1 BASIC CONCEPTS [S. 1 - 4]

THEORY AND ILLUSTRATIONS

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1. INTRODUCTION

1.1 TAX LAWS

Government can raise funds needed for the development and defence of the country by collecti taxes such as Income-tax, excise duties, etc. from the citizens. As the revenue collected from incom tax helps the development of the country, it is said that "income-tax is the price one pays civilisation". Under the Constitution of India, the Central Government has the right to collect income tax. The law governing such collection of income-tax is

- *specified* in the *Income-tax Act, 1961* ("the Act");
- *implemented* according to the rules laid down in the *Income-tax Rules, 1962* ("the Rules");
- *administered* through the *circulars* issued by the Central Board of Direct Taxes ("CBDT")
- *interpreted* by the *judgements* of the Supreme Court and High Courts which settle the lega disputes between the Government and tax-payers.

1.2 SCOPE OF STUDY

We will be studying basically only Sections 1 to 80 of the Act which deal with -

(1) the *basic concepts* of the income-tax law such as what is income, whose income is taxable income of what period is taxable, how the income is to be computed and so on;

(2) the provisions relating to the *computation of total income under various heads* such as Salaries Income from House Properties, Income from Business or Profession, Capital Gains, Income from Other Sources;

(3) the *deductions* available from total income on savings; for blind individuals; on mediclaim insurance; on contribution to pension fund etc.

With this back-ground, let us now begin our detailed study of the Income-tax Act.

1.3 SCHEME OF ACT

Just as a book is divided into chapters and paragraphs, the Income-tax Act is divided first into chapters (from I to XXIII, i.e. 1 to 23). Each chapter is divided into sections (298 in all). Each section deals with a specific matter ("provision") and is further divided into sub-sections, clauses and sub-clauses. Thus, S. 17(2)(c)(i) means section 17, sub-section 2, clause c, sub-clause i. An "*explanation*" to a section clarifies certain word or point of law in the section. A "*proviso*" to a section indicates an exception to the provision or a pre-condition to be satisfied or how the section is to be applied in a peculiar situation. Any change (amendment) in the Act is made through the Finance Act (Budget) passed every year.

2. INCOME-TAX ACT EXTENDS TO WHOLE OF INDIA [S. 1]

S. 1 states that (1) this Act may be called the Income-tax Act, 1961; and (2) it extends to the whole of India. Thus the Act is applicable to *persons residing in India* as well as to the *income arising in India*. "India", for the above purpose, would cover the territory of India; territorial waters, seabed and sub-soil; continental shelf; exclusive economic zone (EEZ); maritime zone and airspace.

3. DEFINITIONS [S. 2]

3.1 INTRODUCTION

To define a word means to indicate its precise meaning. Section 2 of the Act defines some words like Assessment Year, Previous Year, Person, Income etc. The definitions in S.2 of the Act, which is like a mini-dictionary, indicate the precise meaning of such words.

3.2 EXCLUSIVE VS. INCLUSIVE DEFINITIONS

The definitions given in the Act are of two types : Exclusive Definitions and Inclusive Definitions.

A definition is said to be *exclusive* when it defines a term as: ...*means* .... An exclusive definition indicates that the meaning of the term is exactly as defined by law, i.e. no more and no less. These definitions are exhaustive, definite and specific (e.g. definitions of assessment year, previous year, company, resident, non-resident, annual value etc.).

A definition is said to be *inclusive* when it defines a term as: .... *includes*... An inclusive definition indicates that the term includes certain extra items, in addition to the natural and general meaning of the term. Inclusive definitions widen the normal scope of a term (e.g. definitions of person, income, assessment, business etc.).

3.3 IMPORTANCE

S. 2, it may be said, contains a mini-dictionary. It defines and explains the words frequently used in the Act, at one place in the beginning itself. Once defined, these words carry the same meaning throughout the Act. The definitions also help us to understand how the income-tax liability is determined. The definitions provide answers to the following questions:

Q.1 When is the tax liability computed ? (**Ans.** *Assessment Year*).
Q.2 Income earned during what period is taxed ? (**Ans.** *Previous Year*).
Q.3 Whose income is charged to tax ? (**Ans.** *Income of all Persons*).
Q.4 What is charged to tax ? (**Ans.** *Income*).
Q.5 How is Income and Tax computed ? (**Ans.** *Assessment*).
Q.6 Who is liable to pay the tax ? (**Ans.** *Assessee*).

Let us now study the above definitions one by one.

4. ASSESSMENT YEAR [S. 2(9)]
("When" is liability for tax computed ?)

4.1 DEFINITION

Section 2(9) of the Act defines an 'assessment year' as *"the period of twelve months commencing on the first day of April every year"*.

4.2 COMMENTS

An assessment year begins on 1st April of every year and ends on 31st March of next year. For example, the current assessment year 2022-23, has begun on 1st April, 2022 and will end on 31st March, 2023.

A financial year means the period of 12 months from 1st April to the following 31st March. This is the accounting year of the Government. The income earned by a person during one financial year is taxed in the next financial year. The year in which income is earned is called previous year and the next year in which the income is taxed is called assessment year. Thus the total income of a person during the financial year (previous year) 2021-22 will be taxed in the next financial year (assessment year) 2022-23.

5. PREVIOUS YEAR [S. 3]
(Income earned during "what period" is taxed?)

5.1 DEFINITION

Section 3 of the Act defines 'previous year' as follows: *For the purposes of this Act, "previous year" means the financial year immediately preceding the assessment year:*

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

5.2 COMMENTS

Income earned in one year (known as the "previous year") is taxed in the next year (known as "assessment year"). Thus the 'previous year' for the current assessment year 2022-23, is the financial year immediately preceding i.e. the 12 months from 1st April 2021 to 31st March 2022. The total income earned by a person from whatever sources during the period from 1st April 2021 to 31st March 2022 will be taxed in the current assessment year 2022-23. The previous year is uniform for all persons and is to be followed in respect of all types of income, irrespective of the 'accounting year' followed by a person. Thus, if a company follows the period from 1st August to 31st July as 'accounting year', it has to prepare separate Accounts for the period 1st April to 31st March to compute its taxable income.

5.3 PREVIOUS YEAR OF NEW BUSINESS [PROVISO TO S.3]

S. 3 provides that, normally the previous year begins from the 1st April of the financial year. Proviso to S.3 deals with an exception to this rule. If a business or a profession is set up during the financial year, its first previous year would start from the date of setting up of the business (or profession) and end with the immediately falling 31st March. The same rule applies to a new source of income (salary, etc.) coming into existence during the previous year. In such a case, the previous year may consist of a period less than 12 months.

Illustration 1 : (Answer the following in brief)

A new business is set up by Mr. Shah on 1st June, 2021. What will be the previous year under the Income-tax Act ?

Solution :

The previous year in respect of the new business will be the period from 1st June, 2021 to 31st March, 2022 (and the assessment year will be 2022-23).

Illustration 2 :

Mr. A, earlier unemployed, gets a job on 1st August, 2021. What will be the relevant previous year ?

Solution :

His previous year in respect of the income from salary will be the period from 1st August, 2021 to 31st March, 2022 (the assessment year will be 2022-23).

6. PERSON [S. 2(31)]
("Whose" income is charged to tax ?)

6.1 DEFINITION

"Person" includes - (i) an individual, (ii) a Hindu undivided family, (iii) a company, (iv) a firm, (v) an association of persons or a body of individuals, whether incorporated or not, (vi) a local authority and (vii) every artificial juridical person, not falling within any of the preceding sub-clauses.

Explanation : *For the purposes of this clause, an association of persons or a body of individuals or a local authority or an artificial juridical person shall be deemed to be a person, whether or not such person or body or authority or juridical person was formed or established or incorporated with the object of deriving income, profits or gains.*

6.2 COMMENTS

The income earned by every person is taxed. A "person" is classified into different categories, such as an individual, a firm, a company etc. Each category denotes the legal status of a person. Each category is taxed in a different manner in respect of : (a) the *minimum amount of income exempt from tax* (Nil tax upto ₹ 2,50,000 only for an individual or HUF) (b) the *rate of tax* (e.g. higher rate for higher income for an individual and a flat rate on all income for a firm) and (c) the *rules of computation of income* (e.g. allowance for self-occupation of house only for an individual). The definition of a "person" is an "inclusive" one, and not "exclusive". So, any entity not covered by the definition can also be a "person" under the Income-tax laws. An entity (e.g. a Trust) is treated as a 'person' even if its object is not earning of any income (Explanation to S. 2(31)). Let us study the categories listed above to ascertain the scope of the term - a "person".

(1) **Individual :** Individual means a natural person i.e. a human being. It includes a male, female, even a minor or a lunatic.

(2) **Hindu Undivided Family :** A Hindu Undivided Family (HUF) consists of all persons lineally descended from a Hindu ancestor (children and grand children), and their wives and unmarried daughters.

(3) **A Company :** A Company is a taxable entity (person) distinct from its shareholders. Section 2(17) of the Act defines "company" as follows:

(i) any Indian Company,

(ii) any body corporate incorporated under the laws of a country outside India,

(iii) any institution, association, or body which is/was assessed/assessable as a company for any assessment year on or before 1-4-1970,

(iv) any institution, association, or body whether incorporated or not and whether Indian or not, which is declared by the Central Board of Direct Taxes (CBDT) to be a Company.

Thus, a Company means, in brief, an Indian Company, a foreign Company, any entity assessed as a company upto the assessment year 1970-71, and an entity declared to be a company by the CBDT. This definition is much wider than that under the Companies Act.

(4) **Firm :** A firm is a taxable entity distinct from its partners. "Firm" also includes a Limited Liability Partnership of two or more persons carrying on business or profession constituted under the Limited Liability Partnership Act, 2008.

(5) **Association of Persons (AOP) :** An "association of persons" (AOP) means an association in which two or more "persons" join in for a common purpose or a common action for earning income. An AOP can have any "person" i.e. an individual, a firm, a HUF, a Company etc. as a member. Following are the examples of an association of persons: (a) Firm attempted to be formed but where due to legal defect in partnership deed, partnership is not valid (b) Members of former Hindu Undivided Family earning income jointly even after partition of the HUF (c) A Company joining with two other Companies in a joint venture (d) A Trust (e) A Club (f) a Co-operative Society.

(6) **Body of Individuals (BOI) :** A Body of Individuals means a team of individuals carrying on some activity with the object of earning income. An association of persons may consist of non-individuals but a Body of Individuals consists of only "individuals" or human beings and cannot have any other person (e.g. a firm, a HUF etc.) as a member. Further, an association of persons denotes a voluntary, deliberate or contractual coming together. A Body of Individuals, on the other hand, may arise due to operation of law e.g. heirs of a deceased person earning income from property inherited under law of succession.

(7) **Local Authority:** Local Authority means a municipality, a District Board, a Port Commissioner, or any other authority legally entitled to control or manage a municipal or a local fund.

(8) Artificial Juridical Person: Any entity having a separate legal existence, not covered under of the above categories, falls under this category, e.g. a Deity, an Idol, a corporation establish under a special Act (e.g. Life Insurance Corporation), a University, a Bar Council etc.

Illustration 3 : (Answer the following in brief)

What is the status of the following persons under the Income-tax Act ?

(1) Veena Shah
(2) Mr. Shahane - a person of unsound mind
(3) Kumar - a minor
(4) Ram, his wife Sita and two sons - Lav and Kush
(5) M/s Rohit & Mohit - two Chartered Accountants in partnership
(6) Reliance Industries Limited
(7) The Tata Memorial Trust
(8) Sunil Cricket Club
(9) Joint venture among A Ltd., B Ltd., and Mr. X
(10) A, B and C, individuals, constructed a Cinema Theatre jointly and share the rent
(11) Mumbai Municipal Corporation
(12) Pune Cantonment Board
(13) Nhava-Sheva Port Trust
(14) Marathwada University
(15) Roha Gram-panchayat
(16) Tirupati Devsthanam

Solution :

(1) An Individual
(2) An Individual
(3) An Individual
(4) A Hindu Undivided Family
(5) A Firm
(6) A Company
(7) An Association of persons
(8) An Association of persons
(9) An Association of persons
(10) A Body of Individuals
(11) Local Authority
(12) Local Authority
(13) Local Authority
(14) Artificial Juridical Person
(15) Local Authority
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(12) Local Authority
(13) Local Authority
(14) Artificial Juridical Person
(15) Local Authority
(16) Artificial Juridical Person.

7. INCOME [S. 2(24

("What" is charged to tax ?)

7.1 DEFINITION

As per Section 2(24) of the Act the term "Income" includes -

(1) **profits** and gains.

(2) **dividends**.

(3) **voluntary contributions** received by

(a) a charitable or religious trust or institution, or

(b) a specified institution (e.g. a scientific research association, a sports association, a non-charitable or public religious trust, or an university or other educational institution or a hospital or an electoral trust), except contributions specifically received towards the corpus (capital

(4) **perquisites** taxable under the head "Salaries" under S. 17(2) (e.g. rent-free accommodation) **profits in lieu of salary** taxable as salaries under S.17(3) (e.g. Retrenchment Compensation)

(5) **special allowance** or benefit specifically granted to an employee to meet expenses for performance of his duties (e.g. Entertainment Allowance),

(6) allowance to an employee to meet his personal expenses at office, or to compensate him for increased cost of living (e.g. **Dearness Allowance**).

(7) **benefit or perquisite** obtained from a Company by a director or a person having substantial interest in the Company or their relatives (e.g. provision of a motor car).

(8) **benefit or perquisite** obtained by a **representative assessee** (a trustee), or a beneficiary, or any amount paid by the trustee towards any sum due by the beneficiary.

(9) any sum chargeable -

(a) under S.28 (ii) & (iii) of the Act (**compensation** for termination of a contract for directorship or agency; **income from services** to members earned by a trade association etc.); or

(b) under S.41 (profits chargeable to tax as income from business e.g. recovery of bad debts, sale of scientific research asset etc.); or

(c) under S.59 (profits chargeable to tax as income from other sources e.g. recovery of expenses claimed earlier).

(10) **profits** on sale of an import licence, taxable u/s 28(iiia).

(11) **export cash assistance** received from Government, taxable u/s 28(iiib).

(12) **refund of customs or excise duty** received or receivable against exports, taxable u/s 28(iiic).

(13) benefit or **perquisite from business** or profession (e.g. a gift received by a doctor from a patient), taxable u/s 28(iv).

(14) any interest, salary, bonus, commission or **remuneration** due to or received **by a partner from a firm**, to the extent allowed to be deducted under section 40(b), taxable u/s 28(v).

(15) **capital gains** chargeable under S.45 of the Act.

(16) **profits** of any business of **insurance** carried on by a mutual insurance company or a co-operative society, taxable u/s 44 or the First Schedule to the Act.

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

(18) **winnings from lotteries,** prizes by draw of lots or by chance, crossword puzzles, races including horse races, card games, game show, entertainment programme on television in which people compete to win prizes, gambling or betting.

(19) **contributions from employees to Provident Fund,** or Superannuation Fund, or Employees Insurance Fund etc. deducted by the employer from the salaries of the employees.

(20) any sum received under a **Keyman Insurance Policy** (i.e. a policy taken on the owner / Director etc.), including bonus on such policy.

(21) Fair Market Value of **inventory** which is converted into, or **treated as a capital asset** [S.28(iva)].

(22) any sum referred to u/s 28(va) [i.e. **non-compete compensation** etc.]

(23) any **sum** exceeding ₹ 50,000 received without consideration (i.e. a **gift**) by an individual or an HUF, taxable u/s 56(2)(vi).

(24) any **movable / immovable property** worth more than ₹ 50,000 received as **gift**, taxable u/s 56(2)(vii).

(25) any **specified shares** worth more than ₹ 50,000 received as a **gift** u/s 56(2)(viia).

(26) **any consideration** received for issue of shares as **exceeds the fair market value of the shares** taxable u/s 56(2)(viib).

(27) **advance money** for capital asset received during negotiations and then forfeited, taxable u/s 56(2)(ix).

(28) Any sum of moeny or value of **property received without consideration** or for inadequate consideration [S. 56(2)(x)].

(29) Any **compensation** or other payment, due to or received by any person, in connection with **termination of his employment** or the modification of the term and conditions relating thereto [S. 56(2)(xi)].

(30) Assistance in the form of a **subsidy or grant or cash incentive or duty drawback or waiver or concession or reimbursement**, by whatever name called, by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee is included

in the definition of income. The only exclusions are (i) the subsidy or grant or reimburs which has been taken into account for determination of the actual cost of the asset in accord with Explanation 10 to section 43(1); and (ii) the subsidy or grant by the Central Goverr for the purpose of a trust or institution established by the Central/State Government.

7.2 COMMENTS

The above definition of income is "inclusive", and not "exclusive". Since the definition of inc inclusive, it indicates that income, under the Income-tax Act, includes the items listed in the defi above, as well as the items which signify income as generally understood. Let us, therefore, stud general meaning of income.

"Income" means the amounts earned by a person by way of salary, rent, profits, fees, divid interest etc. A person gets income from many sources such as employment (salaries), prope (rent), business or profession (profits or fees), investments in shares (dividends), fixed dep (interest), etc. Income of any nature obtained from whatsoever source is liable to be taxed.

The following principles will help you to understand the general meaning and concept of incor

(1) **Periodical Return :** Income generally means, "that which comes in as the periodical produc one's work, business, lends, or investments" as per the Shorter Oxford Dictionary. Income den a periodical return "coming in" with some regularity from definite sources. Thus, income been compared to the fruit of a tree or the crop of a field. However, any non-periodical or cas income specifically included in the definition of income under the Act is taxable e.g. winnir from lotteries.

(2) **Illegal Income :** Income from illegal activities such as smuggling, black marketing too is taxab

(3) **In Cash or Kind :** Income may be received in cash or in kind, i.e. by way of a thing. Thus Doctor may receive, towards his fees, a car from a patient cured by him; the market value of car will be included in the Doctor's income.

(4) **Income Vs. Capital :** A receipt of money can be either income or capital. A receipt is taxed income : (a) if the receipt is included in the items listed in the definition of income u/s 2(24) the Act, or (b) if the receipt signifies income as generally understood. A capital receipt is n taxable. Income arises from a 'Source', or 'Resources' or 'Capital'. When a 'Source', 'Resourc or 'Capital' is sold or converted into money, it is capital receipt. However, any capital rece specifically included in the definition of income under the Act is taxable e.g. the profit on sale a capital asset, called "capital gains" or compensation for termination of employment or gifts the course of employment or business and so on. *A capital receipt is exempt unless specifica made taxable under the Act; and a revenue receipt is always taxable unless specifically exemp under the Act.* Following are the examples of capital receipts which are not taxable: amou received on maturity of life insurance policy, gift received, loan taken, refund of income-t bonus shares, subsidy received for setting up or expansion of plant, compensation received permanent disablement/death, award received by a non-professional (amateur) sportsman, gratia payment received from employer by the widow of an employee who dies while in serv

(5) **Real Income:** Income must be real and not imaginary. A person cannot earn income by trad with himself or from transferring his funds from one account to another. No income can aris a transfer of goods from Head office to a branch office even if the goods are invoiced at a pr higher than cost. Similarly, no income can arise on passing entries in the accounts on m revaluation of assets or on mere production or purchase of goods till the goods are actually s

(6) **Mutual Activity:** Income has to arise from an outside source. Thus a co-operative society (club) does not earn any income when it collects contributions from its members for comm expenses, as the amounts are not received from an outsider. The members who contribute money are the same members who obtain the common benefits and amenities. Such amou whose contributors and beneficiaries are the same, are known as receipts from "mutual activ which are not treated as income. However, profits of a mutual Insurance Company or a operative Bank, even from such 'mutual' activities are included in the definition of income to make them taxable.

8. ASSESSMENT [S.2(8)]
("How" is income and tax computed ?)

8.1 DEFINITION

Section 2(8) of the Income-tax Act defines this term as follows: *"assessment includes reassessment"*.

8.2 COMMENTS

This is an inclusive definition which indicates that the term assessment includes reassessment, in addition to its normal meaning. **Normally, an assessment means the process of determining and computing the amount of income and the tax due of a person.** The computation of income and tax is to be done in accordance with the provisions of the Income-tax Act.

8.3 PROCEDURE OF ASSESSMENT

The person having taxable income has to prepare a Statement of Income, called a *"Return of Income"*, giving the details of the income earned during the previous year. He has also to compute the tax due himself and voluntarily pay it before filing the Return of Income. The Income Tax Return is to be filed with the Income Tax Department. The *Assessing Officer* appointed under the Income-tax Act makes a scrutiny of such Income-tax Return and thereafter takes steps to make an 'assessment'. Such steps involve sending notices to the tax-payer, asking him to attend the Income-tax office with books of account etc. These steps are called *assessment proceedings*. Once the assessment proceedings are complete, the officer passes an *assessment order* showing the taxable income and the tax due. The assessed income/tax may be different from the figures shown in the Return filed by the tax-payer. This Assessment order fixes the liability of a person to pay the assessed amount of tax. A person from whom tax is due (or against whom assessment proceedings are pending) is called an assessee. **An "assessment" thus fixes the liability of the "assessee" to pay the "assessed" tax on the "assessed" income for the "assessment" year.**

An assessment once completed can also be re-opened under certain circumstances (e.g. tax evasion). Such re-opened assessment is called a re-assessment under the Act. The definition of "assessment" u/s 2(8) clarifies that such "re-assessment" will also be treated as "assessment" under the Act.

9. ASSESSEE [S. 2(7)]
("Who" is liable to pay the tax ?)

9.1 DEFINITION

(1) **Basic Meaning :** As per Section 2(7) of the Act, an *"assessee" means a person by whom any tax or any other sum of money is payable under the Act.* A person is liable to pay tax as well as interest (for late payment of tax) or penalty (for concealment of income, fraud etc.) under the Income-tax Act. Therefore, an assessee basically means a person liable to pay tax or interest or penalty.

(2) **Additional Meaning :** The definition further states that the term also includes the following persons:

(a) every person in respect of whom any *proceeding under the Act* has been taken *for the assessment of* -

(1) his income or the income of any other person in respect of whom he is assessable, or

(2) the loss sustained by him or such other person, or

(3) the refund due to him or such other person; or

(4) fringe benefits.

(b) every person who is *deemed to be an assessee* under the Act (e.g. a representative a trustee etc.)

(c) every person who is *deemed to be an assessee in default* under any provision of the an employer who fails to deduct tax at source from the salaries paid to the employ

(3) In Brief : Thus, an assessee means, in brief :

(a) a person by whom any tax, interest, penalty etc. is due.

(b) a person whose assessment of income, loss, refund or fringe benefits is pending.

(c) a deemed assessee.

(d) an assessee in default.

9.2 PERSON VS. ASSESSEE

Generally, the person who has earned the taxable income, is liable to pay the tax thereon (i.e the "assessee"). But, the term "assessee" is much wider in scope, since sometimes the tax-pay be different from the income-earner. Thus, a legal representative or a successor has to pay tax o income of a deceased person; the guardian has to pay tax on the income of his/her minor chi employer who has failed to deduct tax at source from the salaries of his employees, is liable the tax on the salaries, initially (later it can be recovered from the employees) and so on.

Illustration 4 : (Answer the following in brief)

Are the following persons assessees under the Income-tax Act ?

(1) Income of A is ₹ 40,000 (below the taxable limit). He has not filed his return of income. Inco tax department has not started any proceedings against him.

Ans.: No, as he does not fall under any of the categories mentioned in s. 2(7).

(2) Income of B is ₹ 2,60,000 (more than the taxable limit). He has not filed his return of inco Income-tax department has not started any proceedings against him.

Ans.: Yes, as tax is payable by him.

(3) Income of C is ₹ 20,000 (below the taxable limit). However, he has filed his return of inco Income-tax officer has sent a notice of hearing to him.

Ans.: Yes, as he is a person, in respect of whom, proceedings have been taken under the Ac

(4) Income of D is ₹ 40,000 (below the taxable limit). He has not filed his return of income. How he has failed to deduct tax at source on the interest paid to a lender.

Ans.: Yes, as he is an assessee-in-default.

10. CHARGE OF INCOME-TAX [S

10.1 PROVISION

Put simply, Section 4 of the Act states that -

(1) income-tax shall be charged,

(2) at the rate(s) laid down by the Finance Act,

(3) for that assessment year,

(4) in accordance with and subject to the provisions of this Act,

(5) in respect of the total income,

(6) of the previous year,

(7) of every person.

10.2 COMMENTS

S. 4 is called the "charging" section of the Act, because it fixes the charge or the liability of inc tax. The income-tax liability is determined in the following manner :

(1) Income-tax is an *annual tax* on income.

(2) The rates of income-tax are not specified in the Income-tax Act. The *rates of tax are laid d the Finance Act* passed by the parliament every year. The Finance Act is popularly know

"Budget". The Income-tax Act is a permanent Act, whereas While the liability to charge income-tax is imposed by the Income tax is determined by the Finance Act.

(3) The tax rates are laid down *for each assessment year* by the Finance Act.

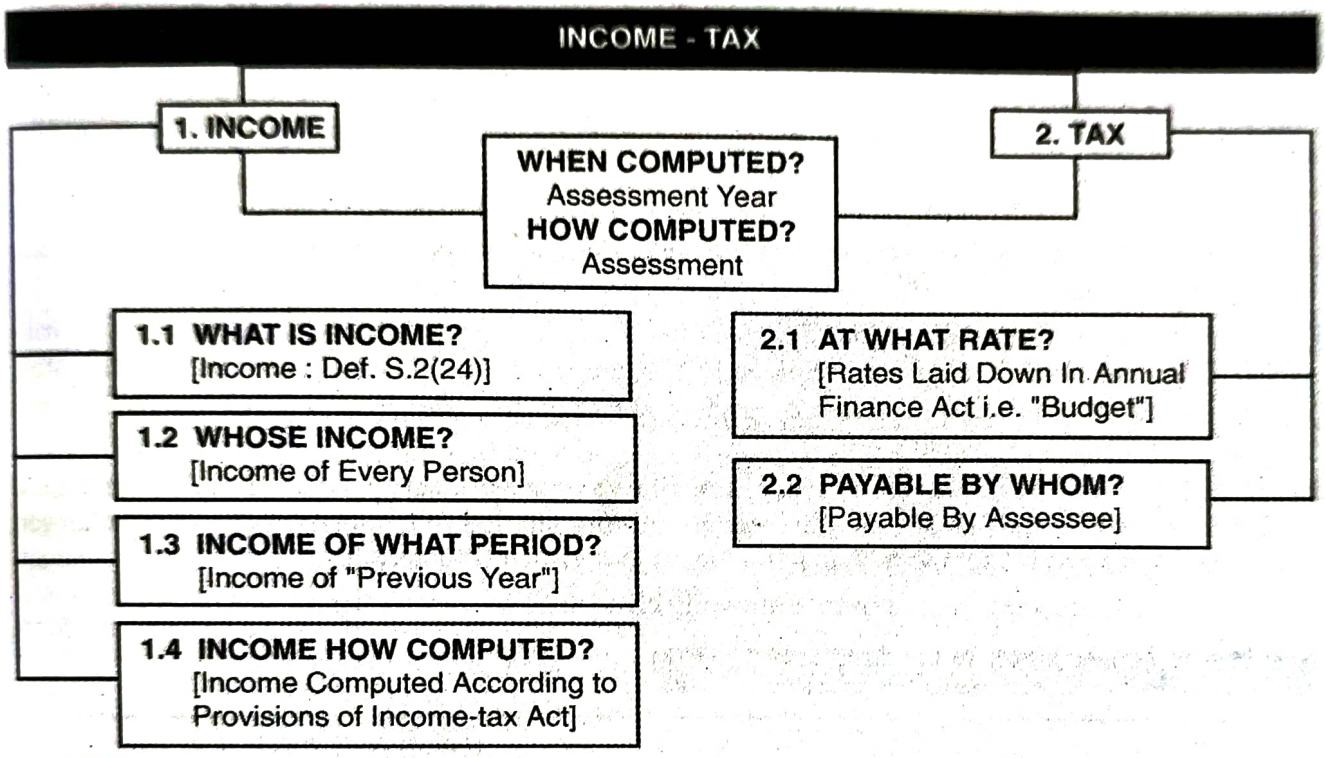
(4) *Total income of* one financial year (*previous year*) is charged to tax in the succeeding financial year (assessment year).

(5) The Total Income is to be *computed in accordance with the provisions of the Income-tax Act applicable for that assessment year*. Thus, for the current assessment year 2022-23, the provisions of the Act as on 1st April 2022 are to be taken into account. The process of determining the income and tax is known as assessment.

(6) The income earned by all types of persons (individual, firm, company etc.) is charged to tax. The person liable to pay the tax is known as the *assessee*.

The basis of charge of Income-tax is summed up in the exhibit below.

EXHIBIT 1 : CHARGE OF INCOME TAX



11. COMPUTATION OF INCOME

Let us take a quick survey of the steps involved in the assessment (computation) of income under the Act (see Exhibit 2 on next page).

(1) Determine Scope of Total Income : The "scope" of income means - what items are to be included in the income, and what items are to be excluded. The scope of income depends upon three factors - (a) whether the person earning the income is resident in India or not, (b) whether the income arises during the previous year and (c) whether the income arises in India or outside.

(a) Residence : What items are to be included in the income depends upon whether a person is a "resident" in India or not. A person is said to be "resident" in India, if, broadly speaking, he has stayed in India for the major part of the previous year (i.e. 6 months or more); otherwise he is called a "non-resident".

(b) Year : The income to be taxed must have arisen during the previous year only, i.e. neither before nor after the previous year.

(c) **Place** : What items are to be included in the taxable income of a person, depends, to whether the income is Indian or Foreign, i.e. arising within or outside India. Broadly, a Resident has to pay Income-tax on Indian as well as Foreign income, while a Non is liable to pay Income-tax only on the Indian income.

Thus, all these factors - residence, year and place of income - taken together determine of income. [This is explained in detail in Chapter 2].

(2) Exclude Exempt Income : The Act grants exemption from tax, on certain items of incom as agricultural income, or Leave Travel Allowance; or to certain persons such as Technicians, Foreign Teachers etc. Such exempted items are to be totally ignored and while computing the taxable income. [This is explained in detail in the concerned chapt

(3) Classify Income Under Different Heads : After determining what is to be included, th step is to classify the income under different "heads of income" prescribed under the A major heads of income are - Salary, Income from Property, Profits from Business, Capital and Income from Other Sources. [This is explained in detail in Chapter 3].

(4) Compute Income Under Each Head : The rules for computing income under each hea different. Such rules prescribe as to what is to be included under each head, what are the ded allowed under that head and so on. This is the most important step in the computation of inc [This is explained in detail in Chapter 4 to 8]. The Act grants exemption from tax, on c items of income, such as agricultural income, or Leave Travel Allowance; or to certain pe such as a Trust etc. Such exempted items are to be totally ignored and excluded while comp the taxable income.

(5) Determine Gross Total Income : Though income is classified and computed under diff heads, in the end, the income under all the heads is added together to arrive at the "Gross Income" of the assessee.

(6) Deduct Claims For Deductions : The Income-tax Act allows certain deductions from the G Total Income. Such deductions are given to encourage savings in National Savings Certific PPF, etc. Deductions are also given on income earned by a handicapped person etc. [Th explained in detail in Chapter 9].

(7) Compute Net Taxable Income : Net Taxable Income is equal to Gross Total Income L Deductions Allowed. This is the final step in the computation of income. Income-tax is charg on such net taxable income. [This is illustrated in detail in Chapter 10].

The above steps are summarised in the following chart :

EXHIBIT 2 : ASSESSMENT OF INCOME

Particulars	(Chapter)	Section	₹
1. DETERMINE SCOPE OF TOTAL INCOME			
1.1 Include Indian + Foreign Income of Resident	(2)	5	
1.2 Include Only Indian Income of Non-Resident			
2. DETERMINE RESIDENCE DURING PREVIOUS YEAR			
2.1 Resident In India	(2)	6	
2.2 Non-Resident			
3. CLASSIFY INCOME UNDER DIFFERENT HEADS			
4. COMPUTE INCOME UNDER EACH HEAD : (Exclude Income Exempt u/s 10)	(3)	14	
4.1 Salary	(4)	15-17	xxx
4.2 Income From House Property	(5)	22-27	xxx
4.3 Profits of Business or Profession	(6)	28-44AE	xxx
4.4 Capital Gains	(7)	45-54	xxx
4.5 Income from Other Sources	(8)	56-59	xxx
5. TOTAL INCOME = ADD INCOME UNDER ALL HEADS = GROSS TOTAL INCOME			

6.	**LESS : DEDUCTIONS**				
6.1	Savings		80[illegible]	[illegible]	
6.2	Contribution to Pension Fund		80E	[illegible]	
6.3	Medical Insurance Premium		80TTA	xxx	
6.4	Maintenance of Handicapped Dependent		80U	xxx	xxxx
6.5	Interest on Loan for Higher Education				
6.6	Interest on Saving Bank A/c				
6.7	Income of Handicapped Person				
7.	**NET TAXABLE INCOME (5 - 6)**	(10)			xxxx

12. RAPID REVISION

Assessment Year [S. 2(9)]: Period of 12 months commencing on 1st April every year.

Previous Year [S. 3] : (a) Financial Year immediately preceding the assessment year. (b) For new business/profession/source, period from date of setting up of new business etc. to immediately falling 31st March.

Person [S. 2(31)] : Individual, Hindu Undivided Family, Company, Firm, Association of Persons, Body of Individuals, Local Authority, Artificial Juridical Person.

Company [S. 2(17)] : (a) Indian Company (b) Body Assessed as Indian Company before 1-4-1970 and (c) Body declared by CBDT to be a Company.

Income [S. 2(24)] : (1) Profits (2) Dividends (3) Voluntary contributions (except towards corpus) received by trusts or specified institutions (4) Perquisites, allowances and benefits (received by employees, directors, persons with substantial interest, representative assessees, beneficiaries, or from business or profession) (5) Compensation received for termination of contract by a director or an agent (6) Profits taxable as income from business or other sources (e.g. bad debts recovered) (7) Profit on sale of import licence (8) Export cash assistance (9) Refund of customs/excise duty (10) Interest or remuneration to a partner from the firm (11) Capital gains (12) Profits from insurance (mutual or co-operative) (13) Windfall gains (14) Deductions by employers from salaries of employees towards P.F., Superannuation, E.S.I. (15) Receipt under Keyman Insurance policy. (16) Non-compete compensation (17) Gift exceeding ₹ 50,000 (18) excess consideration for shares (19) advance for asset forfeited (20) subsidy, grant or cash incentive.

Assessment [S. 2(8)] : (a) Definition : Includes reassessment. (b) General Meaning : Process of computing income and tax.

Assessee [S. 2(7)] : (a) a person by whom any tax, interest, penalty etc. is due, (b) a person whose assessment of income, loss, refund or fringe benefits is pending, (c) a deemed assessee and (d) an assessee in default.

EXERCISES

OUTLINE

No.	Topic	Page
13.	**Theory Questions**	14
13.1	Descriptive Questions [7 or 8 Marks]	14
13.2	Short Notes [5 Marks]	14
14.	**Objective Questions**	15
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14.2	Fill in the Blanks	17
14.3	Match the Following Columns	18
14.4	State Whether True or False	18
14.5	Check Your Answers	19

13. THEORY QUESTIONS [15 MARKS

13.1 DESCRIPTIVE QUESTIONS [7 OR 8 MARKS]

1. Define and explain the following terms : (a) Income (b) Person ***(April 15, 16; Nov. 16)*** (c) Compa (d) Assessment Year (e) Previous Year (f) Assessee.
   [Ans.: (a) Para 7 (b) Para 6 (c) Para 6 (d) Para 4 (e) Para 5 (f) Para
2. What do you mean by "Charge of Income Tax" ? ***[Ans.: Para 1***
3. Discuss the basic principles of charging income - tax. ***[Ans.: Para 1***
4. Define and explain the term "Assessment". ***[Ans.: Para***
5. Discuss the different aspects of tax liability such as : (a) What is liable to be taxed ? (b) Whc income is liable to be taxed ? (c) When is the tax liability computed ? (d) Income earned duri what period is liable to be taxed ? (e) Who is liable to pay the tax? (f) How is the income and ta computed?
   [Ans.: (a) Para 7 (b) Para 6 (c) Para 4 (d) Para 5 (e) Para 9 (f) Para 1
6. Discuss in brief the steps involved in assessment of income under the Income - Tax Act.
   [Ans.: Para 1
7. Explain the procedure of assessment. ***[Ans.: Para 8.***
8. Distinguish between "assessment year" and "previous year". ***[Ans.: Para 4 Vs. Para***
9. Distinguish between "person" and "assessee". ***[Ans.: Para 6 Vs. Para***
10. What are the different categories of persons according to their legal status ? Give an illustrati of each.
    [Ans.: Para 6 + Illustration
11. Define an Assessment Year. Explain its importance in computation of income and tax.
    [Ans.: Para
12. Discuss the statement "Section 4 of the Income - Tax Act, 1961 provides the basis of charge Income Tax". ***[Ans.: Para***

13.2 SHORT NOTES [5 MARKS]

Write a short note on :

1. Assessment year ***[Ans.: Para***
2. Person ***(Nov. 2017)*** ***[Ans.: Para***
3. Previous year ***[Ans.: Para***
4. Assessee ***(April 15, 17)*** ***[Ans.: Para***
5. Assessment ***[Ans.: Para***
6. Income ***[Ans.: Para***

14. OBJECTIVE QUESTIONS

14.1 MULTIPLE CHOICE QUESTIONS

1. Income-tax Act extends to
   (a) Whole of India (b) Whole of India except Jammu & Kashmir
   (c) Whole of Maharashtra only (d) None of these
2. Out of the following which is a revenue receipt ?
   (a) Premium received on issue of new shares
   (b) Annuity received from former employer
   (c) Interest from investments
   (d) None of these
3. A.O.P should consist of :
   (a) Individual only (b) Persons other than individual only
   (c) Both the above (d) None of these
4. Body of individual should consist of :
   (a) Individual only (b) Persons other than individual only
   (c) Both the above (d) None of these
5. A new business was set up on 15-11-2021 and it commenced its business from 1-12-2021. The first previous year in this case shall be :
   (a) 15-11-2021 to 31-3-2022 (b) 1-12-2021 to 31-3-2022
   (c) 2021-22 (d) None of these
6. Shivaji University is assessable under the Income Tax Act as
   (a) An individual (b) An artificial juridical person
   (c) A local authority (d) None of these
7. In which year is the income tax liability computed ?
   (a) Assessment Year (b) Previous Year
   (c) Financial Year (d) Calendar Year
8. Income earned during what period is taxed ?
   (a) Assessment Year (b) Previous Year
   (c) Financial Year (d) Calendar Year
9. Whose income is chargeable to income tax ?
   (a) Income of only Indian Citizens (b) Income of only residents
   (c) Income of all persons (d) Income of only assessees
10. One who is liable to pay the income tax in India -
    (a) Indian citizen (b) Resident in India
    (c) Any person (d) An assessee
11. Assessment year is the period of twelve months commencing on -
    (a) the first day of March every year
    (b) the first day of January every year
    (c) financial year immediately preceding the previous year
    (d) the first day of April every year
12. Previous year means the
    (a) financial year immediately after the assessment year
    (b) the period of twelve months commencing on the first day of April every year
    (c) financial year immediately preceding the assessment year
    (d) calendar year immediately preceding the assessment year
13. Mr. Joshi runs a chemist's shop, accounting year of which is the financial year. On November 9, 2021 he sets up a chemical factory. What is the previous year for the assessment year 2022-23 for the above two businesses.
    (a) 1-4-2021 to 31-3-2022 for both
    (b) 9-11-2021 to 31-3-2022 for both
    (c) 1-1-2021 to 31-12-2021 for both
    (d) Shop: 1-4-2021 to 31-3-2022; and Factory: 9-11-2021 to 31-3-2022

14. A Company joining with two other Companies in a joint venture is treated under Income tax as
(a) a company (b) an association of persons
(c) a body of individuals (d) an artificial juridical person

15. A Charitable Trust is treated under Income tax laws as
(a) a company (b) an association of persons
(c) a body of individuals (d) an artificial juridical person

16. A Club is treated under Income tax laws as
(a) a company (b) an association of persons
(c) a body of individuals (d) an artificial juridical person

17. A Co-operative Society is treated under Income tax laws as
(a) a company (b) an association of persons
(c) a body of individuals (d) an artificial juridical person

18. Life Insurance Corporation is treated under Income tax laws as
(a) a company (b) Local Authority
(c) a body of individuals (d) an artificial juridical person

19. Mumbai University is treated under Income tax laws as
(a) a company (b) an association of persons
(c) a body of individuals (d) an artificial juridical person

20. Indicate which of the following persons will not be taxed as an individual:
(a) X, a partner of a firm
(b) Y, a managing director of A Ltd.
(c) Z, a member of Z HUF
(d) M, Municipal Commissioner of Mumbai in respect of the Income of the Municipal Corp.

21. Provision of a motor car to the wife of the managing director by the company
(a) is exempt from tax
(b) is treated as perquisite in the hands of the managing director
(c) is treated as income of the company
(d) is treated as income of the wife of the managing director

22. Recovery of bad debt is
(a) allowed as deduction from gross income
(b) exempt from tax
(c) chargeable to tax as income from business
(d) chargeable to tax as capital gains

23. Gift from a patient to a doctor is
(a) allowed as deduction from gross income of the patient
(b) exempt from tax for the doctor
(c) chargeable to tax as income from business for the doctor
(d) chargeable to tax as income from other sources for the doctor

24. A capital receipt
(a) is always exempt
(b) is always taxable
(c) is always taxable unless specifically exempted under the Income tax Act
(d) is exempt unless specifically made taxable under the Income tax Act

25. A revenue receipt
(a) is never exempt
(b) is never taxable
(c) is always taxable unless specifically exempted under the Income tax Act
(d) is exempt unless specifically made taxable under the Income tax Act

26. When goods are transferred from Head Office to a branch at a price higher than cost
(a) the profit is treated as taxable income of head office
(b) the profit is treated as taxable income of branch office
(c) the invoice price is treated as taxable income of head office
(d) there is no taxable income

27. A person by whom any tax, interest, penalty etc. is due
    (a) a defaulter (b) a resident
    (c) a citizen (d) an assessee
28. The rates of income tax are laid down by
    (a) the Income tax Act
    (b) the Income tax Rules
    (c) the Finance Act, 1994
    (d) the Finance Act passed by the parliament every year
29. The rates of income tax are laid down
    (a) for each calendar year (b) for each assessment year
    (c) for each previous year (d) for each head of income
30. Total income
    (a) of one calendar year is charged to tax in the succeeding year
    (b) of one financial year is charged to tax in the succeeding calendar year
    (c) of one financial year is charged to tax in the succeeding financial year
    (d) of one financial year is charged to tax in the preceding financial year

14.2 FILL IN THE BLANKS

1. Previous year means the _____ year immediately preceding the assessment year.
2. The first previous year of a newly set up business can be _____ 12 months.
3. A period of twelve months commencing on the first day of April every year is called _____.
4. An assessment is defined under Income-tax Act to include _____ .
5. A person by whom any tax is payable under the act is known as an _____ .
6. The law governing income tax is specified in The Income-tax Act, _____ (1961 / 1962).
7. The rules for implementation of income tax are contained in Income-tax Rules, _____ (1961/1962).
8. Assessment year is defined in Section _____ [2(9) / 2(8)] of the Income-tax Act.
9. Previous year is defined in Section _____ [2 / 3 / 4] of the Income-tax Act.
10. Person is defined in Section _____ [2(31) / 2(24)] of the Income-tax Act.
11. Income is defined in Section _____ [2(8) / 2(24)] of the Income-tax Act.
12. Assessment is defined in Section _____ [2(8) / 2(9)] of the Income-tax Act.
13. Assessee is defined in Section _____ [2(7) / 2(8) / 2(9)] of the Income-tax Act.
14. Charge of income-tax is laid down in Section _____ [2 / 3 / 4] of the Income-tax Act.
15. The legal status under the Income Tax Act of Dhiren a minor son of Kishor, is _____.
16. The legal status under the Income Tax Act of Mukand Steel Ltd., is _____.
17. The legal status under the Income Tax Act of Mumbai University, is _____.
18. The legal status under the Income Tax Act of Safalya Co-op.Housing Society Ltd., is _____.
19. The legal status under the Income Tax Act of New India Bank Ltd., is _____.
20. The legal status under the Income Tax Act of Mumbai Port Trust, is _____.
21. The legal status under the Income Tax Act of Ms. Madhuri Dixit, is _____.
22. The legal status under the Income Tax Act of Baroda Municipal Corporation, is _____.
23. The legal status under the Income Tax Act of Mr. Matwala, a person of unsound mind, is _____.
24. The legal status under the Income Tax Act of A joint family of Mr. Sunil, his wife and two sons, is _____.
25. The legal status under the Income Tax Act of A joint venture between Mr. Contractor, Mr. Painter, and Mr. Cementwala for construction of Kalpataru Building, is _____.
26. The legal status under the Income Tax Act of Mr. Dharmaraja and his four brothers joining together to purchase a lottery ticket and sharing the prize, if any, equally, is _____.

14.3 MATCH THE FOLLOWING COLUMNS

1.

	Column A		Column B
1	Narayanan Murthy	(a)	Company
2	Infosys Technologies Ltd	(b)	Association of Persons
3	Solapur Gram panchayat	(c)	Firm
4	Andheri Sports Club	(d)	Individual
5	Karnataka University	(e)	Body of Individuals
		(f)	Artificial Juridical Person
		(g)	Local Authority

2.

	Column A		Column B
1.	Capital Gains	(a)	Assessment year 2023
2.	Financial year immediately preceding the assessment year	(b)	Income
3.	1-4-2022 to 31-3-2023	(c)	Assessee
4.	Hindu Undivided Family	(d)	Assessee in default
5.	Person with tax liability	(e)	Previous year
		(f)	Person
		(g)	Remittance

3.

	Column A Term		Column B Section of Income-tax Act
1.	Assessment year	(a)	2 (31)
2.	Previous year	(b)	4
3.	Person	(c)	2 (8)
4.	Income	(d)	2 (9)
5.	Assessment	(e)	2 (7)
6.	Assessee	(f)	2 (24)
7.	Charge of income-tax	(g)	3

4.

	Column A Person		Column B Legal Status
1.	Malvany Gram Panchayat	(a)	Association of persons
2.	Sunit Enterprises Private Limited	(b)	Local Authority
3.	M/S Universal Export Agency with two partners Mr. Manmohan Singh and Mr. Montek Singh	(c)	Individual
		(d)	Firm
		(e)	Company
4.	Akhil Bhartiya Mitra Mandal	(f)	Artificial Juridical Person
5.	Hindu idol		
6.	Mr. Shah, proprietor of United Trading Company		

14.4 STATE WHETHER TRUE OR FALSE

Discuss, giving reasons, whether the following statements are true or not :

1. Income means any receipt in cash.
2. A company under the Income - Tax Act means a company as defined under the Compa
3. Previous year always indicates a period of 12 months from 1st April to 31st March.
4. Assessee means a person liable to pay tax on his income.
5. On rendering some service to a garments manufacturing unit M is given a suit as remu It is not an "Income", since he has not received anything in cash.

6. On Sale of goods illegally imported from a foreign country the income is derived from an illegal activity, it is not charge
7. A birthday gift received by V from his father ₹ 20,000 is not taxable
8. Out of ₹ 29,000 per month received by Mrs. V from her husband for house saves approximately ₹ 1,200 per month which is deposited by her in a bank acco "Income" of Mrs. V.
9. Profit on Sale of a house property is capital receipt which is, however, chargeable to tax.
10. Salary, paid to M by his employer X Ltd. out of capital reserve, is not income in the hands of M.
11. Income earned by an assessee during the assessment year is charged to tax during the previous year.
12. Every person does not have to pay Income tax.
13. Gift received by a lawyer from his client is income as per Income Tax Act.
14. Gift received by son on his birthday from parents is income as per Income Tax Act.
15. Money received by dependant parents from their son is income as per Income Tax Act.
16. Income received from smuggling activity is income as per Income Tax Act.
17. Reimbursement of actual travelling expenses to an employee is income as per Income Tax Act.
18. Arrears of bonus, received in lump sum by an employee is income as per Income Tax Act.
19. Extra sales money received on account of devaluation of currency is income as per Income Tax Act.
20. Man of the Match Prize received by a professional sportsman is income as per Income Tax Act.
21. Compensation for death of father in a car accident received from the car owner by the son of the deceased is income as per Income Tax Act.
22. Free tickets for air travel by Air India received by Mr. Vadera who had rented his premises to Air India, in lieu of rent, as per the terms of rent agreement is income as per Income Tax Act.

14.5 CHECK YOUR ANSWERS

14.1

1.	(a)	6.	(b)	11.	(d)	16.	(b)	21.	(b)	26.	(d)
2.	(c)	7.	(a)	12.	(c)	17.	(b)	22.	(c)	27.	(d)
3.	(c)	8.	(b)	13.	(d)	18.	(d)	23.	(c)	28.	(d)
4.	(a)	9.	(c)	14.	(b)	19.	(d)	24.	(d)	29.	(b)
5.	(a)	10.	(d)	15.	(b)	20.	(d)	25.	(c)	30.	(c)

14.2 (1) Financial (2) Less than (3) Assessment year (4) Reassessment (5) Assessee (6) 1961 (7) 1962 (8) 2(9) (9) 3 (10) 2(31) (11) 2(24) (12) 2(8) (13) 2(7) (14) 4 (15) Individual (16) Company (17) Artificial Juridical Person (18) Association of Persons (AOP) (19) Company (20) Local Authority (21) Individual (22) Local Authority (23) Individual (24) Hindu Undivided Family (HUF) (25) Body of Individuals (BOI) (26) Body of Individuals (BOI)

14.3 **(1) :** (1) - (d), (2) - (a), (3) - (g), (4) - (b), (5) - (f)
(2) : (1) - (b), (2) - (e), (3) - (a), (4) - (f), (5) - (c)
(3) : (1) - (d), (2) - (g), (3) - (a), (4) - (f), (5) - (c), (6) - (e), (7) - (b)
(4) : (1) - (b), (2) - (e), (3) - (d), (4) - (a), (5) - (f), (6) - (c)

14.4 **True :** 7, 9, 12, 13, 16, 18, 19, 20, 22
False : 1, 2, 3, 4, 5, 6, 8, 10, 11, 14, 15, 17, 21