

M. COM. SEMESTER III

DIRECT TAXES

UNIT I : DEFINITIONS

Section 2 (7): ASSESSEE

Assessee means a person by whom any tax or any other sum of money is payable under this act.

The term Assessee includes: -

- (a) Every person in respect of whom any proceeding under this act has been taken for the assessment of his income or of the income of any other person in respect of which he is assessable, or of the loss sustained by him or by such person, or of the amount of refund due to him or such other person;
- (b) Every person who is deemed to be an assessee under any provisions of this act;
- (c) Every person who is deemed to be an assessee in default under any provisions of this act.

The term Assessee includes the following persons: -

1. A person by whom any amount by way of tax, interest or penalty is payable under this Act. Whether the proceedings under this Act has been taken or not will be immaterial.
2. A person against whom the proceedings under this Act has been taken. In this case, it will be immaterial whether such a person is liable or not to pay any amount by way of tax thereon.
3. A person who is required to file his return of loss and who is not required to pay any tax thereon.
4. A person who is not liable to pay tax on his net taxable income, but since the tax is deducted at source, he is entitled to claim for refund.
5. A person who is deemed to be an assessee and who is assessable in respect of income or loss of another e.g. the representative of non-resident, the trustees in case of trust.
6. A person who is deemed to be an assessee in default. For instance, an employer who is required to deduct tax from salaries paid by him to his employees and fails to deduct such tax or after deducting tax does not pay it to the Government.

Section 2 (24) : INCOME

Income includes: -

- (a) Profits and Gains,
- (b) Dividend,
- (c) Voluntary contributions received by: -
 1. A charitable or religious trust, or,
 2. Any institution established wholly or partly for charitable or religious purpose, or
 3. An approved scientific research association, or
 4. Any other notified fund or institution established for charitable purposes,

5. Any notified trust or institution wholly for public religious purposes or wholly for public religious & charitable purposes.
- (d) The value of any perquisite or profit in lieu of salary taxable under clauses (2) & (3) of Section 17.
 - (e) Any special allowance or benefit, other than perquisite included under sub-clause (d) specifically granted to the assessee to meet expenses wholly, necessary and exclusively for the performance of the duties of an office or employment of profit.
 - (f) Any allowance granted to the assessee either to meet his personal expenses at the place where the duties of his office or employment of profit are ordinarily performed by him or at a place where he ordinarily resides or to compensate him for the increased cost of living.
 - (g) The value of any benefit or perquisite whether convertible into money or not obtained from a company either by a director or person who has substantial interest in the company or relative of the director or of such person. It also includes any sum which is paid by the company which otherwise would have been payable by the director or such other person.
 - (h) The value of any benefit or perquisite whether convertible into money or not obtained by any representative assessee and any sum paid by the representative assessee in respect of any obligation of any beneficiary which otherwise would have been payable by such beneficiary.
 - (i) Any sum chargeable to income tax as profits and gains of business or profession u/s 28 (ii) and (iii) or Section 41 or Section 59.
 - (j) Any profits on sale of a license granted under the Imports (Control) Order, 1955, made under the Imports and Exports (Control) Act, taxable u/s 28 (iii a).
 - (k) Any cash assistance (by whatever name called) received or receivable by any person against exports under any scheme of the Government of India, taxable u/s 28 (iii b).
 - (l) Any duty of Customs or excise repaid or repayable as drawback to any person against exports under the Customs and Central Excise Duties Drawback Rules, 1971, taxable u/s 28 (iii c).
 - (m) The value of any benefit or perquisite taxable under clause (iv) of Section 28.
 - (n) Any sum chargeable to income-tax under clause (v) of section 28, such as interest, salary, bonus, commission or remuneration received by a partner of the partnership firm from such firm.
 - (o) Any capital gains chargeable u/s 45.
 - (p) Profit or gains of business of insurance carried on by Mutual Insurance Company or by a co-operative society computed in accordance with the provisions of this Act u/s 44.
 - (q) The profits & gains of any business of banking (including providing credit facilities) carried by a co-operative society with its members.
 - (r) Any winning from lottery, crossword puzzles, horse races, card-games and other games of any sort or gambling or betting of any form or nature whatsoever.
 - (s) Any sum received by the assessee from his employees as contribution to any provident fund or superannuation fund or any fund set under the provisions of Employees State Insurance Act 1948 or any other fund for the welfare of such employees.
 - (t) Any sum received under the "Keyman Insurance Policy", means a Life Insurance Policy taken by a person on the life of another person who is or was the employee of the first mentioned person or is connected in any manner whatsoever with the business of the first mentioned person.
 - (u) Any sum received or receivable in cash or in kind under Non-compete agreements or exclusive rights agreements.
 - (v) Amount exceeding ₹ 50,000 received without consideration from non-related person of the assessee.

The aforesaid definition does not define the term "income" but merely describes various receipts as income. It, therefore, follows that in addition to the aforesaid receipts, any other receipt is taxable under the Act if it comes within the general and natural meaning of the term "income".

EXPLANATION: -

Following points should be noted while studying the definition of income: -

1. Personal gift is not considered as income, however, gift received for professional skill is to be considered as income.
2. Income may be received in cash or in kind. It still remains income.
3. It is immaterial for income tax purpose whether income is earned from lawful means or unlawful means.
4. Income may be calculated on receipt or accrual basis depending upon facts & nature of income.
5. Income includes loss i.e. loss is considered as minus income.
6. Pin money received by wife for her personal expenses is not treated as income.
7. Income should be real & not fictional.
8. Awards received by a professional sportsman is an income.

Section 2 (31): PERSON

The term person includes the following: -

- i) An individual
- ii) A Hindu Undivided Family (HUF)
- iii) A Company
- iv) A firm
- v) An association of persons (AOP) or body of individuals (BOI) whether incorporated or not.
- vi) A local authority.
- vii) Every artificial juridical person not falling in the categories mentioned above.

These are seven categories of persons chargeable to tax under the Act. The aforesaid definition is inclusive and not exhaustive. Therefore, any person, not falling in the above- mentioned seven categories, may still fall in the four corners of the term "person" and accordingly may be liable to tax under section 4.

EXPLANATION: -

1. **Individual** : Natural human being e.g. Mr. X.
2. **H.U.F.** : It is the family arising out of Hindu law consisting of all members lineally descended from a Hindu ancestor (children & grandchildren), and their wives & unmarried daughters. E.g. Mr. A as Karta and B, C, D & E as family members.
3. **Company** : Under section 2(17), "company" is defined as –
 - a) any Indian company; or
 - b) any body corporate incorporated under the laws of a foreign country; or
 - c) any institution or association or a body which is assessed or was assessable/assessed as a company for any assessment year commencing on or before April 1, 1970; or

d) any institution, association or a body, whether incorporated or not & whether Indian or non-Indian, which is declared by special order of the Central Board of Direct Taxes to be a company.

Eg. Wipro Ltd.; Reliance India Ltd.

4. **Firm** : A partnership firm e.g. A registered partnership firm with X, Y, Z partners.
5. **AOP/BOI** : It is an Association of Persons for a common cause, e.g. XYZ Housing Society.
6. **Local Authority**: It means a municipality, district board , gram panchayat or any body entrusted by the government the control and management of a municipal or local fund e.g. Thane Municipal Corporation, B.E.S.T. etc.
7. **Artificial Juridical Person** : It includes an idol, a deity, a university, Bar Council etc. e.g. Idols of Gods & Allah, Balaji, Mumbai University etc.

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UNIT 2 : BASIS OF CHARGE

Section 2 (9): ASSESSMENT YEAR

Assessment Year means a period of Twelve months commencing from 1st Day of April every year.

EXPLANATION: -

Assessment year 2017-2018 thus begins on 1st April 2017 and ends on 31st March 2018. This is the year in which income relating to Previous Year 2016-2017 is assessed to tax.

Section 2 (34), Read with Section 3 : PREVIOUS YEAR

Under Section 2 (34) Previous Year means the "Previous Year" as defined in Section 3.

As per Section 3 there will be only one previous year for all the assessee ending on 31st March for all sources of income. E.g. In case of newly set up business previous year will begin from the date of setting up of business & will end with 31st March next. Thus, if a new business is commenced on 18th Dec. 2016, first previous year will be from 18th Dec. 2016 to 31st March 2017 and will cover a period of less than 12 months.

For Income Tax purpose status of the assessee is classified as-

1. Legal Status—Which is decided on the basis of definition of person. Eg. For a Joint Stock Company, legal status is company. For Mr. X legal status is 'individual'.
Legal Status of an assessee decides the rate at which he is required to pay income tax.
2. Residential Status—On the basis of these provisions residential status of the assessee is either – a) Resident or b) Non-Resident.
Residential status decides income on which assessee is supposed to pay tax. Income earned by assessee is either Indian income or/and Foreign income.

Thus, legal status decides rate of tax, whereas, residential status decides income on which tax is to be paid.

RESIDENTIAL STATUS

Every assessee is Either Resident or Non-Resident.

Based on legal status of the assessee there are different provisions, which decide whether a particular assessee is resident or non-resident.

If an assessee becomes Resident as per the provisions of the act then it is to be decided further, whether he is

1. Resident and Ordinary Resident
OR
2. Resident but Not Ordinary Resident.

RESIDENTIAL STATUS OF AN INDIVIDUAL — SEC. 6 (1)

For an individual to become Resident he has to satisfy any one of the following two conditions:

1. He should have been in India in the year for which Residential Status is to be decided for a period amounting to 182 days or more.
OR
2. Within the 4 years preceding to the year for which residential status is to be decided, he should have been in India for a period amounting to 365 days or more and should have been in India for 60 days or more in the year for which Residential Status is to be decided.

Exception to condition 2:

An Indian Citizen or an Indian member of a crew of an Indian ship who leaves India in any previous year for employment outside OR an Indian Citizen or a person of Indian origin who is outside India and comes on a visit to India, in the second part of the condition no.2 the words 60 days should be replaced by 182 days. It is clear that condition no.2 becomes non-functional in case of such assesses.

A person is deemed to be of Indian origin if he or either of his parents or any of his grandparents was born in undivided India.

If an individual becomes a Resident it is to be decided further which type of Resident he is. These provisions are discussed in Section 6 (6).

For an individual to become Resident and Ordinary Resident he has to satisfy both the conditions given below: -

1. He should have been resident in India at least 2 out of 10 previous years, preceding to the previous year in which he is resident.
AND
2. He should have been in India for a period amounting to 730 days or more in 7 years preceding to the previous year in which he is resident.

If assessee does not satisfy any one of the above mentioned conditions (or both) his Residential Status will be Resident but Not Ordinary Resident.

PROBLEMS

1. Mr. X left India on 1st Aug. 2016. His stay during preceding 4 years was as follows: -

2015 – 2016	50
2014– 2015	70
2013 – 2014	90
2012 – 2013	100

Determine his residential status for the A.Y. 2017–18.

2. Mr. Suresh Ahire, an Indian citizen left India for London on 1st August 2016 as he was appointed manager in U.K. based hotel. Determine his Residential Status for A. Y. 2017–18.
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3. Mr. Advani, an Indian citizen who is working as an assistant in a tourist company in Pakistan came to India on holiday on 15th April 2016 and left for Pakistan on 30th June 2016.
Determine his Residential Status for A.Y. 2017–18.
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4. Mr. X left India on 15th Oct 2016. His stay in India during preceding years was as follows:

2015-2016	220
2014-2015	185
2013-2014	90
2012-2013	320
2011-2012	100
2010-2011	200
2009-2010	75
2008-2009	55
2007-2008	365
2006-2007	200
2005-2006	320
2004-2005	300
2003-2004	120

Determine his residential status for the A.Y. 2017-18.

5. Mr. X was a private detective. Prior to 1st Dec, 2015 he had never been outside India. On 1st Dec. 2015 he left India for South Africa as he was asked by the Government of India to find certain details

regarding irregularities in IPL cricket matches and submit a report. He came back to India on 1st June 2016 and was again asked to leave for South Africa on 15th June 2016. He was to come back on 10th Oct. 2016, but unfortunately met with an accident and was killed.

Determine his Residential Status for A.Y. 2017 – 2018.

- 6.** Mrs. X came on a visit to India on 10th April 2016 and left India on 1st Sep.2016. Her stay during preceding years was as follows: -

2015-2016	100
2014-2015	100
2013-2014	100
2012-2013	100

Places of birth

Mr. X--- Bristol, U.K.

Mrs. X---Jamaica

Father of Mr. X – Dubai

Mother of Mr.X—Hamilton

Grandmother of Mr.X - London

Grandfather of Mr.X - Nairobi

Grandmother of Mrs. X - Karachi

Grandfather of Mrs. X – Port of Spain

Mrs. X celebrated her 70th birthday on 15th August 2016.

Determine her residential status for the A.Y. 2017-18.

- 7.** Mr. Tiwari left for Switzerland on 15th March 2014 after staying in India for about 1 year from 1st April 2013. He came back to India on 9th Sept 2016.

Determine his Residential Status for Assessment Year 2017–18.

- 8.** Mr. Harry, an Indian Citizen was born in Germany. He came to India for the first time when he was 10 and never went outside India till he was 25. He left for Germany again in May 2013 and again came back to India in March 2017.

Determine his Residential Status for A.Y. 2017–18.

RESIDENTIAL STATUS OF HUF, FIRM AND AOP OR BOI SEC. 6 (2)

HUF, Firm or AOP is said to be Resident in India in any previous year if the control and management thereof is situated either partly or wholly in India.

RESIDENTIAL STATUS OF COMPANY SEC. 6 (3)

A company is said to be Resident in India in any previous year if:

- 1) It is an Indian company or
 - 2) During the previous year control and management of its affairs is situated wholly in India.
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RESIDENTIAL STATUS OF OTHER ASSESSEES Sec. 6 (4)

Any other assessee is said to be Resident in India in any previous year if the control & management of its affairs is wholly or partly situated in India.

RESIDENT AND ORDINARY RESIDENT: Sec. 6 (6)

1. H.U.F.: - H.U.F. is said to be Ordinary Resident in any previous year if its 'Karta' is resident and Ordinary Resident in that previous year.
 2. Firm, AOP, Company and All Other Assesses: - The term 'Ordinary Resident' is not applicable to other assesses. They are either Resident or Non Resident.
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PROBLEMS

1. During the previous year 2016-17 affairs of a Hindu Undivided family are partly managed from Delhi and partly from Hong-Kong. Don, a Karta of H.U.F., is resident and ordinary resident in India and Tan who also manages the affairs of family is a non-resident in India for the assessment year 2017-18. Determine the residential status of the family for the assessment year 2017-18.

 2. A firm has five partners all of whom are resident in India. The firm owns a tea estate in Sri Lanka, which is managed by an agent who stays in Sri Lanka. Agent looks after the day to day working of the estate. He takes permission of the partners before taking any major decision. Determine the residential status of the firm.

 3. A company is registered in Dubai, having its head office there. However, the majority of the directors and managers resided in India. Sales contracts and other important business functions were controlled by directors in India. What is the residential status of the company?
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SCOPE OF TOTAL INCOME

On what income an assessee will pay tax in India depends upon his residential status. Scope of total income is explained in the following chart: -

INCOME :-

A. INDIAN INCOME

1. Received or deemed to be received in India
2. Accruing or arising or deemed to accrue or arise in India.

B. FOREIGN INCOME

ACCRUING OR ARISING OUTSIDE INDIA & RECEIVED OUTSIDE INDIA :-

1. From a business Controlled from India or Profession setup in India.
2. From a business controlled from outside India or profession set up outside India.

Note : - If in respect of any business, operations are not carried out in India it will be treated as Foreign income even if it is controlled from India. However, if such an income is received in India it will be treated as Indian Income.

TAXABILITY BASED ON RESIDENTIAL STATUS

- | | |
|---------------------------------------|---|
| 1. Resident and Ordinary Resident | : Has to pay Income- tax in India on total income earned by him. i.e. Indian as well as Foreign Income. |
| 2. Resident but Not Ordinary Resident | : Has to pay Income-tax in India on total income earned by him except income from business controlled from outside India or profession setup outside India. |
| 3. Non-Resident | : Has to pay Income-tax in India only on Indian income. |

SECTION 7 : INCOME DEEMED TO BE RECEIVED IN INDIA

Income deemed to be received in India in the previous year is also included in the taxable income of the assessee. The following income shall be deemed to be received in India:

- (a) Annual accretion to the credit balance of an employee in the case of recognised provident fund to the extent provided under the rules.
- (b) Excess contribution of employer in case of recognised provident fund to the extent provided under the rules.
- (c) Transfer balance in a recognised provident fund to the extent as provided under the rules.

SECTION 8 : DIVIDEND INCOME

Any dividend declared by a company or distributed or paid by it shall be deemed to be the income of the previous year in which it is so declared, distributed or paid, as the case may be;

Any interim dividend shall be deemed to be the income of the previous year in which the amount of such dividend is unconditionally made available to the member who is entitled to it.

The following table illustrates scope of total income in respect of various income: -

Particulars	R & OR	R but not OR	NR
1) <u>Any income received in India</u>			
For work done in India	Taxable	Taxable	Taxable
For work done outside India	Taxable	Taxable	Taxable
2) <u>Any income received outside India</u>			
For work done in India	Taxable	Taxable	Taxable
For work done outside India	Taxable	Not-taxable	Not-taxable
3) <u>Income accrued in India</u>			
Received in India	Taxable	Taxable	Taxable
Received out of India	Taxable	Taxable	Taxable
4) <u>Income accrued out of India</u>			
Received in India	Taxable	Taxable	Taxable
Received out of India	Taxable	Not-taxable	Not-taxable
5) Salary paid by Indian Government	Taxable	Taxable	Taxable
6) Dividend or Interest paid by Indian company.	Taxable	Taxable	Taxable
7) <u>Income from property in India</u>			
Received in India	Taxable	Taxable	Taxable
Received out of India	Taxable	Taxable	
8) <u>Profit on sale of assets in India</u>			
Received in India	Taxable	Taxable	Taxable
Received out of India			Taxable
9) Income from business in India controlled from India	Taxable	Taxable	
10) Income from business in India controlled from Dubai.	Taxable	Taxable	Taxable
11) Income from business in Dubai controlled from U.S.A.	Taxable	Not-taxable	Taxable
12) Income from business in Dubai controlled from India.	Taxable	Taxable	Not-taxable
13) Remittance of past untaxed amounts.	Not-taxable	Not-taxable	Not-taxable

SECTION 9: INCOME DEEMED TO ACCRUE OR ARISE IN INDIA

- 1) All income accruing or arising through or from:
 - a. Any business connection in India.
 - b. Any property in India.
 - c. Any asset or source of income in India.
 - d. Transfer of capital asset situated in India.
 - 2) Salaries payable for services rendered in India will be called Indian income.
 - 3) Salary received by Indian National from the Government in respect of services rendered outside India is an Indian income.
 - 4) Any dividend paid by an Indian company is considered as an Indian income.
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PROBLEMS

1. From the following details of income of the assessee find out his gross total income for the A.Y. 2017-18 if he is: -
 - a) R & OR b) R but not OR c) Non Resident
 - (1) Dividend from Indian companies credited to bank account in Iraq ₹ 12,000.
 - (2) Income from business in Sri Lanka controlled from Mumbai ₹ 18,000.
 - (3) Income accrued in Afghanistan & received in Pakistan ₹ 31,000.
 - (4) Income from property in Australia received in Bhutan ₹ 12,000.
 - (5) Interest credited in Bank account in Switzerland ₹ 50,000.
 - (6) Rent from property in Australia received in Nepal ₹ 24,000.
 - (7) Income from business in Mumbai controlled from Dubai ₹ 1,00,000.
 - (8) Past untaxed profit brought to India ₹ 40,000.
2. Mr. Balvinder, an Indian citizen, furnishes the following particulars of his income earned during the previous year relevant to assessment year 2017-18.
 - (a) Pension from an Indian employer received in Sudan ₹ 36,000.
 - (b) Profit from business at Pune and managed from Britain ₹ 48,000.
 - (c) Income earned from business in Kuwait which is controlled from Mumbai (₹ 30,000 received in India) ₹ 54,000.
 - (d) Past untaxed profit brought to India ₹ 1,00,000.
 - (e) Income from agricultural land in Sri Lanka ₹ 10,000 received in India.
 - (f) Profit on sale of plant at Bhopal (1/2 received in U.S.A.) ₹ 38,000.
 - (g) Dividend from German company received in India ₹ 5,000.
 - (h) Profit from business in Rajasthan controlled from Maharashtra ₹ 74,000.
 - (i) Salary earned and received in Saudi Arabia ₹ 48,000.
 - (j) Interest on Bhutan Development Bonds (entire amount received in Sudan) ₹ 40,000.

Determine the gross total income of Mr. Balvinder for the assessment year 2017-18 if he is, (i) Resident and ordinarily Resident (ii) Resident but not ordinarily Resident (iii) Non-Resident.

3. Following is the income of Mr. Khan for the previous year relevant to assessment year 2017–18.

- i) Interest from Indian companies received in Iraq and credited to bank account in Iraq ₹ 12,000.
- ii) Income from business in Sri Lanka controlled from Kerala ₹ 18,000.
- iii) Income accrued in Nepal and received in Pakistan ₹ 31,000.
- iv) Income from property in Japan received in Tibet ₹ 12,000.
- v) Interest credited from Bank account in Switzerland ₹ 50,000.
- vi) Rent from property in Australia received in France ₹ 24,000.
- vii) Income accrued in Switzerland and not received in India ₹ 10,000.
- viii) Income earned in U.S.A. in past but brought in India during the year ₹ 20,000.

Find out his gross total income resident:

- i) Resident and ordinarily resident;
 - ii) Resident but not ordinarily resident;
 - iii) Non-Resident in India.
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4. The following are the sources of income of Shri Manohar for the assessment year 2017-2018. Determine his total taxable income assuming alternatively that he is:

- i) Resident and Ordinarily Resident.
 - ii) Not Ordinarily Resident
 - iii) Non-Resident.
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- (a) Salary from a company (Gross) ₹ 52,000. (Earned in India)
 - (b) Income from profession carried in India ₹ 57,000.
 - (c) Income accrued in U.K. and brought in India ₹ 3,000.
 - (d) Income from a business in Germany ₹ 81,000(The business is controlled from India).
 - (e) ₹ 10,000 received from a bank in France. The money was deposited in the bank account by his brother being the interest and dividend earned by Mr. Manohar in America.
 - (f) ₹ 20,000 salary earned in India deposited by his employer directly in the bank in Switzerland.
 - (g) ₹ 2000 Professional fees earned and received in New York but later remitted to India.
 - (h) ₹ 10,000 income from business, which is carried on in Hong Kong but controlled from New York.



UNIT 3 : EXCLUSIONS FROM TOTAL INCOME (SECTION 10)

Under Section 10 of Income Tax Act of 1961 certain income is exempted from tax either fully or partially. In other words it is a list of tax-free income in the hands of the assessee and though it is an income of the year assessee is not required to pay tax on it.

1. Agricultural income Sec. 10 (1): - For an income to be called an agricultural income conditions to be satisfied are-
 - (a) Rent or revenue should be derived from land.
 - (b) Land should be used for agricultural purpose.
 - (c) The land should be situated in India.

Examples: -

1. Income from lease of agricultural land.
2. Income from land used for agricultural purpose e.g. produce grown for consumption by man (grains, vegetables or fruits) or animals (grass or pastures); cash crops (cotton jute etc.), luxury items such as coffee, tobacco; crops grown for self-consumption etc;
3. Compensation received from Insurance Company for damage to tea garden.
4. Income from growing flowers.
5. Salary or interest on capital received by a partner from a firm engaged in agriculture (as salary or interest is only a way of distributing profits).

Examples of Non agricultural income: -

1. Income not directly derived from land: Interest on arrears of rent; dairy farming, poultry farming, dividend received from a limited company having only agricultural income; salary of a manager of an agricultural estate, rent for land used for storing crops; manufacture of salt from sea-water.
 2. Income without performing basic agricultural operations: Sale of plants which have grown spontaneously (on their own without any sowing of seeds e.g. mushrooms); sale of trees which were already standing on the agricultural estate when purchased.
 3. Income from produce sold by others and not by the cultivator: Sale of agricultural produce received as interest on loan; received as price for water supplied to agricultural land; sale of agricultural produce by a broker.
2. Receipt from H.U.F. Sec. 10 (2): Any amount received by member of H.U.F. out of the family income is exempt from tax.
 3. Partners Share in the profits of the firm Sec. 10 (2A): Partner of the firm is not required to pay tax in individual capacity on his share in profits of the firm.
 4. Leave Travel Concession Sec. 10 (5): It is the amount given by the employer to the employee for traveling while on leave or to settle at any place in India after retirement.

Subject to certain restrictions this income is exempt from tax in respect of travel concession received by an assessee from his employer or former employer:

- (a) For himself & his family in connection with his proceeding to any place in India.
- (b) For himself & his family in connection with his proceeding to any place in India after retirement from service or after termination of his service.

However, exemption under this section is restricted to amount actually spent by the assessee.

For the purpose of this section Family in relation to any individual means:

- i. The spouse and children of the individual.
- ii. The parents, brothers & sisters of the individual or any of them wholly or mainly dependent on the individual.

Exemption under this section is available in respect of 2 journeys performed in a block of 4 calendar years commencing from 1986.

Leave travel allowances received	Actual amount spent by employee	Exemption	Taxable amount
10,000	-----	Nil	10,000
10,000	2,000	2,000	8,000
10,000	9,000	9,000	1,000
10,000	10,000	10,000	Nil
10,000	15,000	10,000	Nil

5. Foreign allowances & perquisites to Government employees outside India Sec. 10 (7).

6. Section 10 (10) Gratuity: Gratuity is the lump sum payment made by the employer, to the employee at the time of his retirement, or to the family members of employee in case of his death. For income tax purpose, Gratuity is considered salary income. However, entire amount received as gratuity is not taxable. Amount that is exempt from tax is covered by following provisions: -

- (a) Gratuity received by government employees: It is fully exempt from tax.
- (b) In case of employees covered by the Payment of Gratuity Act, 1972: - Any gratuity received by an employee covered by the payment of Gratuity Act, 1972 is exempt from tax to the extent of least of the following: -
 - i) 15 days salary (7 days in the case of employees of a seasonal establishment) based on salary last drawn for every completed year of service or part thereof in excess of six months;

- ii) ₹ 10,00,000 w. e. f from 24/05/2010
 - iii) Gratuity actually received
- (c) For employees not covered by the Payment of Gratuity Act, 1972: For other employees, Gratuity received is exempt as per the following: -
- i) Half month's salary for each completed year of service calculated on the basis of average salary drawn for 10 months immediately preceding the month of retirement or death, OR
 - ii) Actual amount received as gratuity, OR
 - iii) Amount fixed by the government from time to time which at present is increased to ₹ 10,00,000 w.e.f from 24/05/2010 whichever is less.

Following points should be noted: -

1. Salary for this purpose means Basic + D.A. for (b) above & Basic + D.A. + Commission at fixed percentage for (c) above.
2. 26 days refer to working days per month. This is important to calculate 15 days (or 7 days) salary.

PROBLEMS

1. Mr. X, non-government employee not covered by Payment Gratuity Act 1972 retired from services of Kedar Automobiles on 31st August 2016 and received ₹ 96,000 as Gratuity after a service of 40 years and 3 months. His average salary during last 10 months immediately preceding his retirement was ₹ 4,500 per month. Compute his taxable gratuity if any.

2. Mr. Y was a non-government employee not covered by Payment of Gratuity Act. He retired on 1st May 2015 after a service of 35 years and 11 months. Since 1st Jan. 2015 he was drawing a monthly salary of ₹ 5,500. Salary was due for increment on 1st Jan. every year @ 10%. On retirement he received ₹ 60,000 as gratuity. Compute taxable Gratuity if any.

3. Mr. A, Income tax officer receives ₹ 2,00,000 as gratuity while he is still working. Is this gratuity taxable?

4. Mr. A, Income tax officer receives gratuity of ₹ 2,00,000 at the time of retirement. Is this gratuity taxable?

5. Mr. D who is working in Reliance Industries Ltd. received Gratuity worth ₹ 5,00,000 while in service. Is this gratuity taxable?

6. Mr. F retired from X Ltd. to whom gratuity act is applicable. Received gratuity of ₹ 6,00,000. His service period is 35 years 11 months and last drawn salary was ₹ 10,000. Is this gratuity taxable?

7. Section 10 (10A) Commutation of Pension: Pension is a periodical payment made by employer to the employee after retirement. This section is also applicable in respect of any payment received by way of commutation of pension received by an individual out of annuity plan of the L.I.C. from a fund set up by the corporation.

There are two options regarding this payment: -

- (a) **Uncommuted Pension:** It is the pension that is to be received periodically. It is fully taxable as salary income in case of all the employees.
- (b) **Commuted Pension:** It is amount received in lump sum in lieu of periodical pension. Regarding commutation, options available are:- a) Commutation of full pension, where no periodical payment will be made, entire pension will be paid in lump sum. b) Part of the pension can be commuted where in respect of uncommuted pension periodical payment will be made.

TAXABILITY OF COMMUTED PENSION

- 1. Any payment on commutation of pension received by all Central and State Government Employees is fully exempt from tax.
- 2. In case of other employees taxability depends on whether employee received gratuity also on retirement.

Exemption is restricted to the following: -

- 1. In case where employee received any gratuity, commuted value of 1/3rd pension is exempt.
- 2. In case where employee did not receive gratuity (i.e. he received only pension) commuted value of half of pension is exempt.

Any payment received by way of commutation of pension from a fund under clauses 23 AAB (i.e. fund set up by LIC of India viz Jeevan Suraksha) under pension scheme approved by controller of Insurance is fully exempt from tax.

New Pension Scheme for Central Govt. Employees

New pension scheme is applicable to new entrants to Government service. As per the scheme it is mandatory for persons entering the service of the Central Government on or after January 1, 2004, to contribute 10 per cent of salary every month towards their pension account. A matching contribution is required to be made by the Government to the said account.

The tax treatment under the new scheme is as follows –

1. Contribution by the Central Government to the pension scheme is first included under the head “Salaries” in hands of the employee.
2. Such contribution is deductible (to the extent of 10 per cent of the salary of the employee) under section 80CCD.
3. Employee’s contribution to the pension scheme (to the extent of 10 per cent of the salary of the employee) is also deductible under section 80CCD.
4. When pension is received out of the aforesaid amount, it will be chargeable to tax in the hands of the recipient.
5. The aggregate amount of deduction under sections 80C, 80CCC & 80CCD cannot exceed ₹ 1, 50,000.
6. “Salary” for the purpose of points 2 and 3 (supra) includes basic salary and dearness allowances (if the terms of employment so provide) but excludes all other allowances and perquisites.
7. No deduction will be allowed under section 80C in respect of amounts on which deduction has been claimed under section 80CCD.

PROBLEMS

1. Mr. A retired from the department of Sales Tax on 1st April 2016. He was entitled to Monthly pension ₹3000 & received gratuity worth ₹ 2,00,000. On 1st Oct 2016 he commuted 50% of the pension for ₹ 2,00,000. Find out his taxable pension for previous year 2016–17.
2. Mr. D retired from the department of Central Excise on 1st Dec. 2016. Monthly pension ₹ 10,000 30% of the pension he commuted for ₹ 4,00,000. He also received gratuity of ₹ 5,00,000. Find out his taxable pension, if any.
3. Mr. A retired from Ganesh Ltd. on 1st April 2016. Monthly pension ₹ 6,000. 70% of the pension he commuted for ₹ 4,20,000 on 1st Oct. 2016. He has received gratuity also. Find out taxable pension
4. Mr. X retired from Parag Ltd. on 1st May 2016. He did not receive gratuity. Monthly Pension ₹ 6,000. On 1st Sep. 30% of the pension was commuted for ₹ 3,00,000. Find out taxable pension.
5. Mr. A retired from KBC Ltd. on 1st Jan. 2017. He was entitled to a monthly pension of ₹ 6,000 but got 80% pension commuted for ₹ 2,10,000. He was also entitled to receive gratuity as per the terms of his employment. Find out taxable pension for A.Y. 2017–18.

- 6 Mr. A retired from Chirag Ltd. on 1st April 2016. Service period 40 years, 6 months. Average salary at the time of retirement ₹ 10,000. p.m. Gratuity received ₹ 3,00,000. Pension per month ₹ 7,500. On 1st April 2016 he commuted 50% of the pension for ₹ 3,00,000. Find out his taxable pension & gratuity for the previous year 2016-17. He is not covered by Gratuity Act.

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8. **Leave Salary Section 10 (10AA):** Leave salary is taxable under the head 'Income from Salary'. However, in certain cases Leave Salary is exempt from income tax. Details of this exemption are given below:

- a. Leave Salary received by an employee of Central or State Government at the time of retirement is totally exempt from tax.
- b. For other employees, if leave salary is received at the time of retirement, least of the following is exempt:

1. Period of earned leave (in months) to the credit of employee at the time of leaving the job but not exceeding 30 days per each completed year of service \times Average monthly salary
2. Leave salary for the period 10 months based on average salary drawn in last 10 months preceding to the date of retirement or
3. Amount as specified by Central Government from time to time which at present is ₹ 3,00,000.
4. Actual amount received as leave encashment.

Salary for this purpose is Basic + DA + Commission at fixed percentage.

Notified limit of ₹3,00,000 applies to all such amount received from one or more employers/current or earlier years. Therefore, for subsequent claims amount exempted earlier will be deducted from the limit.

9. **Retrenchment Compensation Section 10 (10B):** Retrenchment compensation received by a worker under Industrial Disputes Act of 1947 or any other act is exempt on the following basis:

- a. Amount as calculated according to the provisions of the Act or
- b. Amount as specified (not less than 50,000) by the Central Government. For a worker retrenched after 31.12.1996 amount specified is ₹ 5,00,000 or
- c. Amount received. Whichever is less.

10. **Compensation on retirement of an employee of a public sector company Section 10 (10C):**

Payment received by an employee of: -

1. An authority established under Central / State / Provincial Act.
2. Local authority.

3. University (under UGC Act)
4. IIT.
5. Any State or Central Government
6. Public Sector Company
7. Any other Company
8. Co-operative society
9. Any Institute specified by the Government for this purpose.
10. Any institute of management as the Central Government may notify.

Under voluntary retirement or termination of service scheme approved by the Government amount is exempt from income tax upto ₹ 5,00,000.

11. Tax on perquisites paid by employer. Section 10(10CC)

12. Amount received under a Life Insurance Policy Section 10 (10D): Policy amount as well as bonus is fully exempt from tax except amount received under Keyman Insurance Policy and under section 80DD or 80DDA(3) and any sum received under policy issued on or after 1.4.2003 where premium payable in any year exceeds 20% of sum assured. However in such cases sum received on death of a person shall continue to be exempt.

13. Payment from Provident Fund Section 10(11). For details refer chapter 'Salary'.

14. Accumulated balance from a recognised Provident Fund Sec.10 (12).

15. Payment from an approved Super Annuation Fund Section 10(13).

16. House Rent Allowance (Section 10 (13A) and rule 2A):

The **least** of the following is exempt from tax:

- (a) An amount equal to 50 per cent of salary, where residential house is situated at Mumbai, Kolkata, Delhi or Chennai and an amount equal to 40 per cent of salary where residential house is situated at any other place; **OR**
- (b) House rent allowance received by the employee in respect of the period during which rental accommodation is occupied by the employee during the previous year; **OR**
- (c) The excess of rent paid over 10 per cent of salary. "Salary" for the aforesaid purposes means basic salary and includes dearness allowance if terms of employment so provide. It also includes commission based on a fixed percentage of turnover achieved by an employee as per terms of contract of employment, but excludes all other allowances and perquisites.

17. Special Allowance for expenses Section 10 (14):

Any special allowance granted by employer to employee to meet the expenses shall be exempt from tax to the extent spent by an employee on expenses or to the extent specified in the Act. e.g.

Education Allowance is exempt @ ₹ 100 per month per child upto 2 children, Transport Allowance is exempt up to ₹ 800 per month. Children's hostel Allowance @ ₹ 300 Per month up to 2 children.

18. Certain income by way of interest Section 10 (15):

- e.g. a) Interest on P.P.F.
b) Interest on Post Office Savings Account.
c) Interest on Notified Government Securities & Debentures.
d) Interest on Tax-free RBI bonds etc.

19. Scholarships granted to meet the cost of education Section 10 (16).

20. Allowance received by the members of parliament or state legislature Section 10(17).

- a) Daily allowance fully exempt.
b) Allowance received under members of parliament (constituency allowance) Rules of 1986 fully exempt.
c) Any constituency allowance is fully exempt.

21. Section 10 (17A) Awards:

Awards received (in cash or kind) are exempt in respect of Award instituted in the public interest by Central or State Government or any body approved by the Government.

22. Section 10(18): Any income by way of-

- a. Pension received by an individual who has been in the service of the Central or State Government and has been awarded "Param Vir Chakra" or "Maha Vir Chakra" or "Vir Chakra" or such other gallantry award as the Central Government may, by notification in the Official Gazette, specify in this behalf;
b. Family pension received by any member of the family of an individual referred to in sub-clause (i)

23. Income of a member of a scheduled tribe residing in area specified in the constitution or in the states of Nagaland, Manipur & Tripura & in the Union Territories of Arunachal Pradesh & Mizoram or areas covered by Notification issued by Governor of Assam. Section 10(26).

24. Income of resident of Ladakh District. Section 10(26A). This exemption is available subject to certain restrictions.

25. Clubbed income of a minor child Section 10(32): In case income of a minor child is clubbed with that of the parent under section 64(1A) such income is exempt from tax up to maximum of ₹ 1,500 in respect of each minor child.

- 26. Section 10(33):** Any income arising from transfer of units of the US64 where transfer takes place on or after 1.4.2002.
- 27. Section 10(34): Dividend** – Any income by way of dividend referred to in section 115-O.
- 28. Section 10(35):** Any income in respect of Mutual Fund specified under clause 23D.
- 29. Section 10(36):** Any income from transfer of long term capital asset being eligible equity shares purchased on or after 1.3.2003 but before 1.3.2004.
- 30. Section 10(37):** Capital gain on compulsory acquisition of urban agricultural land if compensation is received after 31.3.2004 & land was used by the assessee (or any of his parents) for agricultural purpose during 2 years immediately preceding to transfer.
- 31. Section 10(38):** Long Term Capital Gain on transfer of equity shares/units covered by Securities Transaction Tax (STT).
- 32. Section 10(39):** Income arising from international sporting event held in India where in two or more countries are participating.
- 33. Section 10(44) :** Any income received by any person for or on behalf of the New Pension System Trust.

