation about **such excess amount** or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the excess amount may be deemed to be the income of the assessee for such financial year.

Unexplained expenditure, etc.

Sec. 69C: Where in any financial year an assessee has incurred **any expenditure** and he offers **no explanation about the source of such expenditure or part thereof**, or the explanation, if any, offered by him is not, in the opinion of the Assessing Officer, satisfactory, the amount covered by such expenditure or part thereof, as the case may be, may be deemed to be the income of the assessee for such financial year :

Provided that, notwithstanding anything contained in any other provision of this Act, 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**.

Amount borrowed or repaid on hundi.

Sec. 69D: Where any **amount is borrowed on a *hundi* from, or any amount due thereon is repaid**

to, any person **<u>otherwise than through an account payee cheque</u>** drawn on a bank, the amount so borrowed or repaid shall be <u>deemed to be the income</u> of the person borrowing or repaying the amount aforesaid for the previous year in which the amount was borrowed or repaid, as the case may be :

Provided that, if in any case any amount borrowed on a *hundi* has been deemed under the provisions of this section to be the income of any person, such person shall not be liable to be assessed again in respect of such amount under the provisions of this section on repayment of such amount.

Explanation.—For the purposes of this section, the amount repaid shall include the amount of interest paid on the amount borrowed.

Note: - The following are not the income in actual but indeed they are investment, asset or certain expenditure of the current asset, but then too same are deemed as income in the year in which A.O. finds the same. It is important to note that in respect of the above four these are those investment or expenditures which are not recorded in the books of accounts or recorded but assessee has no explanation about its source or about its expense. And hence is liable for taxation.

Important to note that it will be liable for taxation under other sources or in the business or profession head even though it may pertain to the value of a capital asset.

WHO IS CHARGEABLE TO TAX?

As per Section 2(*31*): -

"**<u>person</u>**" *includes*—

(*i*) an individual,

(*ii*) a Hindu undivided family, (Detail discussion to be done with the Taxation of HUF)

(*iii*) a company,

(*iv*) a firm,

(*v*) an association of persons or a body of individuals, whether incorporated or not,

(*vi*) a local authority, and

(*vii*) every artificial juridical person, not falling within any of the preceding sub-clauses.

> *Explanation.*—For the purposes of this clause, an association of persons or a body of individuals or a local authority or an artificial juridical person shall be deemed to be a person, whether or not such person or body or authority or juridical person was formed or established or incorporated with the object of deriving income, profits or gains;
>
> As per Sec 2(*7*): -
>
> "assessee" means a person by whom any tax or any other sum of money is payable under this Act, and includes—
>
> (*a*) every person in respect of whom any proceeding under this Act has been taken for the assessment of his income or assessment of fringe benefits or of the income of any other person in respect of which he is assessable, or of the loss sustained by him or by such other person, or of the amount of refund due to him or to such other person;
>
> (*b*) every person who is deemed to be an assessee under any provision of this Act;
>
> (*c*) every person who is deemed to be an assessee in default under any provision of this Act;

Representative Assessee: -

In respect of Income	Representative Assessee
1.) of a non- resident specified in Sec.9(1)	Agent of the Non Resident
2.) of a minor, lunatic or idiot	A guardian or manager who is entitled to receive or is in receipt of income.
3.) Which is received by	Such-
- the Courts of Wards;	- Courts of Wards;
- the Administrative-General;	- Administrative general;
- the Official Trustee	- Official Trustee
- any Receiver or Manager	- Receiver or Manager
appointed by or under any order of a court on behalf of or for the benefit of any person	
4.) Which is received by the trustee (s)	Such trustee or trustees

With Best Wishes
Vivek Mehta (CA, CS, MBA)
Ph: +91-9413118508
E-mail: - vivekmehta@icai.org, cavivekmehta@gmail.com

PERIOD OF WHICH INCOME IS TAXABLE?

For the better administration the period has been marked out and laid down by the act itself.

Assessment Year: - Sec 2(9)

"assessment year" means the period of twelve months commencing on the 1st day of April every year;

Previous Year:

- **Sec. 2(34)**: "previous year" means the previous year as defined in section 3;

- **Sec. 3**: For the purposes of this Act, "previous year" means the financial year immediately preceding the assessment year :

Provided that, in the case of a business or profession newly set up, or a source of income newly coming into existence, in the said financial year, the previous year shall be the period beginning with the date of setting up of the business or profession or, as the case may be, the date on which the source of income newly comes into existence and ending with the said financial year.

But there are certain exception wherein the income of the previous year is not taxable in the following assessment year but it is assessed and taxed in the same previous year only but the rate in force are of the actual assessment and the same is laid out in the section 2(37A) and those exception section are 172, 174, 174A, 175 and 176.

Assessment year and Previous year

Assessment year [Sec. 2(9)]	Previous year (Sec. 3)
(a) Means period of 12 months commencing on the first April every year. (b) The year in which tax is levied is called assessment year	(a) Means Financial year immediately preceding the assessment year. (b) The year in respect of which tax is levied is called previous year [i.e. the year in which income in earned.

Exception in case where Previous Year is not the same

In case of	Previous year is the period
Business or profession	Beginning with the date of setting up of the business & ending on

being newly set-up	31st March of that financial year.
A source of income newly coming into existence	Beginning with the date on which the new source of income comes into existence & ending on 31st March of that financial year.

Note – The second and subsequent previous years are always financial year (i.e., April to March).

- **When the income of previous year is not taxable in the immediately following assessment year**: - Normally income of the previous year is taxable in the next following assessment year. However, in following five cases, income is taxed in the year in which it is earned.

	Conditions	Income
Shipping business of non-residents [Sec. 172]	a. The assessee is a non-resident. b. He owns a ship or ship is chartered by the non-resident. c. The ship carries passengers, live stock, mail, goods shipped at any port in India.	7.5% of gross amount receivable on account of such operation (including demurrage charge, handling charge or such similar charges) by the non- resident shall be deemed to be the income of the non-resident. (Note: - It is a recovery Section and it overrides the entire provisions of the Income Tax Act) **Submission of return** • The master of the ship shall submit a return of income before the departure of the ship from Indian Port; or • Such return may be submitted within 30 days of the departure of the ship if the A.O. is satisfied that it will be difficult to submit the return before departure and satisfactory arrangement for payment of tax has been made; and • Unless tax has been paid (or satisfactory arrangement have been made for payment thereof), a port clearance shall not be granted by the Collector of Customs.

Persons leaving India [Sec. 174]	It appears to the Assessing Officer that – a. An individual may leave India during the current assessment year or shortly after it expiry; and b. He has no present intention of returning to India.	The income up to the probable date of his departure from India shall be chargeable to tax in that assessment year. (Note: - Some or part of the income is liable to be taxed on the estimated basis, as the probable date is a future date and taxation is to be done till that point.)
Associations or bodies formed for short duration [Sec. 174A]	a. There is an AOP, BOI, Artificial judicial person formed, registered, incorporated for a *particular event, purpose* (e.g. completing a contract), and b. It appears to the Assessing Officer that abovementioned persons is likely to be dissolved in the assessment year in which it was formed, registered, incorporated or immediately after such assessment year.	The income up to the date of its dissolution shall be chargeable to tax in that assessment year.
Person likely to transfer property to avoid tax [Sec. 175]	Where it appears to the Assessing Officer during the current assessment year that - a. any person is likely to charge, sell, transfer, dispose of, otherwise part with any of his assets (may be movable or immovable) b. with a view to avoiding payment of any liability	The total income up to the date when the Assessing Officer *commences* proceedings under this section shall be taxable in that assessment year. (i.e. period shall start from the last date of assessment (it can be any self or regular) till the date the A.O. starts the proceedings.)

	under the Income Tax Act.	

Discontinued business [Sec. 176]	A business or profession is discontinued in any assessment year.	The income of business or profession up to the date of discontinuation may be chargeable to tax in that assessment year.
		
		If may be noted that -
		
		• The above income is taxable at the *discretion of the Assessing Officer* in the assessment year in which business is discontinued.
		• If such discretion is not exercised, then such income shall be taxed in the normal way (i.e. in the assessment year immediately following the previous year of discontinuance).
		• Any person discontinuing the business or profession has to give notice of such discontinuance to the Assessing Officer within 15 days of the discontinuance.
		• The A.O. may serve a notice on the following persons to furnish a return within specified time (not being less than 7 days).
		    ◦ The person whose income is to be assessed.
		    ◦ In case of a firm – partner at the time of discontinuance.
		    ◦ In case of a company – principal officer.
		• Such notice shall be deemed to be the notice u/s. 142(1)(i).

Common provisions for all five exception

1.Separate Assessment: - Separate assessments are made for each completed previous year or part thereof. In other words income for such period cannot be aggregate for the purpose of assessment.

2.Rate of assessment: - All such assessments are made as per the rate(s) applicable to the assessment year in which it so appears to the Assessing Officer.

Important Note: - First four exceptions are ***mandatory*** (i.e. sec. 172, 174, 174A and 175) on the part of the Assessing Officer but last exception (i.e. 176) is ***discretionary.***

Procedure for determination of the Taxable Income and Tax thereon:

1.	Determination of Residential status	Determine residential status of the assessee
2.	Computation of income	Compute income under several heads of income giving the effect of clubbing of income
3.	Aggregate the income	income under several heads are to be aggregated giving the effect of set-off and carry forward of losses
4.	Deduction under VIA	Provide deductions u/s 80CCC to 80U from GTI
5.	Rounding off of income (u/s 288A)	Total Income shall be rounded to the nearest multiple of Rs.10 (Ignoring Paise)
6.	Compute tax liability	According to applicable rate of tax
7.	Surcharge	To the amount so derived in 6 above add surcharge @ 5%/ 2% *(as per provisions)
8.	Education cess and SHE Cess	To the amount so derived in 7 above add education cess @3% and ascertain total tax liability
9.	Relief	From tax liability so computed subtract relief u/s 86 (AOP, BOI share of individual), 89(1){salaried employee for arrear or advance salary}
10.	Rounding off of tax (u/s 288B)	Tax liability so computed is to be rounded off to nearest multiple of Rs. 10 (Ignoring Paise)
11.	TDS or TCS or Advance tax	Shall be reduced from tax liability to ascertain tax payable

RESIDENTIAL STATUS

Residential status of a person determines the total income of an assessee chargeable to tax, but it is important to understand that this concept has nothing to do with the citizenship or origination of any person, it is completely different from that and it has to be seen for each and every year separately. Further a person can be resident in more than one country at a time, and hence the once and liability to prove his residential status in the country is of the assessee.

Residence in India.

Sec. 6: For the purposes of this Act,—

(*1*) An **individual** is said to be resident in India in any previous year, if he—

(*a*) is in India in that year for a period or periods amounting in all to one hundred and eighty-two days or more ; or

(*c*) having within the four years preceding that year been in India for a period or periods amounting in all to three hundred and sixty-five days or more, is in India for a period or periods amounting in all to sixty days or more in that year.

Explanation.—In the case of an individual,—

(*a*) being a citizen of India, who leaves India in any previous year as a member of the crew of an Indian ship as defined in clause (*18*) of section 3 of the Merchant Shipping Act, 1958 (44 of 1958), or *for* the purposes of employment outside India, the provisions of sub-clause (*c*) shall apply in relation to that year as if for the words "sixty days", occurring therein, the words "one hundred and eighty-two days" had been substituted ;

(*b*) being a citizen of India, or a person of Indian origin within the meaning of *Explanation* to clause (*e*) of section 115C, who, being outside India, comes on a visit to India in any previous year, the provisions of sub-clause (*c*) shall apply in relation to that year as if for the words "sixty days", occurring therein, the words "one hundred and eighty-two days" had been substituted.

(*2*) A Hindu undivided family, firm or other association of persons is said to be resident in India in any previous year in every case except where during that year the control and management of its affairs is situated wholly outside India.

(*3*) A company is said to be resident in India in any previous year, if—

(*i*) it is an Indian company ; or

(*ii*) during that year, the control and management of its affairs is situated wholly in India.

(*4*) Every other person is said to be resident in India in any previous year in every case, except where during that year the control and management of his affairs is situated wholly outside India.

(*5*) If a person is resident in India in a previous year relevant to an assessment year in respect of any source of income, he shall be deemed to be resident in India in the previous year relevant to the assessment year in respect of each of his other sources of income.

(6) A person is said to be "not ordinarily resident" in India in any previous year if such person is— (a) an individual who has been a non-resident in India in nine out of the ten previous years preceding that year, or has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, seven hundred and twenty-nine days or less; or (b) a Hindu undivided family whose manager has been a non-resident in India in nine out of the ten previous years preceding that year, or has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, seven hundred and twenty-nine days or less.

Understanding the things in detail in respect of each class of the person as stated and listed in the act.

It is important to note that act say that a person or a class of person of certain class of a particular class of person shall be resident if they full fill the conditions given in the act, and hence we draw out that the person who does not fulfills the given conditions can be termed as non - resident. Further, we shall note that there is a one more category of the status in case of a resident individual and HUF i.e. 'Not Ordinarily Resident'. Hence we can list and study the status in following category as under:

1. **Individual:**
   a. Resident
      i. Resident (or can be termed as Ordinary Resident)
      ii. Resident but Not Ordinarily Resident
   b. Non – Resident

The residential stay of an individual is looked on the basis of his or her stay in India during the relevant previous year. But the act further classifies three cases and the conditions in which the basic status as to resident or non resident can be stated: -

Case – I	**Case – II**	**Case – III**
Persons covered: - (Who leaves India) - being a citizen of India - who leaves India - as a member of the crew of an Indian Ship - or - for purpose of employment	Person Covered: - (Who comes to India for visit) - being a citizen of India - or - of Indian origin - who stay's outside India - comes on a visit to India	Person Covered: - - others than those who have not been covered in I and II
period or periods amounting in	period or periods amounting in	period or periods amounting in

With Best Wishes
Vivek Mehta (CA, CS, MBA)
Ph: +91-9413118508
E-mail: - vivekmehta@icai.org,
cavivekmehta@gmail.com

all of stay in India: - Atleast 182 days in the relevant previous year	all of stay in India: - Atleast 182 days in the relevant previous year	all of stay in India: - - Atleast 182 days in the relevant previous year Or - Atleast 60 days in the relevant Previous Year and atleast 365 days in immediately 4 preceding year to the relevant previous year.

But for penetrating deep and finding out that whether the person is just resident or is not ordinarily resident, we need to look and take the help of the preceding years and the individual shall have to satisfy given additional condition in order to become Ordinary Resident: -

1. Has been NR in atleast 9 years out the preceding 10 assessment years relevant to the current year
2. Has not been in India for a period of more than 729 days in immediately preceding year

For calculation of a day a period of 24 hours is taken into consideration, but where the time data is not available the date is counted as a full day.

Note: - If any of the above given additional condition is not satisfied but then the individual is said to be Resident but Not Ordinary Resident in India, but the additional condition shall be applicable and shall be checked only if the Basic Conditions are satisfied.

2. **Hindu Undivided Family**
   a. Resident
      i. Resident (or can be termed as Ordinary Resident)
      ii. Resident but Not Ordinarily Resident
   b. Non – Resident

For the First part that is whether resident or non-resident we need to apply the check of control & management, Control and Management wholly or partly is from India than the HUF becomes Resident else it is Non-Resident.

And for further division under the category of resident that an OR or NOR, Karta or the manager of the HUF need to satisfies the additional conditions same as given for the Individual, i.e. both the additional conditions need to be satisfied by the Karta of HUF in his individual capacity and if he satisfies then the HUF becomes Ordinary Resident, else the HUF is NOR.

3. **Company**
    a. Resident
    b. Non – Resident

    Indian Company's – Always resident in India

    Rest Body Corporate – if Control & Management is fully/wholly in India then Resident else Non-Resident

4. **Firm/ AOP/ BOI/ Local Authority/ Artificial Judicial Person (Residuary) {Rest}**
    a. Resident
    b. Non – Resident

    If the part control or management of the body is also done from India then it shall be resident in India.

INCOME CLASSIFICATION – INDIAN OR FOREIGN?

Since the act deals with the taxation in India and the revenue is for the Indian government hence an attempt is made in first to make each and every income as an Indian Income and thus the classification is done on the basis of Receipt of Income and Place of Accrual of Income.

- **Receipt Basis**: - Whenever the first receipt of Income is in India – the Income shall always be treated as Indian Income and shall always be taxable in India. [Note receipt may be hands of assessee himself or any other on behalf of the assessee, but this does not include remittance, i.e. transfer if money from one pocket to another, {Keshav Mills Ltd. Vs. CIT (1953)23 ITR 230 (SC)}, Nor merely passing a book entry would mean the Receipt of Income {CIT Vs. Toshuku Ltd. (1980) 125 ITR 525 (SC)}]

- **Accrual Basis**: - in this case the place of receipt of the Income is irrelevant; if the source of income is situated in India then the same shall be taxable in India.

For certain Income the direct relationship always exists but in some cases there is an Indirect relation and the person always wants to run away from the burden of the tax, and therefore there are certain deeming provisions in the act which entails out that in the listed case it shall be always be an Indian Income, The act list the provisions of the same in two heading, viz: -

1. Income Deemed to be Received in India (Sec. 7)
2. Income Deemed to Accrue or Arise in India (Sec. 9)

SPECIFIC INDIAN INCOME – SECTION 7 & 9

Income deemed to be received.

Sec. 7. The following incomes shall be deemed to be received in the previous year :—

(*i*) the annual accretion in the previous year to the balance at the credit of an employee participating in a recognised provident fund, to the extent provided in rule 6 of Part A of the Fourth Schedule ;

(*ii*) the transferred balance in a recognised provident fund, to the extent provided in sub-rule (4) of rule 11 of Part A of the Fourth Schedule ;

(*iii*) the contribution made, by the Central Government or any other employer in the previous year, to the account of an employee under a pension scheme referred to in section 80CCD.]

Income deemed to accrue or arise in India.

Sec. 9.(1) The following incomes shall be deemed to accrue or arise in India :—

(*i*) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India.

[*Explanation 1*].—For the purposes of this clause—

(*a*) in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India ;

(*b*) in the case of a non-resident, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in India for the purpose of export ;

(*c*) in the case of a non-resident, being a person engaged in the business of running a news agency or of publishing newspapers, magazines or journals, no income shall be deemed to accrue or arise in India to him through or from activities which are confined to the collection of news and views in India for transmission out of India ;

(*d*) in the case of a non-resident, being—

(*1*) an individual who is not a citizen of India ; or

(*2*) a firm which does not have any partner who is a citizen of India or who is resident in India ; or

(*3*) a company which does not have any shareholder who is a citizen of India or who is resident in India,

no income shall be deemed to accrue or arise in India to such individual, firm or company through or from operations[76] which are confined to the shooting of any cinematograph film in India.]

Explanation 2.—For the removal of doubts, it is hereby declared that "business connection" shall include any business activity carried out through a person who, acting on behalf of the non-resident,—

(*a*) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident, unless his activities are limited to the purchase of goods or merchandise for the non-resident; or

(*b*) has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or

(*c*) habitually secures orders in India, mainly or wholly for the non-resident or for that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident:

Provided that such business connection shall not include any business activity carried out through a broker, general commission agent or any other agent having an independent status, if such broker, general commission agent or any other agent having an independent status is acting in the ordinary course of his business:

Provided further that where such broker, general commission agent or any other agent works mainly or wholly on behalf of a non-resident (hereafter in this proviso referred to as the principal non-resident) or on behalf of such non-resident and other non-residents which are controlled by the principal non-resident or have a controlling interest in the principal non-resident or are subject to the same common control as the principal non-resident, he shall not be deemed to be a broker, general commission agent or an agent of an independent status.

Explanation 3.—Where a business is carried on in India through a person referred to in clause (*a*) or clause (*b*) or clause (*c*) of *Explanation 2*, only so much of income as is attributable to the operations carried out in India shall be deemed to accrue or arise in India;

Explanation 4.—For the removal of doubts, it is hereby clarified that the expression "through" shall mean and include and shall be deemed to have always meant and included "by means of", "in consequence of" or "by reason of".

Explanation 5.—For the removal of doubts, it is hereby clarified that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be and shall always be deemed to have been situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India

(*ii*) income which falls under the head "Salaries", if it is earned in India.

Explanation.—For the removal of doubts, it is hereby declared that the income of the nature referred to in this clause payable for—

(*a*) service rendered in India; and

(*b*) the rest period or leave period which is preceded and succeeded by services rendered in India and forms part of the service contract of employment,

shall be regarded as income earned in India ;

(*iii*) income chargeable under the head "Salaries" payable by the Government to a citizen of India for service outside India ;

(*iv*) a dividend paid by an Indian company **outside India** ;

(*v*) income by way of interest payable by—

(*a*) the Government ; or

(*b*) a person who is a resident, **except** where the interest is payable in respect of any debt incurred, or moneys borrowed and used, for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or

(*c*) a person who is a non-resident, **where** the interest is payable in respect of any debt incurred, or moneys borrowed and used, for the purposes of a business or profession carried on by such person in India ;

(*vi*) income by way of royalty payable by—

(*a*) the Government ; or

(*b*) a person who is a resident, **except** where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or

(*c*) a person who is a non-resident, **where** the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India :

Provided that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum consideration for the transfer outside India of, or the imparting of information outside India in respect of, any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process or trade mark or similar property, if such income is payable in pursuance of an agreement made before the 1st day of April, 1976, and the agreement is approved by the Central Government :

Provided further that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum payment made by a person, who is a resident, for the transfer of all or any rights (including the granting of a licence) in respect of computer software supplied by a non-resident manufacturer along with a computer or computer-based equipment under any scheme approved under the Policy on Computer Software Export, Software Development and Training, 1986 of the Government of India.

Explanation 1.—For the purposes of the first proviso, an agreement made on or after the 1st day of April, 1976, shall be deemed to have been made before that date if the agreement is made in accordance with proposals approved by the Central Government before that date; so, however, that, where the recipient of the income by way of royalty is a foreign company, the agreement shall not be deemed to have been made before that date unless, before the expiry of the time allowed under sub-section (1) or sub-section (2) of section 139 (whether fixed originally or on extension) for furnishing the return of income for the assessment year commencing on the 1st day of April, 1977, or the assessment year in respect of which such income first becomes chargeable to tax under this Act, whichever assessment year is later, the company exercises an option by furnishing a declaration in writing to the Assessing Officer (such option being final for that assessment year and for every subsequent assessment year) that the agreement may be regarded as an agreement made before the 1st day of April, 1976.

Explanation 2.—For the purposes of this clause, "royalty" means consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital gains") for—

(*i*) the transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property;

(*ii*) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar *property;

(*iii*) the use of any patent, invention, model, design, secret formula or process or trade mark or similar property;

(*iv*) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill ;

(*iva*) the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in section 44BB;

(*v*) the transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting, but not including consideration for the sale, distribution or exhibition of cinematographic films ; or

(*vi*) the rendering of any services in connection with the activities referred to in sub-clauses (*i*) to [85][(*iv*), (*iva*) and] (*v*).

Explanation 3.—For the purposes of this clause, "computer software" means any computer programme recorded on any disc, tape, perforated media or other information storage device and includes any such programme or any customized

With Best Wishes
Vivek Mehta (CA, CS, MBA)
Ph: +91-9413118508
E-mail: - vivekmehta@icai.org, cavivekmehta@gmail.com

electronic data;

(*vii*) income by way of fees for technical services payable by—

(*a*) the Government ; or

(*b*) a person who is a resident, **except** where the fees are payable in respect of services utilised in a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or

(*c*) a person who is a non-resident, **where** the fees are payable in respect of services utilised in a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India :

Provided that nothing contained in this clause shall apply in relation to any income by way of fees for technical services payable in pursuance of an agreement made before the 1st day of April, 1976, and approved by the Central Government.]

Explanation 1.—For the purposes of the foregoing proviso, an agreement made on or after the 1st day of April, 1976, shall be deemed to have been made before that date if the agreement is made in accordance with proposals approved by the Central Government before that date.

Explanation 2.—For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries".

(2) Notwithstanding anything contained in sub-section (1), any pension payable outside India to a person residing permanently outside India shall not be deemed to accrue or arise in India, if the pension is payable to a person referred to in article 314 of the Constitution or to a person who, having been appointed before the 15th day of August, 1947, to be a Judge of the Federal Court or of a High Court within the meaning of the Government of India Act, 1935, continues to serve on or after the commencement of the Constitution as a Judge in India.

Explanation.—For the removal of doubts, it is hereby declared that for the purposes of this section, income of a non-resident shall be deemed to accrue or arise in India under clause (*v*) or clause (*vi*) or clause (*vii*) of sub-section (1) and shall be included in the total income of the non-resident, whether or not,—

(*i*) the non-resident has a residence or place of business or business connection in

India; or (*ii*) the non-resident has rendered services in India.

Note: - Section 7 enlist only 3 income but the income falling under the section 68, 69, 69A, 69B & 69C, and further deemed income under section 41 and 59 shall also be always deemed to be received in India.

Section 9

The income deemed to accrue or arise in India can be broadly classified in 9 parts of which first 6 parts are taxable on the basis of Territorial Nexus (i.e. the first 6 parts has relation with the place of Working or generation of Income) and whereas the remaining 3 are liable for deemed to accrue or arise in India on the basis of Payer Nexus.

S. No.	Particulars	Whether Indian Income or Not?
1.	Income from Business Connections in India. (Important to Note the meaning of Business Connection in India, it is separately discussed bellow the table)	Yes
2.	Income from any Property Situated in India	Yes
3.	Income from transfer of any capital asset situated in India	Yes
4.	Income from Salaries for Services Rendered in India	Yes
5.	Income from Salaries paid to Indian Citizen by Government of India for Working Abroad.	Yes
6.	Income from Dividend of an Indian Company. (Important to Note Dividend has be defined under the Act u/s 2 (22) and there are total 5 types of Dividend of Which 4 are exempt by the virtue of payment of CDDT on the same and rest is taxable.)	Yes

Payer\Income	7. Interest	8. Royalty	9. Fee for Technical or Professional Services

1. Any Government of Indian Territory	Yes	Yes	Yes
2. Non-Resident Condition: - For Taxability in India as Deemed to accrue or Arise in India for Payee: - That is the money payment is related to the use for any business activity carried on in India.	Yes	Yes	Yes
3. Resident Condition: - For Taxability in India as Deemed to accrue or Arise in India for Payee: - That is the money payment is related to the use for any activity but not for a business activity carried on by it outside India.	Yes	Yes	Yes

Meaning of Business Connection In India

Business Connection involves a relation between a business and its entity wherein the business is carried on by any which yields profits or gains and some activity in India which contributes to the earnings of the Business Entity.

Broadly speaking if any of the following condition is satisfied then it is said and deemed that the organisation has certain business connection in India: -

1. Has a Permanent Establishment: - It means a fixed place of business through which the business of an enterprise is wholly or partly carried on. This especially includes:
    a. a place of management ;
    b. a branch ;
    c. an office ;
    d. a factory ;
    e. a workshop ;
    f. a mine, an oil or gas well, a quarry, or any other place of extraction of natural resources;
    g. a warehouse, in relation to a person providing storage facilities for others ;
    h. a farm, plantation or other place where agriculture, forestry, plantation or related activities are carried on ;
    i. a store or premises used as a sales outlet ;

j. an installation or structure used for the exploration or exploitation of natural resources, but only if so used for a period of more than 120 days in any twelve-month period ;
k. a building site or construction, installation or assembly project or supervisory activities in connection therewith, where such site, project or activities (together with other such sites, projects or activities, if any) continue for a period of more than 120 days in any twelve-month period ;
l. the furnishing of services, other than Royalties and Fees for Included Services, within a Contracting State by an enterprise through employees or other personnel, but only if:
   i. activities of that nature continue within that State for a period or periods aggregating more than 90 days within any twelve-month period ; or
   ii. the services are performed within that State for a Related Enterprise/ Associated Enterprises.

But "Permanent Establishment" does not to include the following:

a. the use of facilities solely for the purpose of storage, display, or occasional delivery of goods or merchandise belonging to the enterprise ;
b. the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display, or occasional delivery or for processing or for collecting information or Purchases for the purpose of Export to Home Country ;
c. the maintenance of a fixed place of business solely for the purpose of advertising, for the supply of information, for scientific research or for other activities which have a preparatory or auxiliary character, for the enterprise.

2. Maintains a Ware-house to store stock or merchandise for supply/ delivery of the orders within the Indian Territory.
3. Maintains a Place to Procure/Receive/ Process the Order of Goods on Behalf of a NR for Supply/ Delivery.

TAXABILITY ON THE BASIS OF RESIDENTIAL STATUS

Nature of Income	OR	NOR	NR
Class I - (Indian income)			
1. Income received, & or deemed to be received in India	T	T	T
2. Income accruing, & or arising or deemed to be accrue or arise in India	T	T	T

With Best Wishes
Vivek Mehta (CA, CS, MBA)
Ph: +91-9413118508
E-mail: - vivekmehta@icai.org, cavivekmehta@gmail.com

Class II - (Foreign income)			
1. Income from a business controlled from India or a profession setup in India	T	T	NT
2. Any other income	T	NT	NT

METHOD OF ACCOUNTING [SEC. 145]

Income under the head, "Profits & gains of business / profession" and "Income from other sources

(Taxable income shall be computed in accordance with either cash or mercantile system of accounting, *regularly* employed by the assessee)

Income under any other head

Method of accounting is irrelevant

&

Taxable income shall be computed as per statutory provisions of the Income Tax Act.

APPLICABILITY OF ACCOUNTING STANDARD (AS)

1. U/s 145(2) the Central Government has power to notify A.S. to be followed by any class of assesses or in respect of any class of income.
2. The Central Government has notified following A.S. applicable to all assessee *following mercantile system* of accounting.
   I. Disclosure of accounting policies.
   II. Disclosure of prior period and extra-ordinary items and changes in accounting policies.

With Best Wishes
Vivek Mehta (CA, CS, MBA)
Ph: +91-9413118508
E-mail: - vivekmehta@icai.org, cavivekmehta@gmail.com