OUTLINE: -

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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.) “MEANS”: 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.) “INCLUDES”: 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.) “MEANS AND INCLUDES”: 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” ***includes***—

(*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*) ***any capital gains* 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.

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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.
- 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.
- 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***
   - **Oberoi Hotel (P) Ltd. Us. CIT (1999) 152 CRT 474 (SC)**
   - **CIT vs. Bombay Burmah Trading Corporation Ltd. (1986) 58 CTR 144 (SC): (1986) 161 ITR 386 (SC)**
- ***Incentive And Subsidy Whether Capital Or Revenue:* -** Subsidy/Assistance which is directly connected with the business activities of the assessee shall form the part of the business receipt and hence it is Revenue Receipt
   - **CIT v. Kisan Sahkari Chini Mills Ltd. [2006] 284 ITR 418.**
   - **Sahney Steel and Press Works Ltd. V. CIT [1997] 228 ITR 253.**
   - **CIT v. Rajaram Maize Products [2001] 251 ITR 427.**
- ***Damages Whether Capital Or Revenue***: - If the damages are to compensate the Capital Loss or Asset, it shall be Capital Receipt and if the compensation is for the loss suffered in business activity, it shall form Revenue Receipt.
   - **CIT VS Saushatra Cement Ltd. [2010] 325 ITR 422 (SC)**
   - **CIT v. Rai Bahadur Jairam Valji [1959] 35 ITR 148 (SC)**
   - **Kettlewell Bullen and co. Ltd. V. CIT [1964] 54 ITR 261; AIR 1965 (SC) 65.**
- ***Loss Of Agency – Compensation Received*: -** After the amendment under section 28, w.e.f. 1.4.2003, the compensation for loss of agency or a Non-Compete Fee shall always and always be treated as Revenue Receipt.
   - **Guffic Chem P. Ltd. VS CIT [2011] 17ITCD131 (SC);[2011] 332ITR602 (SC).**
   - **CIT, Nagpur v. Rai Bahadur Jairam Valji (35 ITR 148)**
- ***Amount Received For Loss Of Reputation And Goodwill:* -** It shall be treated as Capital Receipt.
- ***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.
   - **CIT VS. DINESS BUSIENSS SERVICE P. LTD. (2003) ITR 1 (BOM)**
   - **CIT VS. WIAA CLUB LTD. (1982) 136 ITR 569 (BOM)**
   - **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 capital Receipt.
   - **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 **any sum** is found **credited in the books** of an assessee maintained for any previous year, and the assessee offers no explanation about the nature and source thereof or the **explanation** offered by him **is not**, in the opinion of the Assessing Officer, **satisfactory, the sum so credited may be charged to income-tax as the income** 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 **otherwise than through an account payee cheque** drawn on a bank, the amount so borrowed or repaid shall be deemed to be the income 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*): -

"**person**" *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

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 being newly set-up	Beginning with the date of setting up of the business & ending on 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	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.)

	to India.	
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 under the Income Tax Act.	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.)
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

1. Residential status of a person determines the total income of an assessee chargeable to tax
2. It is a different concept citizenship of any person
3. It has to be seen for each and every year separately.
4. A person can be resident in more than one country at a time, and hence the ounce and liability to prove his residential status in the country is of the assessee.

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

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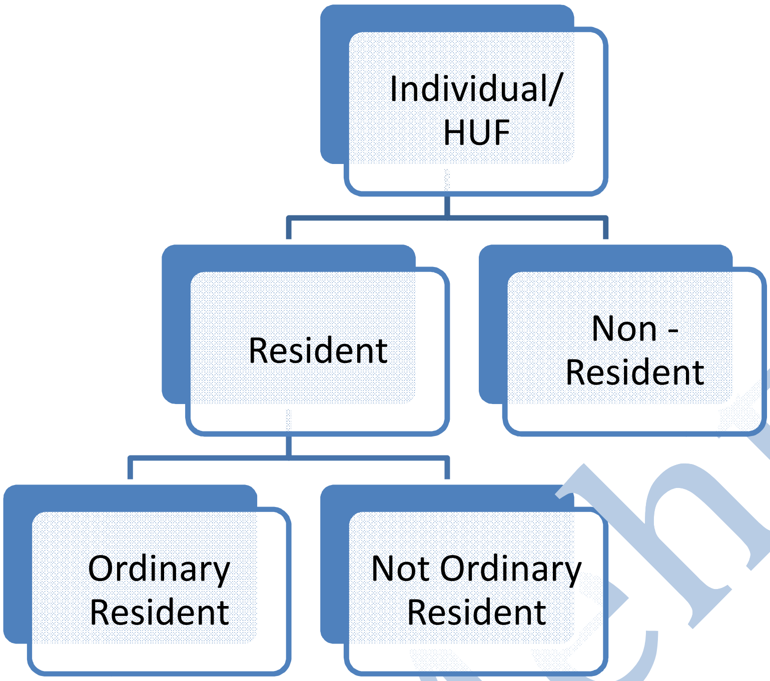

1. **Individual:**
    a. Resident
        i. Resident (or can be termed as Ordinary Resident)
        ii. Resident but Not Ordinarily Resident
    b. Non – Resident

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 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	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	Person Covered: - - others than those who have not been covered in I and II

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employment	India	
period or periods amounting in all of stay in India: - Atleast 182 days in the relevant previous year	period or periods amounting in all of stay in India: - Atleast 182 days in the relevant previous year	period or periods amounting in 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

Or the above Conditions can be presented in the following manner

3. He must be Resident in India for atleast 2 out of 10 immediate preceding years
4. He must have stayed in India for total period of atleast 730 days in immediately preceding 7 years.

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.

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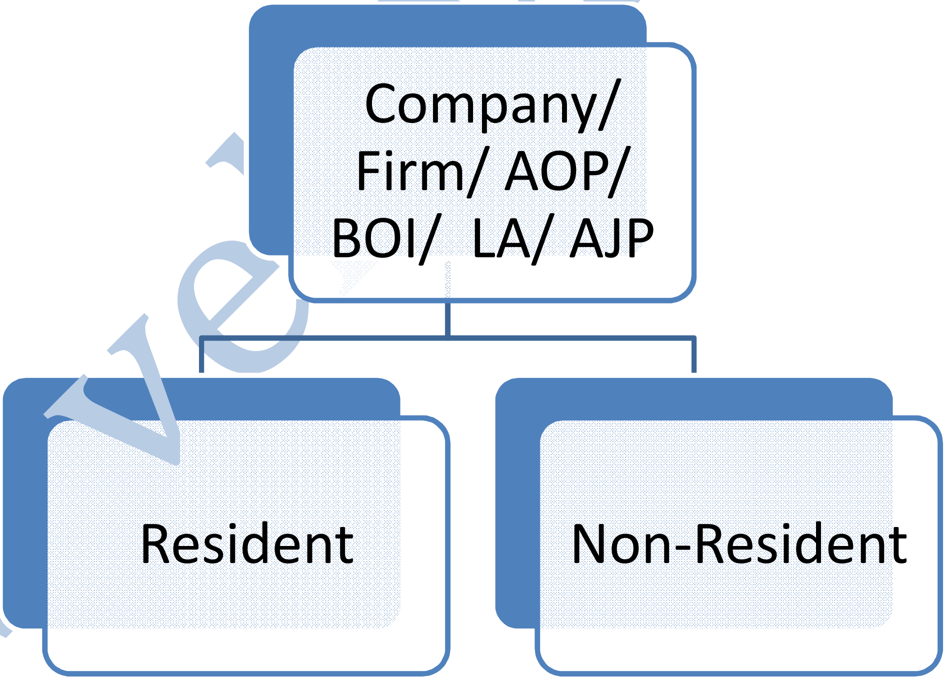
2. **Hindu Undivided Family**
    a. Resident
        i. Resident (or can be termed as Ordinary Resident)
        ii. Resident but Not Ordinarily Resident
    b. Non – Resident

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 are 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

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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?

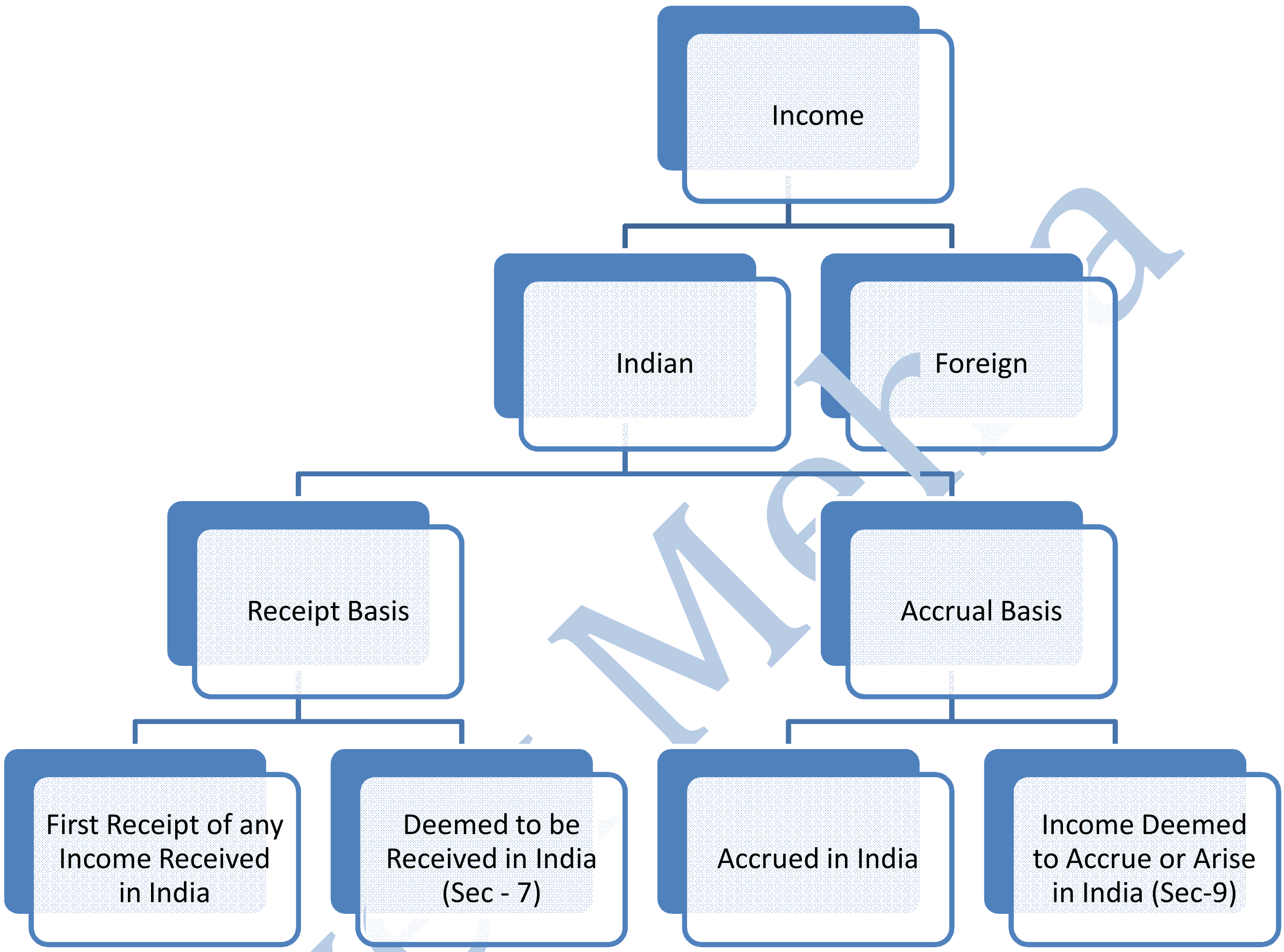
Since the act deals with the taxation in India and the revenue is for the Indian government hence an attempt is made in first to make each and every income as an Indian Income and thus the classification is done on the basis of Receipt of Income and Place of Accrual of Income.

- **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.]

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 includes:
   a. a place of management ; a branch ; an office ; a factory ; a workshop ; a mine, an oil or gas well, a quarry, or any other place of extraction of natural resources; a warehouse, in relation to a person providing storage facilities for others ; a farm, plantation or other place where agriculture, forestry, plantation or related activities are carried on ; a store or premises used as a sales outlet ; an installation or structure used for the exploration or exploitation of natural resources ; 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) ; 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 "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.

But Business Connection In India does not includes: -

1. Purchases of Goods from India for the purpose of Export to Home Country and selling it in Home Country. (Means Import of Goods for selling outside India)
2. Collection of News and Views from India by a NR Organization.
3. Shooting of any cinematographic film in India for the purpose of realizing it abroad and non of the interested party should be resident in India.

TAXABILITY ON THE BASIS OF RESIDENTIAL STATUS

Nature of Income	**R**		**NR**
	OR	**NOR**	
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
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.

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.