UNIT III
COMPUTATION OF INCOME UNDER DIFFERENT HEADS-2

1. What do you understand by the term business and profession as used u/s 28 of the Income Tax Act? What is the Basis of Charge or what are the charging provisions u/s 28 under the head Profits and Gains of Business or Profession.

Ans. Business: “Business” simply means any economic activity carried on for earning profits. Sec. 2(13) has defined the term as “any trade, commerce, manufacturing activity or any adventure or concern in the nature of trade, commerce and manufacture”.
In this connection it is not necessary that there should be a series of transactions in a business and also it should be carried on permanently. Neither repetition nor continuity of similar transactions is necessary.

Profession: As per section 2(36), profession includes vocation or a job requiring some thought, skill and special knowledge like that of C.A., Lawyer, Doctor, Engineer, Architect etc. So, profession refers to those activities where the livelihood is earned by the persons through their intellectual or manual skill.

Basis of Charge or Charging Provision [Section 28]

The following income shall be chargeable to income-tax under the head “Profits and gains of business or profession”,—

(i) The profits and gains of any business or profession which was carried on by the assessee at any time during the previous year; [Section 28(i)]

(ii) any compensation or other payment due to or received by,—any person, by whatever name called, managing the whole or substantially the whole of the affairs of an Indian company, at or in connection with the termination of his management or the modification of the terms and conditions relating thereto; [Section 28(ii)]

(iii) Income derived by a trade, professional or similar association from specific services performed for its members; [Section 28(iii)]

(iv) The value of any perquisite or benefit arising from business or profession, whether convertible into money or not; [Section 28(iv)]

(v) Any interest, commission, salary, remuneration, or bonus due to, or received by, a partner of a firm from such firm; [Section 28(v)]

(vi) Any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy. [Section 28(vi)]

(vii) Income from speculative transactions.

(viii) Any sum, whether received or receivable, in cash or kind, under an agreement for—
(a) not carrying out any activity in relation to any business; or
(b) not sharing any know-how, patent, copyright, trade-mark, licence, franchise or any other business or commercial right of similar nature. [Section 28(va)]

(ix) Any profit on the transfer of the Duty-Free Replenishment Certificate

(x) Any profit on the transfer of the Duty Entitlement Pass Book Scheme

(xi) Profits on sale of a license granted under the Imports (Control) Order, 1955, made under the Imports and Exports (Control) Act, 1947 (18 of 1947)

2. Name the incomes from trading or business which are not taxable under section 28 under the head "Profits and gains of business or profession".

Ans. In the following cases, income from trading or business is not taxable under section 28, under the head "Profits and gains of business or profession":

(i) Rental income in the case of Dealer in Property: Rent of house property is taxable under section 22 under the head "Income from house property", even if property constitutes stock-in-trade of recipient of rent or the recipient of rent is engaged in the business of letting properties on rent.

(ii) Dividend on Shares in the case of a Dealer-in-Shares: Dividends on shares are taxable under section 56(2) (i), under the head "Income from case of a dealer-in-shares other sources", even if they are derived from shares held as stock-in-trade or the recipient of dividends is a dealer-in-shares. Dividend received from an Indian company is not chargeable to tax in the hands of shareholders.

(iii) Winnings from Lotteries, etc: Winnings from lotteries, races, etc., are taxable under the head "Income from other sources" etc. (even if derived as a regular business activity).

3. Define capital gain. Discuss the procedure for computation of capital gain as prescribed by the Income Tax Act 1961.

Ans. Section 45 of Income Tax Act, 1961 provides that any profits or gains arising from the transfer of a capital asset effected in the previous year will be chargeable to income-tax under the head 'Capital Gains'. Such capital gains will be deemed to be the income of the previous year in which the transfer took place.

Method of Computing Capital Gain [Section 48]:

Capital gains are of two types:

(i) Short-term capital gain which arises on the transfer of a short-term capital asset; and

(ii) Long-term capital gain which arises on the transfer of a long-term capital asset.

A format to compute the capital gain is given below:

Computation of Short-Term Capital Gain:

Full Value of Consideration	—	
Less : (a) Expenditure incurred wholly and exclusively in connection with such a Transfer,	—	
(b) Cost of acquisition	—	
(c) Cost of improvement	—	—
Gross short-term capital gains	—	
Less: Exemption, if available, u/s 54B/54D154G/S4GA	—	

Taxable Short-term capital gains.	—	

Computation of Long-Term Capital Gain:

Full value of consideration	—	
Less: (a) Expenditure incurred wholly and exclusively in connection with such a transfer	—	
(b) Indexed Cost of acquisition	—	
(c) Indexed Cost of improvement	—	—
bLong-term capital gains	—	
Less: Exemption if available u/s 54/54B/54D/54EC/54EFJ/54F/54G/54GA/ 54GB		—
Taxable long-term capital gains	—	

4. What is Capital Asset? Name and explain the different types of capital assets.

Ans. As per Section 2(14) of the IT Act, 1961 it is defined as property of any kind held by an assessee whether or not connected with his business or profession, but not including:

(i) Any stock-in-trade and raw materials held for the purposes of his business or profession;

(ii) Personal effects, i.e. to say, movable property (including wearing apparel and furniture, but excluding jewellery, archaeological collections, drawings, paintings, sculptures and any work of art) held for personal use by the assessee or any member of his family dependant on him;

(iii) Agricultural land in India not being situated within the jurisdiction of a municipality or within 8 km. of a municipality as may be notified;

(iv) Gold bonds;

(v) Special Bearer Bonds, 1991; and

(vi) Gold Deposit Bonds.

The most important item that should be noted in this regard is "personal effects" like silver utensils, wearing apparel, etc. which are not treated as capital assets.

Capital assets are of two types:

(i) Long-term capital assets.
(ii) Short-term capital assets.

(i) Short-Term Capital Asset - STCA [Section 2(42A)]: A capital asset held by an assessee for **not more than 36 months** immediately preceding the date of its transfer is known as a short-term capital asset.
Exceptions:

(1) The following assets shall be treated as short-term capital assets if they are held for **not more than 12 months (instead of 36 months mentioned above)** immediately preceding the date of its transfer:

(a) A security including shares (other than unit) listed in a recognised stock exchange in India

(b) A unit of an equity-oriented fund

(c) A zero-coupon bond

(2) The following assets shall be treated as short-term capital assets if they are held for **not more than 24 months (instead of 36 months/12 months mentioned above)** immediately preceding the date of its transfer:

(a) Share of a company (not being a share listed in a recognised stock exchange in India)

(b) An immovable property being land and building or both.

(ii) Long-Term Capital Asset - LTCA [Section 2(29A)]: It means a capital asset which is not a short- term capital asset.
In other words, if the asset is held by the assessee for more than 36 months/24 months/12 months, as the case may be, such an asset will be treated as a long-term capital asset

5. What is meant by cost of acquisition? What are the rules given for the determination of cost of acquisition?

Ans. Cost of Acquisition (COA) means any capital expense at the time of acquiring capital asset under transfer, i.e., to include the purchase price, expenses incurred up to acquiring date in the form of registration, storage etc. expenses incurred on completing transfer.

There are different rules to determine the cost of acquisition. They are:

(a) Assets acquired without paying any price: In case asset is received by way of transfer, under partition of H.U.F., under gift of will, under succession or inheritance on dissolution of firm, on liquidation company under revocable or irrevocable trust or by a parent company to subsidiary company-the cost will be the cost at which assets were acquired by previous owner plus cost of any improvement less depreciation, if any. [Section 49(1)].

(b) Shares of amalgamated company: The cost of shares of amalgamated company shall be the cost of acquisition of shares of amalgamating company. [Section 49(2)].

(c) Depreciating assets: Calculate S.T.C. Gain or Loss as per section 50.

(d) Advance money to be adjusted out of cost of acquisition. (Section 51).

(e) Cost is unascertainable: Fair market value as on the date of acquisition to be taken as cost of acquisition. [Section (56)3]. O Option of FMV on 1-4-2001. If an assessee had opted for F.M.V. on 1-4 2001, it will be cost of acquisition for all purposes. [Section (55)2].

(g) Cost of Shares: Cost of new shares received on amalgamation of companies, on transfer of shares into stock or vice versa or transfer of lower denomination shares into higher denomination shares or vice versa; the cost of acquisition will be the cost at which original shares were acquired. [Section 56(2)(v)].

(h) Cost of Bonus Shares and on renunciation of right shares: with effect from1-4-95 it is to be taken as NIL.

(i) Cost of acquisition of capital asset in case of conversion of inventory into capital asset shall be FMV on the date of conversion.

6. What is meant by cost of improvement?

Ans. Cost of improvement is the capital expenditure incurred by an assessee for making any addition or improvement in the capital asset. It also includes any expenditure incurred in protecting or curing the title. In other words, cost of improvement includes all those expenditures, which are incurred to increase the value of the capital asset. However, any expenditure which is deductible in computing the income under the heads Income from House Property, Profits and Gains from Business or Profession or Income from Other Sources (Interest on Securities) would not be taken as cost of improvement.

7. Mention any ten exempted capital

gain. Ans. Exempted Capital Gains

The exemptions of capital gain can broadly be classified into two broad categories:

A. Exempted Capital Gains u/s 10

B. Exempted Capital Gains u/s 54

A. Exempted Capital Gains u/s 10:

1. Income from sale of shares in certain cases [Section 10(36)]

2. Any income from long term capital asset being self-cultivated urban agricultural land on compulsory acquisition [Section 10(37)]

3. Long Term Capital Gain on transfer of securities covered under Securities Transaction Tax [Section 10(38)

4. Income from transfer of asset of an undertaking engaged in the business of generation, transmission or distribution of power Section 10(40)]

B. Exempted Capital Gains u/s 54

5. Sale of residential House Property (asset is long-term) [Section 54]: That part of capital gain of individual and H.U.F. from sale of such house property which is long-term capital asset, is exempted which is invested in

(i) purchase of another house within one year before or two years after the sale.

(ii) construction of another house within 3 years after the sale.

6. Sale of Self-cultivated agricultural land(urban) [Section 54B]: That part of capital gain from the sale of such land is tax-free which in reinvested in purchase of another piece of land within 2 years after sale. [Available to individual or HUF (HUF w.e.f. A.Y. 2013-14)]

7. Compulsory acquisition of Capital assets [Section 54D): That part of capital gain arising from compulsory acquisition of land, building or any right is such asset used by assessee for 2 years for his own business, shall be tax-free which is reinvested in purchase of another land or building or right in land or building within 3 years of the acquisition. The new asset so acquired cannot be sold or transferred for a period of 3 years, otherwise old exempted gain will be put to tax.

8. Sale of long term capital asset of land or building or both [Section 54EC): Investment of long term capital gain from sale of land or building or both within 6 months from date of sale in Bonds issued by the National Highway Authority of India or by National Rural Electrification Corporation Ltd. or bonds issued by Power Finance Corporation Ltd. or any other notified bonds. Amount of gain so invested shall be exempted. The new bonds so acquired cannot be sold or transferred or pledged for 5 years. Exemption u/s 54EC shall be restricted upto Rs. 50 lakhs on investments made on or after 1-4-2007.

9. Exemption of capital gain on investment in units of specified fund. [Insertion of Section 54EEJ [W.e.f. A.Y. 2017-18]: Any capital gain shall be exempt from tax if the capital gains proceeds are invested by an assessee in units of specified fund, as may be notified by the Central Government in this behalf. The newly acquired units cannot be sold or transferred or pledged for 3 years from the date of acquisition, otherwise old exempted capital gain shall be chargeable to tax. Exemption u/s 54EE in respect of any one or more original asset transferred shall be restricted up to 50 lakhs in any financial year.

10. Sale of any long-term capital assets [Section 54F): Where a long-term asset is transferred and sale price is reinvested in construction or purchase of a residential within three years or one year before or two years after sale, respectively, so much of capital gain shall be exempted as is in proportion of amount invested to net consideration. No exemption if assessee owns another house or acquires another house in one year before or two years after or constructs another house in three years.

8. Mention the different kinds of incomes as chargeable to tax under the head Income from other sources.

Ans. **Incomes which are charged to tax under the head 'Income from other sources'**

'Income from other sources' is the residual head of income. Hence, any income which is not specifically taxed under any other head of income will be taxed under this head.

Further, there are certain incomes which are always taxed under this head. These incomes are as follows:

(i) As per section 56(2)(i), dividends are always taxed under this head. As per Section 115BBDA, Dividend received from Domestic Companies upto Rs 10 Lacs will be exempt from Tax and then any amount received above 10 lacs will be tax at 10%.

(ii) Winnings from lotteries, crossword puzzles, races including horse races, card game and other game of any sort, gambling or betting of any form whatsoever, are always taxed under this head.

(iii) Income by way of interest received on compensation or on enhanced compensation shall be chargeable to tax under the head "Income from other sources", and such income shall be deemed to be the income of the year in which it is received, irrespective of the method of accounting followed.

(iv) Gifts received by an individual or HUF (which are chargeable to tax) are also taxed under this head.

(v) In addition to above, following incomes are charged to tax under this head, if not taxed under the head "Profits and gains of business or profession".

(a) Any contribution to a fund for welfare of employees received by the [Section 56(2)(ic)].

(b) Income by way of interest on securities. [Section 56(2)(id)].

(c) Income from letting out or hiring of plant, machinery or furniture. [Section 56(2)(ii)].

(d) Income from letting out of plant, machinery or furniture along with building; both the lettings are inseparable. [Section 56(2)(iii)].

(e) Any sum received under a Keyman Insurance Policy including bonus. [Section 56(2) (iv)].

9. Write a note tax treatment of Gifts received by Individual & HUF

Ans. Gifts received by Individual & HUF: 56(2)(x) is applicable only when gifts are received by Individual and HUF. Donor or Donee may be Resident or non-Resident.

1. Cash: If aggregate value is less than Rs.50000 than nothing will be taxable. If value exceeds Rs. 50,000, the whole amount will be taxable.

2. Movable Property as Gift:

a) Without consideration: Where any person receives, in any previous year, from any person or persons any property other than immovable property without consideration, the aggregate fair market value of which exceeds fifty thousand rupees, the whole of the aggregate fair market value of such property will be taxable in the hands of receiver.

b) For Inadequate Consideration: Where any person receives, in any previous year, from any person or persons any property other than immovable property for a consideration which is less than the aggregate fair market value of the property by an amount exceeding fifty thousand rupees, the aggregate fair market value of such property as exceeds such consideration.

The excess differential amount will be taxable in the hands of receiver.

3. Immovable Property as Gift:

a) Without Consideration: Where any person receives, in any previous year, from any person or persons any immovable property without consideration and the stamp duty value of which exceeds fifty thousand rupees then in such case, the stamp duty value of such property will be taxable in the hands of receiver.

b) For Inadequate Consideration: Where any person receives, in any previous year, from any person or persons any immovable property for a consideration, the stamp duty value of such property as exceeds such consideration, if the amount of such excess is more than the higher of the following amounts:

(i) the amount of fifty thousand rupees; and

(ii) the amount equal to five per cent of the consideration

The excess differential amount will be taxable in the hands of receiver.

4. Some Exempt gifts: If any gifts are received in following situations or from below mentioned people then those gifts will be fully exempt under Income Tax. Any sum of money or any property received:

(i) from any relative; or
(ii) on the occasion of the marriage of the individual; or
(iii) under a will or by way of inheritance; or
(iv) in contemplation of death of the payer or donor or
(v) from any local authority or
(vi) from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in clause (23C) of section 10; or
(vii) from or by any trust or institution registered under section 12A or section 12AA; or
(viii) by any fund or trust or institution or any university or other educational institution or any hospital or other medical institution or
(ix) from an individual by a trust created or established solely for the benefit of relative of the individual.
(x) any compensation or other payment, due to or received by any person, by whatever name called, in connection with the termination of his employment or the modification of the terms and conditions relating thereto.

10. Explain the deductions allowable in computing income from other sources.
Ans. The taxable income under the head 'income from Other Sources' shall be computed after allowing the following deductions as provided in section 57:

(i) In case of Dividends and Interest on Securities. From the dividend income, a deduction shall be allowed in respect of any sum spent by way of commission or remuneration to a banker or any other person as collection charges for realising the dividend or Interest on Securities.

(ii) Repairs, depreciation, etc. in case of letting of machinery, plant or furniture with or without building: The following deductions shall be allowed from the income earned by letting of machinery, plant or furniture with or without building.

(a) Expenditure incurred on current repairs of plant, machinery, furniture or building.

(b) Insurance premium paid regarding these assets.

(c) Depreciation on plant, machinery and furniture. Depreciation in respect of buildings will be allowed only if the assessee is the owner. It will not be allowed if the assessee is lessee or mortgagee in possession of the building.

(iii) Deduction in respect of employee's contribution in staff welfare schemes [57 (ia)]: Any amount received by employer from his employees as their contribution of provident fund, E.S.I. Fund or superannuation fund is deemed as income u/s 59(ic) if not taxable under the head "profits and gains of business or profession".

In case employer deposits any amount (out of these incomes) in these funds before prescribed due date, such amount is allowed as deduction u/s 57 (ia).

(iv) Standard Deduction out of Family Pension (Section 57 (iia)]: In case of income in the nature of family pension, a deduction of a sum equal to $33\frac{1}{3}\%$ of such pension or * 15,000 whichever is less, shall be allowed.

Family pension means a regular monthly amount payable by employer to the legal heirs of deceased employee.

(v) Deduction from any other income (Section 57(iii)]: Any expenditure which is spent to earn an income changeable to tax under this head shall be deducted from such income.

(vi) Deduction from royalties received by authors (Other than those writing for films)- Actual expenses can be claimed as deduction.

(vii) Deduction regarding interest on compensation or enhanced compensation: In case assessee has received any income of this type, a deduction of a sum equal to 50% of such income shall be allowed and no deduction shall be allowed under other clause of this section.

11. Mention the Expenses not allowed as deductions while computing income chargeable to tax under the head Income from other sources

Ans. Under section 58, following expenditures are not deductible while computing income chargeable to tax under the head "Income from other sources":

(i) Personal expenditure [Section 58(1)(a)(i)].
(ii) Any interest chargeable under the Act which is payable outside India on which tax has not been paid or deducted at source [Section 58(1)(a)(ii)].
(iii) Any amount paid which is taxable under the head "Salaries" and payable outside India on which tax has not been paid or deducted at source [Section 58(1) (a) (iii)].
(iv) Sum paid on account of wealth-tax is not deductible under section 58(1A).
(v) Amount specified under section 40A is not deductible [Section 58(2)].