

# **BUSINESS TAXATION**

**MBA 4<sup>th</sup> Sem.-18MBA401B**

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## **MODULE - I**

### **BASIC CONCEPTS, MEANING AND DEFINITION**

#### **Meaning of tax**

The tax is a compulsory payment that has to be made by individual or other persons to central government, state government or local government. Tax is based on certain will establishment rules or criteria such as income earned, property owned or expenditure made.

#### **Direct and indirect tax**

Direct tax is a payment directly made to the state by the person who bears it.  
Indirect tax is a tax which is paid by one person and borne by another person.

#### **Income tax act**

The income tax act of 1961 has been in effect from the first day of April 1962 (sec 1). It contains 298 sec, sub sections, schedules etc. the income tax rules of 1962 was framed by **central board of Direct Taxes (CBDT)**

#### **Assessment year (sec 2(9))**

Assessment year may be defined as a year in which the income tax of the previous year is to be assessed. It is a period of twelve months starting from April 1 of every year and ending on March 31 of the next year.

#### **Previous year (sec 3)**

For the purposes of this Act, the term “previous year” means that the financial year immediately preceding the assessment year .... Under Income Tax, the returns are filed by assesses after end of the year/ period during which earnings are made and that period is called as previous year/ financial year.

#### **Definition of 'Assessee'**

Section 2(7) of Income Tax Act. As per S. 2(7) of the Income Tax Act, 1961, unless the context otherwise requires, the term “**Assessee**” means a person who is responsible for payment of any tax or any other sum of money under this Act, and includes

#### **Person 2(31)**

It includes an individual and Hindu Undivided Family (HUF), Company, Firm, Association of Person (AOP), Body of Individual (BOI) Local Authority & Artificial Juridical Persons.

#### **AGRICULTURAL INCOME (SEC 2(1A))**

In India, agricultural income refers to income earned or revenue derived from sources that include farming land, buildings on or identified with an agricultural land and commercial produce from a horticultural land. Agricultural income is defined under section 2(1A) of the Income Tax Act, 1961.

#### **Different types of Agricultural Income**

- Rent or Revenue Derived from land.
- Income from Agriculture Operations.
- Income from Farm House/Building Attached to Agricultural Land.

### Non-agricultural income from land

- Income from markets
- Income from stone quarries
- Income from mining royalties
- Income from land used for storing agricultural produce
- Income from supply of water for irrigation purpose
- Income from self-grown, grass and trees
- Income from fisheries
- Remuneration received as manager of an agricultural farm
- Income from interest on arrears of rent of agricultural land

## INCOME EXEMPTED FROM TAX

### Meaning and importance of residential status

The taxability of an individual in India depends upon his residential status in India for any particular financial year. The term residential status has been coined under the income tax laws of India and must not be confused with an individual's citizenship of India. An individual may be a citizen of India but may end up being a non-resident for a particular year. Similarly, a foreign citizen may end up being a resident of India for income tax purposes for a particular year.

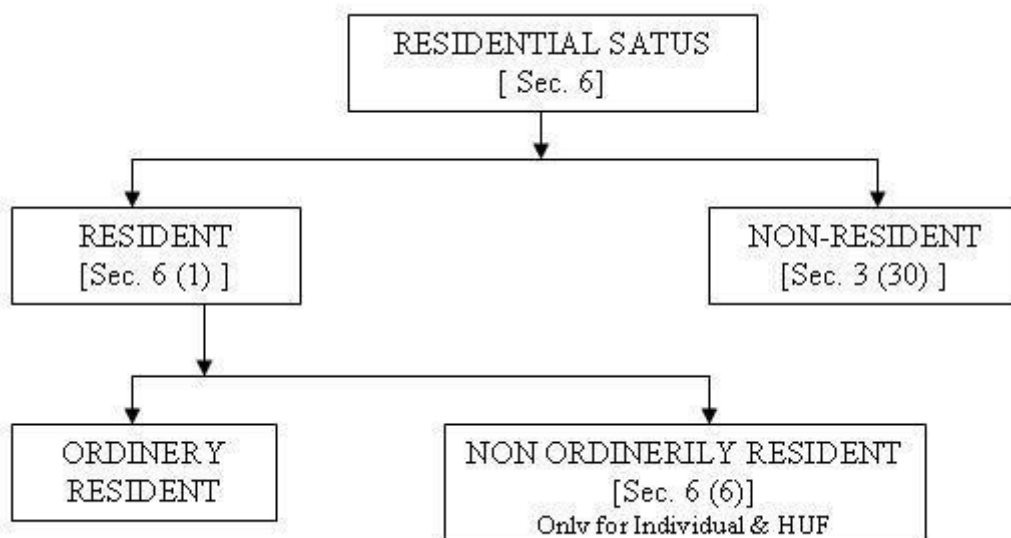
Also to note that the residential status of different types of persons via an individual, a firm, a company etc is determined differently in this article, we have discussed about how the residential status of an individual taxpayer can be determined for any particular financial year

### How to determine residential status?

For the purpose of income tax in India, the income tax laws in India classify taxable persons as:

- A resident
- A resident not ordinarily resident (RNOR)
- A non-resident (NR)

The taxability differs for each of the above categories of taxpayers. Before we get into taxability, let us first understand how a taxpayer becomes a resident, an RNOR or and NR.



### **Resident**

A taxpayer would be qualified as a resident of India if he satisfies any one of the following 2 conditions:

- Stay in India for a year is 182 days or more
- Stay in India for the immediately 4 preceding years is 365 days or more and 60 days or more in the relevant financial year

In the event an individual leaves India for employment during an FY, he will be qualified as a resident of India only if he stays in India for 182 days or more. else the condition (b) above 60 days will not apply to him

### **Resident Not Ordinarily Resident**

If an individual qualifies as a resident, the next step is to determine if he/she is a Resident ordinarily resident (ROR) or an RNOR. He will be a ROR if he meets both the following conditions:

- Has been a resident of India For at least 2 out of 10 years immediately, For the previous years
- Has stayed in India for at least 730 days in 7 immediately after the preceding years

Therefore, if any individual fails to satisfy even one of the above conditions, he would be an RNOR.

### **Non-resident**

An individual satisfying neither of the conditions stated in (a) or (b) above would be an NR for the year.

### **Taxability**

#### **Resident:**

A resident will be charged to tax in India on his global income i.e. income earned in India as well as the income earned outside India.

#### **NR and RNOR:**

Their tax liability in India is restricted to the income they earn in India. They are not in need to pay any tax in India on their foreign income.

Also note that in case of double taxation of income where the same income is getting taxed in India as well as in abroad, one may resort to the Double Taxation Avoidance Agreement (DTAA) that India would have entered into with the other country in order to eliminate the possibility of paying taxes twice.

### **Scope of total income**

Section -5 of Income Tax Act, 1961 provides Scope of total Income in case a person who is a resident, not an ordinarily resident in India and person who is a non-resident which includes. Income can be Income from any source which (a) is received or is deemed to be received in India in such year by or on behalf of such person; or (b) accrues or arises or is deemed to accrue or arise to him in India during such year; or (c) accrues or arises to him outside India during such year.

**Table explaining Scope of total Income under section 5 of Income Tax Act, 1961**

Sr. No	Particulars	Resident Ordinary Resident (ROR)	Resident Ordinary Resident (RNOR) – 5(1)	Not Resident (NR)– 5(2)
1	Income received in India	Taxed	Taxed	Taxed
2	Income Deemed to be receive in India	Taxed	Taxed	Taxed
3	Income accrues or arises in India	Taxed	Taxed	Taxed
4	Income deemed to accrues or arises in India	Taxed	Taxed	Taxed
5	Income accrues or arises outside India	Taxed	NO	NO
6	Income accrues or arises outside India from business/profession controlled/set up in India	Taxed	Taxed	NO
7	Income Other than Above (No Relation In India)	Taxed	NO	NO

Note-

1. Residential status is as per section 6 of Income Tax Act, 1961.
2. Deemed income is not actually accrued but is supposed to be accrued notionally.
3. The income accrued is when the assessee obtains the rights to receive it.
4. Previous year means the financial year immediately preceding the assessment year.

Explanation 1 & 2:-

Income accruing or arising outside India shall not be deemed to be received in India within the meaning of this section by reason only of the fact that it is taken into account in a balance sheet prepared in India.

Income which has been included in the total income of a person on the basis that it has accrued or arisen or is deemed to have accrued or arisen to him shall not again be so included on the basis that it is received or deemed to be received by him in India.

**Certain Examples of incomes which treated as incomes deemed to have accrued or arisen in India:**

- If Mr. X Transfer his Residential Property situated in Delhi then Capital gain arising on transfer of such Capital Asset is deemed to accrue in India. It means Capital gain arising on transfer of property situated in India.
- Income from business connection in India.
- Dividend paid by an Indian company.
- Income from any property, asset or other source of income located in India.

## EXERCISES

Mr. Rajan left India for the first time on 15<sup>th</sup> December 2018 and returned back to India on 2<sup>nd</sup> February 2019. Identify his residential status for the assessment year 2019-20.

### Solution:

Mr. Rajan Singh will get the status "Ordinary Resident", since he satisfies the first basic condition and both the additional conditions.

MR. Williams is an Indian citizen who lives, in India since 1984. During the previous year 2019-2020 he went to Arabia for 325 days. Identify the residential status.

### Solution:

Mr. Williams will get the status "Non-Resident", since he not satisfy the basic conditions itself as he had stayed only for 40 days in the previous year 2019-2020.

From the following details calculate the total income of Mr. Raja, if he is OR, NOR and NR

- dividend from Indian company rs 1,00,000
- dividend from foreign company rs 1,50,000, received in India
- income from business in Kenya but controlled from India rs, 2,00,000
- income accrued in Switzerland rs, 2,50,000, 2/5<sup>th</sup> received in India
- income from business in Indonesia but controlled from Bangladesh rs, 5,00,000

### Solution:

#### Calculation of taxable income of Mr. Raja

S.No	Income	O.R	N.O.R	N.R.
1	Dividend from Indian company	-	-	-
2	Dividend from foreign company, received in India	1,50,000	1,50,000	1,50,000
3	Income from business in Kenya but controlled from India	2,00,000	2,00,000	2,00,000
4	income accrued in Switzerland a. 2/5 received in India {2,50,000*2/5} b. Balance 1,50,000	1,00,000  1,50,000	1,00,000  -	1,00,000  -
5	Income from business in Indonesia but controlled from Bangladesh	5,00,000	-	-
	<b>Total income</b>	<b>11,00,000</b>	<b>4,50,000</b>	<b>2,50,000</b>

Mr. Sunil earns the following income during the previous year 2018-19

- a. Interest from an Indian company received in Germany rs, 1,00,000
- b. Pension from former employer in India received in U.K. Rs, 2,00,000
- c. Income from companies in USA and received in India 1,00,000
- d. Income from agriculture in USA and received in India 10,000
- e. Income from employment in Japan received there rs, 20,000
- f. Past untaxed profits brought to India rs, 50,000

Compute GTI of Sunil for the assessment year 2019-20 if he is,

- i. Resident
- ii. Not ordinarily resident
- iii. Non resident

**Solution:**

**Calculation of taxable income of Mr.Sunil**

Sr	Income	O.R	N.O.R	N.R.
1	Interest from an Indian company received in Germany	1,00,000	1,00,000	1,00,000
2	Pension from former employer in India received in U.K	2,00,000	2,00,000	2,00,000
3	Income from companies in USA and received in India	1,00,000	1,00,000	1,00,000
4	Income from agriculture in USA and received in India	10,000	10,000	10,000
5	Income from employment in Japan received there	20,000	-	-
6	Past untaxed profits brought to India Rs, 50,000	-	-	-
	Total income	4,30,000	4,10,000	4,10,000

## **MODULE -2**

### **INCOME FROM SALARY**

#### **Salary**

Salary comes into existence as a result of employer-employee relationship. In a employer-employee relationship, employee performs his duties and the employer provides him salary.

#### **Allowances**

Allowances are part of salary given to employees to meet some particular requirements such as house rent, conveyance, etc. Allowances may be fully taxable, partially taxable or fully exempt.

#### **House Rent Allowance [S. 10(13A) & Rule 2A]**

The least of the following is exempt from tax:

- 50% of salary, (residential house situated at Mumbai, Kolkata, Delhi or Chennai) and 40% of salary where residential house is situated at any other place;
- Actual house rent allowance received by the employee;
- Excess of rent paid over 10% of salary

#### **Leave Encashment [S. 10(10AA)]**

Encashment of earned leave while in service will be treated as income. S. 17(1)(v)(a).

Encashment of earned leave on retirement would however, be exempt to the extent of least of:

- 10 months' salary calculated on the basis of last 10 months average salary or
- Rs. 3,00,000
- Amount equivalent to earned leave
- Actual amount paid by the employer

Entitlement of earned leave should not exceed 30 days for every year of actual service. Limits provided for aggregate maximum from any number of employers. Encashment of earned leave on retirement would be wholly exempt for employees of Central/State Government.

#### **Special Allowances [S. 10(14)]**

Following prescribed special allowances are exempt:

- Allowance, not in the nature of perquisite, granted to meet expenses wholly, necessarily and exclusively incurred in the performance of duties, to the extent to which actually incurred.
- Allowance granted to meet personal expense at the place where duties of his office are ordinarily performed or at the place where he ordinarily resides or to compensate for increased cost of living as may be prescribed in Rule 2BB.

#### **Nature of allowance prescribed under Rule 2BB**

- For cost of travel on tour or on transfer,
- For ordinary daily charges on account of absence from normal place of duty on tour or for journey in connection with transfer,
- For conveyance in performance of duties, where free conveyance is not provided,
- For expenditure on helper engaged for performance of office duties,

- For encouraging academic, research and training pursuits in educational and research institutions,
- For purchase or maintenance of uniform,
- Special Compensatory Allowance in specified areas to extent specified,
- Tribal Area Allowances in specified states up to Rs. 200 p.m.
- For meeting personal expenditure of employee of transport system running transport vehicle, up to 70% of allowance, maximum of Rs. 6,000 p.m., provided no daily allowance for the said duty is received.
- Children educational allowance @ Rs. 100 p.m. per child, maximum of two children,
- Children hostel allowance @ Rs. 300 p.m. per child, maximum of two children,
- Compensatory Field Area Allowance in specified areas, @ Rs. 2,600 p.m.
- Compensatory modified field area allowance @ Rs. 1,000 p.m.
- Counter insurgency allowance @ Rs. 3,900 p.m. to members of armed forces.
- Transport allowance (TA) granted to meet expenses for commuting between place of residence and place of duty is exempt up to Rs. 800 per month and TA received by blind or orthopedically handicapped is exempt up to Rs. 1,600 per month.
- Underground allowance granted to employee of underground coal mines: Rs. 800 per month.
- Special allowance in the nature of high altitude to members of armed forces: Rs. 1,060 per month for altitude of 9,000 to 15,000 ft. or Rs. 1,600 per month for altitude above 15,000 ft.
- Special compensatory highly active field area allowance to members of armed forces Rs. 4,200 per month.
- Island (duty) allowance to members of armed forces – Rs. 3,250/- per month.
- Perquisites
- Perquisites are benefits such as rent free accommodation, company's car, etc
- Perquisites may be provided in cash or in kind.
- Reimbursement of expenses incurred during office work is not a part of perquisites.
- Unauthorized benefits obtained do not form part of Perquisites
- Perquisites may be fully taxable, partially taxable or fully exempt.
- Fully and Partially Taxable Perquisites

#### **Perquisites not taxable in all cases**

The following perquisites are not taxable under CBDT instructions or by virtue of the Act/Rules:

- The provision of medical facilities as per Para 4(i).
- Free meals provided to all employees in office up to Rs. 50 per employee provided by the employer through paid vouchers usable at eating joints.
- Telephone including mobile phone provided to the employee.
- Perquisites allowed outside India by the Government to a citizen of India for rendering services outside India.
- Sum payable by an employer to pension or deferred annuity scheme.
- Employer's contribution to staff group insurance scheme.
- Actual travelling expenses paid/reimbursed for journeys undertaken for business purposes.
- Payment of annual premium on personal accident policy, if such policy is taken to safeguard the employer's interest. See *CIT vs. Lala Shri Dhar* (1922) 84 ITR 192 (Delhi).
- Rent-free official residence to a High Court or Supreme Court Judge.

- Rent-free furnished residence to official of Parliament.
- Conveyance facility to High Court/Supreme Court Judges.

#### **Perquisites taxable in hands of all employees:**

- Value of rent-free accommodation.
- Value of concession in rent.
- Amount paid by employer in respect of any obligation which otherwise would have been payable by employee.
- Value of any security or sweat equity shares allotted or transferred by employer/former employer as free or concessional cost.
- An amount of contribution to an approved superannuation fund by the employer, to an extent it excess Rs. 1, 00,000/-.
- Any sum payable either directly or through a fund by employer (other than recognized PF, approved superannuation fund etc.) to effect an assurance on the life of the employee or to affect a contract for an annuity.

#### **Determination of the value of prescribed fringe benefit or amenityInterest free or concessional loan**

Value of perquisite w.e.f. 1-4-2000, of the loan given to the employee or any member of his household shall be at the rates charged by State Bank of India in respect of the loans for the same purpose advanced by the employer, on the maximum outstanding monthly balance as reduced by interest actually paid by employee – However, perquisite value for loans (net of amount reimbursed under medical insurance scheme) given for medical treatment of specified disease or petty loans up to Rs. 20,000 is not taxable.

#### **Use of movable assets**

Value of benefit shall be 10% p.a. of the actual cost of asset or the rent charges paid by the employer as reduced by amount paid by the employee.

#### **Transfer of movable assets**

Value of benefit on transfer of movable asset shall be the actual cost of the asset to the employer as reduced by the amount calculated at 10% of such cost for each completed year of use by the employer and further reduced by the payments made by the employee. The normal wear and tear would be computed at 50% in case of computers and electronic items, and 20% in case of motor cars on the reducing balance method.

#### **Perquisites taxable only in hands of specified employees**

Other perquisites are taxable only in the hands of the following specified employees; i.e.,

- Director-employee
- Employee having substantial interest in employer-company
- Employee drawing salary in excess of Rs. 50,000

#### **Rent free accommodation:**

The rent free accommodation provided to employees by their employer is taxable. Since the employees are provided rent free accommodation, the amount of income accruing to them cannot be determined by them. Accordingly, there is prescribed manner for calculating income

chargeable to tax as perquisite. The manner of calculating income chargeable to tax as perquisite for rent free accommodation is as follows:

Category of Employees	Income	
	Unfurnished Accommodation	Furnished Accommodation
1) Provided to a Judge of High Court, Supreme Court 2) Provided to an Officer of Parliament	In case of Rent free Official Residence: Nil	In case of Rent Free Official Residence: Nil
Provided to Central/ State Government employees	(a) License fees determined by the Central/ State Government	(a) Same as Unfurnished Accommodation (b) 10% p.a. Of the cost of furniture If such furniture is hired, then hire charges payable.
Provided to any other employee		
1) Where the accommodation is owned by the employer	(i) 15% of salary in cities having population exceeding 25,00,000 (ii) 10% of salary in cities having population between 10,00,000 and 25,00,000 (iii) 7.5% of salary in other areas	(a) Same as Unfurnished Accommodation (b) 10% p.a. Of the cost of furniture If such furniture is hired, then hire charges payable.
2) Where the accommodation is taken on rent by the employer	Lower of the following: (i) Rent Payable Or (ii) 15% of salary	(a) Same as Unfurnished Accommodation (b) 10% p.a. Of the cost of furniture If such furniture is hired, then hire charges payable.
Accommodation provided in a hotel	Not Applicable since Hotel is presumed to be furnished.	Lower of the following: (i) 24% of salary (ii) Rent (Room Fare/ Charges) Payable

**Concession in rent:**

Some employers provide the employees with accommodation at rates lower than normal market rates. This reduction in rates is known as concession in rent.

**Payment by the employer in respect of an obligation of employee:**

In this case, the amount is liable to be paid by the employee and the employer pays the same.

**Example:** Self Assessment Tax of the employee is paid by the Employer.

**Note:** If the employer pays taxes on behalf of employees on non-monetary perquisites provided to them, then such taxes are exempt in the hands of the employee.

**Valuation of benefit of provision of domestic servants**

If the employee or any member of his household is provided with domestic servants such as sweeper, gardener, watchman or personal assistant then the benefits so received by the employee are taxable as perquisites in the hands of the employee.

**Utility such as gas, electricity or water supplied by employer**

If the employer pays to the utility provider on behalf of the employee or if the employer himself provides such utilities then the benefits so received by the employee are taxable as perquisites in the hands of the employee.

**Free or concessional educational facilities**

If the employer provides free or concessional educational facilities from the educational institutions maintained and owned by the employer or if free educational facilities are allowed in any other educational institution then the benefits so received by the employee are taxable as perquisites in the hands of the employee.

However, if the educational institution is maintained and owned by the employer and the employer provides free or concessional education facilities to the employee himself or his children and the benefits so received by the employee does not exceed Rs. 1,000/- per month then such amount shall not be taxable in the hands of the employee as perquisite.

**Interest-free or concessional loan**

The value of the benefit to the employee as a result of interest-free loan or concessional loan for any purpose provided to the employee or any member of his household is a taxable perquisite.

However, this perquisite will be not being chargeable to tax in any of the following cases:

- If such loan is provided for the purpose of treatment of diseases such as cancer, tuberculosis, etc. However, out of the amount of loan provided, if the employee receives reimbursement from any medical insurance scheme, then such amount shall not be exempt.
- Amount of loans made to an employee does not exceed Rs. 20,000/-.

### **Free or concessional food and non-alcoholic beverages**

If the employer provides free or concessional food and/ or beverages such as tea, coffee etc., then the benefits so received by the employee are taxable as perquisites in the hands of the employee. However, if the following are provided by the employer then they are not taxable in the hands of employees as perquisites:

- Free food and beverages such as tea, coffee etc. provided by the employer to an employee during working hours at office or business premises less than Rs. 50/- per meal.
- Vouchers provided having value less than Rs. 50/- per meal
- Tea or Snacks provided during working hours
- Free food and beverages such as tea, coffee etc. provided during working hours provided in a remote area or an offshore installation.

### **Gifts or Vouchers**

Gift or vouchers received by employees or by member of his household on ceremonies or occasions are taxable perquisites in the hands of the employees. However, if the value of such gifts in totality does not exceed Rs. 5,000/- then such gifts are not taxable as perquisite in the hands of the employees.

### **Reimbursement of credit card expenses**

If the employer reimburses expenses incurred by the employee or any member of his household using a Credit card then the benefits so received by the employee are taxable as perquisites in the hands of the employee.

However, if such expenses are made by the employee exclusively for official purposes and the employer has documented the expenses incurred using the credit card then such reimbursements are not taxable as perquisite in the hands of the employees.

### **Club expenditure**

If the employer pays or reimburses for the periodic subscription of a club for the employee or any member of his household then the benefits so received by the employee are taxable as perquisites in the hands of the employee.

However, if the following are provided by the employer then they are not taxable in the hands of employees as perquisites:

- If the use of health club, sports and such facilities are provided uniformly to all employees by the employer.
- Such expenditure is incurred wholly and exclusively for business purposes and if the expenditure is properly documented by the employer.

### **Gratuity**

Gratuity is a payment received by an employee by his employer as a gratitude for the employee's services to the organization. It is over & above normal salary & other retirement benefits received by an employee.

#### **Taxability of Gratuity**

##### **Pension**

Pension means the employer provides to the employee a fixed monthly amount after his retirement in consideration of past services. Pension can also be called as annuity.

**There are 2 types of pension:****Uncommuted Pension:**

The employer provides the employee with monthly pension till the lifetime of the employee starting post retirement.

**Example:** Manish worked for a company for past 20 years. After retirement the company pays him Rs. 5,000/- per month in appreciation of his past services to the company.

**Commuted Pension:**

The employee may request his employer to pay him a lump sum amount of money on retirement rather than providing a monthly amount. The employee can even request that out of the monthly pension, a certain part let's say 50% be given to him on retirement as a lump sum amount and receive the balance part monthly post retirement. This is known as commuted pension.

**Example:** Manish worked for a company for past 20 years. After retirement the company pays him Rs. 5,000/- per month in appreciation of his past services to the company. Now, Manish request the Company that instead of Rs. 5,000/- per month, he requires the entire amount post his retirement itself. This is a case of commuted pension.

**Provident Fund**

It is a savings scheme wherein a person saves a certain amount of money every year and receives the cumulative amount of money on retirement. There are various types of Provident Funds. They are as follows:

**Public Provident Fund (PPF):**

It is an account which may be opened from a nationalized bank. Only individual can open such PPF Accounts with annual contributions as low as Rs. 500/-.

**Statutory Provident Fund:**

This is applicable only to individuals employed with the Government, railways or all recognized educational institutions. The Government and the employee contribute a certain portion of the employee's salary to this fund monthly.

**Recognized Provident Fund:**

If the Provident Fund is approved by the Commissioner of Income-tax, it is known as Recognized Provident Fund. In recognized provident fund the employer and the employee contribute a certain portion of the salary of the employee to the fund.

**Unrecognized Provident Fund:**

A fund, which is not recognized by Income Tax Authorities, in which the employer and the employee contribute a certain portion of the salary of the employee, is an Unrecognized Provident Fund.

## **Taxability of Provident Fund**

### **Public Provident Fund:**

The amount of Contribution made to PPF in a Financial Year is allowed as Deduction U/s 80C subject to specified conditions. The amount of interest accrued is exempt from tax. If the amounts are withdrawn from PPF in specified manner then such withdrawals are also exempt from tax.

### **Statutory Provident Fund:**

The amount of Contribution made by the Government is exempt from tax. Employee's contribution to Statutory Provident Fund is allowed as Deduction U/s 80C subject to specified conditions. The amount of interest accrued is exempt from tax. The amount received on retirement out of such fund is exempt from tax.

### **Recognized Provident Fund:**

It is a fund, which is recognized by the commissioner of income tax. This type of fund is maintained by business houses, industrial undertakings and banks. Under this fund both employee and employer will contribute. Employee's contribution qualifies for deduction u/s 80C. Employer's contribution over 12% of mentioned salary is taxable. Interest is exempted up to 9.5%

### **Unrecognized Provident Fund:**

The amount of contribution made by the employer is not taxable in the hands of the employee during the years when such amounts are being contributed. Employee's contribution to Unrecognized Provident Fund is not allowed as deduction. The amount of interest accrued is not taxable in the year of accrual. The amount received on retirement out of such fund is required to be bifurcated in 4 categories in order to understand its taxability.

## **SIMPLE FORMAT TO COMPUTE SALARY INCOME**

<b>Basic items</b>		***
1.	Basic salary/wages/remuneration/pay	***
2.	Special pay	***
3.	Bonus	***
4.	Fees	***
5.	Commission	***
6.	Advance salary	***
7.	Arrear salary	***
<b>Allowances</b>		
1.	Fully taxable allowance	***
2.	Partly taxable/partly exempted allowances	***
3.	Fully exempted allowances	Nil
<b>Perquisites</b>		
1.	Taxable for all (specified and unspecified)	***
2.	Taxable for specified employees only	***
3.	Exempted for all (specified and unspecified)	Nil
<b>Special items</b>		
1.	Gratuity	***
2.	Pension	***
3.	Leave encashment	***

4. Provident fund		
<b>Gross salary</b>		***
<b>Deduction u/s 16</b>		
(i) Standard deduction-(limit 40,000)	***	
(ii) Entertainment allowance	***	
(iii) Professional/employment tax	***	***
<b>Income from salary</b>		***

## EXERCISES

### House rent allowance

#### Problem: 1

Mr. Ram resides in Chennai and gets Rs.10, 000 per month as basic salary Rs. 8,000 per month as DA (entering service benefits), Rs.12, 000 per month as HRA. He pays Rs. 10,000 per month as rent. Calculate taxable HRA.

#### Solution:

#### Calculation taxable HRA

Actual HRA	1,44,000
Less: Exempted	98,000
<b>Taxable HRA</b>	<b>45,600</b>

#### Workings

#### Calculation of exempted HRA

Actual HRA	=	1, 44,000
Rent paid-10% of salary	=	98,400
50% of salary	=	1, 08,000

Whichever less is exempted	=	98,400
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#### Problem: 2

The Following are the particulars of Mr.Priyan who is employed in Chennai.

- Basic Salary Rs.4000 p.m
- DA (60% of Basic Salary)
- CCA Rs.250 p.m
- House Rent Allowance Rs.450 p.m (Rent paid Rs.500 p.m)
- During the year he paid professional tax Rs.550
- Education allowances Rs.150 p.m (Per Child)

Calculate Salary Income.

**Solution:**

**Computation of income from salary for the A.Y-2019-20**

Particulars	Amount	Amount
(i) Basic salary (4000*12)		48,000
(ii) DA (48,000*60/100)		28,800
(iii) CCA (250*12)		3,000
(iv) Actual HRA	5400	
Less: Exempted	Nil	5,400
(v) Educational allowance (150*1*12)	1800	
Less: Exempted (100*1*12)	1200	600
<b>Gross salary</b>		<b>85,800</b>
<b>Deduction U/S 16</b>		
(i) Standard deduction	40,000	
(ii) Professional tax	550	40,550
<b>Taxable salary</b>		<b>45,250</b>

**Problem: 3**

The Following are the particulars of income of Mr.Ramesh (an employee of an Individual) for the previous year ended on 31<sup>st</sup> March 2017.

- Salary Rs.4500p.m
- Bonus equal to two month spay
- Dog allowance – Rs.75p.m
- Special Allowance – Rs.60 p.m
- Employee's contribution to a recognized provident fund @ 15% of salary
- Employer's contribution to the fund @ 15% of the salary
- Interest credited to the provident fund @ 9.5% p.a. is Rs.2,800
- He is provided with free lunch in office. The cost per meals Rs.30
- The employer has given him the use of small car which he uses for personal and official purpose. He meets the expenses for personal purpose from out of his pocket.

Compute the income of Mr.Ramesh from salaries for the A.Y. 2019-2020.

**Solution:**

**Computation of income from salary for the A.Y-2019-20**

Particulars	Amount	Amount
(i) Basic salary (4,500*12)		54,000
(ii) Bonus (4,500*2)		9,000
(iii) Dog allowance (75*12)		900
(iv) Special allowance (60*12)		720
(v) Employer contribution to provident fund (54,000*15/100)	8,100	
Less: Exempted up to 12%	6,480	1,620
(vi) Interest on EPF 9.5 %	2,800	
Less: Exempted up to 9.5%	2,800	Nil

(vii) Lunch allowance		Nil
(viii) Small car up to 1600 cc (1,800*12)		21,600
<b>Gross salary</b>		<b>87,840</b>

## MODULE-II

### INCOME FROM HOUSE PROPERTY

#### **Basic of charge**

Annual value of any property is assessable under this head it,

- Assessee is the owner of the property.
- Property is building and attached land.
- Property should not be used by the owner for his business or profession.

#### **Incomes - Exempted from 'House Property Income'**

Under section 10 of the Income-tax Act 1961 following incomes from house property are exempted from tax. These incomes are not to be included in the total income of assessee. Hence no tax is payable on such incomes. These incomes are:

#### **Agricultural House Property [Section 2(1)(c)].**

Income from such house property which is situated on or in the immediate vicinity of agricultural land which is used for agricultural purposes by cultivator is exempted from tax.

#### **Income from Property held under Trust Wholly for Charitable or Religious Purposes [Section 11(1)(a)]:**

Income derived from property held under trust, wholly for charitable and religious purposes, shall be exempt. To the extent such income is applied in India for such purposes; and where any such income is accumulated or set apart for application to such purposes in India, to the extent to which the income so accumulated or set apart is not in excess of 15% of the income from such property.

#### **Income from Property held under trust which is applied in part only for Charitable or Religious purposes [Section 11(1)(b)]:**

Income derived from property held under trust in part only for such purpose, shall be exempt: To the extent such income is applied in India for such purposes, provided, the trust in question is created before the commencement of Income-tax Act, 1961 i.e. before 1.4.1962; and where any such income is finally set apart for application to such purposes in India, to the extent to which the income so accumulated or set apart is not in excess of 15% of the income from such property.

#### **Income from Property held under trust which is applied for Charitable Purposes outside India [Section 11(1)(c)]:**

Income derived from property held under trust, created on or after 1.4.1952 for charitable purpose which tends to promote international welfare in which India is interested, shall be exempt to the extent to which such income is applied to such purpose outside India. Religious trusts are not covered here.

Income derived from property held under a trust for charitable or religious purposes, created before 1.4.1952, shall be exempt to the extent to which such income is applied to such purposes outside India.

In the above two cases, it is necessary that the Board, by general or special order, has directed in either case that it shall not be included in the total income of the person in receipt of such income.

**Self-Occupied but Vacant House [Section 23(3)]**

In case an assessee keeps one of his own houses reserved for self-occupation but is living in a rented house elsewhere due to his employment or profession the income from such house is taken to be NIL.

**The annual value of self-occupied house shall not be NIL:**

If such house or part of the house is actually let during the whole or any part of the previous year; or

Any other benefit there from is derived by the owner from such house.

In the above cases, the annual value shall be determined as per provisions applicable for let out properties i.e. under clause (a), (b) or (c) of section 23(1).

**House used for Own Business or Profession.**

There is no income chargeable to tax under this head from such house property.

Property held by Registered Trade Union [Section 10(24)].

Income from a house property owned by a registered trade union is not to be included in its G.T.I.

**Income from House Property held by following shall be exempted:**

- House property held by a local authority.
- House property held by a scientific research institution.
- House property held at a political party.
- House property held by a university and any other educational institution working for spreading education and not to earn profit.
- House property held by a hospital or medical institution working for the spreading of medical services to people and is not meant for earning profit.
- It is income from a farmhouse.

**One House Property (a palace) owned by a former ruler of Indian states.**

Ex-rulers of Indian states may own many palaces but only one palace of their choice shall be treated as a self-occupied house and shall be exempted.

**One Self-Occupied House**

In case assessed owns one residential house, the net annual value of the same shall be taken as nil but in case he owns more than one house, then only one of his choice but normally of higher value shall be treated as a self-occupied one and other/others are treated as deemed to be let out.

**Income from house property specimen / important provisions**

**For self-occupied:**

Gross Annual Value(GAV)/ Annual Rental Value(ARV)		<b>Nil</b>
<b>Less:</b> Municipal tax paid during the year by the owner		<b>Nil</b>
<b>Net Annual Value(NAV)</b>		<b>Nil</b>
<b>Less: Deduction u/s 24</b>		
(i) Standard deduction-not applicable		
(ii) Interest on loan of pre-construction	***	***
<b>Loss from house property</b>		<b>***</b>

**Overall chart for computation of house property income**

**For letout property:**

(i) Municipal value (or) Fair Rent (whichever is higher)		
(ii) Expected Rent (or) Standard Rent (whichever is lower)		
(iii) Expected Rent (or) Actual Rent (whichever is higher)	***	
<b>Gross Annual Value</b>		<b>***</b>
<b>Less:</b>		
(iv) Local taxes (or) Municipal taxes paid by the Owner during the previous year	***	
(v) Unrealized rent conditions of rule 4 are satisfied	***	***
<b>Annual value</b>		<b>***</b>
<b>Less: Deduction u/s 24</b>		
(i) 30% of Annual value	***	
(ii) Interest on borrowed capital-paid or due	***	***
<b>Income from House Property</b>		<b>***</b>

**Problem: 1**

From the following calculate Gross Annual Value, assuming that there is no vacant period.

<b>particulars</b>	<b>House 1</b>	<b>House 2</b>
MRV	1,05,000	1,05,000
FRV	1,07,000	1,07,000
SR under rent control act	1,35,000	1,35,000
Actual Rent (AR)	1,12,000	98,000
Period in the previous year	12 months	12 months

**Solution:**

**Computation of Gross Annual Value**

particulars	Amount	Amount
MRV	1,05,000	1,05,000
FRV	1,07,000	1,07,000
Whichever is higher	1,07,000	1,07,000
SR	1,35,000	1,35,000
ER (Whichever is higher)	1,07,000	1,07,000
AR	1,12,000	98,000
<b>GROSS ANNUAL VALUE</b>	<b>1,12,000</b>	<b>1,07,000</b>

**Problem: 2**

Mr. Ganesh owns two house properties at Madurai the first house is self-occupied and the second house is let out for residential purpose. The other details of the properties given below.

Particulars	First House (Rs)	Second House (Rs)
Municipal value	5,000	6,000
Municipal Tax	600	800
Rental Income	-	7,200
Land revenue	100	125
Fire insurance premium	150	200
Interest on mortgage	-	300
Collection charges	-	100

The second house remained vacant for a period 2 months during the year. Compute the income from house property.

**Solution:**

**A. Computation of self-occupied house property (HOUSE-1)**

Particulars	Amount	Amount
Gross annual value of the house		Nil
<b>Less:</b> Municipal tax paid by owner		Nil
<b>Annual value</b>		Nil
<b>Less:</b> standard deduction of annual value	Nil	
Interest on loan for self-occupied house	Nil	Nil
<b>Loss from self-occupied house</b>		<b>Nil</b>

B.

**Computation of Income From House Property for the A.y-2019-20 (HOUSE-2)**

Particulars	Amount	Amount
Municipal value	6,000	
Actual Rent (7,200-2 months vacant (600*2) whichever is higher	6,000	6,000
<b>Gross Annual Value</b>		6,000
<b>Less:</b>		
Municipal tax paid by Owner	600	
Unrealized Rent	Nil	600
<b>Annual value</b>		5,200
<b>Less: Deduction U/S 24</b>		
(i) 30% of annual value (5,200*30/100)		
(ii) Interest on loan	1,560	
	300	1,860
<b>Income From House Property</b>		<b>3,340</b>

**Problem: 3**

Mr. Senthil is the owner following house Property particulars in respect of which for the year ended 31/03/2019.

Particulars	House A	House B	House C
Actual Rent	12,000	2,000	Twilling of the House
Standard rent	8,000	2,400	Nil
Municipal Tax	900	200	3,800
Municipal Value	900	2,000	40,000
Municipal Tax paid by Senthil	900	100	Nil
Municipal Tax paid by Tenant	Nil	100	Nil
Repairs	600	2,000	3,000
Vacancy Period	1 Month	Nil	Nil
Interest on Loan for repairs loans	600	900	16,000

House A

Unrealized rent allowed in assessment year 2015-16 received during the year for the House in Rs. 5,000

**Solution:**

**C. Computation of self-occupied house property (HOUSE-1)**

Particulars	Amount	Amount
Gross annual value of the house		Nil
<b>Less:</b> Municipal tax paid by owner		Nil
<b>Annual value</b>		Nil
<b>Less:</b> standard deduction of annual value	Nil	
Interest on loan for self-occupied house	16,000	-16,000
<b>Loss from self occupied house</b>		<b>-16,000</b>

**A. Computation of Income From House Property for the A.y-2019-20 (HOUSE-2)**

Particulars	Amount	Amount
Municipal value	90,000	
Standard rent (Whichever is higher)	8,000	
Expected rent	8,000	
Actual rent(12,000-one month vacant ) (Whichever if higher)	11,000	
<b>Gross Annual Value</b>		11,000
<b>Less:</b>		
Municipal tax paid by Owner	900	
Unrealized Rent	Nil	900
<b>Annual value</b>		10,100
<b>Less: <u>Deduction U/S 24</u></b>		
(i) 30% of annual value (10,100*30/100)	3,030	
(ii) Interest on loan	600	3,630
		6,470
<b>Add: unrealized rent</b>		5,000
<b>Income From House Property</b>		<b>11,470</b>

**B. Computation of Income From House Property for the A.y-2019-20 (HOUSE-2)**

Particulars	Amount	Amount
Municipal value	2,000	
Standard rent (Whichever is lower)	2,400	
Expected rent	2,000	
Actual rent (Whichever is higher)	2,000	
<b>Gross Annual Value</b>		2,000
<b>Less:</b>		
Municipal tax paid by Owner	100	
Unrealized Rent	Nil	100
<b>Annual value</b>		1,900
<b>Less: <u>Deduction U/S 24</u></b>		
(i) 30% of annual value (1,900*30/100)	570	
(ii) Interest on loan	900	1,470
<b>Income From House Property</b>		<b>11,470</b>

## INCOME FROM BUSINESS OR PROFESSION

### Introduction

Provision regarding calculation of profits and gains of business or profession is dealt under section 28 to 44 of income tax act 1961. This head of the act is a major source of revenue to the government.

### Business [section 2(13)]

Definition of “Business” includes any trade, commerce or manufacture or any venture or concern in the nature of trade, commerce or manufacture.

### Profession [section 2(36)]

Profession involves an exercise of intellect and skill based on learning and experience. Vocation refers to any work performed on the strength of one’s natural ability for the work. Regularity and profit motive are not necessary for an activity to be called a vocation.

### OVER ALL CHAT FOR CALCULATION OF INCOME FROM BUSINESS

Particulars	Amount	Amount
Net profit as per P & L A/c		****
<b>Add:</b>		
1.Disallowed Expenses		****
2.Business Income not credited in P & L A/c		****
3.Under valuation of closing stock		****
4.Over valuation of opening stock		****
<b>Less:</b>		
1.Non business income credited in P & L A/c	****	
2.Allowed expenses not debited in P & L A/c	****	
3.Over valuation of closing stock	****	
4.Under valuation of opening stock	****	****
<b>Income From Business</b>		<b>****</b>

### Problem: 1

From the following P&L A/c calculate Income from Business

Particulars	Amount	Particulars	Amount
To Rent	40,000	By gross profit	2,50,000
To Salary to employees	25,000	By house property income	
To Depreciation	10,000	By income from other sources	1,50,000
To Donation	8,000		
To Net profit	5,17,000		2,00,000
	<b>6,00,000</b>		<b>6,00,000</b>

### Adjustments:

- Depreciation to be allowed as per income tax provision Rs. 8,000.
- Business income of Rs. 12,000 is not shown in the P&L A/c.
- Rs. 8,000 of the rent is of personal nature.

**Solution:**

**Calculation of Income from Business**

Date	Particulars	Amount	Amount
	N\P as per P&L A/c		5,17,000
	<b>Add:</b>		
	Donations	8,000	
	Depreciation	10,000	
	Business income not shown P&L A/c	12,000	
	Rent	8,000	38,000
	<b>Less:</b>		5,55,000
	H/P Income		
	IFOS	1,50,000	
	Depreciation	2,00,000	
		8,000	3,58,000
	<b>Income from Business</b>		<b>1,97,000</b>

**Problem: 1**

**From the following P&L A/c calculate Income from Business**

Particulars	Amount	Particulars	Amount
To General expenses	20,000	By Gross profit	5,00,000
To Bad debts	25,000	By Sundry receipt	
To Advance income tax	24,000	By Bad debts recovered	50,000
To Salary to staff	40,000	(earlier allowed as	
To Drawings	40,000	deduction)	12,500
To Interest on capital	24,000	By Interest on debentures	40,000
To Advertisement	9,000	By Interest on deposit with a	
To Excise duty	12,000	company	25,000
To Expenditure on acquisition of patent right (in 2016)	10,000		
To Net profit	4,23,000		
	<b>6,27,500</b>		<b>6,27,500</b>

**Adjustments**

- General expenses include Rs. 2,300 spent as marriage expenses by the proprietor.
- Advertise an expense was spent on 31<sup>st</sup> august 2018.
- Income of Rs. 12,000 accrued during the PY 2018-19 is nit recorded in the P&L A/c.
- An expenditure of Rs, 1,000 relating to business is not show in P&L A/c.
- The proprietor owns two houses from which he gets the income of Rs, 1,80,000

**Solution:**

**Calculation of Income from Business**

Date	Particulars	Amount	Amount
	N\ P as per P&L A/c		4,23,000
	<b>Add:</b>		
	Advance income tax	24,000	
	Drawings	40,000	
	Interest on own capital	24,000	
	General expenses	2,300	
	Income accrued during 2018-19	12,000	
	Patents	10,000	1,12,300
	<b>Less:</b>		
	Depreciation for patents (10,000*25%)		5,35,800
	Expenditure relating to business	2,500	
	Interest on debentures	1,000	
	Interest on deposit with a company	40,000	
		25,000	
			68,500
	<b>Income from Business</b>		<b>4,67,300</b>

**OVER ALL FORMAT FOR PROFESSIONALS LIKE DOCTORS, LAWYERS, ACCOUNTANTS, TAX CONSULTANTS.**

Particulars	Amount	Amount
<b>PROFESSIONAL INCOMES:</b>		
1.Fees [for all professional]		****
2.Operation fees, Visiting fees [for doctors]		****
3.Institute fees [for accountants]		****
4.Legal fee, practicing fees [for lawyers]		****
5.Gift from clients [for all professionals]		****
6.Gift from patients [for doctors]		****
7.Examiner fees [for all professional]		****
8.All other professional receipts		****
<b>Less:</b>		
<b>PROFESSIONAL EXPENSES:</b>		
1. Office and administrative expenses [for all professionals]	****	
2. Clinic expenses and dispensary expenses [for doctors]	****	
3. Cost of books for professional purposes. [for all professionals]	****	
4. Subscription for journals. [for all professionals]	****	
5. Depreciation	****	
a) For office equipments (for all professional)		
b) For surgical equipments ( for doctors)		
6.Any membership fee (for all professionals)	****	
7.Cost of medicine [for doctors] [opening stock +purchases-closing stock]	****	
8.All other professional payments	****	****
<b>Income From Profession</b>		****

From the following receipts and payments A/c of Mr.Vasanth, a tax consultant, calculate income from profession.

Receipts	Amount	Payments	Amount
To balance	3,50,000	By office and admin expenses	60,000
To fees from clients		By salary to staff:	
2019-20          1,00,000		2019-20          40,000	
2018-19          50,000	1,50,000	2018-19          30,000	
To presents from clients	40,000	By repairs	70,000
To winning from lotteries	28,000	By interest on loan for business	8,000
To rent from let out property	75,000	By income tax	
To share of income from firm	12,500	By purchase of car(purchased during January 2019)	12,000
		By balance	6,000
			1,50,000
			3,49,500
	<b>6,55,500</b>		<b>6,55,500</b>

**Solution:**

**Calculation of Income from Profession of Mr. Vasanth**

Date	Particulars	Amount	Amount
	<b>Professional receipts:</b>		
	i) Fess 2019-20                      1,00,000		
	2018-19                      50,000		1,50,000
	ii) Presents from client		40,000
	<b>Less: Professional payments</b>		1,90,000
	iii) Office and admin expenses	60,000	
	iv) Staff salary: 2019-20          40,000		
	2018-19                      30,000	70,000	
	v) Repairs	8,000	
	vi) Interest on loan for business	12,000	
	vii) Depreciation on car purchased during January 2019 (1, 50,000*15%=22,500*50%)	11,250	1,61,250
	<b>Income from Profession</b>		<b>28,750</b>

From the following income and expenditure A/c of Ramana& Co, chartered accountants, calculate income from profession from the details below.

Expenditure	Amount	Incomes	Amount
To charity and donation	1,00,000	By audit fee	3,00,000
To subscription to journals	2,000	By examiner fee	25,000
To institute fee	4,000	By fee for other accounts work	40,000
To office rent	5,000	By dividend from UTI	35,000
To drawings	50,000		
To electricity bill	9,000		
To salary to trainee	20,000		
To net income	2,10,000		
	<b>4,00,000</b>		<b>4,00,000</b>

**Solution:**

**Calculation of Income from Profession of Ramana& Co**

Date	Particulars	Amount	Amount
	<b>Professional Receipts:</b>		
	i) Audit fees		3,00,000
	ii) Examiner fees		25,000
	iii) Fees for other accounting work		40,000
	<b>Less: Professional Payments</b>		3,65,000
	i) Subscription to journal		
	ii) Institute fee	2,000	
	iii) Office rent	4,000	
	iv) Bill of electricity	5,000	
	v) Salary to trainee	9,000	
	vi) Depreciation as per provisions	20,000	
		5,000	
			45,000
	<b>Income from Profession</b>		<b>3,20,000</b>

# CAPITAL GAIN

## 7.1 INTRODUCTION

In this chapter on capital gains, we begin our discussion with the definition of “capital asset” and “transfer”. Thereafter, we will proceed to discuss the various circumstances under which capital gains tax is levied. There are certain transactions which are not to be regarded as transfer for the purposes of capital gains. These transactions have also been discussed in this chapter. For computing long-term capital gains, knowledge of cost inflation index is necessary. Again, there is a separate method of computation of capital gains in respect of depreciable assets. Also, there are exemptions in cases where capital gains/net sales consideration are invested in specified assets. All these aspects are being discussed in this chapter.

Section 45 provides that any profits or gains arising from the **transfer** of a **capital asset** effected in the previous year will be chargeable to income-tax under the head ‘Capital Gains’. Such capital gains will be deemed to be the income of the previous year in which the transfer took place. In this charging section, two terms are important. One is “capital asset” and the other is “transfer”.

## 7.2 CAPITAL ASSET

**Definition:** According to section 2(14), a capital asset means –

- (a) property of any kind held by an assessee, whether or not connected with his business or profession;
- (b) any securities held by a Foreign Institutional Investor which has invested in such securities in accordance with the SEBI regulations.

## 7.3 SHORT TERM AND LONG TERM CAPITAL ASSETS

- **Definition –** As per section 2(42A), short-term capital asset means a capital asset held by an assessee for not more than 36 months immediately preceding the date of its transfer.

As per section 2(29A), long-term capital asset means a capital asset which is not a short-term capital asset.

Thus, a capital asset held by an assessee for more than 36 months immediately preceding the date of its transfer is a long-term capital asset.

## 7.4 SCOPE AND YEAR OF CHARGEABILITY [SECTION 45]

### (1) General Provision [Section 45(1)]

Any profits or gains arising from the transfer of a capital asset effected in the previous year (other than exemptions covered under this chapter) shall be chargeable to income-tax under this head **in the previous year in which the transfer took place.**

**Year of chargeability**- Capital gains are chargeable as the income of the previous year in which the sale or transfer takes place. In other words, for determining the year of chargeability, the relevant date of transfer is not the date of the agreement to sell, but the actual date of sale *i.e.*, the date on which the effect of transfer of title to the property as contemplated by the parties has taken place [*Alapati Venkataramiah v. CIT [1965] 57 ITR 185 (SC)*].

However, as already noted, Income-tax Act has recognised certain transactions as transfer in spite of the fact that conveyance deed might not have been executed and registered. Power of Attorney sales as explained above or co-operative society transactions for acquisition of house are examples in

### (2) Insurance receipts [Section 45(1A)]

Where any person receives any money or other assets under any insurance from an insurer on account of damage to or destruction of any capital asset, as a result of -

- ◆ flood, typhoon, hurricane, cyclone, earthquake or other convulsion of nature; or
- ◆ riot or civil disturbance; or
- ◆ accidental fire or explosion; or
- ◆ action by an enemy or action taken in combating an enemy (whether with or without declaration of war), then,

any profits or gains arising from receipt of such money or other assets shall be chargeable to income-tax under the head "Capital gains" and shall be deemed to be the income of the **such person for the previous year in which such money or other asset was received.**

**Full value of consideration:** In order to compute capital gains, the value of any money or the fair market value of other assets on the date of such receipt shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of such capital assets.

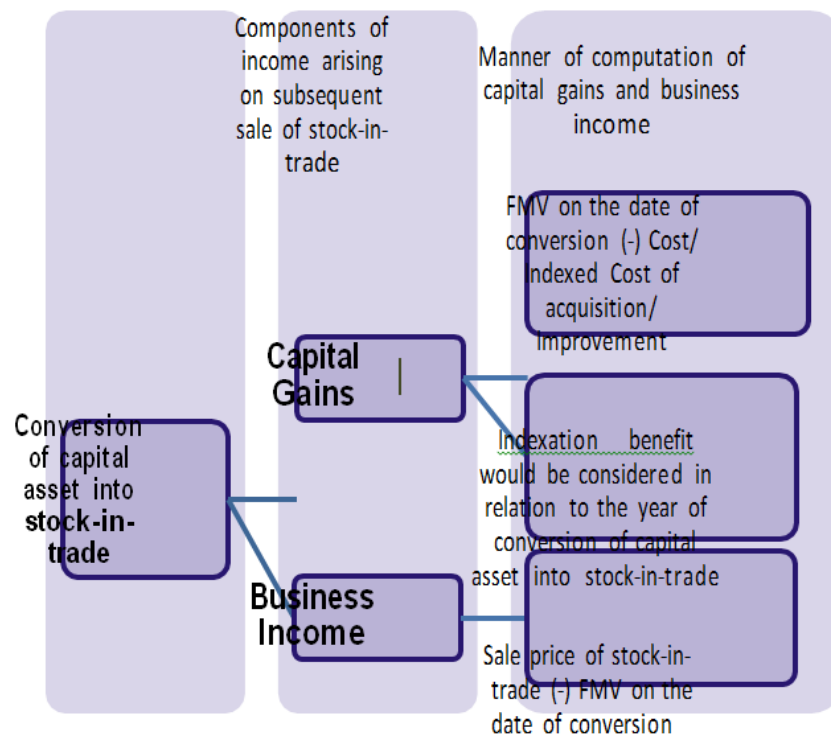
### (3) Conversion or treatment of a capital asset as stock-in-trade [Section 45(2)]

A person who is the owner of a capital asset may convert the same or treat it as stock-in-trade of the business carried on by him. As noted above, the conversion/treatment is a transfer.

As per section 45(2), notwithstanding anything contained in section 45(1), being the charging section, the profits or gains arising from the above conversion or treatment will be chargeable to

income-tax as his income of the previous year in which such stock-in-trade is sold or otherwise transferred by him.

**Full value of consideration:** In order to compute the capital gains, the fair market value of the asset on the date of such conversion or treatment shall be deemed to be the full value of the consideration received as a result of the transfer of the capital asset.



**Note – Both Capital Gains and Business income are chargeable to tax in the year in which stock-in-trade is sold or otherwise transferred.**

#### ILLUSTRATION 1

X converts his capital asset (acquired on June 10, 2003 for ₹ 60,000) into stock-in-trade on March 10, 2020. The fair market value on the date of the above conversion was ₹ 5,50,000. He subsequently sells the stock-in-trade so converted for ₹ 6,00,000 on June 10, 2020. Examine the tax implication.

Cost Inflation Index - F.Y. 2003-04: 109; F.Y. 2019-20: 289; F.Y. 2020-21: 301.

#### SOLUTION

Since the capital asset is converted into stock-in-trade during the previous year relevant to the A.Y. 2020-21, it will be a transfer under section 2(47) during the P.Y. 2019-20. However, the profits or gains arising from the above conversion will be chargeable to tax during the A.Y. 2021-22, since the stock-in-trade has been sold only on June 10, 2020. For this purpose, the fair market value on the date of such conversion (i.e. 10<sup>th</sup> March, 2020) will be the full value of consideration.

The capital gains will be computed after deducting the indexed cost of acquisition from the full value of consideration. The cost inflation index for 2003-04 i.e., the year of acquisition is 109 and the index for the year of transfer i.e., 2019-20 is 289. The indexed cost of acquisition is  $60,000 \times 289/109 = ₹ 1,59,083$ . Hence, ₹ 3,90,917 (i.e. ₹ 5,50,000 – ₹ 1,59,083) will be treated as long-term capital gains chargeable to tax during the A.Y.2021-22. During the same assessment year, ₹ 50,000 (₹ 6,00,000 – ₹ 5,50,000) will be chargeable to tax as business profits.

#### (4) Transfer of beneficial interest in securities [Section 45(2A)]

As per section 45(2A), where any person has had at any time during the previous year any beneficial interest in any securities, then, any profits or gains arising from the transfer made by the depository or participant of such beneficial interest in respect of securities shall be chargeable to tax as the income of the beneficial owner of the previous year in which such transfer took place and shall not be regarded as income of the depository who is deemed to be the registered owner of the securities by virtue of section 10(1) of the Depositories Act, 1996.

**Full value of consideration and period of holding:** For the purposes of section 48 and proviso to section 2(42A), the cost of acquisition and the period of holding of securities shall be determined on the basis of the first-in-first-out (FIFO) method.

When the securities are transacted through stock exchanges, it is the established procedure that the brokers first enter into contracts for purchase/ sale of securities and thereafter, follow it up with delivery of shares, accompanied by transfer deeds duly signed by the registered holders.

- ◆ The seller is entitled to receive the consideration agreed to as on the date of contract.
- ◆ Thus, it is the date of broker's note that should be treated as the date of transfer in case of sale transactions of securities provided such transactions are followed up by delivery of shares and also the transfer deeds.
- ◆ Similarly, in respect of the purchasers of the securities, the holding period shall be reckoned to take place directly between the parties and not through stock exchanges.
- ◆ The date of contract of sale as declared by the parties shall be treated as the date of transfer provided it is followed up by actual delivery of shares and the transfer deeds.

Where securities are acquired in several lots at different points of time, the First-In-First-Out (FIFO) method shall be adopted to reckon the period of the holding of the security, in cases where the dates of purchase and sale could not be correlated through specific numbers of the scrips.

In other words, the assets acquired last will be taken to be remaining with the assessee while assets acquired first will be treated as sold. Indexation, wherever applicable, for long-term assets will be regulated on the basis of the holding period determined in this manner - *CBDT Circular No. 704, dated 28.4.1995*.

Meaning of certain terms:

Term	Meaning
<b>Beneficial owner</b>	A person whose name is recorded as such with a depository.
<b>Depository</b>	A company formed and registered under the Companies Act, 1956 <sup>1</sup> and which has been granted a certificate of registration under section 12(1A) of the Securities and Exchange Board of India Act, 1992.
<b>Security</b>	Such security as may be specified by SEBI.

**(5) Introduction of capital asset as capital contribution [Section 45(3)]**

Where a person transfers a capital asset to a firm, AOP or BOI in which he is already a partner/ member or is to become a partner/ member by way of capital contribution or otherwise, the profits or gains arising from such transfer will be **chargeable to tax as income of the previous year in which such transfer takes place.**

**Full value of consideration:** For this purpose, the full value of the consideration will be deemed to be the amount recorded in the books of account of the firm, AOP or BOI as the value of the capital asset.

**(6) Distribution of capital assets on dissolution of firm/AOP or BOI [Section 45(4)]**

The profits or gains arising from the transfer of capital assets by way of

- distribution of capital assets on the dissolution of a firm or AOP or BOI or
- otherwise

shall be chargeable to tax as the income of the firm etc. of the previous year in which such transfer takes place.

**Full value of consideration:** For this purpose, the fair market value of the asset on the date of such transfer shall be deemed to be the full value of consideration.

The Bombay High Court made a landmark judgment in *Commissioner of Income-tax v. A.N. Naik Associates (2004) 136 Taxman 107*. The Court applied the “mischief rule” about interpretation of statutes and pointed out that the idea behind the introduction of sub-section (4) in section 45 was to plug in a loophole and block the escape route through the medium of the firm. The High Court observed that the expression ‘otherwise’ has not to be read *ejusdem generis* with the expression ‘dissolution of a firm or body of individuals or association of persons’. The expression ‘otherwise’ has to be read with the words ‘transfer of capital assets by way of distribution of capital assets’. If so read, it becomes clear that even when a firm is in existence and there is a transfer of capital asset, it comes within the expression ‘otherwise’ since the object of the amendment was to remove the loophole which existed, whereby capital gains tax was not chargeable. Therefore, the word

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'otherwise' takes into its sweep not only cases of dissolution but also cases of subsisting partners of a partnership, transferring assets in favour of retiring partners.

**Note** - *Since the tax treatment accorded to a LLP and a general partnership is the same, the conversion from a general partnership firm to an LLP will have no tax implications if the rights and obligations of the partners remain the same after conversion and if there is no transfer of any asset or liability after conversion. However, if there is a change in rights and obligations of partners or there is a transfer of asset or liability after conversion, then the provisions of section 45 would get attracted.*

#### **(7) Compensation on compulsory acquisition [Section 45(5)]**

Sometimes, a building or some other capital asset belonging to a person is taken over by the Central Government by way of compulsory acquisition. In that case, the consideration for the transfer is determined by the Central Government or RBI. When the Central Government pays the above compensation, capital gains may arise. Such capital gains are **chargeable as income of the previous year in which such compensation or part thereof, was first received.**

**Enhanced Compensation**- Many times, persons whose capital assets have been taken over by the Central Government and who get compensation from the government go to the court of law for enhancement of compensation. If the court awards a compensation which is higher than the original compensation, the difference thereof will be chargeable to capital gains in the year in which the same is received from the government.

**Cost of acquisition in case of enhanced compensation** - For this purpose, the cost of acquisition and cost of improvement shall be taken to be *nil*.

**Compensation received in pursuance of an interim order deemed as income chargeable to tax in the year of final order** - In order to remove the uncertainty regarding the year in which the amount of compensation received in pursuance of an interim order of the court is to be charged to tax, a proviso has been inserted after clause (b) to provide that such compensation shall be deemed to be income chargeable under the head 'Capital gains' in the previous year in which the final order of such court, Tribunal or other authority is made.

**Reduction of enhanced compensation** - Where capital gain has been charged on the compensation received by the assessee for the compulsory acquisition of any capital asset or enhanced compensation received by the assessee and subsequently such compensation is reduced by any court, tribunal or any authority, the assessed capital gain of that year shall be recomputed by taking into consideration the reduced amount. This re-computation shall be done by way of rectification under section 155.

**Death of the transferor**- It is possible that the transferor may die before he receives the enhanced compensation. In that case, the enhanced compensation or consideration will be chargeable to tax in the hands of the person who receives the same.

## **(8) Taxability of capital gains in case of Specified Agreement [Section 45(5A)]**

**Genuine hardship on account of taxability of capital gains in the year of transfer of property to developer:** The definition of 'transfer', *inter alia*, includes any arrangement or transaction where any rights are handed over in execution of part performance of contract, even though the legal title has not been transferred.

Applying the definition of transfer, under these development agreements, the transfer took place in the year in which the owner of the immovable property, being land or building or both handed over the immovable property to the developer.

Consequently, the capital gains tax liability in the hands of the owner would arise in the year in which the possession of immovable property is handed over to the developer for development of a project, in spite of the fact that the consideration thereof (i.e. the actual constructed property) will be received only after a couple of years.

**Deferment of taxability of capital gains:** With a view to minimise the genuine hardship which the owner of land or building may face in paying capital gains tax in the year of transfer, section 45(5A) provides that

- in case of an assessee **being individual or Hindu undivided family**,
- who enters into a specified agreement for development of a project,
- the capital gain arises from such transfer shall be chargeable to income-tax as income of the **previous year in which the certificate of completion for the whole or part of the project is issued by the competent authority**.

**Meaning of Specified Agreement:** Specified agreement means the registered agreement in which a person owning land or building or both, agrees to allow another person to develop a real estate project on such land or building or both, in consideration of a share, being land or building or both in such project, whether with or without payment of part of the consideration in cash.

**Full value of consideration:** For the purpose of section 48, the stamp duty value of his share, being land or building or both, in the project on the date of issuing of said certificate of completion as increased by any consideration received in cash, if any, shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of the capital asset.

**Non-applicability of the beneficial provision:** It may, however, be noted these beneficial provisions would not apply, where the assessee transfers his share in the project on or before the date of issue of said completion certificate and the capital gain tax liability would be deemed to arise in the previous year in which such transfer took place. In such a case, full value of consideration received or accruing shall be determined by the general provisions of the Act. [Proviso to section 45(5A)]

Meaning of certain terms:

Term	Meaning
<b>Competent authority</b>	The authority empowered to approve the building plan by or under any law for the time being in force
<b>Stamp duty value</b>	The value adopted or assessed or reassessable by any authority of Government for the purpose of payment of stamp duty in respect of an immovable property being land or building or both.

## 7.11 MODE OF COMPUTATION OF CAPITAL GAINS(SECTION 48)

- (1) **Computation of capital gains:** The income chargeable under the head 'capital gains' shall be computed by deducting the following items from the full value of the consideration received or accruing as a result of the transfer of the capital asset:
  - (i) Expenditure incurred wholly and exclusively in connection with such transfer.
  - (ii) The cost of acquisition and cost of any improvement thereto.
- (2) **No deduction in respect of STT paid:** However, no deduction shall be allowed in computing the income chargeable under the head "Capital Gains" in respect of any amount paid on account of securities transaction tax under Chapter VII of the Finance (No.2) Act, 2004.
- (3) **Cost inflation index:** As per second proviso to section 48, for computation of long term capital gains, the cost of acquisition and cost of improvement increased by applying the Cost Inflation Index (CII). Once the CII is applied to the cost of acquisition and cost of improvement, it becomes indexed cost of acquisition and indexed cost of improvement.

This means an amount which bears to the cost of acquisition, the same proportion as CII for the year in which the asset is transferred bears to the CII for the first year in which the asset was held by the assessee or for the year beginning on 1st April, 2001, whichever is later.

Similarly, indexed cost of any improvement means an amount which bears to the cost of improvement, the same proportion as CII for the year in which the asset is transferred bear

**"Cost Inflation Index"** in relation to a previous year means such index as may be notified by the Central Government having regard to 75% of average rise in the Consumer Price Index (Urban) for the immediately preceding previous year to such previous year

**Note -** The benefit of indexation will not apply to the long-term capital gains arising from the transfer of bonds or debentures **other than** –

- (1) Capital indexed bonds issued by the Government; or
- (2) Sovereign Gold Bond issued by the RBI under the Sovereign Gold Bond Scheme, 2015.

In case of depreciable assets (discussed later), there will be no indexation and the capital gains will always be short-term capital gains.

The cost inflation indices for the financial years so far have been notified as under:

Financial Year	Cost Inflation Index
2001-02	100
2002-03	105
2003-04	109
2004-05	113
2005-06	117
2006-07	122
2007-08	129
2008-09	137
2009-10	148
2010-11	167
2011-12	184
2012-13	200
2013-14	220
2014-15	240
2015-16	254
2016-17	264
2017-18	272
2018-19	280
2019-20	289
<b>2020-21</b>	<b>301</b>

- (4) **Full value of consideration of shares, debentures or warrants issued under ESOP in case of transfer under a gift etc.** - In case where shares, debentures or warrants allotted by a company directly or indirectly to its employees under the Employees' Stock Option Plan or Scheme in accordance with the guidelines issued in this behalf by the Central Government are transferred under a gift or irrecoverable trust, then the market value on the date of such transfer shall be deemed to be the full value of consideration received or accruing as a result of transfer of such asset.
- (5) **Special provision for non-residents** - In order to give protection to non-residents who invest foreign exchange to acquire capital assets, the first proviso to section 48 provides that, in the case of non-residents, capital gains arising from the transfer of shares or debentures of an Indian company is to be computed as follows:
- The cost of acquisition, the expenditure incurred wholly and exclusively in connection with the transfer and the full value of the consideration are to be converted into the same foreign currency with which such shares were acquired.
  - The resulting capital gains shall be reconverted into Indian currency.

The aforesaid manner of computation of capital gains shall be applied for every purchase and sale of shares or debentures of an Indian company. Rule 115A is relevant for this purpose. Benefit of indexation will not be applied in this case.

## 7.12 ASCERTAINMENT OF COST IN SPECIFIED CIRCUMSTANCES [SECTION 49]

A person becomes the owner of a capital asset not only by purchase but also by several other methods. Section 49 gives guidelines as to how to compute the cost under different circumstances.

- (1) **Cost to previous owner deemed as cost of acquisition of asset:** In the following cases, the cost of acquisition of the asset shall be deemed to be cost for which the previous owner of the property acquired it. To this cost, the cost of improvement to the asset incurred or borne by the previous owner or the assessee must be added:

Where the capital asset became the property of the assessee:

- (i) on any distribution of assets on the total or partition of a HUF;
- (ii) under a gift or will;
- (iii) by succession, inheritance or devolution;
- (iv) on any distribution of assets on the liquidation of a company;
- (v) under a transfer to revocable or an irrevocable trust;
- (vi) under any transfer of capital asset by a holding company to its wholly owned subsidiary Indian company or by a subsidiary company to its 100% holding Indian company, referred to in section 47(iv) and 47(v) respectively;
- (vii) under any transfer referred to in section 47(vi) of a capital asset by amalgamating company to the amalgamated Indian company, in a scheme of amalgamation;
- (viii) under any transfer referred to in section 47(via) of shares held in an Indian company, in a scheme of amalgamation, by amalgamating foreign company to the amalgamated foreign company;
- (ix) under any transfer referred to in section 47(viaa) by a banking company to the banking institution, in a scheme of amalgamation of the banking company with a banking institution;
- (x) under any transfer of a capital asset, being a share of a foreign company, which derives directly or indirectly its value substantially from the share(s) of an Indian company, held by the amalgamating foreign company to the amalgamated foreign company, in the scheme of amalgamation referred to under section 47(viab);
- (xi) under any transfer referred to in section 47(vib), of a capital asset by the demerged company to the resulting Indian company, in a scheme of demerger;
- (xii) by any transfer of a capital asset, being share(s) held in an Indian company, by the demerged foreign company to the resulting foreign company, in a scheme of demerger referred to in section 47(vic);
- (xiii) by any transfer of a capital asset in a business reorganization under section 47(vica), by the predecessor co-operative bank to the successor co-operative bank;
- (xiv) by any transfer by a shareholder, in a business reorganisation referred to under section 47(vicb), of a capital asset being a share or shares held by him in the predecessor co-operative bank, if the transfer is made in consideration of the allotment to him of any share or shares in the successor co-operative bank;

- (xv) by transfer of a capital asset, being a share in a foreign company, which derives, directly or indirectly, its value substantially from the share or shares of an Indian company, held by the demerged foreign company to the resulting foreign company in the scheme of demerger referred under section 47(vic);
- (xvi) by any transfer of capital asset or intangible asset on succession of a firm by a company in a business carried on by it or any transfer of a capital asset on succession of an AOP/BOI by a company on demutualisation or corporatisation of a recognized stock exchange referred to in section 47(xiii);
- (xvii) under any transfer under section 47(xiiib) of a capital asset or intangible asset by a private company or unlisted public company to a LLP;
- (xviii) by any transfer of capital asset or intangible asset on succession of a sole proprietorship concern by a company in a business carried on by it, fulfilling the conditions mentioned in section 47(xiv);
- (xix) by conversion by an individual of his separate property into a HUF property, by the mode referred to in section 64(2).

Accordingly, section 2(42A) provides that in all such cases, for determining the period for which the capital asset is held by the transferee, the period of holding of the asset by the previous owner shall also be considered.

#### ILLUSTRATION 5

*Neerja was carrying on the textile business under a proprietorship concern, Neerja Textiles. On 21.07.2020 the business of Neerja Textiles was succeeded by New Look Textile Private Limited and all the assets and liabilities of Neerja Textiles on that date became the assets and liabilities of New Look Textile Private Limited and Neerja was given 52% share in the share capital of the company. No other consideration was given to Neerja on account of this succession.*

*The assets and liabilities of Neerja Textiles transferred to the company include an urban land which was acquired by Neerja on 19.7.2013 for ₹ 9,80,000. The company sold the same on 30.03.2021 for ₹ 15,00,000.*

*Examine the tax implication of the above-mentioned transaction and compute the income chargeable to tax in such case(s).*

*Cost Inflation Index: F.Y. 2013-14: 220; F.Y. 2020-21: 301*

### 7.13 COST OF ACQUISITION [SECTION 55]

- (1) Goodwill of a business or a trademark or brand name associated with a business or a right to manufacture, produce or process any article or thing, or right to carry on any business or profession, tenancy rights, stage carriage permits and loom hours

- (i) **In case of acquisition from previous owner:** In the case of the above capital assets, if the assessee has purchased them from a previous owner, the cost of acquisition means the amount of the purchase price.
- (ii) **In case of self-generated assets** - There are circumstances where it is not possible to visualise cost of acquisition.

For example, suppose a doctor starts his profession. With the passage of time, the doctor acquires lot of reputation. He opens a clinic and runs it for 5 years. After 5 years he sells the clinic to another doctor for ` 10 lacs which includes ` 2 lacs for his reputation or goodwill.

Now a question arises as to how to find out the profit in respect of goodwill. It is obvious that the goodwill is self-generated and hence it is difficult to calculate the cost of its acquisition. However, it is certainly a capital asset.

The Supreme Court in *CIT v. B.C. Srinivasa Setty [1981] 128 ITR 294 (SC)* held that in order to bring the gains on sale of capital assets to charge under section 45, it is necessary that the provisions dealing with the levy of capital gains tax must be read as a whole.

Section 48 deals with the mode of computing the capital gains. Unless the cost of acquisition is correctly ascertainable, it is not possible to apply the provisions of section 48. Self-generated goodwill is such a type of capital asset where it is not possible to visualise cost of acquisition. Once section 48 cannot be applied, the gains thereon cannot be brought to charge.

This decision of the Supreme Court was applicable not only to self-generated goodwill of a business but also to other self-generated assets like tenancy rights, stage carriage permits, loom hours etc.

In order to supersede the decision of the Supreme Court cited above, section 55 was amended. Accordingly, in case of self-generated assets namely, goodwill of a business or a trademark or brand name associated with a business or a right to manufacture, produce or process any article or thing, or right to carry on any business or profession, tenancy rights, stage carriage permits, or loom hours, the cost of acquisition will be taken to be *nil*.

- (iii) **In case of other modes** - In the following cases, cost of acquisition of goodwill of a business or a trademark or brand name associated with a business or a right to manufacture, produce or process any article or thing, or right to carry on any business or profession, tenancy rights, stage carriage permits and loom hours shall not be *nil*, but will be deemed to be the cost for which the previous owner of the property acquired it: Where the capital asset became the property of the assessee —
- (a) On any distribution of assets on the total or partial partition of a Hindu undivided family.
  - (b) Under a gift or will.
  - (c) By succession, inheritance or devolution.

- (d) On any distribution of assets on the liquidation of a company.
- (e) Under a transfer to a revocable or an irrevocable trust.
- (f) Under any transfer referred to in section 47(iv)/ (v)/ (vi)/ (via)/ (viaa)/ (viab)/ (vib)/ (vic)/(vica)/ (vicb)/ (vicc)/ (xiii)/ (xiiib) or (xiv)
- (g) Where the assessee is a Hindu undivided family, by the mode referred to in section 64(2).

**Cost of Acquisition of assets: At a Glance**

Sl. No.	Nature of asset	Cost of acquisition
1	Goodwill of business, trademark, brand name etc., - - Self generated - Acquired from previous owner	Nil Purchase price
2	<b>Rights Shares:</b>  Original shares (which form the basis of entitlement of rights shares)  Rights entitlement (which is renounced by the assessee in favour of a person)  Rights shares acquired by the assessee  Rights shares which are purchased by the person in whose favour the assessee has renounced the rights entitlement	Amount actually paid for acquiring the original shares  Nil  Amount actually paid for acquiring the rights shares  Purchase price paid to the renouncer of rights entitlement as well as the amount paid to the company which has allotted the rights shares.
3.	Equity shares received on demutualisation or corporatisation of a recognised stock exchange	Cost of acquisition of such shares shall be the cost of acquiring his original membership of the exchange.
4.	Clearing or trading right acquired on demutualisation or corporatisation of a recognised stock exchange	NIL
5.	<b>Long term capital assets being,</b> - <b>equity shares</b> in a company on which STT is paid both at the time of purchase and transfer or - <b>unit of equity oriented fund or unit of business trust</b> on which STT is paid at the time of transfer, <b>acquired before 1st February, 2018</b>	Cost of acquisition shall be the higher of (i) cost of acquisition of such asset; and (ii) lower of - the fair market value of such asset; and - the full value of consideration received or accruing as a result of the transfer of the capital asset.

6.	<b>Any other capital asset</b> Where such capital asset became the property of the assessee before 1.4.2001	Cost of the asset to the assessee, or FMV as on 1.4.2001, at the option of the assessee. <b>However, in case of capital asset being land or building, FMV as on 1.4.2001 shall not exceed stamp duty value as on 1.4.2001.</b>
	Where capital assets became the property of the assessee by way of distribution of assets on total or partial partition of HUF, under a gift or will, by succession, inheritance, distribution of assets on liquidation of a company, etc.	Cost to the previous owner or FMV as on 1.4.2001, at the option of the assessee. <b>However, in case of capital asset being land or building, FMV as on 1.4.2001 shall not exceed stamp duty value as on 1.4.2001.</b>
7.	Where cost of the property in the hands of previous owner <b>cannot be ascertained</b>	The <b>FMV on the date on which the capital asset become the property of the previous owner</b> would be considered as cost of acquisition.

#### ILLUSTRATION 6

ABC Ltd. converts its capital asset acquired for an amount of ₹ 50,000 in June, 2003 into stock-in-trade in the month of November, 2017. The fair market value of the asset on the date of conversion is ₹ 4,50,000. The stock-in-trade was sold for an amount of ₹ 6,50,000 in the month of September, 2020. What will be the tax treatment?

Financial year	Cost Inflation Index
2003-04	109
2017-18	272
2020-21	301

#### SOLUTION

The capital gains on the sale of the capital asset converted to stock-in-trade is taxable in the given case. It arises in the year of conversion (i.e. P.Y. 2017-18) but will be taxable only in the year in which the stock-in-trade is sold (i.e. P.Y. 2020-21). Profits from business will also be taxable in the year of sale of the stock-in-trade (P.Y. 2020-21).

The long-term capital gains and business income for the A.Y.2021-22 are calculated as under:

Particulars	₹	₹
<b>Profits and Gains from Business or Profession</b>		
Sale proceeds of the stock-in-trade	6,50,000	
Less: Cost of the stock-in-trade (FMV on the date of conversion)	4,50,000	2,00,000
<b>Long Term Capital Gains</b>		
Full value of the consideration (FMV on the date of the conversion)	4,50,000	
Less: Indexed cost of acquisition (₹ 50,000 x 272/109)	1,24,771	3,25,229

**Note:** For the purpose of indexation, the cost inflation index of the year in which the asset is converted into stock-in-trade should be considered.

### ILLUSTRATION 7

Ms. Usha purchases 1,000 equity shares in X Ltd., an unlisted company, at a cost of ₹ 30 per share (brokerage 1%) in January 1996. She gets 100 bonus shares in August 2000. She again gets 1,100 bonus shares by virtue of her holding in February 2006. Fair market value of the shares of X Ltd. on April 1, 2001 is ₹ 80.

On 1<sup>st</sup> January 2021, she transfers all her shares @ ₹ 200 per share (brokerage 2%).

Compute the capital gains taxable in the hands of Ms. Usha for the A.Y. 2021-22

Cost Inflation Index for F.Y. 2001-02: 100, F.Y.2005-06: 117 & F.Y.2020-21: 301.

### SOLUTION

#### Computation of capital gains for the A.Y. 2021-22

Particulars	₹
<b>1000 Original shares</b>	
Sale proceeds (1000 × ₹ 200)	2,00,000
Less : Brokerage paid (2% of ₹ 2,00,000)	4,000
Net sale consideration	1,96,000
Less : Indexed cost of acquisition [₹ 80 × 1000 × 301/100]	2,40,800
<b>Long term capital loss (A)</b>	<b>(44,800)</b>
<b>100 Bonus shares</b>	
Sale proceeds (100 × ₹ 200)	20,000
Less: Brokerage paid (2% of ₹ 20,000)	400
Net sale consideration	19,600
Less: Indexed cost of acquisition [₹ 80 × 100 × 301/100] [See Note below]	24,080
<b>Long term capital loss (B)</b>	<b>(4,480)</b>
<b>1100 Bonus shares</b>	
Sale proceeds (1100 × ₹ 200)	2,20,000
Less: Brokerage paid (2% of ₹ 2,20,000)	4,400
Net sale consideration	2,15,600
Less: Cost of acquisition	NIL
<b>Long term capital gain (C)</b>	<b>2,15,600</b>
<b>∴ Long term capital gain (A+B+C)</b>	<b>1,66,320</b>

**Note:** Cost of acquisition of bonus shares acquired before 1.4.2001 is the FMV as on 1.4.2001 (being the higher of the cost or the FMV as on 1.4.2001).

### ILLUSTRATION 8

On January 31, 2021, Mr. A has transferred self-generated goodwill of his profession for a sale consideration of ₹ 70,000 and incurred expenses of ₹ 5,000 for such transfer. You are required to compute the capital gains chargeable to tax in the hands of Mr. A for the A.Y. 2021-22.

### SOLUTION

The transfer of self-generated goodwill of profession is not chargeable to tax. It is based upon the Supreme Court's ruling in *CIT vs. B.C. Srinivasa Shetty*.

### ILLUSTRATION 9

Mr. R holds 1,000 shares in Star Minus Ltd., an unlisted company, acquired in the year 2001-02 at a cost of ₹ 75,000. He has been offered right shares by the company in the month of August, 2020 at ₹ 160 per share, in the ratio of 2 for every 5 held. He retains 50% of the rights and renounces the balance right shares in favour of Mr. Q for ₹ 30 per share in September 2020. All the shares are sold by Mr. R for ₹ 300 per share in January 2021 and Mr. Q sells his shares in December 2020 at

₹ 280 per share. What are the capital gains taxable in the hands of Mr. R and Mr. Q?

Financial year	Cost Inflation Index
2001-02	100
2020-21	301

## SOLUTION

### Computation of capital gains in the hands of Mr. R for the A.Y.2021-22

Particulars	₹
<b>1000 Original shares</b>	
Sale proceeds (1000 × ₹ 300)	3,00,000
Less: Indexed cost of acquisition [₹ 75,000 × 301/100]	2,25,750
Long-term capital gain (A)	74,250
<b>200 Right shares</b>	
Sale proceeds (200 × ₹ 300)	60,000
Less : Cost of acquisition [₹ 160 × 200] <b>[Note 1]</b>	32,000
Short-term capital gain (B)	28,000
<b>Sale of Right Entitlement</b>	
Sale proceeds (200 × ₹ 30)	6,000
Less : Cost of acquisition <b>[Note 2]</b>	NIL
Short-term capital gain (C)	6,000
<b>Capital Gains (A+B+C)</b>	<b>1,08,250</b>

**Note 1:** Since the holding period of these shares is less than 24 months, they are short term capital assets and hence cost of acquisition will not be indexed.

**Note 2:** The cost of the rights renounced in favour of another person for a consideration is taken to be nil. The consideration so received is taxed as short-term capital gains in full. The period of holding is taken from the date of the rights offer to the date of the renouncement.

### Computation of capital gains in the hands of Mr. Q for the A.Y.2021-22

Particulars	₹
Sale proceeds (200 shares × ₹ 280)	56,000
Less: Cost of acquisition [200 shares × (₹ 30 + ₹ 160)] <b>[See Note below]</b>	38,000
<b>Short-term capital gain</b>	<b>18,000</b>

## **INCOME FROM OTHER SOURCES**

## 8.1 INTRODUCTION

Any income, profits or gains includible in the total income of an assessee, which cannot be included under any of the preceding heads of income, is chargeable under the head 'Income from other sources'. Thus, this head is the **residuary head of income** and brings within its scope all the taxable income, profits or gains of an assessee which fall outside the scope of any other head. Therefore, when any income, profit or gain does not fall precisely under any of the other specific heads but is chargeable under the provisions of the Act, it would be charged under this head.

## 8.2 INCOMES CHARGEABLE UNDER THIS HEAD [SECTION 56]

### (1) Income chargeable only under the head 'Income from other sources':

#### (i) Dividend income [Section 56(2)(i)]

The term 'dividend' as used in the Act has a wider scope and meaning than under the general law.

*Dividend [covered by sections 2(22)(a) to (e)]:*

According to section 2(22), the following receipts are deemed to be dividend:

- (a) **Distribution of accumulated profits, entailing the release of company's assets** - Any distribution of accumulated profits, whether capitalised or not, by a company to its shareholders is dividend if it entails the release of all or any part of its assets.

**Note:** If accumulated profits are distributed in cash, it is dividend in the hands of the shareholders. Where accumulated profits are distributed in kind, for example by delivery of shares etc. entailing the release of company's assets, the market value of such shares on the date of such distribution is deemed dividend in the hands of the shareholder.

- (b) **Distribution of debentures, deposit certificates to shareholders and bonus shares to preference shareholders** - Any distribution to its shareholders by a company of debenture, debenture stock or deposit certificate in any form, whether with or without interest, and any distribution of bonus shares to preference shareholders to the extent to which the company possesses accumulated profits, whether capitalised or not, will be deemed as dividend.

The market value of such bonus shares is deemed as dividend in the hands of the preference shareholder.

In the case of debentures, debenture stock etc., their value is to be taken at the market rate and if there is no market rate they should be valued according to accepted principles of valuation.

**Note:** Bonus shares given to equity shareholders are not treated as dividend.

## INCOME FROM OTHER SOURCES

- (c) **Distribution on liquidation** - Any distribution made to the shareholders of a company on its liquidation, to the extent to which the distribution is attributable to the accumulated profits of the company immediately before its liquidation, whether capitalised or not, is deemed to be dividend income.

**Note:** Any distribution made out of the profits of the company after the date of the liquidation cannot amount to dividend. It is a repayment towards capital.

- (d) **Distribution on reduction of capital** - Any distribution to its shareholders by a company on the reduction of its capital, to the extent to which the company possessed accumulated profits, whether capitalised or not, shall be deemed to be dividend.

- (e) **Advance or loan by a closely held company to its shareholder** – Any payment by a company in which the public are not substantially interested of any sum by way of advance or loan to any shareholder who is the beneficial owner of 10% or more of the voting power of the company will be deemed to be dividend to the extent of the accumulated profits. If the loan is not covered by the accumulated profits, it is not deemed to be dividend.

**Advance or loan by a closely held company to a specified concern** - Any payment by a company in which the public are not substantially interested, to any concern (i.e. HUF/ Firm/ AOP/ BOI/ Company) in which a shareholder, having the beneficial ownership of at least 10% of the equity shares is a member or a partner and in which he has a substantial interest (i.e. at least 20% share of the income of the concern) will be deemed to be dividend.

Also, any payments by such a closely held company on behalf of, or for the individual benefit of any such shareholder will also be deemed to be dividend. However, in both cases the ceiling limit of dividend is to the extent of accumulated profits.

**Exceptions:** The following payments or loan given would not be deemed as dividend:

- (i) **Loan granted in the ordinary course of business** - If the loan is granted in the ordinary course of its business and lending of money is a substantial part of the company's business, the loan or advance to a shareholder or to the specified concern is not deemed to be dividend.
- (ii) **Dividend paid is set off against the deemed dividend** - Where a loan had been treated as dividend and subsequently, the company declares and distributes dividend to all its shareholders including the borrowing shareholder, and the dividend so paid is set off by the company against the previous borrowing, the adjusted amount will not be again treated as a dividend.

**Note:** Subsequent repayment of loan or charge of interest at market rate does not make any difference in the applicability of section 2(22)(e).

## INCOME FROM OTHER SOURCES

### Other exceptions

Apart from the exceptions cited above, the following also do not constitute “dividend” -

- (i) **Distribution in respect of non-participating shares issued for full cash consideration**  
– Any distribution made in accordance with (c) or (d) in respect of any share issued for full cash consideration and the holder of such share is not entitled to participate in the surplus asset in the event of liquidation.
- (ii) **Payment on buy back of shares** - Any payment made by a company on purchase of its own shares from a shareholder in accordance with the provisions of section 77A of the Companies Act, 1956<sup>1</sup>;
- (iii) **Distribution of shares to the shareholders on demerger by the resulting company** - Any distribution of shares on demerger by the resulting company to the shareholders of the demerged company (whether or not there is a reduction of capital in the demerged company).

### Meaning of “accumulated profits”

Accumulated profits in point (a), (b), (d) and (e) above include all profits of the company up to the date of distribution or payment of dividend.

Building & Machinery Depreciation fund not to be included in accumulated profits. - *CIT v. Jaldu Rama Rao* (1983) 140 ITR 168 (Andhra Pradesh)

Accumulated profits include in point (c) all profits of the company up to the date of liquidation whether capitalised or not. But where liquidation is consequent to the compulsory acquisition of an undertaking by the Government or by any corporation owned or controlled by the Government, the accumulated profits do not include any profits of the company prior to the 3 successive previous years immediately preceding the previous year in which such acquisition took place.

In the case of an amalgamated company, the accumulated profits, whether capitalized or not, of the amalgamating company on the date of amalgamation shall be included in the accumulated profits, whether capitalized or not or loss, as the case may be, of the amalgamated company.

## INCOME FROM OTHER SOURCES

### *Basis of charge of dividend*

*Any income by way of dividend received from a company, whether domestic or foreign, is taxable in the hands of shareholder at normal rates of tax.*

*However, dividend distributed by a domestic company before 1.4.2020 and received by the shareholders on or after 1.4.2020 and on which dividend distribution tax under section 115-O<sup>2</sup>, if applicable, has been paid would be exempt in the hands of the shareholders except dividend chargeable to tax u/s 115BBDA.*

*Tax on certain dividends distributed by domestic companies before 1.4.2020 but received on or after 1.4.2020 [Section 115BBDA]*

- (i) Any income by way of aggregate dividend **in excess of ` 10 lakh** distributed by domestic companies before 1.4.2020 but received on or after 1.4.2020 shall be chargeable to tax in

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<sup>2</sup> Upto F.Y. 2019-20, domestic company was liable to pay additional income-tax u/s 115-O @15% [30%, in respect of deemed dividend u/s 2(22)(e)] on dividend distributed by it, consequent to which dividend was exempt in the hands of shareholder u/s 10(34) except dividend chargeable to tax u/s 115BBDA.

## INCOME FROM OTHER SOURCES

### (ii) Meaning of certain terms

Term	Meaning
<b>Specified assessee</b>	<p>A person, resident in India, other than</p> <ul style="list-style-type: none"> <li>➤ domestic company</li> <li>➤ a fund or institution or trust or any university or other educational institution or any hospital or other medical institution referred to in section 10(23C)(iv)/(v)/(vi)/(via)</li> <li>➤ a trust or institution registered under section 12A or 12AA</li> </ul>
<b>Dividend</b>	Includes dividend referred under section 2(22)(a) to (d) but shall not include sub-clause (e) thereof.

- (iii) Further, the taxation of dividend income in excess of ₹ 10 lakh shall be on gross basis i.e., no deduction in respect of any expenditure or allowance or set-off of loss shall be allowed to the assessee in computing the income by way of dividends.

### Casual Income [Section 56(2)(ib)]

Casual income means income in the nature of winning from lotteries, crossword puzzles, races including horse races, card games and other games of any sort, gambling, betting etc. Such winnings are chargeable to tax at a flat rate of 30% under section 115BB and tax is deductible at source @ 30% on such income in case it exceeds ₹ 10,000.

### (ii) Consideration received in excess of FMV of shares issued by a closely held company to be treated as income of such company, where shares are issued at a premium [Section 56(2)(viib)]

- (a) Section 56(2)(viib) brings to tax the consideration received from a resident person by a company, other than a company in which public are substantially interested, which is in excess of the fair market value (FMV) of shares.
- (b) Such excess is to be treated as the income of a closely held company taxable under section 56(2) under the head "Income from Other Sources", in cases where consideration received for issue of shares exceeds the face value of shares i.e. where shares are issued at a premium i.e., (Issue price of share – FMV of such share) x No. of shares.
- (c) Fair market value of the shares shall be the higher of, the value as may be –
- (1) determined in accordance with the prescribed method<sup>3</sup>; or
  - (2) substantiated by the company to the satisfaction of the Assessing Officer, based on the value of its assets on the date of issue of shares.

For the purpose of computation of FMV, the value of assets would include the value of intangible assets being goodwill, know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature.

## INCOME FROM OTHER SOURCES

					$\text{₹ } 1,00,000 [10,000 \times \text{₹ } 10 (\text{₹ } 130 - \text{₹ } 120)]$ shall be treated as income in the hands of A (P) Ltd.
<b>Example 2</b>					
B (P) Ltd.	20,000	100	120	110	The provisions of section 56(2)(viib) are attracted since the shares are issued at a premium. However, no sum shall be chargeable to tax in the hands of B (P) Ltd. under the said section as the shares are issued at a price less than the FMV of shares.
<b>Example 3</b>					
C (P) Ltd.	30,000	100	90	98	Section 56(2)(viib) is not attracted since the shares are issued at a discount, though the issue price is greater than the FMV.
<b>Example 4</b>					
D (P) Ltd.	40,000	100	90	110	The provisions of section 56(2)(viib) are attracted in this case since the shares are issued at a premium. The excess of the issue price of the shares over the FMV would be taxable under section 56(2)(viib). Therefore, $\text{₹ } 8,00,000 [40,000 \times \text{₹ } 20 (\text{₹ } 110 - \text{₹ } 90)]$ shall be treated as income in the hands of D (P) Ltd.

(d) However, these provisions would not be attracted where consideration for issue of shares is received:

- (1) by a Venture Capital Undertaking (VCU) from a Venture Capital Fund (VCF) or Venture Capital Company (VCC) or a specified fund;

"Specified Fund" means a fund established or incorporated in India in the form of a trust or a company or a limited liability partnership or a body corporate which has been granted a certificate of registration as a Category I or a Category II Alternative Investment Fund and is regulated under the Securities and Exchange Board of India (Alternative Investment Fund) Regulations, 2012 made under the Securities and Exchange Board of India Act, 1992.

"Trust" means a trust established under the Indian Trusts Act, 1882 or under any other law for the time being in force;

## INCOME FROM OTHER SOURCES

- (2) by a company from a class or classes of persons as notified by the Central Government for this purpose.

Accordingly, the Central Government has, vide Notification No. 13/2019, dated 5-03- 2019, notified that the provisions of section 56(2)(viib) shall not apply to consideration received by a company for issue of shares that exceeds the face value of such shares, if the said consideration received from a person, being a resident, by a company which fulfills the conditions specified by the Ministry of Commerce and Industry in the Department for Promotion of Industry and Internal Trade and files the declaration referred to in the said notification. In effect, vide this notification, the Central Government has notified the conditions to be fulfilled by a company which issues shares rather than the class or classes of persons to whom such shares are issued.

The Ministry of Commerce and Industry in the Department for Promotion of Industry and Internal Trade has, vide Notification No. G.S.R. 127(E) dated 19.2.2019, specified in para 4 thereunder, that a startup shall be eligible for exemption under clause (ii) of the proviso to section 56(2)(viib), if it fulfills the following conditions:

- (i) It has been recognized by the Department for Promotion of Industry and Internal Trade as start up as per this notification or any earlier notification on the subject.
- (ii) Aggregate amount of paid up capital and share premium of the startup after issue or proposed issue of shares, if any, does not exceed, twenty five crore rupees.

However, in computing the aggregate amount of paid up share capital, the amount of paid up share capital and share premium of twenty five crore rupees in respect of shares issued to any of the following persons shall not be included:

- (a) a non-resident
- (b) a venture capital company or a venture capital fund

Further, consideration received by such startup for shares issued or proposed to be issued to a specified company shall also be exempt and shall not be included in computing the aggregate amount of paid up share capital and share premium of twenty five crore rupees. For this purpose, a specified company means a company whose shares are frequently traded within the meaning of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 and whose net worth on the last date of financial year preceding the year in which shares are issued exceeds one hundred crore rupees or turnover for the financial year preceding the year in which shares are issued exceeds two hundred fifty crore rupees.

## INCOME FROM OTHER SOURCES

- (iii) It has not invested in any of the following assets –
- (a) building or land appurtenant thereto, being a residential house, other than that used by the Startup for the purposes of renting or held by it as stock-in-trade, in the ordinary course of business;
  - (b) land or building, or both, not being a residential house, other than that occupied by the Startup for its business or used by it for purposes of renting or held by it as stock-in-trade, in the ordinary course of business;
  - (c) loans and advances, other than loans or advances extended in the ordinary course of business by the Startup where the lending of money is substantial part of its business;
  - (d) capital contribution made to any other entity;
  - (e) shares and securities;
  - (f) a motor vehicle, aircraft, yacht or any other mode of transport, the actual cost of which exceeds ten lakh rupees, other than that held by the Startup for the purpose of plying, hiring, leasing or as stock-in-trade, in the ordinary course of business;
  - (g) jewellery other than that held by the Startup as stock-in-trade in the ordinary course of business;
  - (h) any other asset, whether in the nature of capital asset or otherwise, of the nature specified in section 56(2)(vii)(d)(iv) to (ix) i.e., archaeological collections, drawings, paintings, sculptures, any work of art or bullion.

However, the Startup should not invest in any of the assets mentioned above for the period of seven years from the end of the latest financial year in which shares are issued at premium;

### (a) Immovable property [Land or building or both]:

#### I. If an immovable property is received

- (a) **Without consideration:** the stamp duty value of such property would be taxed as the income of the recipient, if it exceeds ₹ 50,000.
- (b) **For Inadequate consideration:** If consideration is less than the stamp duty value of the property and the difference between the stamp duty value and consideration is more than the higher of –
  - (i) ₹ 50,000 and
  - (ii) **10%** of consideration,

the difference between the stamp duty value and the consideration shall be chargeable to tax in the hands of the assessee as “Income from other sources”.

**Note:** The above limit shall be considered for **each property separately**.

- #### II. Value of property to be considered where the date of agreement is different from date of registration:
- Taking into consideration the possible time gap between the date of agreement and the date of registration, the stamp duty value may be taken as on the date of agreement instead of the date of registration, if the date of the agreement fixing the amount of consideration for the transfer of the immovable property and the date of registration are not the same, provided whole or part of the consideration has been paid by way of an account payee cheque or an accountpayee bank draft or by use of electronic clearing system (ECS) through a bank account **or through such**

## INCOME FROM OTHER SOURCES

**prescribed electronic mode** on or before the date of agreement.

*The prescribed electronic modes notified are credit card, debit card, net banking, IMPS (Immediate payment Service), UPI (Unified Payment Interface), RTGS (Real Time Gross Settlement), NEFT (National Electronic Funds Transfer), and BHIM (Bharat Interface for Money) Aadhar Pay as other electronic modes of payment [CBDT Notification No. 8/2020 dated 29.01.2020].*

- III. **If the stamp duty value of immovable property is disputed by the assessee, the Assessing Officer may refer the valuation of such property to a Valuation Officer.** In such a case, the provisions of section 50C and section 155(15) shall, as far as may be, apply for determining the value of such property. As per section 50C, if such value is less than the stamp duty value, the same would be taken for

determining the value of such property, for computation of income under this head in the hands of the buyer.

**(b) Movable Property [Property other than immovable property]:**

If movable property is received

- (i) **Without consideration:** The aggregate fair market value of such property on the date of receipt would be taxed as the income of the recipient, if it exceeds ₹ 50,000.
  - (ii) **For inadequate consideration:** If the difference between the aggregate fair market value and such consideration exceeds ₹ 50,000, such difference would be taxed as the income of the recipient.
- (c) **Applicability of section 56(2)(x):** The provisions of section 56(2)(x) would apply only to the specified property which is the nature of a capital asset of the recipient and not stock-in-trade, raw material or consumable stores of any business of the recipient. Therefore, only transfer of a specified capital asset, without consideration or for inadequate consideration would attract the provisions of section 56(2)(x).
- (d) **The table below summarizes the scheme of taxability of gifts –**

	Nature of asset	Taxable value
1	Money	The whole amount if the same exceeds ₹ 50,000.
2	Movable property	<p><b>(i) Without consideration:</b> The aggregate fair market value of the property, if it exceeds ₹ 50,000.</p> <p><b>(ii) Inadequate consideration:</b> The difference between the aggregate fair market value and the consideration, if such difference exceeds ₹ 50,000.</p>
3	Immovable property	<p><b>(i) Without consideration:</b> The stamp value of the property, if it exceeds ₹ 50,000.</p> <p><b>(ii) Inadequate consideration:</b> The difference between the stamp duty value and the consideration, if such difference is more than the higher of ₹ 50,000 and <b>10%</b> of consideration.</p>

- (e) **Non-applicability of section 56(2)(x):** However, any sum of money or value of property received in the following circumstances would be outside the ambit of section 56(2)(x) -
- (i) from any relative; or
  - (ii) on the occasion of the marriage of the individual; or
  - (iii) under a will or by way of inheritance; or

## INCOME FROM OTHER SOURCES

- (iv) in contemplation of death of the payer or donor, as the case may be; or
- (v) from any local authority as defined in the *Explanation* to section 10(20); or
- (vi) from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in section 10(23C); or
- (vii) from or by any trust or institution registered under section 12A or section 12AA; or
- (viii) by any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in Section 10(23C)(iv)/(v)/(vi)/(via).
- (ix) by way of transaction not regarded as transfer under section 47(i)/(iv)/(v)/(vi)/(via)/(viaa)/(vib)/(vic)/(vica)/(vicb)/(vid)/(vii).
- (x) from an individual by a trust created or established solely for the benefit of relative of the individual.
- (xi) from such class of persons and subject to such conditions, as may be prescribed.

Accordingly, CBDT has, vide Notification No. 40/2020, dated 29<sup>th</sup> June, 2020, notified that the provisions of section 56(2)(x) would not be applicable to the following transactions –

S.No.	Property	Received by	Condition
1.	Any immovable property, being land or building or both	a resident of an unauthorized colony in the National Capital Territory of Delhi	where the Central Government by notification in the Official Gazettee, regularised the transactions of such immovable property based on the latest Power of Attorney, Agreement to Sale, Will, possession letter and other documents including documents evidencing payment of consideration for conferring or recognising right of ownership or transfer or mortgage in regard to such immovable property in favour of such resident.
	<b>Resident means</b> a person having physical possession of property on the basis of a registered sale deed or latest set of Power of Attorney, Agreement to Sale, Will, possession letter and other documents including documents evidencing payment of consideration in respect of a property in unauthorised colonies and includes their legal heirs but does not include tenant, licensee or permissive user.		

## INCOME FROM OTHER SOURCES

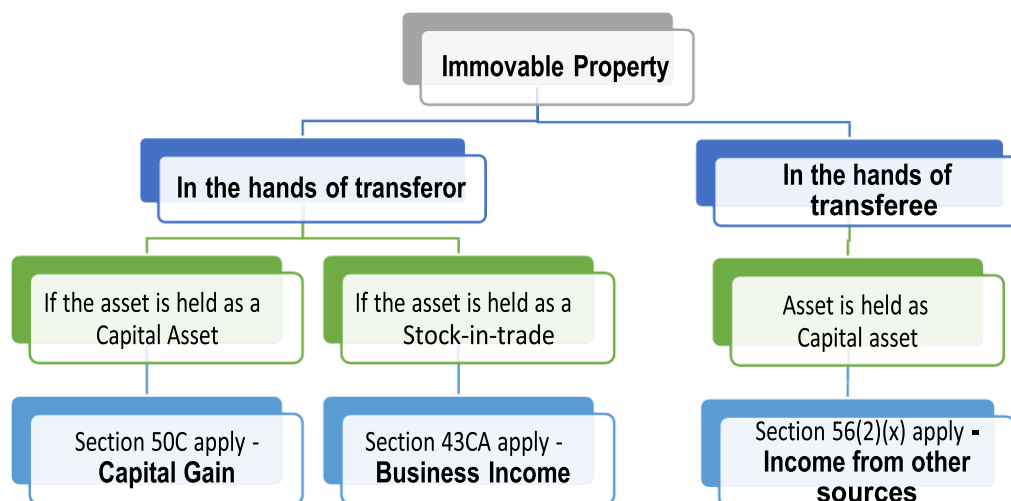
	<b>Unauthorised colony means</b> a colony or development comprising of a contiguous area, where no permission has been obtained for approval of layout plan or building plans and has been identified for regularisation of such colony in pursuance to the notification number S.O. 683(E), dated the 24th March, 2008, of the Delhi Development Authority.		
2.	Any movable property, being unquoted shares, of a company and its subsidiary and the subsidiary of such subsidiary	Shareholder	Where, (i) the Tribunal, on an application moved by the Central Government under section 241 of the Companies Act, 2013, has suspended the Board of Directors of such company and has appointed new directors nominated by the Central Government under section 242 of the said Act; and (ii) share of company and its subsidiary and the subsidiary of such subsidiary has been received pursuant to a resolution plan approved by the Tribunal under section 242 of the Companies Act, 2013 after affording a reasonable opportunity of being heard to the jurisdictional Principal Commissioner or Commissioner.
	A company shall be a subsidiary of another company, if such other company holds more than half in nominal value of the equity share capital of the company;		
3.	Any movable property, being equity shares, of the reconstructed bank	Investor or investor bank	where the said share has been allotted by the reconstructed bank under the scheme at a price specified in sub-paragraph (3) of paragraph 3 of the Yes Bank Limited Reconstruction Scheme, 2020.

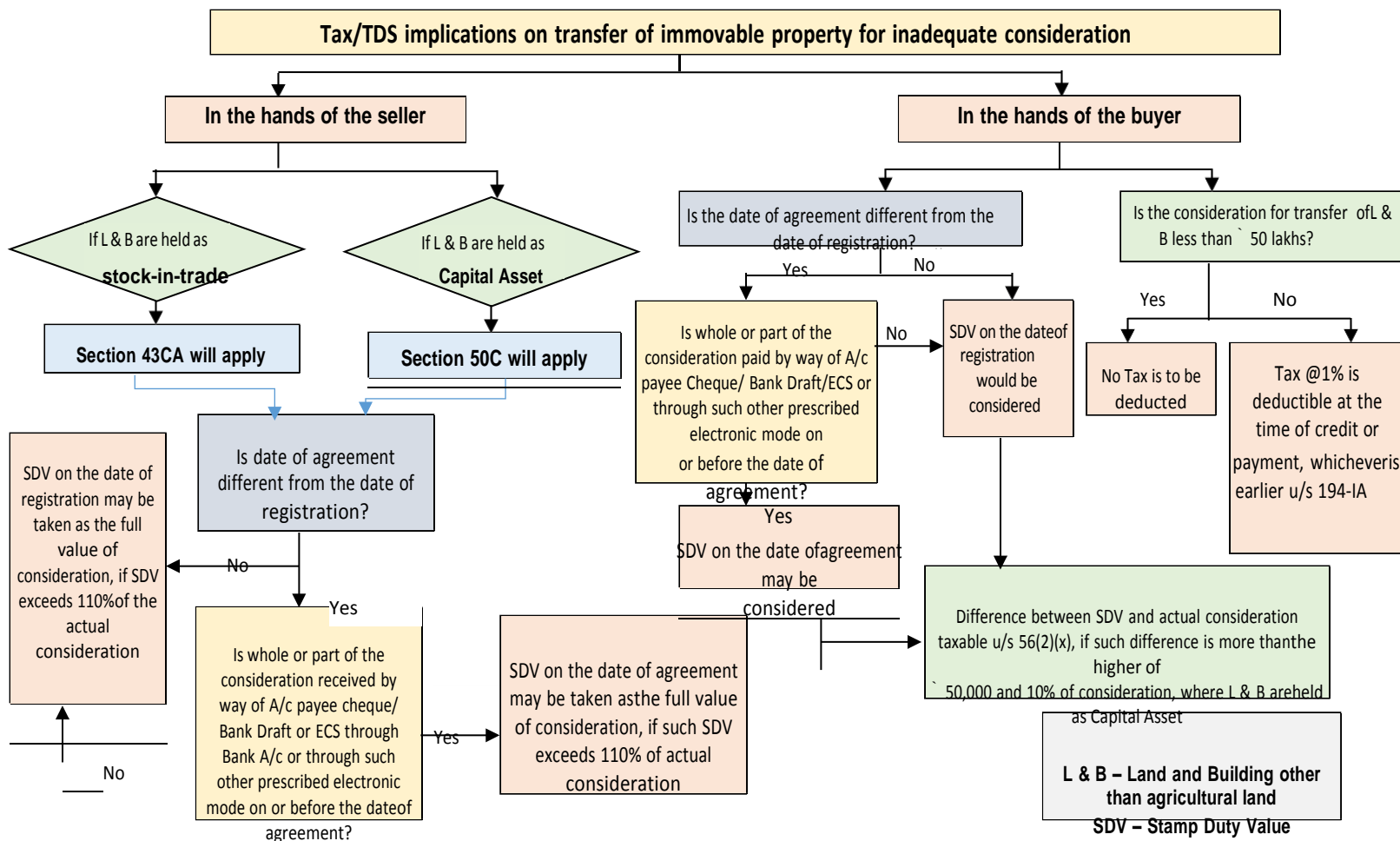
## INCOME FROM OTHER SOURCES

(f) **Meaning of certain terms:**

Term	Meaning
<b>Property</b>	A <b>capital asset</b> of the assessee, namely,- (a) immovable property being land or building or both, (b) shares and securities, (c) jewellery, (d) archaeological collections, (e) drawings, (f) paintings, (g) sculptures, (h) any work of art or bullion.
<b>Relative</b>	<b>(a) In case of an individual –</b> (i) spouse of the individual; (ii) brother or sister of the individual; (iii) brother or sister of the spouse of the individual; (iv) brother or sister of either of the parents of the individual; (v) any lineal ascendant or descendant of the individual; (vi) any lineal ascendant or descendant of the spouse of the individual; (vii) spouse of any of the persons referred to above. <b>(b) In case of Hindu Undivided Family, any member thereof.</b>

### SUMMARY





## INCOME FROM OTHER SOURCES

### ILLUSTRATION 3

Mr. A, a dealer in shares, received the following without consideration during the P.Y.2020-21 from his friend Mr. B, -

- (1) Cash gift of ₹ 75,000 on his anniversary, 15<sup>th</sup> April, 2020.
- (2) Bullion, the fair market value of which was ₹ 60,000, on his birthday, 19<sup>th</sup> June, 2020.
- (3) A plot of land at Faridabad on 1<sup>st</sup> July, 2020, the stamp value of which is ₹ 5 lakh on that date. Mr. B had purchased the land in April, 2009.

Mr. A purchased from his friend Mr. C, who is also a dealer in shares, 1000 shares of X Ltd. @ ₹ 400 each on 19<sup>th</sup> June, 2020, the fair market value of which was ₹ 600 each on that date. Mr. A sold these shares in the course of his business on 23<sup>rd</sup> June, 2020.

Further, on 1<sup>st</sup> November, 2020, Mr. A took possession of property (building) booked by him two years back at ₹ 20 lakh. The stamp duty value of the property as on 1<sup>st</sup> November, 2020 was ₹ 32 lakh and on the date of booking was ₹ 23 lakh. He had paid ₹ 1 lakh by account payee cheque as down payment on the date of booking.

On 1<sup>st</sup> March, 2021, he sold the plot of land at Faridabad for ₹ 7 lakh.

Compute the income of Mr. A chargeable under the head "Income from other sources" and "Capital Gains" for A.Y.2021-22.

### SOLUTION

#### Computation of "Income from other sources" of Mr. A for the A.Y.2021-22

	Particulars	₹
(1)	Cash gift is taxable under section 56(2)(x), since it exceeds ₹ 50,000	75,000
(2)	Since bullion is included in the definition of property, therefore, when bullion is received without consideration, the same is taxable, since the aggregate fair market value exceeds ₹ 50,000	60,000
(3)	Stamp value of plot of land at Faridabad, received without consideration, is taxable under section 56(2)(x)	5,00,000
(4)	Difference of ₹ 2 lakh in the value of shares of X Ltd. purchased from Mr. C, a dealer in shares, is not taxable as it represents the stock-in-trade of Mr. A. Since Mr. A is a dealer in shares and it has been mentioned that the shares were subsequently sold in the course of his business, such shares represent the stock-in-trade of Mr. A.	-
(5)	Difference between the stamp duty value of ₹ 23 lakh on the date of booking and the actual consideration of ₹ 20 lakh paid is taxable under section 56(2)(x) since the difference exceeds ₹ 1 lakh being, the higher of ₹ 50,000 and 10% of consideration.	3,00,000
<b>Income from Other Sources</b>		<b>9,35,000</b>

## INCOME FROM OTHER SOURCES

### Computation of "Capital Gains" of Mr. A for the A.Y.2021-22

Particulars	₹
Sale Consideration	7,00,000
Less: Cost of acquisition [deemed to be the stamp value charged to tax under section 56(2)(x) as per section 49(4)]	5,00,000
<b>Short-term capital gains</b>	<b>2,00,000</b>

**Note** – The resultant capital gains will be short-term capital gains since for calculating the period of holding, the period of holding of previous owner is not to be considered.

#### ILLUSTRATION 4

Discuss the taxability or otherwise of the following in the hands of the recipient under section 56(2)(x) of the Income-tax Act, 1961 -

- (i) Akhil HUF received ₹ 75,000 in cash from niece of Akhil (i.e., daughter of Akhil's sister). Akhil is the Karta of the HUF.
- (ii) Nitisha, a member of her father's HUF, transferred a house property to the HUF without consideration. The stamp duty value of the house property is ₹ 9,00,000.
- (iii) Mr. Akshat received 100 shares of A Ltd. from his friend as a gift on occasion of his 25<sup>th</sup> marriage anniversary. The fair market value on that date was ₹ 100 per share. He also received jewellery worth ₹ 45,000 (FMV) from his nephew on the same day.
- (iv) Kishan HUF gifted a car to son of Karta for achieving good marks in XII board examination. The fair market value of the car is ₹ 5,25,000.

#### SOLUTION

	Taxable/ Non-taxable	Amount liable to tax (₹)	Reason
(i)	Taxable	75,000	Sum of money exceeding ₹ 50,000 received without consideration from a non-relative is taxable under section 56(2)(x). Daughter of Mr. Akhil's sister is not a relative of Akhil HUF, since she is not a member of Akhil HUF.
(ii)	Non-taxable	Nil	Immovable property received without consideration by a HUF from its relative is not taxable under section 56(2)(x). Since Nitisha is a member of the HUF, she is a relative of the HUF. However, income from such asset would be included in the hands of Nitisha under 64(2).
(iii)	Taxable	55,000	As per provisions of section 56(2)(x), in case the aggregate fair market value of property, other than immovable property, received without consideration exceeds ₹ 50,000,

## INCOME FROM OTHER SOURCES

			the whole of the aggregate value shall be taxable. In this case, the aggregate fair market value of shares (₹ 10,000) and jewellery (₹ 45,000) exceeds ₹ 50,000. Hence, the entire amount of ₹ 55,000 shall be taxable.
(iv)	Non-taxable	Nil	Car is not included in the definition of property for the purpose of section 56(2)(x), therefore, the same shall not be taxable.

### ILLUSTRATION 5

Mr. Hari, a property dealer, sold a building in the course of his business to his friend Mr. Rajesh, who is a dealer in automobile spare parts, for ₹ 90 lakh on 1.1.2021, when the stamp duty value was ₹ 150 lakh. The agreement was, however, entered into on 1.9.2020 when the stamp duty value was ₹ 140 lakh. Mr. Hari had received a down payment of ₹ 15 lakh by a crossed cheque from Mr. Rajesh on the date of agreement. Discuss the tax implications in the hands of Mr. Hari and Mr. Rajesh, assuming that Mr. Hari has purchased the building for ₹ 75 lakh on 12<sup>th</sup> July, 2019.

Would your answer be different if Hari was a share broker instead of a property dealer and Mr. Rajesh was a property dealer instead of dealer in automobile spare parts?

### SOLUTION

#### Case 1: Tax implications if Mr. Hari is a property dealer

In the hands of Mr. Hari	In the hands of Mr. Rajesh
<p>In the hands of Hari, the provisions of section 43CA would be attracted, since the building represents his stock-in-trade and he has transferred the same for a consideration less than the stamp duty value; and the stamp duty value exceeds 110% of consideration.</p> <p>Under section 43CA, the option to adopt the stamp duty value on the date of agreement can be exercised only if whole or part of the consideration has been received on or before the date of agreement by way of account payee cheque or draft or by use of ECS through a bank account or through credit card, debit card, net banking, IMPS (Immediate payment Service), UPI (Unified Payment Interface), RTGS (Real Time Gross Settlement), NEFT (National Electronic Funds Transfer), and BHIM (Bharat Interface for Money) Aadhar Pay on or before the date of agreement. In this case, since the down payment of ₹ 15 lakh is received on the date of agreement by crossed cheque and not account payee cheque, the option cannot be exercised.</p>	<p>Since Mr. Rajesh is a dealer in automobile spare parts, the building purchased would be a capital asset in his hands. The provisions of section 56(2)(x) would be attracted in the hands of Mr. Rajesh who has received immovable property, being a capital asset, for inadequate consideration and the difference between the consideration and stamp duty value exceeds ₹ 9,00,000, being the higher of ₹ 50,000 and <b>10% of consideration.</b></p> <p>Therefore, ₹ 60 lakh, being the difference between the stamp duty value of the property on the date of registration (i.e., ₹ 150 lakh) and the actual consideration (i.e., ₹ 90 lakh) would be taxable under section 56(2)(x) in the hands of Mr. Rajesh, since the payment on the date of agreement is made by crossed cheque and not account payee cheque/draft or ECS or through credit card, debit card, net banking, IMPS</p>

## INCOME FROM OTHER SOURCES

Therefore, ` 75 lakh, being the difference between the stamp duty value on the date of transfer i.e., ` 150 lakh, and the purchase price i.e., ` 75 lakh, would be chargeable as <b>business income</b> in the hands of Mr. Hari, since stamp duty value exceeds <b>110% of the consideration</b> .	<i>(Immediate payment Service), UPI (Unified Payment Interface), RTGS (Real Time Gross Settlement), NEFT (National Electronic Funds Transfer), and BHIM (Bharat Interface for Money) Aadhar Pay.</i>
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### Case 2: Tax implications if Mr. Hari is a stock broker

In the hands of Mr. Hari	In the hands of Mr. Rajesh
<p>In case Mr. Hari is a share broker and not a property dealer, the building would represent his capital asset and not stock-in-trade. In such a case, the provisions of section 50C would be attracted in the hands of Mr. Hari, since building is transferred for a consideration less than the stamp duty value; and the stamp duty value exceeds 110% of consideration.</p> <p>Thus, ` 75 lakh, being the difference between the stamp duty value on the date of registration (i.e., ` 150 lakh) and the purchase price (i.e., ` 75 lakh) would be chargeable as short-term capital gains.</p> <p>It may be noted that under section 50C, the option to adopt the stamp duty value on the date of agreement can be exercised only if whole or part of the consideration has been received on or before the date of agreement by way of account payee cheque or draft or by use of ECS through a bank account or through credit card, debit card, net banking, IMPS (Immediate payment Service), UPI (Unified Payment Interface), RTGS (Real Time Gross Settlement), NEFT (National Electronic Funds Transfer), and BHIM (Bharat Interface for Money) Aadhar Pay on or before the date of agreement. In this case, since the down payment of ` 15 lakhs has been received on the date of agreement by crossed cheque and not account payee cheque, the option cannot be exercised.</p>	<p>In case Mr. Rajesh is a property dealer and not a dealer of automobile spare parts, the building would represent his stock-in-trade and not a capital asset. In such a case, the provisions of section 56(2)(x) would not be attracted in the hands of Mr. Rajesh and no amount will be taxable in the hands of Mr. Rajesh for purchase of the said building.</p>

## INCOME FROM OTHER SOURCES

### (vii) Compensation or any other payment received in connection with termination of his employment [Section 56(2)(xi)]

Any compensation or any other payment, due to or received by any person, by whatever name called, in connection with the termination of his employment or the modification of the terms and conditions relating thereto shall be chargeable to tax under this head. However, if it is received from employer, then it is

### (2) Income chargeable under the head “Income from other sources” only if not chargeable under the head “Profits and gains of business or profession” -

taxable u/s 17(3)(i) under the head “Income from Salaries”.

- (i) Any sum received by an employer-assessee from his employees as contributions to any provident fund, superannuation fund or any other fund for the welfare of the employees.
- (ii) Income from letting out on hire, machinery, plant or furniture.
- (iii) Where letting out of buildings is inseparable from the letting out of machinery, plant or furniture, the income from such letting.
- (iv) Interest on securities

**However, the following Interest income arising to certain persons would be exempt under section 10(15):**

- (a) Income by way of interest, premium on redemption or other payment on notified securities, bonds, annuity certificates or other savings certificates is exempt subject to such conditions and limits as may be specified in the notification.

Interest on Post Office Savings Bank Account would be exempt from tax to the extent of:

- (1) ₹ 3,500 in case of an individual account.
- (2) ₹ 7,000 in case of a joint account.

- (b) Interest payable —

- (1) by public sector companies on certain specified bonds and debentures subject to the conditions which the Central Government may specify by notification, including the condition that the holder of such bonds or debentures registers his name and holding with that company;

Accordingly, the Central Government has specified tax free bonds issued by India Infrastructure Company Ltd. and tax free, secured, redeemable, non-convertible Bonds of the Indian Railway Finance Corporation Ltd. (IRFCL), National Highways Authority of India (NHAI), Rural Electrification Corporation Ltd. (RECL), Housing and Urban Development Corporation Ltd. (HUDCL), Power Finance Corporation (PFC), Jawaharlal Nehru Port Trust, Dredging Corporation of India Limited, Ennore Port Limited and The Indian Renewable

## INCOME FROM OTHER SOURCES

Energy Development Agency Limited, the interest from which would be exempt under this section.

- (2) by Government of India on deposit made by an employee of the Central or State Government or a public sector company in accordance with the scheme as may be notified of the moneys due to him on account of his retirement while on superannuation or otherwise. It is significant that this scheme is not applicable to non-Government employees.

The term 'industrial undertaking' means any undertaking which is engaged in:

- (i) the manufacture or processing of goods; or
- (ii) the manufacture of computer software or recording of programmes on any disc, tape, perforated media or other information device; or
- (iii) the business of generation or generation and distribution of electricity or any other form of power; or
- (iv) the business of providing telecommunication services; or
- (v) mining; or
- (vi) construction of ships, or
- (vii) the business of ship-breaking; or
- (viii) the operation of ships or aircrafts or construction or operation of rail systems.

For the purposes of the clause, "interest" shall not include interest paid on delayed payment of loan or default if which is more than 2% p.a. over the rate of interest payable in terms of such loan. Interest would include hedging transaction charges on account of currency fluctuation.

- (c) **Bhopal Gas Victims** - Section 10(15)(v) provides exemption in respect of interest on securities held by the Welfare Commissioner, Bhopal Gas Victims, Bhopal, in the Reserve Bank's Account No. SL/DH 048. Recently, in terms of an order of the Supreme Court to finance the construction of a hospital at Bhopal to serve the victims of the gas leak, the shares of the Union Carbide Indian Ltd., have been sold. The scope of the above exemption has been extended to interest on deposits for the benefit of the victims of the Bhopal Gas Leak disaster. Such deposits can be held in such account with the RBI or with a public sector bank as the Central Government may notify in the Official Gazette.
- (d) Interest on Gold Deposit Bond issued under the Gold Deposit Scheme, 1999 or deposit certificates issued under the Gold Monetization Scheme, 2015 notified by the Central Government.

## INCOME FROM OTHER SOURCES

- (e) Interest on bonds, issued by –
- (1) a local authority; or
  - (2) a State Pooled Finance Entity

and specified by the Central Government by notification in the Official Gazette.

**“State Pooled Finance Entity”** means such entity which is set up in accordance with the guidelines for the Pooled Finance Development Scheme notified by the Central Government in the Ministry of Urban Development.

Accordingly, the Central Government has specified the “Tax-free Pooled Finance Development Bonds” under Pooled Finance Development Fund Scheme of Government of India, interest from which would be exempt under section 10(15).

### (3) Keyman Insurance Policy

Any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy is chargeable under the head “Income from other sources” if such income is not chargeable under the head “Profits and gains of business or profession” or under the head “Salaries” i.e. if such sum is received by any person other than the employer who took the policy and the employee in whose name the policy was taken.

### (4) Residual Income

Any income chargeable to tax under the Act, but not falling under any other head of income shall be chargeable to tax under the head “Income from other sources” e.g. Salary received by an MPs/MLAs will not be chargeable to income-tax under the head ‘Salary’ but will be chargeable as “Income from other

#### ***Interest from non-SLR Securities of Banks: Whether chargeable under the head “Profits and gains of business or profession” or “Income from other sources”? [Circular No. 18, dated 2.11.2015]***

*The issue addressed by this circular is whether in the case of banks, expenses relatable to investment in non-SLR securities need to be disallowed under section 57(i), by considering interest on non-SLR securities as “Income from other sources.”*

*Section 56(1)(id) provides that income by way of interest on securities shall be chargeable to income-tax under the head “Income from Other Sources”, if the income is not chargeable to income-tax under the head “Profits and Gains of Business and Profession”.*

*The CBDT clarified that the **investments made by a banking concern are part of the business of banking**. Therefore, the income arising from such investments is attributable to the business of banking falling **under the head “Profits and Gains of Business and Profession”**.*

sources” under section 56.

## INCOME FROM OTHER SOURCES

### 8.3 APPLICABLE RATE OF TAX IN RESPECT OF CASUAL INCOME [SECTION 115BB]

- (1) This section provides that income by way of winnings from lotteries, crossword puzzles, races including horse races or card games and other games of any sort or from gambling or betting of any form would be taxed at a flat rate of 30% *plus* surcharge, if applicable, plus **health and education cess @4%**.
- (2) No expenditure or allowance can be allowed from such income.
- (3) Deduction under Chapter VI-A is not allowable from such income.
- (4) Adjustment of unexhausted basic exemption limit is also not permitted against such income.

### 8.4 DEDUCTIONS ALLOWABLE [SECTION 57]

The income chargeable under the head “Income from other sources” shall be computed after making the following deductions:

- (1) ***In the case of dividend or income in respect of units of a mutual fund specified under section 10(23D) or income in respect of units of a specified company defined in the Explanation to section 10(35) : Interest expenditure to earn such income is allowed as deduction subject to a maximum of 20% of such income included in the total income, without deduction under this section.***
- (2) **In the case of interest on securities:** Any reasonable sum paid by way of commission or remuneration to a banker or any other person for the purpose of realising such interest on behalf of the assessee.
- (3) **Income consists of recovery from employees as contribution to any provident fund etc. in terms of section 2(24)(x):** A deduction will be allowed in accordance with the provisions of section 36(1)(va) i.e. to the extent the contribution is remitted before the due date under the respective Acts.
- (4) **Where the income to be charged under this head is from letting on hire of machinery, plant and furniture, with or without building:** The following items of deductions are allowable in the computation of such income:
  - (i) the amount paid on account of any current repairs to the machinery, plant or furniture.
  - (ii) the amount of any premium paid in respect of insurance against risk of damage or destruction of the machinery or plant or furniture.
  - (iii) the normal depreciation allowance in respect of the machinery, plant or furniture, due thereon.

## INCOME FROM OTHER SOURCES

- (5) **In the case of income in the nature of family pension:** A deduction of a sum equal to 33-1/3 percent of such income or ₹ 15,000, whichever is less, is allowable.

For the purposes of this deduction "family pension" means a regular monthly amount payable by the employer to a person belonging to the family of an employee in the event of his death.

### **Exemption in respect of family pension**

1. *The family pension received by the widow or children or nominated heirs, **of a member of the armed forces (including para-military forces)** of the Union, where the death of such member has occurred in the course of operational duties, in specified circumstances would, however, be exempt under section 10(19).*
2. *The family pension received by any member of the family of an individual who had been in the service of Central or State Government and had been awarded "Param Vir Chakra" or "Vir Chakra" or "Vir Chakra" or other notified gallantry awards would be exempt under section 10(18)(ii).*

- (6) **Any other expenditure not being in the nature of capital expenditure** laid out or expended wholly and exclusively for the purpose of making or earning such income.
- (7) **In case of income by way of interest on compensation/ enhanced compensation received chargeable to tax under section 56(2)(viii):** Deduction of 50% of such income. No deduction would be allowable under any other clause of section 57 in respect of such income.

### ILLUSTRATION 6

*Interest on enhanced compensation received by Mr. G during the previous year 2020-21 is ₹ 5,00,000. Out of this interest, ₹ 1,50,000 relates to the previous year 2017-18, ₹ 1,65,000 relates to previous year 2018-19 and ₹ 1,85,000 relates to previous year 2019-20. Discuss the tax implication, if any, of such interest income for A.Y.2021-22.*

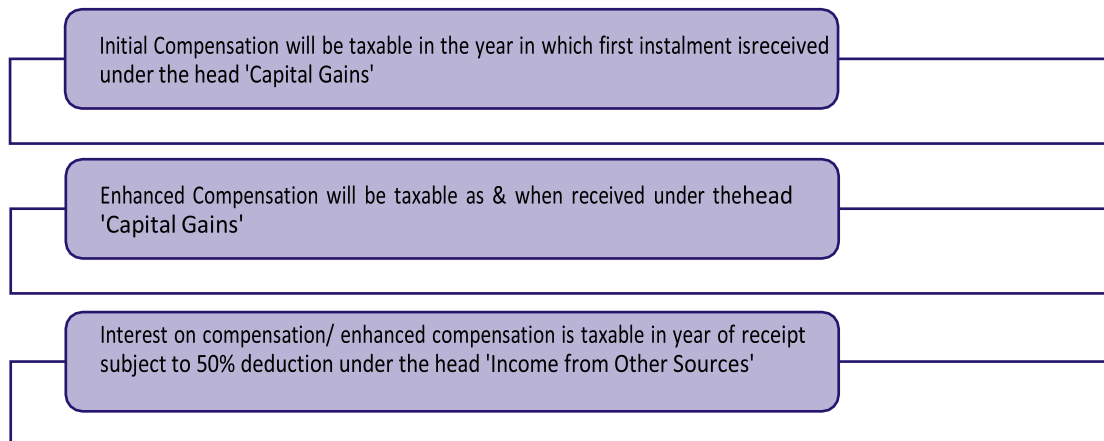
### SOLUTION

The entire interest of ₹ 5,00,000 would be taxable in the year of receipt, namely, P.Y.2020-21.

Particulars	₹
Interest on enhanced compensation taxable u/s 56(2)(viii)	5,00,000
Less: Deduction under section 57(iv) @50%	2,50,000
<b>Interest chargeable under the head "Income from other sources"</b>	<b>2,50,000</b>

## INCOME FROM OTHER SOURCES

**Chart summarising the taxability of compensation / enhanced compensation (including interest) received on compulsory acquisition:**



### 8.6 DEDUCTIONS NOT ALLOWABLE [SECTION 58]

No deduction shall be made in computing the “Income from other sources” of an assessee in respect of the following items of expenses:

**(1) In the case of any assessee:**

- (i) any personal expense of the assessee;
- (ii) any interest chargeable to tax under the Act which is payable outside India on which tax has not been paid or deducted at source.
- (iii) any payment taxable in India as salaries, if it is payable outside India unless tax has been paid thereon or deducted at source.

- (2) Any expenditure in respect of which a payment is made to a related person or made in cash in excess of ₹ 10,000:** In addition to these disallowances, section 58(2) specifically provides that the disallowance of any expenditure in respect of which a payment is made to a related person, to the extent the same is considered excessive or unreasonable by the Assessing Officer, having regard to the FMV. and disallowance of payment or aggregate of payments exceeding ₹ 10,000 made to a person during a day otherwise than by account payee cheque or draft or ECS through bank account or through such other prescribed electronic mode such as **credit card, debit card, net banking, IMPS, UPI, RTGS, NEFT, and BHIM Aadhar Pay** covered by section 40A will be applicable to the computation of income under the head ‘Income from other sources’ as well.

## INCOME FROM OTHER SOURCES

- (3) **Disallowance of 30% of expenditure:** 30% of expenditure shall not be allowed, in respect of a sum which is payable to a resident and on which tax is deductible at source, if
- such tax has not been deducted or;
  - such tax after deduction has not been paid on or before the due date of return specified in section 139(1).

- (4) **No deduction in respect of any expenditure incurred in connection with casual income:** No deduction in respect of any expenditure or allowance in connection with income by way of earnings from lotteries, cross word puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever shall be allowed in computing the said income.

The prohibition will not, however, apply in respect of the income of an assessee, being the owner of race horses, from the activity of owning and maintaining such horses. In respect of the activity of owning and maintaining race horses, expenses incurred shall be allowed even in the absence of any stake money earned. Such loss shall be allowed to be carried forward in accordance with the provisions of section 74A.

### 8.7 DEEMED INCOME CHARGEABLE TO TAX [SECTION 59]

The provisions of section 41(1) are made applicable, so far as may be, to the computation of income under this head. Accordingly, where a deduction has been made in respect of a loss, expenditure or liability and subsequently any amount is received or benefit is derived in respect of such expenditure incurred or loss or trading liability allowed as deduction, then it shall be deemed as income in the year in which the amount is received or the benefit is accrued.

### 8.8 METHOD OF ACCOUNTING [SECTION 145]

Income chargeable under the head “Income from other sources” has to be computed in accordance with the cash or mercantile system of accounting regularly employed by the assessee.

Under section 145(2), the Central Government is empowered to notify in Gazette from time to time, income computation and disclosure standards to be followed by any class of assesses or in respect of any class of income.

Accordingly, Central Government has notified ten ICDSs to be followed by all assesseees (other than an individual or a HUF who is not required to get his accounts of the previous year audited in accordance with the provisions of section 44AB) following the mercantile system of accounting, for the purpose of computation of income chargeable to income-tax under the head “Profits and gains from business or profession” or “Income from other sources”.

Text of notified ICDSs is given as an Annexure at the end of this module.

## 1. GENESIS OF GST IN INDIA

In the year 2000, the then Prime Minister mooted the concept of GST and set up a committee to design a Goods and Services Tax (GST) model for the country. In 2003, the Central Government formed a task force on Fiscal Responsibility and Budget Management, which in 2004 strongly recommended fully integrated 'GST' on national basis.



Subsequently, the then Union Finance Minister, Shri P. Chidambaram, while presenting the Union Budget (2006-2007), announced that GST would be introduced from April 1, 2010. Since then, GST missed several deadlines and continued to be shrouded by the clouds of uncertainty.

The talks of ushering in GST, however, gained momentum in the year 2014 when the NDA Government tabled the Constitution (122<sup>nd</sup> Amendment) Bill, 2014 on GST in the Parliament on 19<sup>th</sup> December, 2014. The Lok Sabha passed the Bill on 6<sup>th</sup> May, 2015 and Rajya Sabha on 3<sup>rd</sup> August, 2016. Subsequent to ratification of the Bill



by more than 50% of the States, Constitution (122<sup>nd</sup> Amendment) Bill, 2014 received the assent of the President on 8<sup>th</sup> September, 2016 and became the **Constitution (101<sup>st</sup> Amendment) Act, 2016**, which paved the way for introduction of GST in India.

In the following year, on 27<sup>th</sup> March, 2017, the Central GST legislations - Central Goods and Services Tax Bill, 2017, Integrated Goods and Services Tax Bill, 2017, Union Territory Goods and Services Tax Bill, 2017 and Goods and Services Tax (Compensation to States) Bill, 2017 were introduced in Lok Sabha. Lok Sabha passed these

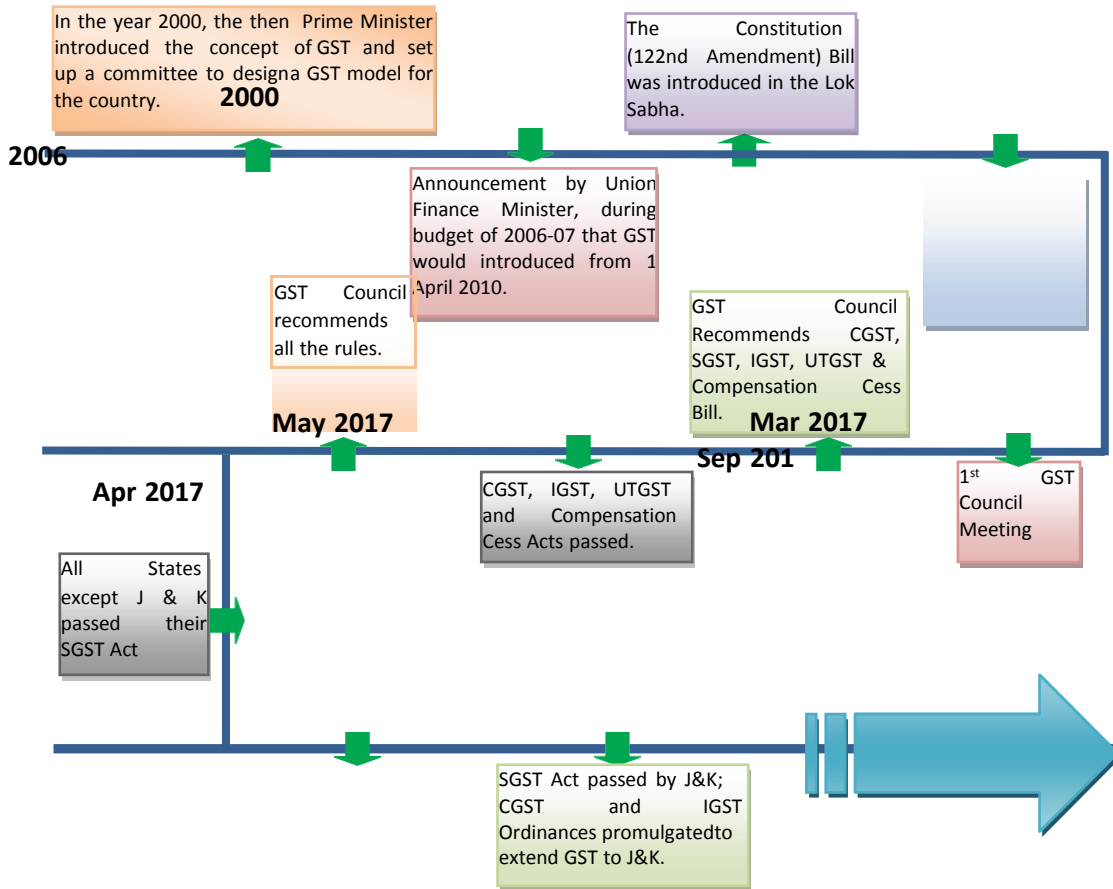


bills on 29<sup>th</sup> March, 2017 and with the receipt of the President's assent on 12<sup>th</sup> April, 2017, the Bills were enacted. The enactment of the Central Acts was followed by the enactment of the State GST laws by various State Legislatures. Telangana, Rajasthan, Chhattisgarh, Punjab, Goa and Bihar were among the first ones to pass their respective State GST laws. By 30<sup>th</sup> June, 2017, all States and Union Territories had passed their respective SGST and UTGST Acts except Jammu and Kashmir. With effect from 1<sup>st</sup> July, 2017, the historic indirect tax reform - GST

## GST IN INDIA – AN INTRODUCTION

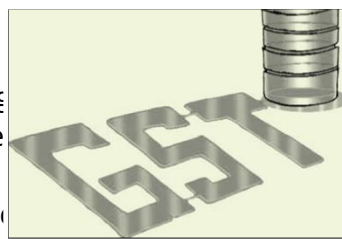
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introduce d. GST law was extended to Jammu and Kashmir on 8<sup>th</sup> July, 2017.



GST is a path breaking indirect tax reform which attempts to create a common national market. GST has subsumed multiple indirect taxes like excise duty, service tax, VAT, CST, luxury tax, entertainment tax, entry tax, etc.

VAT and GST are often used inter-changeably as the latter denotes comprehensiveness of VAT by coverage of goods and services. France was the first country to implement VAT/GST in 1954. Presently, more than 160 countries have implemented VAT/GST in some form or the other bearing this tax



has the capacity to raise revenue in the most transparent and neutral manner. Most of the countries follow unified GST i.e., a single tax applicable throughout the country. However, in federal polities like Brazil and Canada, a dual GST system is prevalent. Under dual system, GST is levied by both the federal and the State Governments. India has adopted dual GST model because of its unique federal nature.



## 2. CONCEPT OF GST



Before we proceed with the finer nuances of Indian GST, let us first understand the basic concept of GST.

- ❑ GST is a value added tax levied on supply i.e., manufacture or sale of goods and provision of services. **VALUE ADDED TAX**
- ❑ GST offers comprehensive and continuous chain of tax credits from the producer's point/service provider's point upto the retailer's level/consumer's level thereby taxing only the value added at each stage of supply chain. **CONTINUOUS CHAIN OF TAX CREDITS**
- ❑ The supplier at each stage is permitted to avail credit of GST paid on the purchase of goods and/or services can set off this credit against the GST payable on the supply of goods and services to be made by him. Thus, only the final consumer bears the GST charged by the last supplier in the supply chain, with set-off benefits at all the previous stages. **BURDEN BORNE BY FINAL CONSUMER**
- ❑ Since, only the value added at each stage is taxed under GST, there is no tax on tax or cascading of taxes under GST system. The same can be understood better with the help of the following **example:** **NO CASCADING OF TAXES**

## GST IN INDIA – AN INTRODUCTION

Manufacturer (₹)	Distributor (₹)	Retailer (₹)	Consumer (₹)
Cost: 1,00,000 GST @ 18%= 18,000	Cost: 1,00,000 Profit: 11,200 Sale Price :1,11,200 GST @ 18% <b>20,016</b>	Cost: 1,11,200 Profit: 24,640 Sale Price :1,35,840 GST@ 18% <b>24,451.20</b>	Cost: 1,60,291.2 (1,35,840+24,451.20)
Input Tax Credit= NIL	Input Tax Credit= 18,000	Input Tax Credit= Rs. 20,016	Input Tax Credit= NIL

## GST IN INDIA – AN INTRODUCTION

<b>Paid to Government</b> GST = 18,000	<b>to</b>	<b>Paid to Government</b> GST = 2,016 (Output tax – Input tax)	<b>to</b>	<b>Paid to Government</b> GST= 4,435.20 (Output tax – Input tax)	<b>to</b>	<b>Tax Borne by the Consumer</b> 18,000+2,016+4,435.20= 24,451.20
Value Addition = 1,00,000		Value Addition= 11,200		Value Addition= 24,640		Value Addition= NIL
GST @ 18% = 18,000		GST @ 18%= 2,016		GST @ 18%= 4,435.20		

### 3. NEED FOR GST IN INDIA





## Deficiencies in the value added taxation system

Under the earlier indirect tax regime, despite the introduction of the principle of taxation of value added in India – at the Central level in the form of CENVAT

(Central Excise) and at the State level in the form of State VAT - its application always remained piecemeal and fragmented on account of the following reasons:

- ❑ Certain transactions were subject to double taxation and were taxed as both goods and services, since under the earlier regime, distinction between goods and services was often blurred.



**(1)** Under earlier tax regime, software was subject to both service tax and VAT. This was so because both sale of goods and provision of service were involved and therefore taxable event under both the Statutes i.e. respective VAT law and service tax law got triggered. This aspect has been taken care of under GST law.

- ❑ CENVAT did not include chain of value addition in the distributive trade after the stage of production. Similarly, in the State-level VAT, CENVAT load on the goods was not removed leading to the cascading of taxes. Below mentioned example illustrates that under earlier indirect tax regime, when the goods were manufactured and sold, both central excise duty (CENVAT) and State-Level VAT were levied.



**(2)** Under earlier tax regime, if goods were manufactured for ₹ 1000/- and excise duty was payable @ 12.5% and VAT was payable @ 14.30%, the billing was being done as under:

Assessable value of goods under excise law	₹ 1000
Excise duty @ 12.5%	₹ 125
Taxable value for VAT	₹ 1,125
VAT @ 14.30%	₹ 160.88
Total invoice value	₹ 1,285.88

- ❑ Though CENVAT and State-Level VAT were essentially value added taxes, set off of one against the credit of another was not possible as CENVAT was a central levy and State-Level VAT was a State levy.
- ❑ There were several taxes in the States, such as, Luxury Tax, Entertainment Tax, etc. which were not subsumed in the VAT. Hence for a single transaction, multiple taxes in multiple forms were required to be paid.
- ❑ VAT on goods was not integrated with tax on services, at the State level, to remove the cascading effect of service tax. With service sector being the

## GST IN INDIA – AN INTRODUCTION

fastest growing sector in the economy, the exclusion of services from the tax base of the States potentially eroded their tax- buoyancy.

- CST was another source of distortion in terms of its cascading nature since it was non-VATABLE. Being an origin based tax, CST was also against one of the basic principles of consumption taxes that tax should accrue to the jurisdiction where consumption takes place.



(3) Under earlier tax regime, if a dealer in Delhi purchases goods from a manufacturer in Punjab for ₹ 1000 + ₹ 20 (2% CST) = ₹ 1020/- and sells such goods within Delhi for ₹ 1200/-. The tax rate on sales is 12.5% and hence output tax liability is ₹ 150/-. Credit of ₹ 20/- is not allowed while making payment of ₹ 150/- and hence the dealer has to pay ₹ 150 as VAT.

Non-inclusion of several local levies in State VAT such as luxury tax, entertainment tax, etc.

Cascading of taxes on account of (i) levy of Non-VATable CST and (ii) inclusion of CENVAT in the value for imposing VAT

No CENVAT after manufacturing stage

Non-integration of VAT & service tax

Double taxation of certain transactions as both goods and services



## GST – A cure for ills of existing indirect tax regime



### GOODS AND SERVICES TAX (GST)

The crucial piece in India's development strategy

Creating one Economic India

Filip to 'Make in India' initiative

Unfettered flow of goods & services

Increased economic activity to boost employment



A comprehensive tax structure covering both goods and services viz. Goods and Services Tax (GST) addresses most of the above stated issues. Simultaneous introduction of GST at both Centre and



## GST IN INDIA – AN INTRODUCTION

State levels has integrated taxes on goods and services for the purpose of set-off relief and ensures that both the cascading effects of CENVAT and service tax are removed and a continuous chain of set-off from the original producer's point/service provider's point upto the retailer's level/ consumer's level is established.

In the GST regime, the major indirect taxes have been subsumed in the ambit of GST. The erstwhile concepts of manufacture or sale of goods or rendering of services are no longer applicable since the tax is now levied on "Supply of Goods and/or services".

### 4. FRAMEWORK OF GST AS INTRODUCED IN INDIA

#### Dual GST:

India has adopted a **Dual GST model** in view of the federal structure of the country. Consequently, Centre and States simultaneously levy GST on taxable supply of goods or services or both which, takes place within a State or Union Territory. Thus, tax is imposed concurrently by the Centre and States, i.e. Centre and States simultaneously tax goods and services. Now, the Centre also has the power to tax intra-State sales & States are also empowered to tax services. GST extends to whole of India including the State of Jammu and Kashmir.

#### Dual GST



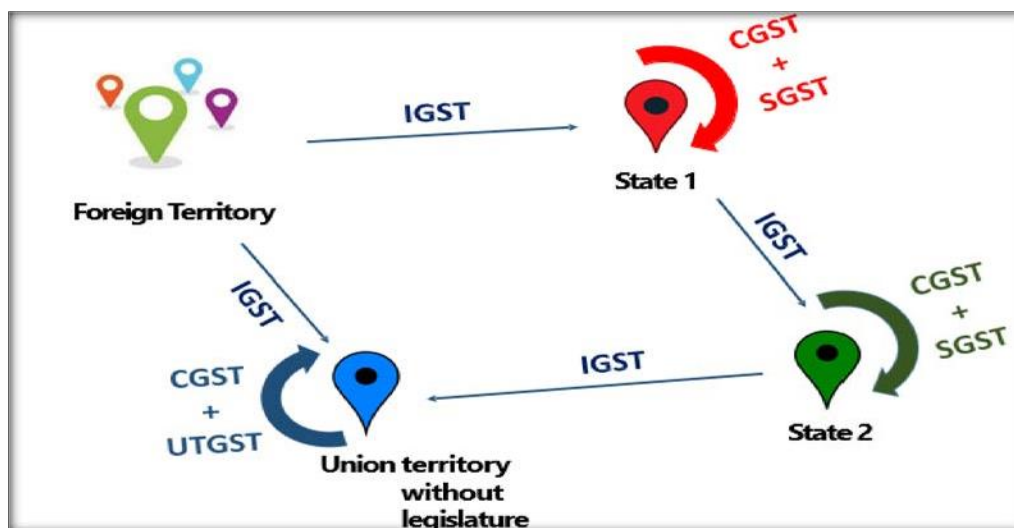
### I. CGST/SGST/UTGST/IGST

GST is a destination based tax applicable to all transactions involving supply of goods or services or both for a

**CGST/SGST/UTGST/IGST**

consideration subject to exceptions thereof. GST in India comprises of Central Goods and Services Tax (CGST) - levied and collected by Central Government, State Goods and Services Tax (SGST) - levied and collected by State Governments/Union Territories with Legislatures and Union Territory Goods and Services Tax (UTGST) - levied and collected by Union Territories without Legislatures, on intra-State supplies of taxable goods and/or services. As a general rule, where the location of the supplier and the place of supply of goods or services are in the same State/Union territory, it is treated as intra-State supply of goods or services respectively.

Further, where the location of the supplier and the place of supply of goods or services are in (i) two different States or (ii) two different Union Territories or (iii) a State and a Union territory, it is treated as inter-State supply of goods or services respectively. Inter-State supplies of taxable goods and/or services are subject to Integrated Goods and Services Tax (IGST). IGST is the sum total of CGST and SGST/UTGST and is levied by Centre on all inter-State supplies.



### II. Legislative Framework

There is single legislation – CGST Act, 2017 - for levying CGST. Similarly, Union Territories without

**Legislative Framework**

Legislatures [i.e. Andaman and Nicobar Islands, Lakshadweep, **Ladakh, Dadra and Nagar Haveli & Daman and Diu** and Chandigarh] are governed by UTGST Act, 2017 for levying UTGST. States and Union territories with their own legislatures [i.e. Delhi, **Jammu and Kashmir** and Puducherry] have their own GST legislation for levying SGST.



(4) In Ladakh, CGST and UTGST is levied on supply of goods or services or both. In Delhi, CGST and SGST is levied on supply of goods or services or both.

Though there are multiple SGST legislations, the basic features of law, such as chargeability, definition of taxable event and taxable person, classification and valuation of goods and services, procedure for collection and levy of tax and the like are uniform in all the SGST legislations, as far as feasible. This is necessary to preserve the essence of dual GST.

### III. Classification of goods and services

HSN (Harmonised System of Nomenclature) is for classifying the goods under the GST. Chapters referred in the Rate Schedules for goods are the Chapters of the First Schedule to the Customs Tariff Act, 1975.

**Classification of goods and services**

A new **Scheme of Classification of Services** has been devised wherein the services of various descriptions have been classified under various sections, headings and groups. Each group consists of various Service Codes (Tariff).

### IV. Composition Scheme

In GST regime, tax (i.e. CGST and SGST/UTGST for State supplies and IGST for inter-State supplies) is paid by every taxable person and in this regard provisions have been prescribed in the law.

**Composition Scheme**

However, for providing relief to small businesses, primarily manufacturers, suppliers of food articles, traders, etc., making intra-State supplies, a simpler method of paying taxes is prescribed, known as Composition Levy. **The scope of this scheme has now been extended to small service providers also.**

### V. Registration

Every supplier of goods and/ or services is required to obtain registration in the State/UT from where he makes the

**Registration**

## GST IN INDIA – AN INTRODUCTION

taxable supply if his aggregate turnover exceeds the threshold limit during a FY. Different threshold limits have been prescribed for various States and Union Territories depending upon the fact whether the supplier is engaged exclusively in supply of goods, or exclusively in supply of services or in supply of both goods and services. The threshold limit prescribed for various States/UTs are as follows:

States with threshold limit of ₹ 10 lakh for both goods and services	States with threshold limit of ₹ 20 lakh for both goods and services	States with threshold limit of ₹ 20 lakh for services and ₹ 40 lakh for goods**
<ul style="list-style-type: none"><li>• Manipur</li><li>• Mizoram</li><li>• Nagaland</li><li>• Tripura</li></ul>	<ul style="list-style-type: none"><li>• Arunachal Pradesh</li><li>• Meghalaya</li><li>• Sikkim</li><li>• Uttarakhand</li><li>• Puducherry</li><li>• Telangana</li></ul>	<ul style="list-style-type: none"><li>• Jammu and Kashmir</li><li>• Assam</li><li>• Himachal Pradesh</li><li>• All other States</li></ul>

*\*\*persons engaged exclusively in intra-State supply of goods*

### VI. Exemptions

Apart from providing relief to small-scale business, the law also contains provisions for granting exemption from payment on essential goods and/or services.

**Exemptions**

### VII. Seamless flow of credit

Since GST is a destination-based consumption tax, revenue of SGST ordinarily accrues to the consuming States. The inter-State supplier in the

exporting State is allowed to set off the available credit against the IGST payable on inter-State supply made by him (*order of utilisation of credit is explained below*).

**Seamless flow of credit**

## GST IN INDIA – AN INTRODUCTION

The buyer in the importing State is allowed to avail the credit of IGST paid on inter-State purchases made by him.

Thus, unlike the earlier scenario where the credit chain used to break in case of inter-State sales on account of non-VATable CST, under GST regime there is a seamless credit flow in case of inter-State supplies too.

The revenue of inter-State sale does not accrue to the exporting State and the exporting State transfers to the Centre the credit of SGST/UTGST used in payment of IGST.

The Centre transfers to the importing State the credit of IGST used in payment of SGST/UTGST.

**Order of utilization of credit** - There is a specified order in which ITC should be utilized. First, IGST credit should be utilized towards IGST payment, and then towards payment of CGST and SGST/UTGST in any order and in any proportion.

After entire ITC of IGST is utilized, ITC of CGST should be utilized for payment of CGST and IGST in that order. Thereafter, ITC of SGST /UTGST should be utilized for payment of SGST/UTGST and IGST in that order.

**It may be noted that ITC of CGST cannot be utilized for payment of SGST/UTGST and vice versa.** Also, ITC of SGST/UTGST should be utilized for payment of IGST, only after ITC of CGST has been utilized fully.

The seamless flow of credit under GST, in case of intra-State and inter-State supplies, can be better understood with the help of the following illustrations:

### Intra-State Supply

#### ILLUSTRATION 1

In case of local supply of goods/ services, the supplier would charge dual GST i.e., CGST and SGST at specified rates on the supply.

##### *I. Supply of goods/ services by A to B*

	Amount (in `)
Value charged for supply of goods/ services	10,000

## GST IN INDIA – AN INTRODUCTION

Add: CGST @ 9%	900
Add: SGST @ 9%	<u>900</u>
Total price charged by A from B for local supply of goods/ services	<u>11,800</u>

The CGST & SGST charged on B for supply of goods/services will be remitted by A to the appropriate account of the Central and State Government respectively.

A is the first stage supplier of goods/services and hence, does not have credit of CGST, SGST or IGST.

### *II. Supply of goods/services by B to C – Value addition @ 20%*

B will avail credit of CGST and SGST paid by him on the purchase of goods/services and will utilise such credit for being set off against the CGST and SGST payable on the supply of goods/services made by him to C.

	Amount (in `)
Value charged for supply of goods/ services (` 10,000 x 120%)	12,000
Add: CGST @ 9%	1080
Add: SGST @ 9%	<u>1080</u>
Total price charged by B from C for local supply of goods/ services	<u>14160</u>

### *Computation of CGST, SGST payable by B to Government*

	Amount (in `)
CGST payable	1080
Less: Credit of CGST	<u>900</u>
CGST payable to Central Government	<u>180</u>

## GST IN INDIA – AN INTRODUCTION

SGST payable	1080
Less: Credit of SGST	<u>900</u>
SGST payable to State Government	<u>180</u>

*Note: Rates of CGST and SGST have been assumed to be 9% each for the sake of simplicity.*

### *Statement of revenue earned by Central and State Government*

Transaction	Revenue to Central Government (₹)	Revenue to State Government (₹)
Supply of goods/services by A to B	900	900
Supply of goods/services by B to C	180	180
Total	1080	1080

### Inter-State Supply

#### ILLUSTRATION 2

In case of inter-State supply of goods/ services, the supplier would charge IGST at specified rates on the supply.

#### *1. Supply of goods/services by X of State 1 to A of State 1*

	Amount (in ₹)
Value charged for supply of goods/services	10,000
Add: CGST @ 9%	900
Add: SGST @ 9%	<u>900</u>
Total price charged by X from A for intra-State supply of goods/services	<u>11,800</u>

## GST IN INDIA – AN INTRODUCTION

X is the first stage supplier of goods/services and hence, does not have any credit of CGST, SGST or IGST.

### II. *Supply of goods/services by A of State 1 to B of State 2 – Value addition @ 20%*

	Amount (in `)
Value charged (for supply of goods/services 10,000 x 120%)	12,000
Add: IGST @ 18%	<u>2,160</u>
Total price charged by A from B for inter-State supply of goods/services	<u>14,160</u>

#### Computation of IGST payable to Government

	Amount (in `)
IGST payable	2,160
Less: Credit of CGST	900
Less: Credit of SGST	<u>900</u>
IGST payable to Central Government	<u>360</u>

The IGST charged on B of State 2 for supply of goods/services will be remitted by A of State 1 to the appropriate account of the Central Government. State 1 (Exporting State) will transfer SGST credit of ` 900 utilised in the payment of IGST to the Central Government.

### III. *Supply of goods/services by B of State 2 to C of State 2 – Value addition @ 20%*

B will avail credit of IGST paid by him on the purchase of goods/services and will utilise such credit for being set off against the CGST and SGST payable on the local supply of goods/services made by him to C.

## GST IN INDIA – AN INTRODUCTION

	Amount (in `)
Value charged for supply of goods/ services(` 12,000 x 120%)	14,400
Add: CGST @ 9%	1,296
Add: SGST @ 9%	<u>1,296</u>
Total price charged by B from C for local supply of goods/services	<u>16,992</u>

### *Computation of CGST, SGST payable to Government*

	Amount (in `)
CGST payable	1,296
Less: Credit of IGST	<u>1,296</u>
CGST payable to Central Government	<u>Nil</u>
SGST payable	1,296
Less: Credit of IGST (` 2,160 - ` 1,296)	<u>864</u>
SGST payable to State Government	<u>432</u>

Central Government will transfer IGST credit of ` 864 utilised in the payment of SGST to State 2 (Importing State).

*Note: Rates of CGST, SGST and IGST have been assumed to be 9%, 9% and 18% respectively for the sake of simplicity.*

### *Statement of revenue earned by Central and State Governments*

Transaction	Revenue to Central Government (`)	Revenue to Government of State 1 (`)	Revenue to Government of State 2 (`)
Supply of goods/services by X to A	900	900	

## GST IN INDIA – AN INTRODUCTION

Supply of goods/services by A to B	360		
Transfer by State 1 to Centre	900	(900)	
Supply of goods/services by B to C			432
Transfer by Centre to State 2	(864)		864
Total	1,296	Nil	1,296

### VIII. GST Common Portal

Before GST, since, the Centre and State indirect tax administrations worked under different laws, regulations, procedures and formats, their IT infrastructure and systems were also independent of each other. Integrating them for GST implementation was complex since it required integrating the entire indirect tax ecosystem so as to bring all the tax administrations (Centre, State and Union Territories) to the same level of IT maturity with uniform formats and interfaces for taxpayers and other external stakeholders.

Besides, GST being a destination based tax, the inter-State trade of goods and services (IGST) needed a robust settlement mechanism amongst the States and the Centre. A Common Portal was needed which could act as a clearing house and verify the claims and inform the respective Governments to transfer the funds. This was possible only with the help of a strong IT Infrastructure.

Resultantly, Common GST Electronic Portal – [www.gst.gov.in](http://www.gst.gov.in) – a website managed by Goods and Services Network (GSTN) [a company incorporated under the provisions of section 8 of the Companies Act, 2013] is set by the Government to establish a uniform interface for the tax payer and a common and shared IT infrastructure between the Centre and States.

The GST portal is accessible over Internet (by taxpayers and their CAs/Tax Advocates etc.) and Intranet by Tax Officials etc. The portal is one single common portal for all GST related services.

A common GST system provides linkage State/ UT Commercial Tax Departments, Central Tax authorities, Taxpayers, Banks and other stakeholders. The eco-system consists of all stakeholders starting from taxpayer to tax professional to tax officials to GST portal to Banks to accounting authorities.

### **GST Common Portal**



The functions of the GSTN include facilitating registration; forwarding the returns to Central and State authorities; computation and settlement of IGST; matching of tax payment details with banking network; providing various MIS reports to the Central and the State Governments based on the taxpayer return information; providing analysis of taxpayers' profile.

However, it is important to note that the Common GST Electronic Portal provides electronic way bill is

bill is

[www.ewaybillgst.gov.in](http://www.ewaybillgst.gov.in) [managed by the National Informatics Centre, Ministry of Electronics & Information Technology, Government of India].

E-way bill is an electronic document generated on the GST portal evidencing movement of goods.



### IX. GSPs/ASPs

GSTN has selected certain Information Technology, Information Technology enabled Services and financial technology companies, to be called GST Suvidha Providers (GSPs). GSPs develop applications to be used by taxpayers for interacting with the GSTN.

### **GSPs/ASPs**

They facilitate the tax payers in uploading invoices as well as filing of returns and act as a single stopshop for all related services.

They customize products that address the needs of different segments of users. GSPs may take the help of Application Service Providers (ASPs) who act as a link between taxpayers and GSPs.



GST Suvidha Provider

### X. Compensation Cess

A GST Compensation Cess at specified rate

#### Compensation Cess

has been imposed under the Goods and Services Tax (Compensation to States) Cess Act, 2017 on the specified luxury items or demerit goods, like pan masala, tobacco, aerated waters, motor cars



etc., computed on value of taxable supply. Compensation cess is leviable on intra-State supplies and inter-State supplies with a view to provide for compensation to the States for the loss of revenue arising on account of implementation of the GST.

Compensation is to be provided to a State for a period of 5 years from the date on which the State brings its SGST Act into force

### XI. GST – A tax on goods and services

GST is levied on all goods and services, except alcoholic liquor for human consumption and petroleum crude, diesel, petrol, ATF and natural gas.

- ❑ Alcoholic liquor for human consumption outside the realm of GST. manufacture/production of alcoholic continues to be subjected to **State excise duty** and inter-State/intra-State sale of the same is subject to **CST/VAT** respectively.



- ❑ Petroleum crude, diesel, petrol, ATF and natural gas are concerned, they are not presently leviable to GST. GST will be levied on these

products from a date to be notified on the recommendations of the GST Council.

- ❑ Till such date, **central excise duty** continues to be levied on manufacture/production of petroleum crude, diesel, petrol, ATF and natural gas and inter-State/intra-State sale of the same is subject to **CST/ VAT** respectively.
- ❑ **Tobacco:** Tobacco is within the purview of GST, i.e. GST is leviable on tobacco. However, Union Government has also retained the power to levy excise duties on tobacco and tobacco products manufactured in India. Resultantly, **tobacco is subject to GST as well as central excise duty.**
- ❑ **Opium, Indian hemp and other narcotic drugs and narcotics:** Opium, Indian hemp and other narcotic drugs and narcotics are within the purview of GST, i.e. GST is leviable on them. However, State Governments have also retained the power to levy excise duties on such products manufactured in India. Resultantly, Opium, Indian hemp and other narcotic drugs and narcotics are **subject to GST as well as State excise duties.**

## GST IN INDIA – AN INTRODUCTION

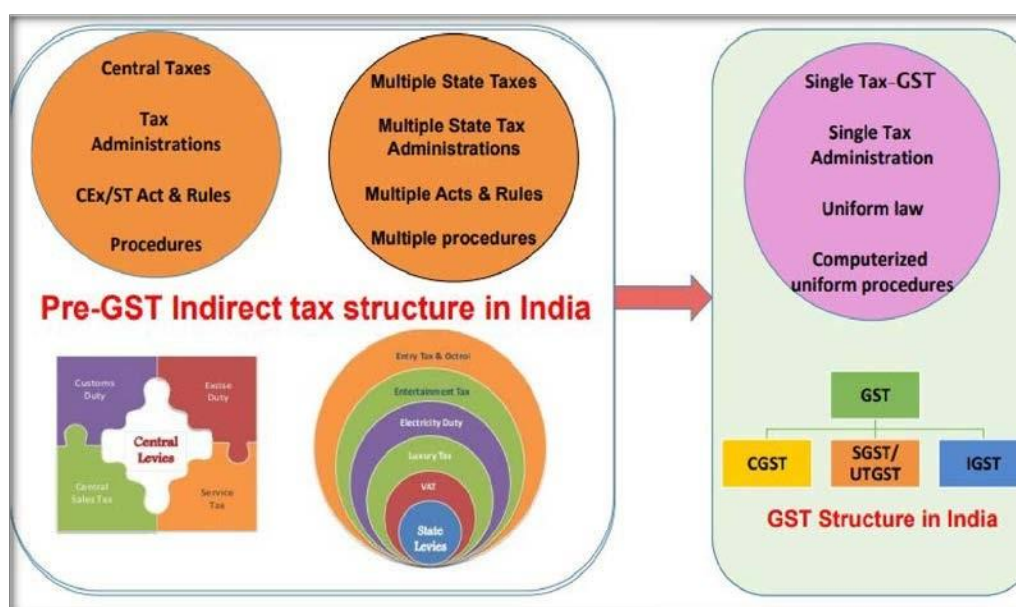
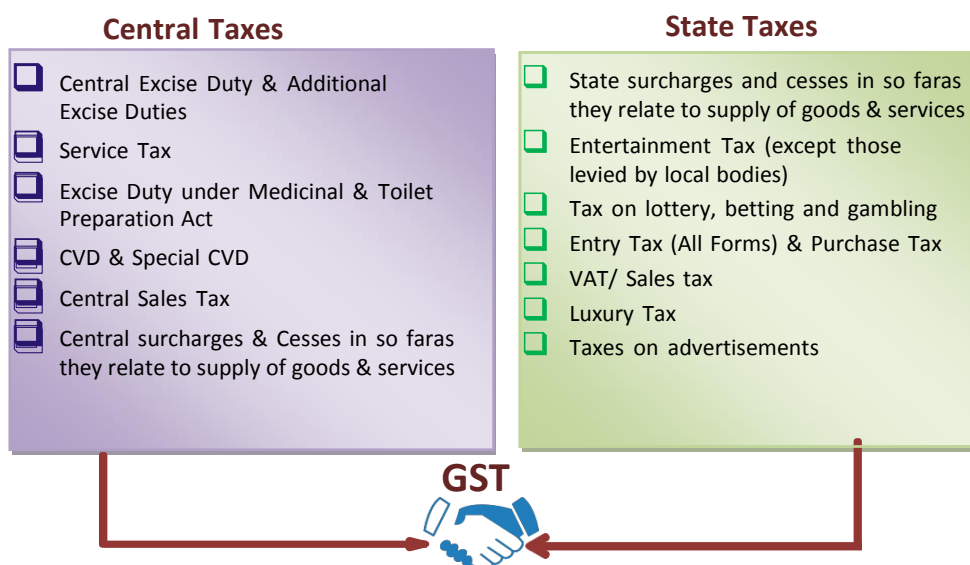
- ❑ Further, real estate sector has been kept out of ambit of GST, i.e. GST will not be levied on sale/purchase of immovable property.

### Taxes subsumed in GST



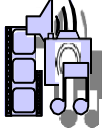

The various central, state and local levies were examined to identify their possibility of being subsumed under GST. While identifying, the following principles were kept in mind:

- (i) Taxes or levies to be subsumed should be primarily in the nature of indirect taxes, either on the supply of goods or on the supply of services.
- (ii) Taxes or levies to be subsumed should be part of the transaction chain which commences with import/ manufacture/ production of goods or provision of services at one end and the consumption of goods and services at the other.
- (iii) The subsuming of taxes should result in free flow of tax credit in intra and inter-State levels. The taxes, levies and fees that were not specifically related to supply of goods & services would not be subsumed under GST.
- (iv) Revenue fairness for both the Union and the States individually would need to be attempted.

Taking the above principles into account, following taxes were subsumed in the GST:



### Within GST or outside GST?

	Alcohol for human consumption	Power to tax remains with the State
	Five petroleum products – crude oil, diesel, petrol, natural gas and ATF	GST Council to decide the date from which GST will be applicable
	Entertainment tax levied by local bodies	Power to levy tax remains with the local bodies
	Tobacco	Within the purview of GST. Power to levy excise duties, also retained.

## 5. BENEFITS OF GST

GST is a win-win situation for the entire country. It brings benefits to all the stakeholders of industry, Government and the consumer. The significant benefits of GST are discussed hereunder:

- ❑ **Creation of unified national market:** GST has made India a common market with common tax rates and procedures. Further, it has removed the economic barriers resulting in an integrated economy at the national level.



- ❑ **Boost to 'Make in India' initiative:** GST has given a major boost to the 'Make in India' initiative of the Government of India by making goods and services produced in India competitive in the national as well as international market. This will make India a manufacturing hub.



- ❑ **Enhanced investment and employment:** The subsuming of major Central and State taxes in GST, complete and comprehensive set-off of input tax on goods and services and phasing out of Central Sales Tax (CST) has reduced

the cost of locally manufactured goods and services. Resultantly, the competitiveness



of Indian goods and services in the international market has increased which has given boost to investments and



Indian exports. With a boost in exports and manufacturing activity, more employment is likely to be generated and GDP is likely to be increased.

### Simplified tax structure

- ❑ **Ease of doing business:** Simpler tax regime with exemptions along with reduction in multiplicity of taxes

**EASE OF DOING BUSINESS**

## GST IN INDIA – AN INTRODUCTION

GST has led to simplification and uniformity in tax structure. The uniformity in laws, procedures and tax rates across the country makes doing business easier.

- ❑ **Certainty in tax administration:** Common system of classification of goods and services across the country ensures certainty in tax administration across India.

### Easy tax compliance

- ❑ **Automated procedures with greater use of IT:** There are simplified and automated procedures for various processes such as registration, returns, refunds, tax payments. All interaction is through the common GSTN portal, therefore, less public interface between the taxpayer and the tax administration.
- ❑ **Reduction in compliance costs:** The compliance cost is lesser under GST as multiple record-keeping for a variety of taxes is not needed, therefore, there is lesser investment of resources and manpower in maintaining records. The uniformity in laws, procedures and tax rates across the country goes a long way in reducing the compliance cost.

### Advantages for trade and industry

- ❑ **Benefits to industry:** GST has given more relief to trade and industry through a more comprehensive and wider coverage of input tax set-off and service tax set-off, subsuming of several Central and State



## GST IN INDIA – AN INTRODUCTION

taxes in the GST and phasing out of CST. The transparent and complete chain of set-offs which results in widening of tax base and better tax compliance also leads to lowering of tax burden on an average dealer in trade and industry.

- ❑ **Mitigation of ill effects of cascading:** By subsuming most of the Central and State taxes into a single tax and by allowing a set-off of prior-stage taxes for the transactions across the entire value chain, it helps in mitigating the ill effects of cascading, improving competitiveness and improving liquidity of the businesses.

- ❑ **Benefits to small traders and g**

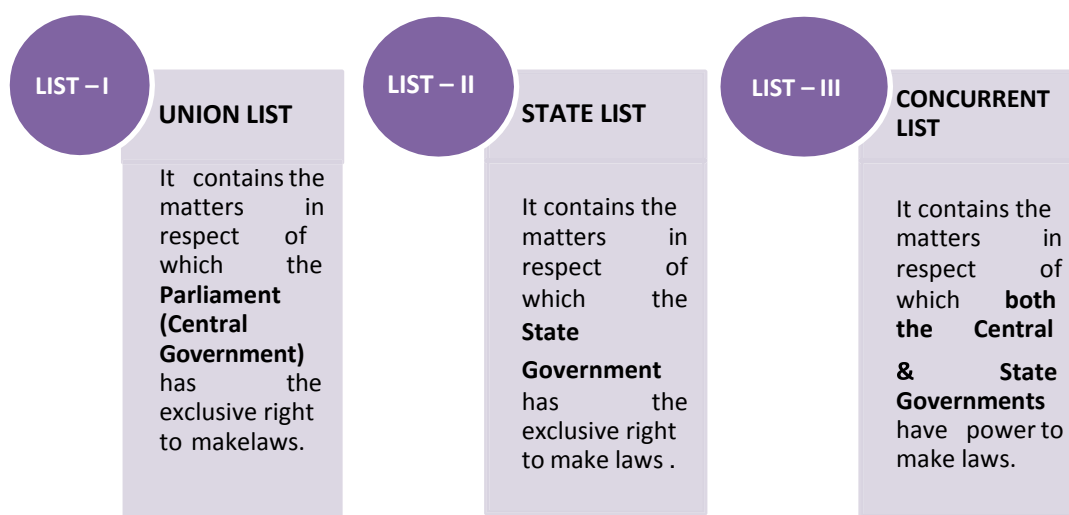


## GST IN INDIA – AN INTRODUCTION

Parliament and on the Legislature of a State by Article 245 of the Constitution. The said Article provides as under:

- ❑ Subject to the provisions of this Constitution, Parliament may make laws for the whole or any part of the territory of India, and the legislature of a State may make laws for the whole or any part of the State.
- ❑ No law made by the Parliament shall be deemed to be invalid on the ground that it would have extra-territorial operation.

- II. Article 246: It gives the respective authority to Union and State Governments for levying tax. Whereas Parliament may make laws for the whole of India or any part of the territory of India, the State Legislature may make laws for whole or part of the State.
- III. Seventh Schedule to Article 246: It contains three lists which enumerate the matters under which the Union and the State Governments have the authority to make laws.



Entries 82 to 91 of List I enumerate the subjects where the Central Government has power to levy taxes. Entries 45 to 63 of List II enumerate the subjects where the State Governments have the power to levy taxes. Parliament has a further power to make any law for any part of India not comprised in a State even if such matter is included in the State List.

## GST IN INDIA – AN INTRODUCTION

Income tax is levied by virtue of Entry 82 - Taxes on income other than agricultural income and customs duty vide Entry 83 - Duties of customs including export duties of the Union List.

Power to levy Goods and Services Tax (GST) has been conferred by Article 246A of the Constitution which was introduced by the Constitution (101<sup>st</sup> Amendment) Act, 2016. Before discussing the significant provisions of the Constitution (101<sup>st</sup> Amendment) Act, 2016, let us first understand why there arose a need for such constitutional amendment.

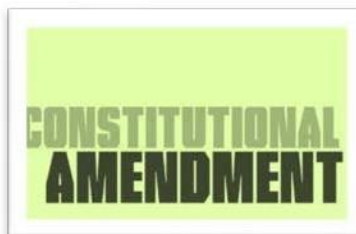
### Need for constitutional amendment

The Constitutional provisions hitherto had delineated separate powers for the Centre and the States to impose various taxes. Whereas the Centre levied excise duty on all goods produced or manufactured in India, the States levied Value Added Tax once the goods entered the stream of trade upon completion of manufacture.

In the case of inter-State sales, the Centre had the power to levy a tax (the Central Sales Tax), but the tax was collected and retained entirely by the States (from where the movement of goods start). Services were exclusively taxed by the Centre together with applicable cesses, if any. Besides, there were State specific levies like entry tax, Octroi, luxury tax, entertainment tax, lottery and betting tax, local taxes levied by Panchayats etc.

With respect to goods imported from outside the country into India, Centre levied basic customs duty and additional duties of customs together with applicable cesses, if any.

Introduction of the GST required amendment in the Constitution so as to enable integration of the central excise duty, additional duties of customs, State VAT and certain State specific taxes and service tax in a comprehensive Goods and Services Tax and to empower both Centre and the States to levy and collect it.



Consequently, Constitution (101<sup>st</sup> Amendment Act), 2016 (hereinafter referred to as CAA) was passed. It has 20 sections. Newly inserted Article 279A empowering President to constitute GST Council was notified on 12.09.2016. Remaining provisions were notified with effect from 16.09.2016.

CAA also provides for compensation to States for loss of revenue on account of introduction of goods and services tax. Parliament shall, by law, on the recommendation of the Goods and Services Tax Council, provide for compensation to the States for loss of revenue arising on account of implementation of the goods and services tax for a period of five years.

### Significant provisions of Constitution (101<sup>st</sup> Amendment) Act, 2016

#### Key changes in brief

- ☐ Concurrent powers on Parliament and State Legislatures to make laws governing taxes on goods and services.
- ☐ Levy of integrated goods and services tax on inter-State transactions of goods and services to be levied and collected by the Central Government and apportioned between the Union and the States in the manner provided by Parliament by Law as per the recommendation of the GST Council.
- ☐ Principles for determining the place of supply and when a supply takes place in the course of inter-State trade or commerce shall be formulated by the Parliament, by law.
- ☐ GST will be levied on all supply of goods and services except alcoholic liquor for human consumption.
- ☐ On the following products GST shall not be levied, till a date to be notified on the recommendations of the GST Council:
  - ☒ Petroleum Crude
  - ☒ High Speed Diesel
  - ☒ Motor Spirit (commonly known as Petrol)
  - ☒ Natural Gas
  - ☒ Aviation Turbine Fuel
- ☐ The Union Government shall retain the power to levy duties of excise on the aforesaid products besides tobacco and tobacco products manufactured or produced in India.
- ☐ Article 279A of the Constitution empowers the President to constitute a joint forum of the Centre and States namely, Goods & Services Tax Council (GST Council).

## GST IN INDIA – AN INTRODUCTION

- ❑ The provisions relating to GST Council came into force on 12th September, 2016. President constituted the GST Council on 15th September, 2016.
- ❑ The Union Finance Minister is the Chairman of this Council and Ministers in charge of Finance/Taxation or any other Minister nominated by each of the States & UTs with Legislatures are its members. Besides, the Union Minister of State in charge of Revenue or Finance is also its member. The function of the Council is to make recommendations to the Union and the States on important issues like tax rates, exemptions, threshold limits, dispute resolution etc.
- ❑ The concept of 'declared goods of special importance' under the Constitution is done away with. Presently, certain restrictions are placed on the powers of States in regard to tax on such goods.
- ❑ Transitional provisions to take care of any inconsistency with respect to any law relating to tax on goods or services or both, in force in any State. Such tax to continue to be in force until amended or repealed or until expiration of one year from commencement of GST, whichever is earlier

### Key changes in detail

Significant amendments made by Constitution Amendment Act are discussed below in detail:

#### IV. Article 246A: Power to make laws with respect to Goods and Services Tax:

##### **Newly inserted Article 246A**

- (1) Notwithstanding anything contained in Articles 246 and 254, Parliament, and, subject to clause (2), the Legislature of every State, have power to make laws with respect to goods and services tax imposed by the Union or by such State.**
- (2) Parliament has exclusive power to make laws with respect to goods and services tax where the supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.**

**Explanation—The provisions of this article, shall, in respect of goods and services tax referred to in clause (5) of article 279A, take effect from the date recommended by the Goods and Services Tax Council.**

## GST IN INDIA – AN INTRODUCTION

- ❑ This article grants power to Centre and Governments to make laws with respect to GST imposed by Centre or such State.
- ❑ Centre has the exclusive power to make laws with respect to GST incase of inter-State supply of goods and/or services.
- ❑ However, in respect to the following goods, the aforesaid provisions shall apply from the date recommended by the GST Council:

### Article 246A



- ❑ The provisions of Article 246A are notwithstanding anything contained in Articles 246 and 254. Article 254 deals with the supremacy of the laws made by Parliament.

### V. Article 248 amended: Residuary powers of legislation amended

- ❑ Article 248 grants the residuary powers to Parliament to make laws with respect to any matter not enumerated in the Concurrent List or State List. Such power shall include the power of making any law imposing a tax not mentioned in either of those Lists.
- ❑ This article has been amended. Now, this power has been subjected to Article 246A, namely the power to make laws with respect to goods and service tax to be imposed by the Centre and States.

### Article 248

### VI. Power of Parliament to legislate with respect to a matter in the State List, in the national interest/in case of emergency, extended to GST provided under Article 246A

- ❑ Article 249 grants the Parliament the power to make laws with respect to a matter in the State list in national interest in a case where the Council of States has declared a resolution

### Article 249

supported by not less than two-thirds of the members present and voting on any matter enumerated in the State List.

- ❑ Similarly, Article 250 grants the Parliament the power to make laws with respect to any of the matters enumerated in the State List if a proclamation of Emergency is in operation. **Article 250**
- ❑ Articles 249 and 250 have been amended to grant power to Parliament to make laws with respect to the Goods and Services Tax provided under Article 246A also alongwith the matters in the State list, in the national interest/in case of emergency.

### VII. Article 268: Duties levied by the Centre but collected and appropriated by the States

- ❑ Article 268 pertains to the duties levied by the Centre but collected and appropriated by the States. It stipulates that such stamp duties and such duties of excise on medicinal and toilet preparations as are mentioned in the Union List shall be levied by the Government of India but shall be collected in the case where such duties are leviable within any Union territory, by the Government of India, and in other cases, by the States within which such duties are respectively leviable. **Article 268**
- ❑ The CAA omits “and such duties of excise on medicinal and toilet preparations” from Article 268.
- ❑ Duties of excise on medicinal and toilet preparations have been subsumed into the goods and service tax to be levied by the Centre and States.

### VIII. Article 268A: Article 268A empowering Union to levy service tax omitted

Service tax was levied in 1994 under the residual entry 97 of the Union list. Article 268A was inserted in the Constitution (88<sup>th</sup>) Amendment Act, 2003 to usher in service tax under a separate entry 92C in the Union List. However, it was not notified ever since. This article has been omitted by the CAA. **Article 268A**

IX. Article 269A: Levy and collection of GST on inter-State supply

*Newly inserted article 269A.*

**Levy and collection of goods and services tax in course of inter-State trade or commerce**

- (1) *Goods and services tax on supplies in the course of inter-State trade or commerce shall be levied and collected by the Government of India and such tax shall be apportioned between the Union and the States in the manner as may be provided by Parliament by law on the recommendations of the Goods and Services Tax Council.*

**Explanation —** For the purposes of this clause, supply of goods, or of services, or both in the course of import into the territory of India shall be deemed to be supply of goods, or of services, or both in the course of inter-State trade or commerce.

- (2) *The amount apportioned to a State under clause (1) shall not form part of the Consolidated Fund of India.*
- (3) **Where an amount collected as tax levied under clause (1) has been used for payment of the tax levied by a State under article 246A, such amount shall not form part of the Consolidated Fund of India.**
- (4) *Where an amount collected as tax levied by a State under article 246A has been used for payment of the tax levied under clause (1), such amount shall not form part of the Consolidated Fund of the State.*
- (5) **Parliament may, by law, formulate the principles for determining the place of supply, and when a supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.**

- ☐ Article 269A stipulates that GST on supplies in the course of inter-State trade or commerce shall be levied and collected by the Government of India and such tax shall be apportioned between the Union and the States in the manner as may be provided by Parliament by law on the recommendations of the Goods and Services Tax Council.

**Article 269A**

- ☐ Further, import of goods or services or both into India will also be deemed to be supply of goods and/ or services in the course of Inter-State trade or Commerce. This will give power to Central Government to levy IGST on the import transactions which were earlier subject to Countervailing duties under the Customs Tariff Act, 1975.
- ☐ Where an amount collected as IGST has been used for payment of SGST or vice versa, such amount shall not form part of the Consolidated Fund of India/State<sup>1</sup> respectively. This is to facilitate transfer of funds between the Centre and the States.
- ☐ Parliament is empowered to formulate the principles regarding place of supply and when supply of goods, or of services, or both occurs in inter-State trade or commerce.

X. Article 270: Distribution of the goods and services tax (GST) between the Centre and the States

- ☐ Article 270 is amended to provide for distribution of the goods and services tax between the Centre and the

**Article 270**

States, by order of the President after considering recommendations of the Finance Commission.

- ❑ This applies for those tax amounts apportioned or payable to the Central Government for taxes levied by it under articles 246A(1) and (2) and Clause (1) of 269A.

### XI. Article 271 amended

Article 271 empowers Parliament to increase any of the duties, or taxes referred to in articles 269 or 270 and further provides that such surcharge is not shareable and remains with the Centre. Now this article is amended to exclude GST from its purview.

#### Article 271

### XII. Definitions of 'Goods and Services Tax', 'Services' and 'State' incorporated under Article 366

- ❑ The terms **Goods and Services Tax**, **services** and **State** have been defined under respective clauses of Article 366 as follows:

- ✓ **Goods and services tax** means any tax on supply of goods, or services or both except taxes on the supply of the alcoholic liquor for human consumption. Consequently, GST can be levied on supply of all goods and services except alcoholic liquor for human consumption.
- ✓ **Services** means anything other than goods.
- ✓ **State**, with reference to articles 246A, 269A and article 279A, includes a Union territory with Legislature.

#### Article 366(12A)

#### Article 366(26A)

#### Article 366(26B)

- ❑ **Definition of "goods"**: The term goods has already been defined under clause (12) of Article 366 in an inclusive manner to provide that **"goods includes all materials, commodities, and articles"**.


### XIII. Article 286: Article 286 imposing restrictions as to imposition of tax on the sale or purchase of goods amended

- ❑ Article 286 which restrains the States from framing laws for imposition of any tax on the sale or purchase of goods where such sale or purchase takes place outside the State or in course of the import of the goods into, or export of the goods out of, the territory of India.
- ❑ This article has been amended to incorporate the changes arising out of GST by substituting the words "sale or purchase" with "supply" and words "goods" with "goods or services or both".
- ❑ Consequently, States have no right to impose GST on inter-State supply of goods or services or both. It will be levied by Union Government under Article 269A as mentioned earlier.

#### Article 286

- ❑ Further, clause (3) of Article 286 which stipulates that any law of a State shall, in so far as it imposes, or authorises the imposition, of a tax on the sale or purchase of goods declared by Parliament by law to be of special importance in inter-State trade or commerce, be subjected to such restrictions and conditions in regard to the system of levy, rates and other incidents of the tax, as Parliament may, by law, specify, has been omitted.

### XIV. GST Council: Article 279A

- ❑ Article 279A of the Constitution empowers the President to constitute a joint forum of the Centre and States, namely, Goods & Services Tax Council (GST Council).The diagram shows a central oval labeled 'GST COUNCIL' surrounded by 16 small human figures, representing the members of the council.
- ❑ The provisions relating to GST Council came into force on 15th September, 2016. President constituted the GST Council on 15th September, 2016.
- ❑ The GST Council shall consist of the following members, namely:—
  - (a) the Union Finance Minister is the Chairperson;
  - (b) the Union Minister of State in charge of Revenue or Finance is the Member;
  - (c) the Minister in charge of Finance or Taxation or any other Minister nominated by each State Government are the Members.
- ❑ The Members of the GST Council referred to clause (c) above shall, as soon as may be, choose one amongst themselves to be the Vice- Chairperson of the Council for such period as they may decide.
- ❑ The GST Council shall make recommendations to the Union and the States on—
  - (a) the taxes, cesses and surcharges levied by the Union, the States and the local bodies which may be subsumed in the goods and services tax;
  - (b) the goods and services that may be subjected to, or exempted from the goods and services tax;
  - (c) model Goods and Services Tax Laws, principles of levy, apportionment of Goods and Services Tax levied on supplies in the course of inter-State trade or commerce under article 269A and the principles that govern the place of supply;
  - (d) the threshold limit of turnover below which goods and services may be exempted from goods and services tax;
  - (e) the rates including floor rates with bands of goods and services tax;
  - (f) any special rate or rates for a specified period, to raise additional resources during any natural calamity or disaster;
  - (g) special provision with respect to the States of Arunachal Pradesh, Assam, Jammu and Kashmir, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, Himachal Pradesh and Uttarakhand [*Such States are referred as Special Category States*]; and
  - (h) any other matter relating to the goods and services tax, as the Council may decide.
- ❑ GST Council shall recommend the date on which the goods and services tax be levied on petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural

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gas and aviation turbine fuel.

- ❑ While discharging the functions conferred by this article, the GST Council shall be guided by the need for a harmonised structure of goods and services tax and for the development of a harmonised national market for goods and services.
- ❑ One-half of the total number of Members of the GST Council shall constitute the quorum at its meetings.
- ❑ The GST Council shall determine the procedure in the performance of its functions.
- ❑ Every decision of the GST Council shall be taken at a meeting, by a majority of not less than three-fourths of the weighted votes of the members present and voting, in accordance with the following principles, namely:
  - (a) the vote of the Central Government shall have a weightage of one-third of the total votes cast, and
  - (b) the votes of all the State Governments taken together shall have a weightage of two-thirds of the total votes cast, in that meeting.
- ❑ No act or proceedings of the Goods and Services Tax Council shall be invalid merely by reason of—
  - (a) any vacancy in, or any defect in, the constitution of the Council; or
  - (b) any defect in the appointment of a person as a Member of the Council; or
  - (c) any procedural irregularity of the Council not affecting the merits of the case.
- ❑ The Goods and Services Tax Council shall establish a mechanism to adjudicate any dispute —
  - (a) between the Government of India and one or more States; or
  - (b) between the Government of India and any State or States on one side and one or more other States on the other side; or
  - (c) between two or more States, arising out of the recommendations of the Council or implementation thereof.



### XV. Article 368 amended

Article 368 has been amended to include Article 279A within its purview. Consequently, at least two-thirds of the majority in each House of the Parliament and ratification by at least half of the States is specifically required to make any amendment in Article 279A relating to GST Council.

## Article 368

### TEST YOUR KNOWLEDGE

1. List some of the benefits that GST accrues to the economy.
2. Explain with the help of examples how a particular transaction of goods and services is taxed simultaneously under Central GST (CGST) and State GST (SGST)?
3. Why was the need to amend the Constitution of India before introducing the GST?
4. GST is a destination-based tax on consumption of goods or services or both. Discuss the validity of the statement.

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5. *Discuss the leviability of GST or otherwise on the following:*
  - (a) *Alcoholic liquor for human consumption*
  - (b) *Petroleum crude, diesel, petrol, ATF and natural gas*
  - (c) *Tobacco*
  - (d) *Opium, Indian hemp and other narcotic drugs and narcotics*
6. *Under Goods and Services Tax (GST), only value addition is taxed and burden of tax is to be borne by the final consumer. Examine the statement.*
7. *Which are the commodities which have been kept outside the purview of GST? Examine the status of taxation of such commodities after introduction of GST?*
8. *A dual GST has been implemented in India. Elaborate.*
9. *Discuss Article 269A pertaining to levy and collection of GST on inter-State supply.*
10. *Discuss Article 246A which grants the power to make laws with respect to Goods and Services Tax.*

## ANSWERS

1. GST accrues following benefits to the economy:
  - (a) **Creation of unified national market:** GST has made India a common market with common tax rates and procedures. Further, it has removed the economic barriers resulting in an integrated economy at the national level.
  - (b) **Boost to 'Make in India' initiative:** GST has given a major boost to the 'Make in India' initiative of the Government of India by making goods and services produced in India competitive in the national as well as international market. This will make India a manufacturing hub.
  - (c) **Enhanced investment and employment:** The subsuming of major Central and State taxes in GST, complete and comprehensive set-off of input tax on goods and services and phasing out of Central Sales Tax (CST) has reduced the cost of locally manufactured goods and services. Resultantly, the competitiveness of Indian goods and services in the international market has increased which has given boost to investments and Indian exports. With a boost in exports and manufacturing activity, more employment is likely to be generated and GDP is likely to be increased.
2. The Central GST and the State GST is levied simultaneously on every intra-State supply of goods or services or both made by registered persons except the exempted goods and services as well as goods and services which are outside the purview of GST. Further, both are levied on the same price or value. The same can be better understood with the help of following examples:

**Example I:** Suppose that the rate of CGST is 10% and that of SGST is 10%. When a wholesale dealer of steel in Uttar Pradesh supplies steel bars and rods to a construction company which is also located within the same State for, say ₹ 100, the dealer would charge CGST of ₹ 10 and SGST of ₹ 10 in addition to the basic price of the goods. He would be required to deposit the CGST component into a Central Government account while the SGST portion into the account of the concerned State Government (viz. U.P.). It is important to note that he might not actually pay ₹ 20 (₹ 10 + ₹ 10) in cash as he would be entitled to set-off this liability against the

CGST or SGST paid on his eligible purchases (inputs, input services and capital goods) assuming that all his purchases are intra-State. However, for paying CGST, he would be allowed to use only the credit of CGST paid on his purchases while for U.P. GST he can utilize the credit of U.P. GST alone. In other words, CGST credit cannot, in general, be used for payment of SGST. Nor can SGST credit be used for payment of CGST.

**Example II:** Suppose, again the rate of CGST is 10% and that of SGST is 10%. When an advertising company located in Mumbai supplies advertising services to a company manufacturing soap also located within the State of Maharashtra, let us say ₹ 100, the ad company would charge CGST of ₹ 10 as well as Maharashtra GST of ₹ 10 at the basic value of the service. He would be required to deposit the CGST component into a Central Government account while the Maharashtra GST portion into the account of the Maharashtra Government. He might not actually pay ₹ 20 (₹ 10 + ₹ 10) in cash as it would be entitled to set-off this liability against the CGST or SGST paid on his eligible purchases (say, of inputs such as stationery, office equipment, services of an artist etc.) assuming that all his purchases are intra-State. However, for paying CGST, he would be allowed to use only the credit of CGST paid on its purchase while for Maharashtra GST, he can utilise the credit of Maharashtra GST alone. In other words, CGST credit cannot, in general, be used for payment of SGST. Nor can SGST credit be used for payment of CGST.

3. Earlier, the fiscal powers between the Centre and the States were clearly demarcated in the Constitution with almost no overlap between the respective domains. The Centre had the powers to levy tax on the manufacture of goods (except alcoholic liquor for human consumption, opium, narcotics etc.) while the States had the powers to levy tax on the sale of goods. In the case of inter-State sales, the Centre had the power to levy the Central Sales Tax but the tax was collected and retained entirely by the States. As for services, it was the Centre alone that was empowered to levy service tax.

Introduction of the GST necessitated the amendments in the Constitution so as to simultaneously empower the Centre and the States to levy and collect this tax. The Constitution of India was amended by the Constitution (101<sup>st</sup> Amendment) Act, 2016 for this purpose. Article 246A of the Constitution introduced thereby empowered the Centre and the States to simultaneously levy and collect the GST.

4. The given statement is valid. GST is a destination-based tax on consumption of goods or services or both. GST is known as destination-based tax since the tax would accrue to the taxing authority which has jurisdiction over the place of consumption which is also termed as place of supply.

For example, if A in Delhi produces the goods and sells the goods to B in Haryana. In this case, the tax would accrue to the State of Haryana and not to the State of Delhi. On the other hand, under pre-GST regime, origin-based taxation was prevailing in such cases. Under origin-based taxation, the tax used to accrue to the State from where the transaction originated. In the given case, under origin-based taxation, the central sales tax would have been levied by Centre and collected by the State of Delhi and not by the State of Haryana.

5. **(a) Alcoholic liquor for human consumption:** is outside the realm of GST. The manufacture/production of alcoholic liquor continues to be subjected to State excise duty and inter-State/intra-State sale of the same is subject to CST/VAT respectively.
- (b) Petroleum crude, diesel, petrol, ATF and natural gas:** As regards petroleum crude, diesel, petrol, ATF and natural gas are concerned, they are not presently leviable to

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GST. GST will be levied on these products from a date to be notified on the recommendations of the GST Council.

Till such date, central excise duty continues to be levied on manufacture/production of petroleum crude, diesel, petrol, ATF and

natural gas and inter-State/intra-State sale of the same is subject to CST/VAT respectively.

- (c) **Tobacco:** Tobacco is within the purview of GST, i.e. GST is leviable on tobacco. However, Union Government has also retained the power to levy excise duties on tobacco and tobacco products manufactured in India. Resultantly, tobacco is subject to GST as well as central excise duty.
  - (d) **Opium, Indian hemp and other narcotic drugs and narcotics:** Opium, Indian hemp and other narcotic drugs and narcotics are within the purview of GST, i.e. GST is leviable on them. However, State Governments have also retained the power to levy excise duties on such products manufactured in India. Resultantly, Opium, Indian hemp and other narcotic drugs and narcotics are subject to GST as well as State excise duties.
6. The statement is correct. Goods and Services Tax is a destination-based tax on consumption of goods and services. It is levied at all stages right from manufacture up to final consumption with credit of taxes paid at previous stages available as setoff. Resultantly, only value addition is taxed and burden of tax is to be borne by the final consumer.
  7. Article 366(12A) of the Constitution as amended by 101<sup>st</sup> Constitutional Amendment Act, 2016 defines the Goods and Services tax (GST) as a tax on supply of goods or services or both, except supply of alcoholic liquor for human consumption. Therefore, alcohol for human consumption is kept out of GST by way of definition of GST in the Constitution. Five petroleum products viz. petroleum crude, motor spirit (petrol), high speed diesel, natural gas and aviation turbine fuel have temporarily been kept out of the purview of GST; GST Council shall decide the date from which they shall be included in GST. The erstwhile taxation system (CST/VAT & central excise) still continues in respect of the said commodities.
  8. A dual GST has been implemented in India with the Centre and States simultaneously levying it on a common tax base. The GST levied by the Centre on intra-State supply of goods and / or services is called the Central GST (CGST) and that levied by the States/ Union territory is called the State GST (SGST)/ Union GST (UTGST). Similarly, Integrated GST (IGST) is levied and administered by Centre on every inter-State supply of goods and/or services.

India is a federal country where both the Centre and the States have been assigned the powers to levy and collect taxes through appropriate legislation. Both the levels of Government have distinct responsibilities to perform according to the division of powers prescribed in the Constitution for which they need to raise resources. A dual GST, therefore, keeps with the Constitutional requirement of fiscal federalism.

9. Article 269A of the Constitution stipulates that Goods and Services Tax on supplies in the course of inter-State trade or commerce shall be levied and collected by the Government of India and such tax shall be apportioned between the Union and the States in the manner as may be provided by Parliament by law on the recommendations of the Goods and Services Tax Council.

Here, supply of goods, or of services, or both in the course of import into the territory of India shall be deemed to be supply of goods, or of services, or both in the course of inter-State trade or commerce.

The amount so apportioned to a State shall not form part of the Consolidated Fund of India. Where an amount collected as IGST has been used for payment of SGST or vice versa, such amount shall not form part of the Consolidated Fund of India/State respectively. This is to facilitate transfer of funds between the Centre and the States.

Parliament is empowered to formulate the principles for determining the place of supply, and when a supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.

- 10.** Article 246A stipulates that Parliament, and, the Legislature of every State, have power to make laws with respect to goods and services tax imposed by the Union or by such State.

Parliament has exclusive power to make laws with respect to goods and services tax where the supply of goods, or of services, or both takes place in the course of inter-State trade or commerce.

However, in respect to petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas and aviation turbine fuel, the aforesaid provisions shall apply from the date to be notified by the Government on the recommendations by the GST Council.