CHAPTER 6. DISALLOWANCES

AS PER SEC 40A(1) THE FOLLOWING DISALLOWANCES SHALL BE MADE NOTWITHSTANDING ANYTHING CONTAINED IN ANY OTHER PROVISION OF THE INCOME-TAX ACT:

SECTION 40A(2): PAYMENTS TO SPECIFIED PERSONS NOT DEDUCTIBLE UNDER CERTAIN CIRCUMSTANCES

Sub-section (2) of section 40A provides that where the assessee incurs any expenditure in respect of which a payment has been or is to be made to a specified person (See column (2) of Table below) so much of the expenditure as is considered to be excessive or unreasonable shall be disallowed by the Assessing Officer. While doing so he shall have due regard to:

(a) the fair market value of the goods, service of facilities for which the payment is made; or
(b) the legitimate needs of the business or profession carried on by the assessee; or
(c) the benefit derived by or accruing to the assessee from such a payment.

<table>
<thead>
<tr>
<th>Assessee</th>
<th>Specified Person</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual</td>
<td>1. Any relative of the individual assessee</td>
</tr>
<tr>
<td></td>
<td>2. Any person who carries on a business or profession, if</td>
</tr>
<tr>
<td></td>
<td>• the individual has a substantial interest in the business of that person or</td>
</tr>
<tr>
<td></td>
<td>• any relative of the individual has a substantial interest in the business of that person</td>
</tr>
<tr>
<td>Company, Firm, HUF or AOP</td>
<td>1. Any director, partner of the firm or member of the family or association or any relative of such director, partner or member or</td>
</tr>
<tr>
<td></td>
<td>2. Any person who carries on a business or profession, in which the Company/Firm/HUF/AOP or director of the company, partner of the firm or member of the family or association or any relative of such director, partner or member has substantial interest</td>
</tr>
<tr>
<td>All assessees</td>
<td>The following are specified persons:</td>
</tr>
<tr>
<td></td>
<td>Person who has substantial interest in the assessee’s business</td>
</tr>
<tr>
<td></td>
<td>Other related persons of such person, who has a substantial interest in the assessee’s business</td>
</tr>
<tr>
<td></td>
<td>Any individual</td>
</tr>
<tr>
<td></td>
<td>• Any relative of such individual</td>
</tr>
<tr>
<td></td>
<td>Company / AOP / Firm / HUF</td>
</tr>
<tr>
<td></td>
<td>• Any director of such company, partner of such firm or the member of such family or association or</td>
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</table>

6.1
Relative in relation to an Individual means the spouse, brother or sister or any lineal ascendant or descendant of that individual [Section 2(41)].

Substantial interest in a business or profession
A person shall be deemed to have a substantial interest in a business or profession if -
- in a case where the business or profession is carried on by a company, such person is, at any time during the previous year, the beneficial owner of equity shares carrying not less than 20% of the voting power and
- in any other case, such person is, at any time during the previous year, beneficially entitled to not less than 20% of the profits of such business or profession.

SECTION 40A(3) & (3A): PAYMENTS MADE OTHERWISE THAN BY ACCOUNT PAYEE CHEQUE OR ACCOUNT PAYEE BANK DRAFT OR OTHER MODE
According to section 40A(3), where the assessee incurs any expenditure, in respect of which payment or aggregate of payments made to a person in a day otherwise than by an account payee cheque drawn on a bank or by an account payee bank draft or use of electronic system through bank account or such other electronic mode as may be prescribed exceeds Rs. 10,000, such expenditure shall not be allowed as a deduction.

(Underlined and bold words are amended by Finance Act (No.2) 2019)

The provision applies to all categories of expenditure involving payments for goods or services which are deductible in computing the taxable income.

Example:
If, in respect of an expenditure of Rs. 32,000 incurred by X Ltd., 4 cash payments of Rs. 8,000 are made on a particular day to one Mr. Y – one in the morning at 10 a.m., one at 12 noon, one at 3 p.m. and one at 6 p.m., the entire expenditure of Rs. 32,000 would be disallowed under section 40A(3), since the aggregate of cash payments made during a day to Mr. Y exceeds Rs. 10,000.
Cash Payment made in excess of Rs. **10,000** deemed to be the income of the subsequent year, if an expenditure has been allowed as deduction in any previous year on due basis:

In case of an assessee following mercantile system of accounting, if an expenditure has been allowed as deduction in any previous year on due basis, and payment has been made in a subsequent year otherwise than by account payee cheque or account payee bank draft or use of electronic clearing system through a bank account or such other electronic mode as may be prescribed, then the payment so made shall be deemed to be the income of the subsequent year if such payment or aggregate of payments made to a person in a day exceeds **Rs. 10,000** [Section 40A(3A)].

(Underlined and bold words are amended by Finance Act (No.2) 2019)

Rule 6ABBA:

The following shall be the other electronic modes for the purposes of clause (d) of first proviso to section 13A, clause (f) of sub-section (8) of section 35AD, sub-section (3), sub-section (3A), proviso to sub-section (3A) and sub-section (4) of section 40A, second proviso to clause (1) of Section 43, sub-section (4) of section 43CA, proviso to sub-section (1) of section 44AD, second proviso to sub-section (1) of section 50C, second proviso to sub-clause (b) of clause (x) of sub-section (2) of section 56, clause (b) of first proviso of clause (i) of Explanation to section 80JJAA, section 269SS, section 269ST and section 269T, namely:-

(a) Credit Card;
(b) Debit Card;
(c) Net Banking;
(d) IMPS (Immediate Payment Service);
(e) UPI (Unified Payment Interface);
(f) RTGS (Real Time Gross Settlement);
(g) NEFT (National Electronic Funds Transfer); and
(h) BHIM (Bharat Interface for Money) Aadhar Pay;

Increase in limit of cash payment, where payment made to transport operator:

This limit of **Rs. 10,000** has been raised to **Rs. 35,000** in case of payment made to transport operators for plying, hiring or leasing goods carriages. Therefore, payment or aggregate of payments up to **Rs. 35,000** in a day can be made to a transport operator otherwise than by way of account payee cheque or account payee bank draft or use of electronic clearing system through a bank account or such other electronic mode as may be prescribed. In all other cases, the limit would continue to be **Rs. 10,000**.

(Underlined and bold words are amended by Finance Act (No.2) 2019)
Cases and circumstances in which a payment or aggregate of payments exceeding ten thousand rupees may be made to a person in a day, otherwise than by an account payee cheque/ account payee bank draft/ use of ECS through a bank account [Rule 6DD]:

As per this rule, no disallowance under section 40A(3) shall be made and no payment shall be deemed to be the profits and gains of business or profession under section 40A(3A) where a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or account payee bank draft or use of electronic clearing system through a bank account or such other electronic mode as may be prescribed, exceeds ten thousand rupees in the cases and circumstances specified hereunder, namely:

(i) **Loan transactions:** It does not apply to loan transactions because advancing of loans or repayments of the principal amount of loan does not constitute an expenditure deductible in computing the taxable income. However, interest payments of amounts exceeding Rs.10,000 at a time are required to be made by account payee cheques or drafts or electronic clearing system or such other electronic mode as may be prescribed, as interest is a deductible expenditure.

(ii) **Payment made by commission agents:** This requirement does not apply to payment made by commission agents for goods received by them for sale on commission or consignment basis because such a payment is not an expenditure deductible in computing the taxable income of the commission agent. For the same reason, this requirement does not apply to advance payment made by the commission agent to the party concerned against supply of goods. However, where commission agent purchases goods on his own account but not on commission basis, the requirement will apply. The provisions regarding payments by account payee cheque or draft or electronic clearing system or such other electronic mode as may be prescribed, apply equally to payments made for goods purchased on credit.

Cases and circumstances in which a payment or aggregate of payments exceeding ten thousand rupees may be made to a person in a day, otherwise than by an account payee cheque [Rule 6DD]:

As per this rule, no disallowance under section 40A(3) shall be made and no payment shall be deemed to be the profits and gains of business or profession under section 40A(3A) where a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or account payee bank draft or use of electronic clearing system through a bank account or such other electronic mode as may be prescribed, exceeds ten thousand rupees in the cases and circumstances specified hereunder, namely:

(a) where the payment is made to
   (i) the Reserve Bank of India or any banking company;
   (ii) the State Bank of India or any subsidiary bank;
   (iii) any co-operative bank or land mortgage bank;
   (iv) any primary agricultural credit society or any primary credit society;
   (v) the Life Insurance Corporation of India;
(b) where the payment is made to the Government and, under the rules framed by it, such payment is required to be made in legal tender;
(c) where the payment is made by
   (i) any letter of credit arrangements through a bank;
   (ii) a mail or telegraphic transfer through a bank;
   (iii) a book adjustment from any account in a bank to any other account in that or any other bank;
   (iv) a bill of exchange made payable only to a bank;
   (v) a credit card;
   (vi) a debit card.

(d) where the payment is made by way of adjustment against the amount of any liability incurred by the payee for any goods supplied or services rendered by the assessee to such payee;

(e) where the payment is made for the purchase of -
   (i) agricultural or forest produce; or
   (ii) the produce of animal husbandry (including livestock, meat, hides and skins) or dairy or poultry farming; or
   (iii) fish or fish products; or
   (iv) the products of horticulture or apiculture,
   to the cultivator, grower or producer of such articles, produce or products;

   **Note -**
   (i) The expression ‘fish or fish products’ (iii) above would include ‘other marine products such as shrimp, prawn, cuttlefish, squid, crab, lobster etc.’.
   (ii) The ‘producers’ of fish or fish products for the purpose of Rule 6DD(e) would include, besides the fishermen, any headman of fishermen, who sorts the catch of fish brought by fishermen from the sea, at the sea shore itself and then sells the fish or fish products to traders, exporters etc.

However, the above exception will not be available on the payment for the purchase of fish or fish products from a person who is not proved to be a ‘producer’ of these goods and is only a trader, broker or any other middleman, by whatever name called.

(f) where the payment is made for the purchase of the products manufactured or processed without the aid of power in a cottage industry, to the producer of such products;

(g) where the payment is made in a village or town, which on the date of such payment is not served by any bank, to any person who ordinarily resides, or is carrying on any business, profession or vocation, in any such village or town;

(h) where any payment is made to an employee of the assessee or the heir of any such employee, on or in connection with the retirement, retrenchment, resignation, discharge or death of such employee, on account of gratuity, retrenchment compensation or similar terminal benefit and the aggregate of such sums payable to the employee or his heir does not exceed fifty thousand rupees;

(i) where the payment is made by an assessee by way of salary to his employee after deducting the income-tax from salary in accordance with the provisions of section 192 of the Act, and when such employee -
   (i) is temporarily posted for a continuous period of fifteen days or more in a place other than his normal place of duty or on a ship; and
   (ii) does not maintain any account in any bank at such place or ship;

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(j) where the payment was required to be made on a day on which the banks were closed either on account of holiday or strike;
(k) where the payment is made by any person to his agent who is required to make payment in cash for goods or services on behalf of such person;
(l) where the payment is made by an authorised dealer or a money changer against purchase of foreign currency or travelers cheques in the normal course of his business.

**SECTION 40A(7): EMPLOYER'S CONTRIBUTION TO GRATUITY FUND**

No deduction shall be allowed in respect of any provision made by the assessee for the payment of gratuity to his employees on their retirement or termination of employment.

(Refer Compendium for example)

**SECTION 40A(9): EMPLOYER'S CONTRIBUTION TO UNAPPROVED GRATUITY FUND, UNRECOGNIZED PROVIDENT FUND OR UNAPPROVED SUPERANNUATION FUND IS DISALLOWED**

No deduction shall be allowed in respect of any sum paid by the assessee as an employer towards setting up or formation of, or as contribution to, any fund, trust, company, association of persons, body of individuals, society or any institution except where such sum is required to be paid under any law in force or where such sum is paid for an approved gratuity fund, recognised provident fund or approved superannuation fund or pension scheme referred to in section 80CCD.

**AMOUNT SPECIFICALLY NOT DEDUCTIBLE UNDER SECTION 40**

**NOTWITHSTANDING ANYTHING CONTAINED IN SECTION 30 TO 38, NO DEDUCTION SHALL BE ALLOWED IN RESPECT OF THE FOLLOWING:**

**SECTION 40(a)(i): NON-COMPLIANCE OF PROVISIONS OF TDS WHERE PAYMENT IS MADE TO NON-RESIDENT**

Any interest, royalty, fees for technical services or other sum chargeable under this Act, which is payable, -

(a) outside India;
(b) in India to a non-resident, not being a company or to a foreign company, on which tax is deductible at source under Chapter XVIIB and such tax has not been deducted or, after deduction, has not been paid on or before the due date of filing of return specified under section 139(1).

It is also provided that where in respect of any such sum, where tax has been deducted in any subsequent year, or has been deducted in the previous year but paid after the due date of filing of return under section 139(1), such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.

*Provided further that where an assessee fails to deduct the whole or any part of the tax in accordance with the provisions of Chapter XVII-B on any such sum but is not deemed to be an assessee in default under the first proviso to section 201(1), then, for the purpose of*
this sub-clause, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the Non Resident payee referred to in the said proviso.

(Added by Finance Act (No. 2), 2019)

<table>
<thead>
<tr>
<th>Date on which TDS should have been deducted</th>
<th>Actual Date of Deduction</th>
<th>Time limit as per section 200(1)for depositing TDS</th>
<th>Date of payment of TDS</th>
<th>Previous year in which deductible</th>
</tr>
</thead>
<tbody>
<tr>
<td>26.06.2020</td>
<td>26.06.2020</td>
<td>07.07.2020</td>
<td>31.03.2021</td>
<td>2020-21</td>
</tr>
<tr>
<td>31.03.2021</td>
<td>31.03.2021</td>
<td>30.04.2021</td>
<td>30.06.2021</td>
<td>2020-21</td>
</tr>
<tr>
<td>16.05.2020</td>
<td>16.05.2020</td>
<td>07.06.2020</td>
<td>Not deposited</td>
<td>Not deductible</td>
</tr>
</tbody>
</table>

Clarification regarding disallowance of ‘other sum chargeable’ under section 40(a)(i) [Circular No. 3/2015, dated 12-02-2015]

If there has been a failure in deduction or in payment of tax deducted in respect of any interest, royalty, fees for technical services or other sum chargeable under the Act either payable in India to non-corporate non-resident or a foreign company or payable outside India, then, disallowance of the related expenditure/ payment is attracted under section 40(a)(i) while computing income chargeable under the head “Profits and gains of business or profession”.

The interpretation of the term ‘other sum chargeable’ in section 195 has been clarified in this circular i.e. whether this term refers to the whole sum being remitted or only the portion representing the sum chargeable to income-tax under the Act.

In its Instruction No. 2/2014, dated 26.02.2014, the CBDT has clarified that the Assessing Officer shall determine the appropriate portion of the sum chargeable to tax as mentioned in section 195(1), to ascertain the tax liability on which the deductor shall be deemed to be an assessee in default under section 201, in cases where no application is filed by the deductor for determining the sum so chargeable under section 195(2).

In this circular, the CBDT has, in exercise of its powers under section 119, clarified that for the purpose of making disallowance of ‘other sum chargeable’ under section 40(a)(i), the appropriate portion of the sum which is chargeable to tax shall form the basis of disallowance. Further, the appropriate portion shall be the same as determined by the Assessing Officer having jurisdiction for the purpose of section 195(1). Also, where the determination of ‘other sum chargeable’ has been made under sub-section (2), (3) or (7) of section 195 of the Act, such a determination will form the basis for disallowance, if any, under section 40(a)(i).
SECTION 40(a)(ia): NON-COMPLIANCE OF PROVISION OF TDS WHERE PAYMENT IS MADE TO A RESIDENT

Section 40(a)(ia) provides that 30% of any sum payable to a resident, on which tax is deductible at source under Chapter XVII-B, shall be disallowed if –

(i) such tax has not been deducted; or

(ii) such tax, after deduction, has not been paid on or before the due date specified in section 139(1).

If in respect of such sum, tax has been deducted in any subsequent year or has been deducted during the previous year but paid after the due date specified in section 139(1), 30% of such sum shall be allowed as deduction in computing the income of the previous year in which such tax has been paid.

For instance, tax on royalty paid to Mr. A, a resident, has been deducted during the previous year 2020-21, the same has to be paid by 31st July/ 30th September 2021, as the case may be. Otherwise, 30% of such royalty would be disallowed in computing the income for A.Y. 2021-22. If in respect of such royalty, tax deducted during the P.Y.2020-21 has been paid after 31st July/ 30th September 2021, 30% of such royalty would be allowed as deduction in the year of payment.

Provided further that where an assessee fails to deduct the whole or any part of the tax in accordance with the provisions of Chapter XVII-B on any such sum but is not deemed to be an assessee in default under the first proviso to section 201(1), then, for the purpose of this sub-clause, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the resident payee referred to in the said proviso.

(Second Proviso added by Finance Act, 2012)

ANALYSIS OF AMENDMENT IN SECTION 40(a)(ia) BY FINANCE ACT, 2012 AND IN SECTION 40(a)(i) BY FINANCE ACT (NO. 2) 2019:

1. Section 201(1) provides that if an assessee:
   (a) fails to deduct TDS; or
   (b) after deduction, fails to pay the TDS, then he shall be deemed to be an assessee in default under section 220 & 221. Consequently, he is liable to pay:
      (i) Penalty under section 221 which can be up to the amount of TDS not deducted/not paid.
      (ii) Interest under section 220 @ 1% p.m. from the date the tax was deductible / payable till the date of passing of an order under section 201.

2. It is well established law laid down by various courts that the deductor shall be treated as an assessee in default only if:
   • Deductor has failed to deduct TDS; and
   • Deductee has also failed to pay the tax directly.

Therefore, deductor cannot be treated as an assessee in default where deductor has failed to deduct TDS but deductee has paid the tax directly.

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The Finance Act, 2012/2019 seeks to incorporate the above provisions in section 201(1) by inserting Proviso in section 201(1).

3. The amendments are for resident or Non resident deductee.

4. The amendment to section 201(1) i.e. First proviso to section 201(1) provides as under:
   - If the deductor fails to deduct the whole or any part of tax in accordance with the Chapter of TDS.
   - on the sum paid to a resident or Non resident; or
   - on the sum credited to the account of a resident or Non resident,
   - then such deductor shall not be deemed to be an assessee in default in respect of such TDS if:
     • the resident or Non resident payee has furnished his return of income under section 139.
     • the resident or Non resident payee has taken into account such sum for computing income in such return of income; and
     • the resident or Non resident payee has paid the tax due on income declared by him in such return of income.

The deductor has to furnish a certificate to this effect from a Chartered Accountant in the prescribed form. (Rule 31ACB and Form 26A)

5. The amendment also provides that deductor shall have to pay interest under section 201(1A) @ 1% per month or part of the month from the date the tax was so deductible to the date of furnishing of return of income by the resident or Non resident payee. The interest shall be levied on the amount of TDS not deducted / short deducted by the deductor.

6. Section 40(a)(ia)/ 40(a)(i) has been amended by Finance Act, 2012/2019 to provide that:
   - where assessee has failed to deduct TDS in accordance with Chapter of TDS
   - and he is not treated as an assessee in default under the first proviso to section 201(1)
   - then, for the purpose of section 40(a)(ia) /40(a)(i)
   - it shall be deemed that the assessee has deducted and paid the tax on such sum
   - on the date of furnishing of return of income by the resident or Non Resident payee
   - and deduction of such expenditure shall be allowed accordingly.

**ILLUSTRATON**

A company A Ltd. whose due date of filing of return is 30th September pays the following sums without deduction of TDS:

(i) Rs 2,00,000 to Mr. X, a resident, as rent (Due date of filing of return for Mr. X is 31st July)

(ii) Rs 5,00,000 to Y Ltd., a resident company, as professional fees (Due date of filing of return for Y Ltd. is 30th Nov.)

The above sums were paid on 1st July, 2020 without deduction of TDS.
For previous year 31.03.2021, X and Y Ltd have included the above sums in their respective return of income and have paid tax thereon. Returns have been filed by X and Y Ltd. on 31st August, 2021 and 30th Nov, 2021 respectively.

Company A Ltd has taken certificate from Chartered Accountant to the above effect. Now following are the consequences:

(i) Company A Ltd. shall not be treated as an assessee in default for payment of Rs. 2,00,000 made to Mr. X without deducting TDS. Company A Ltd. shall pay interest @ 1% p.m. from 1st July, 2020 to 31st August, 2021 on TDS of Rs. 20,000. The expenditure of Rs. 2,00,000 shall be allowed to company A Ltd. in previous years 31.03.2021 as per provision of section 40(a)(ia).

(ii) Company A Ltd. shall not be treated as an assessee in default for payment of Rs. 5,00,000 to Y Ltd. without deducting TDS. Company A Ltd shall pay interest @ 1% p.m. from 1st July, 2020 to 30th Nov, 2021 on TDS of Rs. 50,000. 30% of expenditure of Rs. 5,00,000 shall be allowed to Company A Ltd. in previous year 31.03.2022 as per provisions of section 40(a)(ia). 30% of the said expenditure shall be disallowed in previous 31.03.2021 since deduction and payment of TDS is deemed to be made on 30.11.2021 i.e. after the due date 30.09.2021 of company A Ltd.

Whether section 40(a)(ia) is attracted when amount is not ‘payable’ to a sub-contractor but has been actually paid?

**PALAM GAS SERVICE V. CIT [2017] (SC)**

**Facts of the case:** The assessee, Palam Gas Service, is engaged in the business of purchase and sale of LPG cylinders. The assessee had arranged for the transportation to be done through three sub-contractors within the meaning of section 194C. During the relevant assessment year, when the assessee made freight payments of Rs.20,97,689 to the sub-contractors, it did not deduct tax at source. The Assessing Officer disallowed the freight expenses as per section 40(a)(ia) on account of failure to deduct tax. The assessee contended that section 40(a)(ia) did not apply as the amount was not ‘payable’ but had been actually paid.

**Issue:** Whether the provisions of Section 40(a)(ia) would be attracted when the amount is not 'payable' to a sub-contractor but has been actually paid? Would the obligation to deduct tax depend on the method of accounting followed by an assessee?

**Supreme Court’s Observations:** The Supreme Court noted the difference in opinion amongst the various High Courts. On the one hand, the High Courts of Punjab & Haryana, Madras, Calcutta and Gujarat held that Section 40(a)(ia) extended to amounts actually paid. The Allahabad High Court had, however, held otherwise. The Supreme Court agreed with the observations of the majority High Courts and held that section 40(a)(ia) covers not only those cases where the amount is payable but also when it is paid. Accordingly, the judgment of the Allahabad High Court in CIT v. Vector Shipping Services (P.) Ltd. [2013] 357 ITR 642 stands overruled.

The Supreme Court reaffirmed that the obligation to deduct tax at source is mandatory and applicable irrespective of the method of accounting adopted. If the assessee follows the mercantile system of accounting, then, the moment amount was credited to the
account of the payee on accrual of liability, tax was required to be deducted at source. If the assessee follows cash system of accounting, then, tax is required to be deducted at source at the time of making payment.

**Supreme Court’s Decision:** The Supreme Court, accordingly, upheld the decision of the majority High Courts that section 40(a)(ia) would be attracted for failure to deduct tax in both cases i.e., when the amount is payable or when the amount is paid, as the case may be, depending on the system of accounting followed by the assessee.

### SECTION 40(a)(ii): INCOME TAX

1. Income-tax payable under Income-tax Act is not deductible. Even the income-tax paid under the tax laws of a foreign country is not allowable as deduction. For such tax, relief can be claimed under section 90 or section 90A or section 91, as the case may be.
2. Service tax is allowable as deduction under section 37(1), subject to section 43B.

### SECTION 40(a)(iia): WEALTH TAX

Any sum paid on account of wealth tax chargeable under the Wealth tax Act, 1957 or similar statute outside India.

**KEY POINT:**

Valuation fees paid for valuation of assets does not represent wealth tax and is allowable as deduction.

### SECTION 40(a)(iib): FEE OR CHARGES PAID BY STATE GOVERNMENT UNDERTAKING

Any amount—

(A) paid by way of royalty, licence fee, service fee, privilege fee, service charge or any other fee or charge, by whatever name called, which is levied exclusively on; or

(B) which is appropriated, directly or indirectly, from,

a State Government undertaking by the State Government.

**ANALYSIS**

State Government undertakings are liable to Income Tax. If they pay dividends to the State Government then, such dividend is not deductible as an expense and such dividend is also liable to Dividend Distribution Tax. State Governments instead of taking dividends, started taking out money from these undertakings in form of royalty, licence fee, service fee, privilege fee, service charge or any other fee or charge, which were exclusive levies on such undertakings. This was done so that such payments were allowed as deduction and State Government gets the money without any payment of dividend distribution tax by such undertakings.

In order to levy tax on such withdrawals by State Governments from such undertakings, the amendment has been bought by Finance Act, 2013, wherein any exclusive payments in form of royalty, licence fee, service fee, privilege fee, service charge or any other fee or charge to State Government by such undertakings has been specifically disallowed.
It may be noted that disallowance will be attracted if:

(i) Levy is by State Government. No disallowance shall be attracted if levy is by Central Government.

(ii) It should be exclusive on the State Government undertakings. If levy is non-exclusive, i.e., applicable to others also, disallowance shall not be attracted.

**SECTION 40(a)(iii): TDS ON SALARY PAYABLE OUTSIDE INDIA OR TO A NON-RESIDENT**

Any sum which is chargeable under the head ‘Salaries’ if it is payable outside India or to a non-resident and if the tax has not been paid thereon nor deducted therefrom under Chapter XVII-B.

**SECTION 40(a)(iv): EMPLOYER’S CONTRIBUTION TOWARDS PROVIDENT FUND OR ANY OTHER FUND**

Any payment to a provident fund or other fund established for the benefit of employees of the assessee, unless the assessee has made effective arrangements to secure that the tax shall be deducted at source from any payments made from the fund which are chargeable to tax under the head "Salaries". (*To be discussed later)*

**SECTION 40(a)(v): PAYMENT OF TAX ON BEHALF OF EMPLOYEE**

In case of an employee, deriving income in the nature of perquisites (other than monetary payments), the amount of tax on such income paid by his employer is exempt from tax in the hands of that employee.

Correspondingly, such payment is not allowed as deduction from the income of the employer. Thus, the payment of tax on perquisites by an employer on behalf of employee will be exempt from tax in the hands of employee but will not be allowable as deduction in the hands of the employer.

**SECTION 43B: CERTAIN DEDUCTIONS ALLOWED ON ACTUAL PAYMENT**

Notwithstanding anything contained in any other provisions of the Income Tax Act, a deduction otherwise allowable under the Act in respect of:

(a) any sum payable by the assessee by way of *tax, duty, cess or fee*, by whatever name called, under any law for the time being in force, or

(b) any sum payable by the assessee as an *employer by way of contribution* to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of the employees, or *(To be discussed later)*

(c) any *bonus or commission* payable to the employees, or

(d) any sum payable by the assessee as *interest on any loan or borrowing from any public financial institution* or a State Financial Corporation or a State Industrial Investment Corporation, in accordance with the terms and conditions of the agreement governing such loan or borrowing, or

(da) any sum payable by the assessee as *interest on any loan or borrowing from a deposit taking NBFC or systematically important non-deposit taking NBFC*, in accordance with the terms and conditions of the agreement governing such loan or borrowing, or *(See Note Below)*
(e) any sum payable by the assessee as interest on any LOAN OR ADVANCE from a scheduled bank in accordance with the terms and conditions of the agreement governing such loan or advance. {"Scheduled bank" includes a cooperative bank}.

(f) any sum payable by the assessee as an employer in lieu of any leave to the credit of his employee, (i.e. provision for leave encashment)

(g) any sum payable by the assesse to the Indian Railways for the use of railway assets.

shall be allowed as deduction only in the previous year in which such sum is actually paid by him. This is irrespective of the previous year in which the liability to pay such sum was incurred by the assessee according to the method of accounting employed by him.

Systemically important non-deposit taking NBFC – It means a non-banking financial company (NBFC) which is not accepting or holding public deposits and is having total assets of not less than Rs. 500 crores as per the last audited balance sheet and is registered with RBI under the provisions of the Reserve Bank of India Act.

Deposit taking NBFC - “Deposit taking NBFC” means a non-banking financial company which is accepting or holding public deposits and is registered with RBI under the provisions of the Reserve Bank of India Act.

Further where deduction i.r.o of clause (da) is already claimed on accrual basis till PY 2018-2019, then no deduction shall be allowed on actual payment if paid in PY 2019-2020 or subsequent years. {Explanation 3AA to Sec 43B}

KEY POINTS:

1. The provisions of section 43B shall not apply in relation to any sum which is actually paid by the assessee on or before the due date applicable in his case for furnishing the return of income under section 139(1) in respect of the previous year in which liability to pay such sum was incurred by the assessee.

2. Conversion of interest into a loan or borrowing or advance or payable in other manner

   Explanation 3C, 3CA & 3D clarifies that if any sum payable by the assessee as interest on any such loan or borrowing or advance referred to in (d), (da) and (e) above, is converted into a loan or borrowing or advance, the interest so converted and not “actually paid” shall not be deemed as actual payment, and hence would not be allowed as deduction. The clarificatory explanations only reiterate the rationale that conversion of interest into a loan or borrowing or advance does not amount to actual payment.

   The manner in which the converted interest will be allowed as deduction has been clarified in Circular No.7/2006 dated 17.7.2006. The unpaid interest, whenever actually paid to the bank or financial institution, will be in the nature of revenue expenditure deserving deduction in the computation of income. Therefore, irrespective of the nomenclature, the deduction will be allowed in the previous year in which the converted interest is actually paid.
Illustration:

**Case I: INCLUSIVE ACCOUNTING:**
Following entries have been made in the books of account of the assessee:

1. Bank A/c Dr. 2,00,000
   To Sales 2,00,000

2. Sales Tax Dr. 10,000
   To Sales Tax Payable 10,000

<table>
<thead>
<tr>
<th>Profit and Loss Account</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales Tax</td>
</tr>
<tr>
<td>Net Profit</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>

Assume that sales tax payable has not been paid till due date of filing of return of income.

**Computation of Total Income**

Net Profit as per P&L A/c 1,90,000
Add: Sales Tax disallowed u/s 43B 10,000

**Total Income** 2,00,000

**Case II: EXCLUSIVE ACCOUNTING**

If in the above case, following entry is passed in the books of account of the assessee:

<table>
<thead>
<tr>
<th>Account</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank A/c</td>
<td>2,00,000</td>
</tr>
<tr>
<td>To Sales</td>
<td>1,90,000</td>
</tr>
<tr>
<td>To Sales Tax Payable</td>
<td>10,000</td>
</tr>
</tbody>
</table>

- As per Supreme Court in **CHOWRINGEE SALES BUREAU**, sales tax should be routed through Profit and Loss Account. It is the duty of the Assessing Officer to route sales tax through Profit and Loss Account.

**Therefore, Computation of Total Income in Case II:**

<table>
<thead>
<tr>
<th>Account</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Profit as per P&amp;L A/c</td>
<td>1,90,000</td>
</tr>
<tr>
<td>Add: Sales Tax disallowed u/s 43B</td>
<td>10,000</td>
</tr>
<tr>
<td><strong>Total Income</strong></td>
<td>2,00,000</td>
</tr>
</tbody>
</table>
CONTRARY DECISIONS OF SEVERAL HIGH COURT’S

COMMISSIONER OF INCOME-TAX VS. AIMIL LTD. (DELHI HIGH COURT)

Employees' contribution towards provident fund and ESI would qualify for deduction even if paid after due date prescribed under Provident Fund Act/ESI Act but before due date of filing of return.

Delhi High Court held that section 2(24) enumerates different components of income. It, inter alia, stipulates that income includes any sum received by the assessee from his employees as contributions to any provident fund or superannuation fund or any fund set up under the provisions of the Employees' State Insurance Act, 1948, or any other fund for the welfare of such employees. It is clear from the above that as soon as employees' contribution towards provident fund or ESI is received by the assessee-employer by way of deduction or otherwise from the salary/wages of the employees, it will be treated as 'income' at the hands of the assessee. It clearly follows therefrom that if the assessee does not deposit this contribution with provident fund/ESI authorities, it will be taxed as income in the hands of the assessee. However, on making deposit with the concerned authorities, the assessee becomes entitled to deduction under the provisions of section 36(1)(va). Section 43B(b), however, stipulates that such deduction would be permissible only on actual payment. This is the scheme of the Act for making an assessee entitled to get deduction from income insofar as employees' contribution is concerned.

If the employees' contribution is not deposited by the due date prescribed under the relevant Acts and is deposited late, the employer not only pays interest on delayed payment but can incur penalties also, for which specific provisions are made in the Provident Fund Act as well as in the ESI Act. Therefore, the Act permits the employer to make the deposit with some delay, subject to the aforesaid consequences. Insofar as the Income-tax Act is concerned, the assessee can get the benefit if the actual payment is made before due date of filing of return under section 139(1).

CIT V. KICHHA SUGAR CO. LTD. (UTTARAKHAND)

Can the amount of employees' contribution towards provident fund, deducted and credited to the employee's PF account by the employer- assessee after the "due date" under the EPF & Miscellaneous Provisions Act, 1952, but before the due date of filing return of income under the Income-tax Act, 1961, be allowed as deduction while computing business income of the employer-assessee?

The High Court observed that the "due date" referred to in section 36(1)(va) must be read in conjunction with the "due date" referred to in the first proviso to section 43B. A combined reading of both the sections would make it clear that the due date referred to in section 36(1)(va) is the due date as mentioned in section 43B i.e., the due date of filing of return of income.

Therefore, any amount of employees' contribution paid by the employer-assessee to the provident fund authorities after the due date under the Employees Provident Fund & Miscellaneous Provisions Act, 1952 (EPF & MP Act) but before the due date of filing the return for the previous year, shall be allowable as deduction in the hands of the employer-assessee.

ALTERNATE VIEW:

Can employees contribution to Provident Fund and Employee’s State Insurance be allowed as deduction where the assessee-employer had not remitted the same on or before the “due date” under the relevant Act but remitted the same on or before the due date for filing of return of income under section 139(1)?
Facts of the case: The assessee collected employees’ contribution to Provident Fund and ESI which were remitted, after the due date under the relevant Acts but before the ‘due date’ for filing the return specified in section 139(1). The assessing authority held that the amount collected by way of employees’ contribution to PF and ESI are income under section 2(24)(x) and their remittance is governed by section 36(1)(va). The time limit prescribed for remitting the contribution is the ‘due date’ prescribed under the Provident Funds Act, Employees’ State Insurance Act, rule, order or notification issued thereunder or under any standing order, award, contract or service or otherwise.

Issue: The issue under consideration is whether extended time limit upto the due date of filing the return contained in section 43B would be available in respect of remittances which are governed by section 36(1)(va).

High Court’s Observations: The High Court noted that section 43B(b) pertaining to employer’s contribution cannot be applied with respect to employees’ contribution which is governed by section 36(1)(va). So far as the employee’s contribution is concerned, the Explanation to section 36(1)(va) continues to remain in the statute and there is no provision for applying the extended time limit provided under section 43B for remittance of employee’s contribution. The amount of employee’s contribution to PF and ESI is an income upon recovery from salary and its remittance within the ‘due date’ as specified in Explanation to section 36(1)(va) makes it eligible for deduction. Employees’ contribution recovered by the employer is not eligible for extended time limit upto the due date of filing of return, which is available under section 43B in the case of employer’s own contribution.

High Court’s Decision: The High Court, accordingly, held that the delayed remittance of employees’ contribution beyond the ‘due date’ prescribed in section 36(1)(va), is not deductible while computing the business income, even though such remittance has been made before the due date of filing of return of income under section 139(1).

Note: A contrary view was expressed by Uttrakhand High Court in the case of CIT v. Kichha Sugar Co. Ltd. (2013) 356 ITR 351 holding that the employees' contribution to provident fund, deducted from the salaries of the employees of the assessee, shall be allowed as deduction from the income of the employer-assessee, if the same is deposited by the employer-assessee with the provident fund authority on or before the due date of filing the return for the relevant previous year.
CHAPTER 7. RECOVERY OF EXPENDITURE & REMISSION AND CESSION OF TRADING LIABILITY

SEE COMPENDIUM FOR THE DISCUSSION

KEY POINT:
"Successor in business" means -

(i) Where there has been an amalgamation of a company with another company, the amalgamated company.
(ii) Where a firm carrying on business or profession is succeeded by another firm, the other firm.
(iii) Where the first mentioned person is succeeded by any other person in the business or profession, the other person.
(iv) Where there has been a demerger, the resulting company.

1. **SECTION 41(1) APPLIES TO TRADING LIABILITIES ONLY**
The assessee took a personal loan from Mr. A of Rs. 1,00,000. Subsequently the assessee and Mr. A decided that the loan need not be repaid and therefore the assessee wrote off the loan to the credit of profit and loss account. Held that section 41(1) is attracted when there is a remission or cessation of trading liability. In the present case, the loan is not a trading liability and therefore section 41(1) is not attracted. Section 56(2)(vii) shall be attracted if assessee is an individual or HUF and the loan so waived shall be taxable in his hands as Income from other sources.

However, Supreme Court in the case of T.V. Sundaram Iyengar & Sons held that where the assessee transfers unclaimed advances from the trade parties to Profit & Loss Account, then the assessee has become richer by the amount transferred to Profit & Loss Account. The said amount is not taxable under section 41(1) but shall be taxable under section 28. Supreme Court held that such amounts though not allowed as deduction earlier and transferred to Profit & Loss Account would constitute trading receipts taxable under section 28. Therefore, on the basis of this Supreme Court judgement if trade advances are written off to the credit of Profit & Loss account, then although section 41(1) is not attracted but the said sum shall be taxable under section 28.

2. **POLYFLEX INDIA (P) LTD. v. CIT (SC)**
The assessee company paid excise duty on certain goods in the year 1986 and was allowed as deduction. The assessee challenged the levy of excise duty and the High Court on 01.01.2008 decided in favour of the assessee and held that excise duty was not payable by it. The excise duty was refunded to the assessee on 20.01.2008. The Department filed a SLP in Supreme Court against the order of High Court and the SLP was still pending in Supreme Court. The Assessing Officer invoked section 41(1) in Assessment Year 2008-09 and taxed the excise duty refunded in Assessment Year 2008-09. The assessee contended that there was no remission/ cessation of trading liability within the meaning of section 41(1) so long as the issue was pending determination by Supreme Court.

7.1
Section 41(1) is attracted if in the assessment of any year an allowance or deduction has been made in respect of any loss, expenditure or trading liability and subsequently the assessee:

(i) has obtained any amount in respect of such loss or expenditure, or
(ii) obtained any benefit in respect of such trading liability by way of remission or cessation thereof.

If either of the above two happens, the deeming section 41(1) comes into play. The Supreme Court held that no doubt the remission or cessation of trading liability takes place only if the matter is not pending in any litigation and has been finally decided in favour of the assessee. If the matter of remission/cessation of liability is pending before any Court, then it will not amount to remission or cessation of trading liability.

The Supreme Court held that in the present case, the question was not of remission or cessation of the trading liability since there was no trading liability as the assessee has already paid the excise duty. As per Supreme court, in the present case the first part of section 41(1) is attracted namely:

(iii) has obtained any amount in respect of such loss or expenditure

As per Supreme Court, section 41(1) is a deeming fiction and it comes into play as soon as assessee receives any amount in respect of such loss or expenditure. It is irrelevant that such receipt has been disputed by the Department in future appeal. The deeming fiction of section 41(1) comes into play as soon as the amount is received and therefore in the present case, the Assessing Officer was justified in invoking section 41(1) in Assessment Year 2008-09.

3. **ROLLATAINERS LTD. V. CIT (DEL)**
   Can the provisions of section 41(1) be invoked both in respect of waiver of working capital loan utilized for day-to-day business operations and in respect of waiver of term loan taken for purchasing a capital asset?

The provisions of section 41(1) are attracted in respect of waiver of the working capital loan utilized for day-to-day business operations, since it amounted to remission of a trading liability. However, in the case of waiver of term loan for purchasing capital assets, the provisions of section 41(1) are not attracted since it cannot be treated as remission or cessation of a trading liability.

4. **CIT V. SOFTWORKS COMPUTERS P. LTD. (BOM.)**
   Can waiver of loan or advance taken for the purpose of relocation of office premises be treated as a revenue receipt liable to tax?

The Bombay High Court held that since the advance taken by the assessee-company was utilized by it for the purpose of relocating its office premises i.e., for acquisition of a capital asset, namely, a new office, the waiver of the same cannot be said to be waiver or remission of trading liability to attract taxability under the Act. **Waiver of such advance, being capital in nature, is not taxable under the Act.**

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Recovery of Expenditure & Remission and Cessation of Trading Liability AJ Education NeXt

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CHAPTER 8. MISCELLANEOUS ISSUES

SECTION 14A: EXPENDITURE INCURRED IN RELATION TO INCOME NOT INCLUDIBLE IN TOTAL INCOME

(1) For the purposes of computing the total income under Chapter IV (i.e. the five heads of income), no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to income which does not form part of total income under the Income-tax Act.

(2) The Assessing Officer shall determine the amount of expenditure incurred in relation to such income which does not form part of the total income under this Act in accordance with such method as may be prescribed, if the Assessing Officer, having regard to the accounts of the assessee, is not satisfied with the correctness of the claim of the assessee in respect of such expenditure in relation to income which does not form part of the total income under this Act.

(3) The provisions of sub-section (2) shall also apply in relation to a case where an assessee claims that no expenditure has been incurred by him in relation to income which does not form part of the total income.

RULE 8D: METHOD FOR DETERMINING AMOUNT OF EXPENDITURE IN RELATION TO INCOME NOT INCLUDIBLE IN TOTAL INCOME

(1) Where the Assessing Officer, having regard to the accounts of the assessee of a previous year, is not satisfied with -
   (a) the correctness of the claim of expenditure made by the assessee; or
   (b) the claim made by the assessee that no expenditure has been incurred in relation to income which does not form part of the total income under the Act, he shall determine the amount of expenditure in relation to such income in accordance with the provisions of sub-rule (2).

(2) The expenditure in relation to income which does not form part of the total income shall be the aggregate of following amounts, namely:
   (i) the amount of expenditure directly relating to income which does not form part of total income;
   (ii) an amount equal to one percent of the annual average of the monthly averages of the opening and closing balances of the value of investment, income from which does not or shall not form part of total income:

Provided that the amount referred to in clause (i) and clause (ii) shall not exceed the total expenditure claimed by the assessee.
Clarification regarding disallowance of expenses under section 14A in cases where corresponding exempt income has not been earned during the financial year [Circular No. 5/2014, dated 11.2.2014]

Section 14A provides that no deduction shall be allowed in respect of expenditure incurred relating to income which does not form part of total income. A controversy has arisen as to whether disallowance can be made by invoking section 14A even in those cases where no income has been earned by an assessee, which has been claimed as exempt during the financial year.

The CBDT has, through this Circular, clarified that the legislative intent is to allow only that expenditure which is relatable to earning of income. Therefore, it follows that the expenses which are relatable to earning of exempt income have to be considered for disallowance, irrespective of the fact whether such income has been earned during the financial year or not. The above position is clarified by the usage of the term “includible” in the heading to section 14A [Expenditure incurred in relation to income not includible in total income] and Rule 8D [Method for determining amount of expenditure in relation to income not includible in total income], which indicates that it is not necessary that exempt income should necessarily be included in a particular year’s income, for triggering disallowance. Also, the terminology used in section 14A is “income under the Act” and not “income of the year”, which again indicates that it is not material that the assessee should have earned such income during the financial year under consideration.

In effect, section 14A read along with Rule 8D provides for disallowance of expenditure even where the taxpayer has not earned any exempt income in a particular year.

Whether section 14A is applicable in respect of deductions, which are permissible and allowed under Chapter VI-A?

CIT V. KРИBHCO (2012) (DELHI)

The High Court observed that section 14A is not applicable for deductions, which are permissible and allowed under Chapter VIA. Section 14A is applicable only if an income is not included in the total income as per section 10 of the Income-tax Act, 1961. Deductions under Chapter VIA are different from the exclusions/exemptions provided under Section 10. Section 14A of the Income-tax Act, 1961 ['Act'] provides for disallowance of expenditure in relation to income not "includible" in total income.

SECTION 43D: INTEREST INCOME ON BAD AND DOUBTFUL DEBTS

(i) In the case of
- a public financial institution or
- a scheduled bank or
- a co-operative bank other than primary agricultural credit society or a primary co-operative agricultural and rural development bank or
- a State financial corporation or
- a State industrial investment corporation or
- a deposit taking NBFC or
- a systematically important non-deposit taking NBFC {FA 2019}
the income by way of interest on such categories of bad and doubtful debts, as may be prescribed having regard to the guidelines issued by the Reserve Bank of India in relation to such debts, shall be chargeable to tax in the previous year in which it is credited to the profit and loss account by the said institutions etc. for that year or in the previous year in which it is actually received by them, whichever is earlier. [Sub-clause (a)].

(ii) In the case of a public company, the income by way of interest in relation to such categories of bad and doubtful debts as may be prescribed having regard to the guidelines issued by the National Housing Bank established under the National Housing Bank Act, 1987 in relation to such debts shall be chargeable to tax in the previous year in which it is credited to the profit and loss account by the said public company for that year or in the previous in which it is actually received by it, whichever is earlier. [Sub-clause (b)].

SECTION 44AA: MAINTENANCE OF ACCOUNTS BY CERTAIN PERSONS CARRYING ON PROFESSION OR BUSINESS

(Refer Compendium for the provision)

1. Sec 44AA(1) provides that every person carrying on the legal, medical, engineering or architectural profession or accountancy or technical consultancy or interior decoration or any other profession as has been notified by the Central Board of Direct Taxes in the Official Gazette must statutorily maintain such books of accounts and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of the Income-tax Act, 1961.

Notified professions: The professions notified so far are as the profession of authorised representative; the profession of film artist (actor, camera man, director, music director, art director, dance director, editor, singer, lyricist, story writer, screen play writer, dialogue writer and dress designer); the profession of Company Secretary; and information technology professionals.

SECTION 271A: PENALTY FOR FAILURE TO KEEP OR MAINTAIN BOOKS OF ACCOUNTS, DOCUMENTS, ETC.

If any person fails to keep and maintain any such books of account and other documents as required by section 44AA, in respect of any previous year, then the Assessing Officer or CIT (Appeals) may direct that such person shall pay, by way of penalty, a sum of Rs. 25,000.

SECTION 44AB: AUDIT OF ACCOUNTS OF CERTAIN PERSONS CARRYING ON BUSINESS OR PROFESSION

(i) Who are required to get the accounts audited? It is obligatory in the following cases for a person carrying on business or profession to get his accounts audited before the “specified date” by a Chartered Accountant:

(1) if the total sales, turnover or gross receipts in business exceeds Rs. 100 lakh in any previous year; or

(2) if the gross receipts in profession exceeds Rs. 50 lakhs in any previous year; or

(3) where the assessee is covered under section 44AE, (44BB or 44BBB) and claims that the profits and gains from business are lower than the profits and gains from profession.
misellaneous issues  AJ Education NeXt

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Gains computed on a presumptive basis. In such cases, the normal monetary limits for tax audit in respect of business would not apply.

(4) Where the assessee is carrying on a notified profession under section 44AA, and he claims that the profits and gains from such profession are lower than the profits and gains computed on a presumptive basis under section 44ADA and his income exceeds the basic exemption limit.

(5) Where the assessee is covered under section 44AD(4) and his income exceeds the basic exemption limit.

**AMENDMENT MADE BY FINANCE ACT 2020**

**Rationalisation of provisions relating to tax audit in certain cases.**

Under section 44AB of the Act, every person carrying on business is required to get his accounts audited, if his total sales, turnover or gross receipts, in business exceed or exceeds one crore rupees in any previous year. In case of a person carrying on profession he is required to get his accounts audited, if his gross receipt in profession exceeds, fifty lakh rupees in any previous year.

In order to reduce compliance burden on small and medium enterprises, it is proposed to increase the threshold limit for a person carrying on business from one crore rupees to five crore rupees in cases where,-

(i) aggregate of all receipts in cash during the previous year does not exceed five per cent of such receipt; and

(ii) aggregate of all payments in cash during the previous year does not exceed five per cent of such payment.

Further, the due date for filing return of income under sub-section (1) of section 139 is proposed to be amended by:-

(A) providing 31st October of the assessment year (as against 30th September) as the due date for an assessee referred to in clause (a) of Explanation 2 of sub-section (1) of Section 139 of the Act;

(ii) **Audit Report:** The person mentioned above would have to furnish by the specified date a report of the audit in the prescribed forms. For this purpose, the Board has prescribed under Rule 6G, Forms 3CA/3CB/3CD containing forms of audit report and particulars to be furnished therewith.

(iii) **Accounts audits under other statutes are considered:** In cases where the accounts of a person are required to be audited by or under any other law before the specified date, it will be sufficient if the person gets his accounts audited under such other law before the specified date and also furnish by the said date the report of audit in the prescribed form in addition to the report of audit required under such other law.

Thus, for example, the provision regarding compulsory audit does not imply a second or separate audit of accounts of companies whose accounts are already required to be audited under the Companies Act, 2013. The provision only requires that companies should get their accounts audited under the Companies Act, 2013 before the specified date and in addition to the report required to be given by the
The requirement of audit under section 44AB does not apply to a person who declares profits and gains on a presumptive basis under section 44AD and his total sales, turnover or gross receipts does not exceed Rs. 2 crores.

Further, the requirement of audit under section 44AB does not apply to a person who derives income of the nature referred to in (sections 44B and 44BBA).

"specified date", in relation to the accounts of the assesse of the previous year relevant to an assessment year, means date one month prior to the due date for furnishing the return of income under sub-section (1) of section 139. (FA 2020)

It may be noted that under section 271B, penal action can be taken for not getting the accounts audited and for not filing the audit report by the specified date.

Note - The Institute has brought out a Guidance Note dealing with the various aspects of tax audit under section 44AB. Students are advised to read the same carefully.

SECTION 271B: PENALTY FOR FAILURE TO GET ACCOUNTS AUDITED UNDER SECTION 44AB

If any person

(i) fails to get his accounts audited under section 44AB in respect of any previous year, or
(ii) fails to furnish a report of such audit by the specified date as defined in section 44AB,

then the Assessing Officer shall direct that such person shall pay, the way of penalty, a sum equal to 1/2 % of the total sales, turnover or gross receipts in the business, or of the gross receipts in profession, in such previous year, or a sum of Rs. 1,50,000, whichever is less.

EXPENDITURE ON ISSUE OF SHARES AND DEBENTURES

1. PUNJAB STATE INDUSTRIAL DEVELOPMENT CORPORATION LTD. (SUPREME COURT) 1997

The fees paid to the Registrar of Companies for expansion of authorised capital of the company is directly related to the Capital expenditure incurred by the company and although incidentally that would certainly help in the business of the company and also in profit making, but still it retains the nature of capital expenditure since the expenditure was directly related to the expansion of the capital base of the company. Therefore, the amount paid to ROC as filing fees for enhancement of capital, is not a revenue expenditure and is not deductible.
2. BROOKE BOND INDIA LTD. (SUPREME COURT) 1997

Expenditure incurred by a company in connection with issue of shares with a view to increase its share capital, is directly related to the expansion of capital base of the company and is capital expenditure, even though it may incidentally help in the business of the company and its profit making. The expenditure is not deductible as revenue expenditure and is a capital expenditure which has no tax treatment.

3. CIT V. GENERAL INSURANCE CORPORATION [SUPREME COURT]

Issuance of bonus shares does not result in any inflow of fresh funds or increase in the capital employed; the capital employed remains the same. Issuance of Bonus share by capitalisation of reserves is merely a reallocation of company's fund. If that be so, then it cannot be held that the company has acquired a benefit or advantage of enduring nature. The total funds available with the company will remain the same and issue of bonus shares will not result in any change in the capital structure of the company. Issue of bonus shares does not result in the expansion of capital base of the company.

Thus, the expenditure incurred in connection with issuance of bonus shares is a revenue expenditure. However, expenditure incurred to increase the authorised capital is a capital expenditure, which is not allowed as deduction.

4. INDIA CEMENTS LIMITED (SUPREME COURT)

As per Supreme Court in India Cements Ltd., any expenditure incurred for raising loans or debentures is fully allowed as deduction. Therefore, expenses on issue of non-convertible as well as convertible bonds/debentures is allowed as deduction as per Supreme Court in India Cements Ltd.

5. MADRAS INDUSTRIAL INVESTMENT CORPORATION LTD. (SC)

FACTS:
The appellant-company issued debentures in September, 2014, at a discount. The total discount on the issue of Rs. 15 crores amounted to Rs. 30 lakhs. For the assessment year 2015-16, the appellant-company wrote off Rs. 1,25,000 out of the total discount of Rs. 30 lakhs being the proportionate amount of discount for the period of six months ending with 31st March, 2015, taking into account the period of 12 year which was the period of redemption and dividing the discount of Rs. 30 lakhs over the period of 12 years.

DECISION:

When a company issues debenture at a discount, it incurs a liability to pay a larger amount than what it has borrowed. The liability to pay the discounted amount over and above the amount received for the debentures, is a liability which has been incurred by the company for the purposes of its business in order to generate funds for its business activities. The amounts so obtained by issue of debentures are used by the company for the purposes of its business. This would, therefore, be expenditure.

Ordinarily, revenue expenditure which is incurred wholly and exclusively for the purpose of business must be allowed in its entirety in the year in which it is incurred. It cannot be spread over a number of years even if the assessee has written it off in his books, over a period of years. However, the facts may justify an assessee who has incurred expenditure in a particular year to spread and claim it over a period of ensuing years. In fact, allowing the entire
Expenditure in one year might give a very distorted picture of the profits of a particular year. Issuing debentures is an instance where, although the assessee has incurred the liability to pay the discount in the year of issue of debentures, the payment is to secure a benefit over a number of years. There is a continuing benefit to the business of the company over the entire period. The liability should, therefore, be spread over the period of the debentures.

The Supreme Court held that the liability to pay the discounted amount over and above the amount received for the debentures was a liability incurred by the company for the purposes of its business in order to generate funds for its business activities. It was, therefore, expenditure. The appellant-company had, in its return, correctly claimed a deduction only in respect of the proportionate part of discount of Rs. 1,25,000 over the relevant accounting period in question. This was also in conformity with the accounting practice of showing the discount in the "discount on debentures account" which was written off over the period of the debentures. The appellant-company was entitled to deduct a sum of Rs. 1,25,000 out of the discount of Rs. 30,00,000 in the relevant assessment year. Balance shall be deducted in the balance number of years.

6. CIT V. KODAK INDIA LTD. (SUPREME COURT) [2001]

Expenditure incurred for public issue of shares is capital expenditure.

The assessee had acted to increase its share capital because it had been directed by the Reserve Bank of India so to do. This was because it had to reduce its non-residential holding to forty percent. It was submitted that the only way in which the assessee could do business after the Reserve Bank directive was to issue share capital to comply with it.

Held that whichever way one looked at it, the object of the assessee was to increase its share capital, whether it did so to continue to do business after the Reserve Bank directive or otherwise. The expenditure incurred for the public issue of shares was capital expenditure.

7. CIT V. S.M. HOLDING & FINANCE (P.) LTD. (BOM.) [2003]

Where assessee-company had issued zero-interest unsecured redeemable convertible debentures of Rs. 100 each redeemable after 10 years at a premium of 100%, 10% of the total premium payable by assessee after 10 years was deductible in assessment year in question

FACTS OF THE CASE:

The assessee-company had issued zero-interest unsecured redeemable convertible debentures of Rs. 100 each redeemable after 10 years at a premium of 100%. The assessee claimed that the premium payable by it was Rs. 5,47,50,000 after the expiry of 10 years. However, the assessee claimed deduction of Rs. 54,75,000 per annum. The Assessing Officer added back that figure to the income of the assessee on the ground that the liability was not ascertainable during the accounting year ending 31.03.2013 and that it was a contingent liability.

HELD:

Held that in the annual reports of the company and also in the audit reports given by the auditors, it had been certified that zero-interest unsecured redeemable convertible debentures of Rs. 100 each redeemable after 10 years at a premium of 100% had been issued during the assessment year in question. There was no reason to discard this note of the auditor. In view thereof the assessee's claim was to be allowed.
Would the expenditure incurred for issue of convertible debentures be treated as revenue expenditure or capital expenditure?

Held that the expenditure incurred on the issue of debentures shall be treated as revenue expenditure even in case of convertible debentures, i.e. the debentures which had to be converted into shares at a later date.

Can share issue expenses incurred by a company be treated as capital in nature, if the public issue could not ultimately materialize on account of non-clearance by SEBI?

Facts of the case:
The assessee-company incurred share issue expenses of Rs.35.39 lakh for its proposed public issue, which could not ultimately materialize due to non-clearance by the SEBI. It claimed such expenses as revenue in nature, on the ground that the same was incurred for augmenting its working capital. The claim of the assessee was, however, rejected by the Assessing Officer.

High Court's Decision:
The High Court noted that the assessee-company had taken steps to go in for a public issue and incurred share issue expenses for the same. However, it could not go in for the public issue by reason of the orders issued by the SEBI just before the proposed issue. Though the efforts were aborted, the fact remains that the expenditure incurred was only for the purpose of expansion of the capital base. The capital nature of the expenditure would not be lost on account of the abortive efforts. The expenditure, therefore, constitutes a capital expenditure.

AMENDMENT MADE BY FINANCE ACT 2018:
Income from construction and service contracts [Section 43CB]
The profits and gains arising from a construction contract or a service contract shall be computed on the basis of percentage of completion method (POCM) in accordance with the notified ICDS i.e., ICDS III: Construction Contracts. However, the profits and gains arising from a service contract shall be computed on the basis of

<table>
<thead>
<tr>
<th>Method</th>
<th>Condition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Project completion method</td>
<td>If the duration of the contract is not more than 90 days</td>
</tr>
<tr>
<td>Straight line method</td>
<td>If the contract involves indeterminate number of acts over a specific period of time</td>
</tr>
</tbody>
</table>

For the purpose of percentage of completion method, project completion method or straight-line method –
(i) the contract revenue shall include retention money;
(ii) the contract cost shall not be reduced by any incidental income in the nature of interest, dividends or capital gains.
CHAPTER 9. PRESUMPTIVE INCOME

SECTION 44AD: SPECIAL PROVISION FOR COMPUTING PROFITS AND GAINS OF BUSINESS ON PRESUMPTIVE BASIS

1. Notwithstanding anything to the contrary contained in sections 28 to 43C,
   - in case of an eligible assessee
   - engaged in an eligible business
   - a sum equal to 8% of the total turnover or gross receipts of the assessee in the previous year on account of such business,
   - or as the case may be, a sum higher than the aforesaid sum claimed to have been earned by the eligible assessee,
   - shall be deemed to be the income under the head "Profits and gains of Business or Profession".

The existing rate of deemed total income of eight per cent will become six per cent in respect of the amount of such total turnover or gross receipts received by an account payee cheque or account payee bank draft or use of electronic clearing system through a bank account or such other electronic mode as may be prescribed during the previous year or before the due date specified in sub-section (1) of section 139 in respect of that previous year. However, the existing rate of deemed profit of 8% referred to in section 44AD of the Act, shall continue to apply in respect of total turnover or gross receipts received in any other mode.

(Underlined and bold words are amended by Finance Act (No.2) 2019)

(i) Eligible business: The presumptive taxation scheme under section 44AD covers all small businesses with total turnover/gross receipts of up to Rs. 200 lakhs (except the business of plying, hiring and leasing goods carriages covered under section 44AE).

(ii) Eligible assessee: Resident individuals, HUFs and partnership firms (but not LLPs) and who has not claimed deduction under any of the section 10AA or deduction under any provisions of Chapter VIA under the heading “C.—Deductions in respect of certain incomes” in the relevant assessment year would be covered under this scheme.

(iii) Presumptive rate of tax: The presumptive rate of tax would be 8% of total turnover or gross receipts.

However, the presumptive rate of 6% of total turnover or gross receipts will be applicable in respect of amount which is received

- by an account payee cheque or
- by an account payee bank draft or
- by use of electronic clearing system through a bank account
- by such other electronic mode as may be prescribed {Finance Act (No. 2)}.
during the previous year or on or before the due date of filing of return under section 139(1) in respect of that previous year.

However, the assessee has the option to declare in his return of income, an amount higher than the presumptive income so calculated, claimed to have been actually earned by him.

(2) **No further deduction would be allowed:** All deductions allowable under sections 30 to 38 shall be deemed to have been allowed in full and no further deduction shall be allowed.

(3) **Written down value of the asset:** The WDV of any asset of such business shall be deemed to have been calculated as if the assessee had claimed and had been actually allowed the deduction in respect of depreciation for each of the relevant assessment years.

(4) **Relief from maintenance of books of accounts and audit:** The intention of widening the scope of this scheme is to reduce the compliance and administrative burden on small businessmen and relieve them from the requirement of maintaining books of account. Such assessees opting for the presumptive scheme are not required to maintain books of account under section 44AA or get them audited under section 44AB.

(5) **Higher threshold for non-audit of accounts for assessees opting for presumptive taxation under section 44AD:** Section 44AB makes it obligatory for every person carrying on business to get his accounts of any previous year audited if his total sales, turnover or gross receipts exceed Rs. 1 crore.

However, if an eligible person opts for presumptive taxation scheme as per section 44AD(1), he shall not be required to get his accounts audited if the total turnover or gross receipts of the relevant previous year does not exceed Rs. 2 crores.

(6) **Advance tax:** Further, since the threshold limit of presumptive taxation scheme has been enhanced to Rs. 2 crores, the eligible assessee is now required to pay advance tax by 15th March of the financial year.

(7) **Persons not eligible for presumptive taxation scheme:** The following persons are specifically excluded from the applicability of the presumptive provisions of section 44AD -

(a) a person carrying on profession as referred to in section 44AA(1); or
(b) a person earning income in the nature of commission or brokerage; or
(c) a person carrying on any agency business.

(8) **Not eligible to opt for presumptive taxation under this section for 5 assessment years:** Where an eligible assessee declares profit for any previous year in accordance with the provisions of this section and he declares profit for any of the
five consecutive assessment years relevant to the previous year succeeding such previous year not in accordance with the provisions of sub-section (1), he shall not be eligible to claim the benefit of the provisions of this section for five assessment years subsequent to the assessment year relevant to the previous year in which the profit has not been declared in accordance with the provisions of sub-section (1). [Section 44AD(4)].

Example:

Let us consider the following particulars relating to a resident individual, Mr. A, being an eligible assessee whose gross receipts do not exceed Rs. 2 crore in any of the assessment years between A.Y. 2021-22 to A.Y. 2023-24-

<table>
<thead>
<tr>
<th>Particulars</th>
<th>A.Y.2021-22</th>
<th>A.Y.2022-23</th>
<th>A.Y.2023-24</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross receipts (Rs.)</td>
<td>1,80,00,000</td>
<td>1,90,00,000</td>
<td>2,00,00,000</td>
</tr>
<tr>
<td>Income offered for taxation (Rs.)</td>
<td>14,40,000</td>
<td>15,20,000</td>
<td>10,00,000</td>
</tr>
<tr>
<td>% of gross receipts</td>
<td>8%</td>
<td>8%</td>
<td>5%</td>
</tr>
<tr>
<td>Offered income as per presumptive taxation scheme u/s 44AD</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
</tr>
</tbody>
</table>

In the above case, Mr. A, an eligible assessee, opts for presumptive taxation under section 44AD for A.Y. 2021-22 and A.Y. 2022-23 and offers income of Rs.14.40 lakh and Rs.15.20 lakh on gross receipts of Rs.1.80 crore and Rs.1.90 crore, respectively.

However, for A.Y. 2023-24, he offers income of only Rs. 10 lakhs on turnover of Rs. 2 crores, which amounts to 5% of his gross receipts. He maintains books of account under section 44AA and gets the same audited under section 44AB. Since he has not offered income in accordance with the provisions of section 44AD(1) for five consecutive assessment years, after A.Y. 2021-22, he will not be eligible to claim the benefit of section 44AD for next five assessment years succeeding A.Y. 2023-24 i.e., from A.Y.2024-25 to 2028-29.

(9) Books of accounts and Audit if sub-section (4) attracted: An eligible assessee to whom the provisions of sub-section (4) are applicable and whose total income exceeds the basic exemption limit has to maintain books of account under section 44AA and get them audited and furnish a report of such audit under section 44AB. [Section 44AD(5)].

SECTION 44ADA: SPECIAL PROVISION FOR COMPUTING PROFITS AND GAINS OF PROFESSION ON PRESUMPTIVE BASIS

(INSERTED BY FINANCE ACT 2016)

(1) Eligible business: The presumptive taxation scheme under section 44ADA for estimating the income of an assessee:
- who is engaged in any profession referred to in section 44AA(1) such as legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or any other profession as is notified by the Board in the Official Gazette; and
- whose total gross receipts does not exceed Rs. 50 lakhs rupees in a previous year,

(2) **Presumptive rate of tax:** Presumptive rate of tax would be a sum equal to 50% of the total gross receipts, or, as the case may be, a sum higher than the aforesaid sum claimed to have been earned by the assessee.

(3) **Eligible Assessee**

(4) **No further deduction would be allowed:** Under the scheme, the assessee will be deemed to have been allowed the deductions under section 30 to 38. Accordingly, no further deduction under those sections shall be allowed.

(5) **Written down value of the asset:** The written down value of any asset used for the purpose of the profession of the assessee will be deemed to have been calculated as if the assessee had claimed and had actually been allowed the deduction in respect of depreciation for the relevant assessment years.

(6) **Relief from maintenance of books of accounts and audit:** The eligible assessee opting for presumptive taxation scheme will not be required to maintain books of account under section 44AA(1) and get the accounts audited under section 44AB in respect of such income.

(7) **Option to claim lower profits:** An assessee may claim that his profits and gains from the aforesaid profession are lower than the profits and gains deemed to be his income under section 44ADA(1); and if such total income exceeds the maximum amount which is not chargeable to income-tax, he has to maintain books of account under section 44AA and get them audited and furnish a report of such audit under section 44AB.

(8) **Advance Tax:** Further, since the presumptive taxation regime has been extended for professionals also, the eligible assessee is now required to pay advance tax by 15th March of the financial year.
SECTION 44AE: SPECIAL PROVISION FOR COMPUTING PROFITS AND GAINS OF BUSINESS OF PLYING, HIRING OR LEASING GOODS CARRIAGES

(1) **Eligible business:** This section provides for estimating business income of an owner of goods carriages from the plying, hire or leasing of such goods carriages;

(2) **Eligible assessee:** The scheme applies to persons **owning not more than 10 goods vehicles at any time during the previous year**;

(3) **Presumptive Income:** The estimated income from each goods vehicle, being a heavy goods vehicle or other than heavy goods vehicle would be

<table>
<thead>
<tr>
<th>Goods Carriage</th>
<th>Presumptive Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>Heavy goods vehicle</td>
<td>Rs. 1,000 per ton of gross vehicle weight or unladen weight, as the case may be, for every month or part of a month during which such vehicle is owned by the assessee for the previous year.</td>
</tr>
<tr>
<td>Other than heavy goods vehicle</td>
<td>Rs. 7,500 for every month or part of a month</td>
</tr>
</tbody>
</table>

The assessee can also declare a higher amount in his return of income. In such case, the latter will be considered to be his income;

(4) **All other deduction deemed to be allowed:** The assessee will be deemed to have been allowed the deductions under sections 30 to 38. Accordingly, the written down value of any asset used for the purpose of the business of the assessee will be deemed to have been calculated as if the assessee had claimed and had actually been allowed the deduction in respect of depreciation for each of the relevant assessment years.

(5) **Salary and interest to partners is allowed:** Where the assesse is a firm, the salary and interest paid to its partner are allowed to be deducted subject to the conditions and limit specified under section 40(b).

(6) **Not requirement to maintain books of accounts and get the accounts audited:** The assessee joining the scheme will not be required to maintain books of account under section 44AA and get the accounts audited under section 44AB in respect of such income.

(7) **Option to claim lower profits:** An assessee may claim lower profits and gains than the deemed profits and gains subject to the condition that the books of account and other documents are kept and maintained as required under section 44AA and the assessee gets his accounts audited and furnishes a report of such audit as required under section 44AB.
(8) Meaning of certain terms

<table>
<thead>
<tr>
<th>S. No</th>
<th>Term</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1)</td>
<td>Heavy goods vehicle</td>
<td>any goods carriage, the gross vehicle weight of which exceeds 12,000 kilograms.</td>
</tr>
<tr>
<td>(2)</td>
<td>Gross vehicle weight</td>
<td>total weight of the vehicle and load certified and registered by the registering authority as permissible for that vehicle.</td>
</tr>
<tr>
<td>(3)</td>
<td>Unladen weight</td>
<td>the weight of a vehicle or trailer including all equipment ordinarily used with the vehicle or trailer when working but excluding the weight of driver or attendant and where alternative parts or bodies are used the unladen weight of the vehicle means the weight of the vehicle with the heaviest such alternative body or part.</td>
</tr>
</tbody>
</table>

Special provisions for computing profits and gains on presumptive basis: A summary

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Section 44AD</th>
<th>Section 44ADA</th>
<th>Section 44AE</th>
</tr>
</thead>
</table>
| (1) Eligible Assessee | Resident individual, HUF or Partnership firm (but not LLP) engaged in eligible business and who has not claimed deduction under section 10AA or Chapter VIA under the heading “C – Deductions in respect of certain incomes” Non-applicability of section 44AD in respect of the following persons:  
- A person carrying on profession specified u/s 44AA(1);  
- A person earning income in the nature of commission or brokerage;  
- A person carrying on any agency business. | Resident assessee engaged in any profession specified u/s 44AA(1), namely, legal, medical, engineering, architectural profession or profession of accountancy or technical consultancy or interior decoration or notified profession (authorized representative, film artist, company secretary, profession of information technology) | An assessee owning not more than 10 goods carriages at any time during the P.Y. |
<p>| (2) Eligible business/ profession | Any business, other than business referred to in section 44AE, whose total turnover | Any profession specified under section 44AA(1), whose total gross | Business of plying, hiring or leasing goods carriages            |</p>
<table>
<thead>
<tr>
<th><strong>Presumptive Income</strong></th>
<th><strong>AJ Education NeXt</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>gross receipts in the P.Y. ≤ <strong>Rs. 200 lakhs</strong></td>
<td>receipts ≤ <strong>Rs. 50 lakhs</strong> in the relevant P.Y.</td>
</tr>
<tr>
<td><strong>(3) Presumptive rate/Presumptive income</strong></td>
<td>For each heavy goods vehicle <strong>Rs. 1,000 per ton of gross vehicle weight or unladen weight, as the case may be, for every month or part of a month and for other than heavy goods vehicle, Rs. 7,500 per month or part of a month during which such vehicle is owned by the assessee or an amount claimed to have been actually earned from such vehicle, whichever is higher.</strong></td>
</tr>
<tr>
<td>8% of total turnover/sales/ gross receipts or a sum higher than the aforesaid sum claimed to have been earned by the assessee. 6% of total turnover/gross receipts in respect of the amount of total turnover/ sales/ gross receipts received by A/c payee cheque/ bank draft/ ECS during the P.Y. or before due date of filing of return u/s 139(1) in respect of that P.Y.</td>
<td>50% of total gross receipts of such profession or a sum higher than the aforesaid sum claimed to have been earned by the assessee.</td>
</tr>
<tr>
<td><strong>(4) Non-allowability of deductions while computing presumptive income</strong></td>
<td>Deductions allowable under sections 30 to 38 shall be deemed to have been given full effect to and no further deduction shall be allowed. Even in case of a firm, salary and interest paid to partners is not deductible.</td>
</tr>
<tr>
<td>Even in case of a firm, salary and interest paid to partners is not deductible.</td>
<td>In case of a firm, salary and interest paid to partners is deductible subject to the conditions and limits in section 40(b)</td>
</tr>
<tr>
<td><strong>(5) Written down value of asset</strong></td>
<td>WDV of any asset of an eligible business/profession shall be deemed to have been calculated as if the eligible assessee had claimed and had been actually allowed depreciation for each of the relevant assessment years.</td>
</tr>
<tr>
<td><strong>(6) Requirement of maintenance of books of account u/s 44AA and audit u/s 44AB</strong></td>
<td>If the assessee claims his profits to be lower than the profits computed by applying the presumptive rate, he has to maintain books of account and other documents u/s 44AA(1) and If the assessee claims his profits to be lower than the profits computed by applying the presumptive rate, he has to maintain books of account u/s 44AA(2) and</td>
</tr>
</tbody>
</table>

**Notes:**
- Presumptive Income: AJ Education NeXt
- Gross receipts: ≤ Rs. 200 lakhs
- Receipts: ≤ Rs. 50 lakhs in the relevant P.Y.
- Presumptive rate: 8% of total turnover/sales/ gross receipts or a sum higher than the aforesaid sum claimed to have been earned by the assessee.
- Presumptive income: 6% of total turnover/gross receipts in respect of the amount of total turnover/ sales/ gross receipts received by A/c payee cheque/ bank draft/ ECS during the P.Y. or before due date of filing of return u/s 139(1) in respect of that P.Y.
- Non-allowability of deductions: Deductions allowable under sections 30 to 38 shall be deemed to have been given full effect to and no further deduction shall be allowed.
- Written down value of asset: WDV of any asset of an eligible business/profession shall be deemed to have been calculated as if the eligible assessee had claimed and had been actually allowed depreciation for each of the relevant assessment years.
- Requirement of maintenance of books of account u/s 44AA and audit u/s 44AB: If the assessee claims his profits to be lower than the profits computed by applying the presumptive rate, he has to maintain books of account and other documents u/s 44AA(1) and If the assessee claims his profits to be lower than the profits computed by applying the presumptive rate, he has to maintain books of account u/s 44AA(2) and.
| A.Y.2026-27), say, for A.Y. 2023-24, would disentitle the assessee from claiming profits on presumptive basis for five successive AYs subsequent to the AY relevant to the PY of such non-declaration (i.e., from A.Y. 2024-25 to A.Y.2028-29). In such a case, the assessee would have to maintain books of account and other documents u/s 44AA(2) and get his accounts audited u/s 44AB, if his total income > basic exemption limit for that year. | get his accounts audited u/s 44AB. |

**Note** - If a person is not covered under presumptive tax provisions mentioned above, audit of books of account u/s 44AB is mandatory, if, in a case where he carries on business, his total sales, turnover or gross receipts in business > **Rs. 1 crore** in that P.Y. and in a case where he carries on profession, his gross receipts in profession > **Rs. 50 lakh** in that P.Y.
**DISALLOWANCES**

**CHAPTER 6**

**DISALLOWANCES**

<table>
<thead>
<tr>
<th>Disallowances</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Sec 40A</strong></td>
</tr>
<tr>
<td>2. 40A(3)/(3A): Cash &gt; Rs 10,000.</td>
</tr>
<tr>
<td>5. 40(a)(iib): Fees charged by State Govt.</td>
</tr>
</tbody>
</table>

**Sec 40A(2): Excess Payment to Relatives:**

- **Assessee Incurs Expenditure**
- **(+) made payment to Specified person**
- **If AO considers to be unreasonable and Excessive**
- **(+) A.O. may disallow**
  - Having regard to Fair Market Value & Legitimate needs of business.

- If the Co. sells goods of Rs 1,00,000 to director whereby the FMV of goods sold is Rs 1,50,000 then, A.O. can't invoke Sec 40A(2) as it is applicable only to expenditure and not income.
## Sec 40A(3)

| Assessee incurs a expenditure (Revenue) | (+) Payment OR Aggregate of Payments | (+) To a person in a single day of a sum exceeding Rs 10,000** |

By other than “Account payee crossed cheque OR Bank Draft OR ECS or such other electronic mode as may be prescribed.

Such other Electronic Mode would include CC/DD/Net Banking/IMPS/UPPI/RTGS/NEFT/BHIM. {Rule 6ABBA}

** For payment made to transporters the Limit is Rs 35,000.

## Sec 40A(3A)

<table>
<thead>
<tr>
<th>P.Y. 2020-21</th>
<th>P.Y. 2021-22</th>
</tr>
</thead>
<tbody>
<tr>
<td>Salary a/c</td>
<td>80K</td>
</tr>
<tr>
<td>To Salary (o/s) (This is not paid but still allowed on Accrual Basis in PY 2020-21)</td>
<td>80K</td>
</tr>
<tr>
<td></td>
<td>Rs 80,000 is paid to a person in single day by cash in PY 2021-22.</td>
</tr>
<tr>
<td># RESULT:-</td>
<td>It can’t be disallowed u/s 40A(3) as it is not allowed in P.Y. 2021-22 but as per Sec 40A(3A) it will be deemed to be PGBP Income of P.Y. 2021-22</td>
</tr>
</tbody>
</table>

### I. Depreciation disallowance u/s 32 and capital Expenditure u/s 35AD on cash payment:

1. In order to discourage cash transactions even for CAPEX, a proviso has been attached to Sec 43(1), which states that where an assessee incurs any exp for
acquisition of any asset, in respect of which payments or aggregate of payments made to a person on a day otherwise than by A/c payee cheque drawn or A/c payee bank draft or use of ECS or such other electronic mode as may be prescribed exceeds Rs. 10,000, then such expenditure shall be ignored for the purpose of determination of actual cost of such asset. (FA 2019)

Further, 35AD(8)(f) states that any expenditure in respect of which payment or aggregate of payment made to a person in a day otherwise than by A/c payee cheque or bank draft or ECS or such other electronic mode as may be prescribed exceeds Rs. 10,000, no deduction shall be allowed in respect of such expenditure.

<table>
<thead>
<tr>
<th>Rule 6DD: Exception</th>
</tr>
</thead>
<tbody>
<tr>
<td>Circular No. 10/2008, Dated 5-12-2008: Clarification Regarding Rule 6DD</td>
</tr>
<tr>
<td>“Fish or Fish Products”</td>
</tr>
<tr>
<td>Would include other marine products, such as shrimp, prawns, cuttlefish, squid, crabs, lobsters, etc.</td>
</tr>
</tbody>
</table>

40A(2) vs 40A(3) the Interlinking:

Sec 40A(7) :- Provision for Payment of Gratuity is Disallowed

| Actuarial Valuation | 18,00,000 |
| (-) Amount available in Gratuity fund | (15,00,000) |
| Prov for payment of Gratuity Disallowed u/s 40A(7) | 3,00,000 |
Gratuity liability is determined by Actuary in the year of retirement or termination of employment. Suppose, determined liability comes to Rs 18,00,000. Now, the employer is liable to pay this Rs 18,00,000 to employee on retirement. However, amount available in Grant Fund is Rs 15,00,000. Employer passed the following entry in BOA:

<table>
<thead>
<tr>
<th>Gratuity A/c</th>
<th>Dr</th>
<th>3,00,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Prov. for Gratuity A/c</td>
<td>3,00,000</td>
<td></td>
</tr>
</tbody>
</table>

This amount is disallowed u/s 40A(7). However, when this Rs 300,000 is actually paid to employee, it will be allowed as deduction.

**Sec 40A(9)**: Contribution to Unrecognized Provident Fund etc. is Disallowed.

→ CASE I:- If an employer contributes Rs 60,000 p.a. to Recognised P.F. etc then this contribution itself is allowed as deduction in respective years u/s 36(1).

→ CASE II:- If an employer contributes Rs 60,000 to an unrecognized P.F. then this contribution every year will be disallowed by virtue of sec 40A(9). However when this amount is actually discharged to employees it will be allowed in the hands of employer.

---

**Sec 40(a)(i):** Payments to N.R. or Foreign Company of any Interest, Royalty, Fees for Technical Services or other sum chargeable Payable

<table>
<thead>
<tr>
<th>In India</th>
<th>OR</th>
<th>Outside India</th>
</tr>
</thead>
<tbody>
<tr>
<td>To a NR OR foreign Company</td>
<td>Deduct Tax</td>
<td>AND</td>
</tr>
</tbody>
</table>

* 100% expenditure will be disallowed if the tax is not deducted OR after deducting is not paid till the due date specified u/s 139(1).
* Where in respect of any such sum, where tax has been deducted in any subsequent year, or has been deducted in the previous year but paid after the due date of filing of return, then it will be allowed in the P.Y. in which payment is made.

* Where assessee has failed to deduct TDS & he is not treated as Assessee in default u/s 201(1), then for the purpose of sec 40(a)(i) it shall be deemed that assessee has deducted and paid the tax on such amount on the date of furnishing of return by Non Resident payee & deduction of such expenditure will be allowed.

* All the aforesaid sums must be taxable in the hands of the recipient under IT Act, 1961. (Refer Past Questions for Illustration)

Circular No. 3/2015 dated 12/02/2015

Doubts have been raised about interpretation of the term “other sum chargeable” i.e. whether this term refers to the whole sum being remitted abroad or only the portion representing the sum chargeable to IT under relevant provision of the Act.

CBDT clarifies that for the purpose of making disallowance u/s 40(a)(i) the appropriate portion of the sum which is chargeable to tax under the Act shall form the basis of such disallowances & it has to be determined by A.O. considering facts & circumstances.

Sec 40(a)(ia): Payment to Residents Payee

| Deduct Tax | AND | Deposit till time limit specified u/s 139(1) i.e.Due Date of filing of Return. |

Note:- If tax is not deducted or after deducting it is not paid then 30% of expenditure will be disallowed. (FA 2014).

Where in respect of any such sum, where tax has been deducted in any subsequent year, or has been deducted in the previous year but paid after the due date of filing of return, then 30% expenditure will be allowed in the P.Y. in which payment is made.
Sec 201(1): Assessee in Default

If an assessee

- Fails to deduct TDS
- OR
- After deduction fails to pay TDS

Then he shall be deemed to be “Assessee in Default”

Consequently, he is liable to pay:

1. **Penalty u/s 221** which can be up to TDS not deducted or not paid.
2. **Interest u/s 220 @ 1% p.m.**

*It is well established law laid down by various courts that deductor shall be treated as “Assessee in default” only if:*

1. Deductor has **failed to deduct TDS** AND
2. Deductee has also **failed to pay** tax directly.

2nd Proviso to Sec 40(a)(ia)

Where assessee has **failed to deduct TDS** & he is **not treated as Assessee in default u/s 201(1)**, then for the purpose of **sec 40(a)(ia)** it shall be **deemed** that assessee has **deducted and paid** the tax on such amount **on the date of furnishing of return by Resident payee** & deduction of such expenditure will be allowed.

Very much needed Clarificatory Judgement:

It was held by SC in the case of Palam Gas Services that disallowance u/s 40(a)(ia) shall **apply not only in** respect of those amount which are **payable** during the PY but is **also applicable in** respect of those amount which are **paid** during the PY.

Further, disallowance u/s 40(a)(ia) is applicable **not only to** assesses following mercantile system but also **cash system**. The above judgement is also applicable to **sec 40(a)(i)**.

As per **Sec 40(a)(iii)** any payment which is chargeable under the head **Salaries**, if it is payable outside India or to a **Non Resident** and if the **tax has not been paid**...
**DISALLOWANCES**

Thereon nor deducted therefrom under CH XVII-B then the salary expenditure is disallowed.

<table>
<thead>
<tr>
<th>Sec 40(a)(ii)</th>
<th>Sec 40(a)(ia)</th>
<th>Sec 40(a)(iib)</th>
<th>Sec 40(a)(v)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income tax is disallowed.</td>
<td>Wealth tax is disallowed.</td>
<td>Royalty, fees, service charges etc. paid by State Govt. undertaking to State Govt.</td>
<td>Employer paying tax on Non monetary perquisites of Employees. Such perquisite is Exempt. (10(10CC))</td>
</tr>
</tbody>
</table>

**Sec 43B:**- Certain Deductions Allowed only on Actual Payment

Notwithstanding anything contained in any of the provision of IT Act, following deductions will be allowed on actual payment:

(a) **Tax, duty, cess or fees** under any other law OR

(b) **Employer’s** contribution to any provident fund or superannuation fund or gratuity fund or any fund for the welfare of EE’S OR

(c) **Bonus or commission** payable to Employees OR

(d) **Interest** on any loan or borrowing from public Financial Institutions or state Finance Corp. or State Industrial Investm Corporation OR

(e) **Interest** on any loan or advance from scheduled Bank (including Cooperative Banks) or **NBFC** OR

(f) **Any Leave Salary** OR

(g) Any expenditure which is payable to Indian Railways for use of Railway Assets shall be allowed as deduction only in the year in which it is ACTAULLY PAID.

**Note:**

1) The above deductions will be **allowed in the year** in which it incurred even if it is paid till due date of return specified u/s 139(1).
2) However, if the payment is not made till due date of filling of return, then it will be allowed in the year of actual payment.

3) A bank guarantee given by a company towards disputed tax liabilities does not amount to actual payment and hence it is not allowed as deduction.

4) Whether GST is Inclusive of Turnover or Exclusive provisions of Sec 43B will be applicable.

**Employee Related Issues:**

**Treatment of Employees Contribution in the hands of Employer :-**

The intention of the legislature is far clear that EE’s contribution is not subject to the due date mentioned u/s 43B, but it is the funds due date only. However, Delhi H.C. in the case of Aimil Ltd & Uttrakhand H.C. in Kiccha Sugar Co. Ltd has given a contradictory view by holding that the due date should be read as mentioned in Sec 43B.

However, Gujarat High Court has disallowed the Employees Contribution if payment is made after 15 days.

**Explanation 3C, 3CA & 3D to Sec 43B**

For removal of doubts, it is hereby declared that a deduction of interest under clause (d)(da) & (e) is available only if it is actually paid & not if it is just converted into new Loan.

**Circular 7/2006 Dated 17/7/2006:-**

Any O/S interest which is converted into a loan will be allowed as deduction in the year in which such converted loan is actually paid irrespective of nomenclature being loan.

ALL THE BEST
### Sec 41(1):- Recovery of Expenditure & Remission & Cessation of Trading Liability (Deemed Income)

<table>
<thead>
<tr>
<th>Sec 41(1)</th>
<th>Sec 41(1)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Where any <em>loss or expenditure</em> has been <em>allowed</em> as deduction AND subsequently such amount is <em>received/written off</em> in respect of such loss or expenditure then it is deemed to be <em>Business Income</em>.</td>
<td>Remission or cessation of Trading liability is also deemed to be Business Income.</td>
</tr>
<tr>
<td>If <em>working cap loan</em> is <em>waived off</em> (trading liab.) then Sec 41(1) is applicable.</td>
<td>If loan of FA is waived off. (Non-trading liab) Sec 41(1) is Not Applicable.</td>
</tr>
</tbody>
</table>

1. This section is **applicable** even in the year in which business has ceased.
2. This section is **applicable** in the hands of **successor** if it is recovered by it, where deduction was claimed by predecessor.
3. * If loan of Fixed Asset is **waived by CG/SG/Authority/Body/Agency** then it is Income as per Sec 2(24)(xviii). If Loan is waived by a Company/Firm/LLP etc then it is not taxable. (This is discussed earlier in the Chapter of Depreciation)

### Sec 41(1) applicable in case of Unilateral Cessation of Trading Liability

<table>
<thead>
<tr>
<th>Mr. A: Seller</th>
<th>Mr. B: Buyer</th>
</tr>
</thead>
<tbody>
<tr>
<td>B/S</td>
<td>B/S</td>
</tr>
<tr>
<td>Debtors 1,00,000</td>
<td>Crs. 100000</td>
</tr>
</tbody>
</table>

Where Mr. B i.e. buyer ceases a liability of Rs 1,00,000, then also Sec 41(1) is applicable even though such amount is not written off as bad debt by Mr. A as it amount to unilateral cessation of Trading Liability.
DEEMED INCOMES

Polyflex India (P) Ltd v/s CIT (SC)
The assessee Co. paid excise duty under protest & took the deduction of the same. The assessee challenged the levy of such duty in H.C. & subsequently H.C. decided the case in the favour of the assessee. Department gave the refund of such E.D. to the assessee on the direction of H.C. Further, department challenged H.C. decision in S.C.
The issue under consideration is whether Sec 41(1) will be applicable when the assessee has received the money & matter is pending in S.C.

Judgement
Sec 41(1) is a deeming fiction which comes into play as soon as assessee receives any amount in respect of such expenditure or losses. It is irrelevant that such receipt has been disputed by the department in further appeal. A.O. is justified in invoking sec 41(1) in the year in which assessee received the money.

Note:
Assessee has received the refund, therefore it is taxable in the year of receipt. In case, the refund is not received but only the order of HC is passed, then such amount won't be taxable till the time amount is received.

Recovery of Bad Debts
As per Sec 41(4) Recovery of Bad Debts which was allowed a deduction will be deemed to be business income irrespective of whether the business exists or not.
Further it was held by Supreme Court in the case of P.K. Kaimal that bad debts claimed by Predecessor and recovered by successor is not chargeable to tax.

ALL THE BEST
Sec 14A: - Expenditure Incurred Disallowed in Respect of Exempt Income under this Act

→ No deduction shall be allowed in the respect of expenditure incurred for earning exempt income under this ACT.
→ The A.O. shall determine the amount of expenditure disallowed in prescribed manner (Rule 8D)

Rule 8D: Method for determining amount of expenditure disallowed in respect to Exempt Income.

(i) Amount of Expenditure Directly relating to exempt income.

AND

(ii) an amount equal to one percent of the annual average of the monthly averages of the opening and closing balances of the value of investment, income from which does not or shall not form part of total income.

Circular 5/2014

Doubts have been raised by industry whether disallowances can be made even in those cases where no income has been earned by an assessee which has been claimed as exempt during the Financial year.

CBDT has put an emphasis on term income should be exempt under this Act & not under the year in which the expenditure is disallowed.

CIT vs Kribhco (2012) (Delhi)

The High Court observed that Sec 14A is not applicable for deductions, which are permissible and allowed under Chapter VIA. Sec 14A is applicable only if an income is not included in the total income as per Sec 10 of the Income-tax Act, 1961. Deductions under Chapter VIA are different from the exclusions/exemptions provided under Sec 10.

Sec 14A of the Income-tax Act, 1961 ['Act'] provides for disallowance of expenditure in relation to income not "includible" in total income.
**MISCELLANEOUS ISSUES**

**Sec 43D:** - Interest Income on Bad & Doubtful Debts

In case of public Financial Institutions OR State Financial Corporation OR State Industrial Investment Corp. OR Scheduled Bank OR COOPERATIVE BANKS or NBFC OR Public Company [whose object is providing L.T. Finance for Construction & Purchases of Houses in India], the Interest on Bad & Doubtful Debts shall be taxable in the year in which the Interest is recovered or credited to BOA whichever is earlier.

**Sec 44AA: Maintenance of Books of Accounts**

<table>
<thead>
<tr>
<th>Specified Profession</th>
</tr>
</thead>
<tbody>
<tr>
<td>Existing</td>
</tr>
<tr>
<td>Keep &amp; maintain BOA if GR &gt; 1.5L in All 3 preceding PY's</td>
</tr>
<tr>
<td>New</td>
</tr>
<tr>
<td>Keep &amp; maintain BOA, if GR is likely to be greater than 1.5 lakhs</td>
</tr>
</tbody>
</table>

⇒ Note:- All the above BOA should be maintained for 6 PY’s from the end of Relevant AY’s.

**Business and other Non-Specified Professions**

<table>
<thead>
<tr>
<th>In case of existing business or profession</th>
<th>Other than Individual &amp; HUF</th>
<th>Individual &amp; HUF</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. If PGBP exceeds in any of the 3 preceding PYs (OR)</td>
<td>1,20,000</td>
<td>2,50,000</td>
</tr>
<tr>
<td>2. If Turnover exceeds in any of the 3 preceding PYs</td>
<td>10,00,000</td>
<td>25,00,000</td>
</tr>
</tbody>
</table>

**If business or profession is newly set up**

<table>
<thead>
<tr>
<th>In case of existing business or profession</th>
<th>Other than Individual &amp; HUF</th>
<th>Individual &amp; HUF</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. If PGBP is likely to exceed (OR)</td>
<td>1,20,000</td>
<td>2,50,000</td>
</tr>
<tr>
<td>2. If Turnover is likely to exceed</td>
<td>10,00,000</td>
<td>25,00,000</td>
</tr>
</tbody>
</table>

**Sec 271A:** - Penalty for failure to keep & maintain BOA, other documents, etc.
A.O. or CIT (Appeals) may direct that such person shall pay by way of penalty a sum of Rs. 25,000.

**Sec 44AB: - Tax Audit**

1. In Case of Business the T/O > Rs. 1 Cr
2. In Case of Profession the T/O/GR > Rs. 50 Lacs
3. If an eligible assessee opts for Sec 44AD, then he should not get his BOA audited unless the T/O exceeds Rs. 2cr. This increase in limit from 1cr to 2cr of tax audit is only applicable to assessee opting for Sec 44AD. In other words, if the assessee claims that his actual profits are lower than deemed profits, then he has to conduct tax audit.

**Amendment made by Finance Act 2020**

In order to reduce compliance burden on small and medium enterprises, it is proposed to increase the threshold limit for a person carrying on business from one crore rupees to five crore rupees in cases where,

(i) aggregate of all receipts in cash during the previous year does not exceed five per cent of such receipt; and

(ii) aggregate of all payments in cash during the previous year does not exceed five per cent of such payment.

**Due Date:** One month prior to Due Date u/s 139(1).

**Sec 271B: - Penalty for failure to get Accounts Audited**

It is 0.5% of Turnover or Rs. 1,50,000 whichever is lower.

**Expenditure on Issue of Shares & Debentures or other Long Term Borrowings:**

1. It was held in case of Punjab State Industrial Development Corp. Ltd. (SC) that fees paid to ROC for expansion of authorized capital of the Company is directly related to capital Expenditure, hence not allowable.
MISCELLANEOUS ISSUES

(2) It was held that in the case of Brooke Bond India Ltd, expenditure incurred by Co. in connection with a view to increase its share capital is directly related to expansion of capital base of the company and such exp. will be considered as capital expenditure as the benefit from them will be enduring in nature.

(3) It was held in the case of General Insurance Corporation that issuance of bonus shares does not result in any inflow of fresh funds or increase in the capital employed; the capital employed remains same. It is merely capitalization of reserves of company’s fund. Thus, it is revenue in nature.

(4) It was held by Supreme Court in the case of India Cements Ltd that any expenditure incurred for raising loans or debentures is fully allowed as deduction. Therefore, expenses on issue of non convertible as well as convertible bonds/ debentures is allowed as deduction.

(5) It was held in the case of Madras Industrial Investment Corp. that discount on issue of debentures will be allowed as deduction over the life of debentures.

(6) It was held in the case of Kodak India Ltd expenditure incurred on issue of Shares will always be capital in nature. It was further held that, whichever way one looked at it, the object of the assessee was to increase its share capital, whether it did so to continue the business after the RBI directive.

(7) It was held in the case of S.M. Holding & Finance (P) Ltd. (Bom. H.C.)(2009) that premium on redemption of debentures is allowable as deduction and there should not be any argument regarding its certainty.

(8) It was held in the case of ITC Hotels Ltd that expenditure in respect of issue of convertible debentures shall be treated as revenue expenditure, even though it will be converted at a Later Stage.

Alternative View:
However, some courts have held that such expenditure is done for enduring benefits and therefore, nature of such expenditure will be capital and hence, not allowable.

(9) It was held in the case of Mascon Technical Services Ltd that the expenditure on issue of shares will be capital in nature notwithstanding the fact that public issue was not materialize due to non clearance by SEBI.

• All the above 9 judgements are relevant if the case does not fall under Sec 35D.

ALL THE BEST
Chapter 9
Presumptive Incomes

Sec 44AD: - Notwithstanding anything to contrary Contained in Sec 28 to Sec 43C.

<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Individuals, HUF,</td>
<td>Any Business except Sec 44AE &amp; T/O, GR, Sales ≤ 2 Cr.</td>
</tr>
<tr>
<td>Partnership Firm but not an LLP.</td>
<td>All Resident.</td>
</tr>
</tbody>
</table>

Then Deemed profits = 8% of T/O.

Note:
FA 2017 has inserted a new proviso u/s 44AD(1) to provide that deemed profits would be 6% of Total T/O received during the FY or before D/D of filing of Return u/s 139(1) provided it is received by any of the following modes:
1. A/c Payee Cheque
2. A/c Payee Bank Draft
3. Use of ECS
4. such other electronic mode as may be prescribed (Finance Act 2019)

However, the existing rate of 8% would continue to apply in respect of Total T/O received by any other mode.

→ Conditions to get covered u/s 44AD:-
1. Assessee should not claim deduction under the head “Deduction in respect of certain Incomes” i.e. deduction under CH VI A from 80-IA to 80RRB {Profit Linked Deductions}
2. Sec 44AD is not Applicable for certain assessees:-
   → Any profession {Refer 44ADA}
   → Any person earning any income in the nature of commission or brokerage.
   → Any person carrying on any agency business.

→ Notes:-
- Disallowances u/s 40A(3) can’t be made because Sec 44AD over rides Sec 28 to Sec 43C.
Any deduction u/s 30 to 38 shall be deemed to have been already allowed.

The WDV of any asset shall be deemed to have been calculated as if depreciation is actually allowed.

Deduction u/s 80C to Sec 80GGC can be claimed.

Unabsorbed depreciation u/s 32(2) can’t be set off. However, brought forward losses u/s 72 can be set off.

If an assessee claims that his actual profits are lower than deemed profits u/s 44AD, then

- Keep and maintain BOA as per Sec 44AA
- Conduct Tax Audit u/s 44AB.

Note: However above option will have serious consequences from Finance Act 2016 onwards.

Amendments made by Finance Act 2016 in Sec 44AD

1) It is also amended that expenditure in the nature of salary, remuneration, interest etc paid to the partner as per Sec 40(b) shall not be deductible while computing the income u/s 44AD. (Not allowed for 44ADA also but allowed for 44AE)

2) It is also amended that where an eligible assessee declares profit for any previous year in accordance with the provisions of this sec and he declares profit for any of the five consecutive AY’s relevant to the PY succeeding such PY not in accordance with the provision of 44AD, then he shall not be eligible to claim the benefit of this Sec for 5 AY’s subsequent to the AY relevant to the PY in which the profits have not been declared in accordance with the provisions of Sec 44AD. (Same provision also there in Sec 115BBF)

3) The eligible assessee shall be required to pay Advance tax once by 15th March of the Financial year. (Same in sec 44ADA but u/s 44AE pay 4 times)
**Sec 44ADA : Presumptive Income To SPECIFIED Professionals**

A new sec 44ADA is inserted in the Act, to provide for presumptive Income of an assessee who is engaged in any profession which is specified under Sec 44AA(1) such as,

- Legal, Medical, engineering, Architecture, Accountancy, Technical consultancy or interior Decoration or any other profession as notified by BOARD and

Whose gross Receipts does **not exceeds Rs. 50L** in a previous year. Then Deemed profits are **50% of Gross Receipt**.

- This benefit is available to **all Resident assesse**.

- The **restriction of 5 yrs** as applicable in 44AD is not applicable here.

- The eligible assesse shall be **required to pay Advance tax once by 15th March of the Financial year**.

[Rest all same as Sec 44AD]

---

**Sec 44AE:- Deemed income in case of business of plying, hiring or leasing goods carriage**

This Sec is applicable if the assesse does not own more than 10 Goods Carriage at any time during the PY.

**Light Motor Vehicle:** Deemed Income = Rs. 7,500 per month or part of the month per vehicle for no. of months vehicles are owned by the assesse (All whether R or not)

**Heavy Motor Vehicle:** Deemed Income = Rs. 1,000 per ton, per month or part of the month, per vehicle for no. of months vehicles are owned by the assesse. (All whether Resident or Non-Resident)

- Heavy Motor Vehicle = Gross Vehicle weight > 12000 kgs.
- Deduction of remuneration & interest to a Firm is allowed as per sec 40(b). (Not allowed in sec 44AD/ADA)
- Pay Advance Tax 4 Times (In Sec 44AD/ADA it was only once)
- **If an assesse claims that his actual profits are lower than deemed profits u/s 44AE, then**

Keep and maintain BOA u/s 44AA  
Conduct Tax Audit u/s 44AB  

**ALL THE BEST**

CA AARISH KHAN
CHAPTER 27 – PAST QUESTIONS

Note: These are past exam questions taken from the study material of ICAI as updated by Finance Act 2019. As and when the New Finance Act 2020 as well as new ICAI Study Material will be released I will provide you a complete Question Bank with solutions (HARD COPY) as updated by Finance Act 2020. Till then a student can refer these questions for their practice purpose. Once you will get the New Question Bank, there after ignore this chapter from here.

QUESTIONS ON PROFITS & GAINS FROM BUSINESS & PROFESSION

Question 1
Examine critically the following cases in the context of provisions contained in the Income-tax Act, 1961 relevant for Assessment Year 2020-21. Support the answers with relevant case laws and workings.

(a) Mr. Janak is proprietor of M/s. Yash Texnit which is engaged in garment manufacturing business. The entire block of Plant & Machinery chargeable to depreciation @ 15%, has 20 different machinery items as at 31-03-2020. One of the machineries used for packing had become obsolete and was discarded by Mr. Janak in July’19.

Assessee filed its return for A.Y. 2020-21 claiming total depreciation of Rs. 40 lacs which includes Rs. 4 lacs being the depreciation claimed on the machinery item discarded by Mr. Janak. The A.O. disallowed the claim of depreciation of Rs. 4 lacs during the course of scrutiny assessment.

Comment on the validity of action taken by A.O.

(b) X. Ltd. issued debentures in the previous year 2019-20, which were to be matured at the end of 5 years. The debenture holder was given an option of one time upfront payment of Rs. 60 per debenture on account of interest which was to be immediately paid by the company. As per the option exercised by the debenture holders, company paid interest upfront to them in the first year itself and the same was claimed as deduction in the return of the company. But in the accounts, the interest expenditure was shown as deferred expenditure to be written off over a period of five years. During the course of assessment, the Assessing Officer spread the upfront interest paid over a period of five year term of debentures and allowed only one-fifth of the amount in the previous year 2019-20. Examine the correctness of the action of Assessing Officer.

Answer

(a) The issue under consideration is whether disallowance of depreciation made by the Assessing Officer with regard to the discarded asset, in arriving at the written down value of the block of assets, is justified.

One of the conditions for claim of depreciation under section 32 is that the eligible asset must have been put to use for the purpose of business or profession.

The other aspect to considered is whether merely discarding an obsolete machinery, which is physically available, will attract the expression “moneys payable” appearing in section 43(6), so as to deduct its value from the written down value of the block.
The facts in the present case are similar to facts in the case of CIT v. Yamaha Motor India Pvt. Ltd. (2010) 328 ITR 297, wherein the Delhi High Court observed that the expression "used for the purposes of the business" in section 32 when used with respect to discarded machinery would mean the use in the business, not only in the relevant financial year/previous year, but also in the earlier financial years.

The discarded machinery may not be actually used in the relevant previous year but depreciation can be claimed as long as it was used for the purposes of business in the earlier years provided the block continues to exist in the relevant previous year. Therefore, the condition for claiming depreciation in respect of the discarded machine would be satisfied if it was used in the earlier previous years for the business.

For the purpose of section 43(6), “moneys payable” means the sale price, in case of sale, or the insurance, salvage or compensation moneys payable in respect of the asset. In this case, the machinery has not been sold as machinery or scrap or disposed off, and it continues to exist. Hence, there is no “moneys payable” in this case, which alone is deductible while computing the WDV of the block to which it belongs.

Applying the rationale of the above case, the action of the Assessing Officer in disallowing Rs. 4 lakhs, being the depreciation claim attributable to discarded machinery, on the ground that the same was not put to use in the relevant previous year, is invalid, since the said machinery was put to use in the earlier previous years.

(b) The issue under consideration is whether, in a case where debentures are issued with maturity at the end of five years, and the debenture holders are given an option of upfront payment of interest in the first year itself, can the entire upfront interest paid, be claimed as deduction by the company in the first year or should the same be deferred over a period of five years; and would the treatment of such interest as deferred revenue expenditure in the books of account have any impact on the tax treatment.

The facts of the case are similar to the facts in Taparia Tools Ltd. v. JCIT (2015) 372 ITR 605, wherein the above issue came up before the Supreme Court. In that case, it was observed that under section 36(1)(iii), the amount of interest paid in respect of capital borrowed for the purposes of business or profession, is allowable as deduction.

The moment the option for upfront payment was exercised by the subscriber, the liability of X Ltd. to make the payment in that year had arisen. Not only had the liability arisen in the previous year in question, it was even quantified and discharged as well in that very year.

As per the rationale of the Supreme Court ruling in Taparia Tools Ltd.’s case, when the deduction of entire upfront payment of interest is allowable as per the Income-tax Act, 1961, the fact that a different treatment was given in the books of account could not be a factor which would bar the company from claiming the entire expenditure as a deduction.

Accordingly, the action of the Assessing Officer in spreading the upfront interest paid over the five year term of debentures and restricting the deduction in the P.Y.2018-19 to one-fifth of the upfront interest paid is not correct. The company is eligible to claim the entire amount of interest paid upfront as deduction under section 36(1)(iii) in the P.Y.2019-20.
Question 2

Compute the quantum of depreciation available under section 32 of the Income-tax Act, 1961 in respect of the following items of Plant and Machinery purchased by PQR Textile Ltd., by paying through account payee cheque, which is engaged in the manufacture of textile fabrics, for the year ended 31-3-2020:

<table>
<thead>
<tr>
<th>Items purchased after 30th November 2019:</th>
</tr>
</thead>
<tbody>
<tr>
<td>New machinery installed on 1-5-2019</td>
</tr>
<tr>
<td>New Windmill purchased and installed on 18-6-2019.</td>
</tr>
<tr>
<td>Items purchased after 30th November 2019:</td>
</tr>
<tr>
<td>Lorries for transporting goods to sales depots</td>
</tr>
<tr>
<td>Fork-lift-trucks, used inside factory</td>
</tr>
<tr>
<td>Computers installed in office premises</td>
</tr>
<tr>
<td>Computers installed in factory</td>
</tr>
<tr>
<td>New imported machinery</td>
</tr>
</tbody>
</table>

The new imported machinery arrived at Chennai port on 30-03-2020 and was installed on 3-4-2020. All other items were installed during the year ended 31-3-2020.

The company was newly started during the year.

Also, compute the WDV of the various blocks of assets as on 1.4.2020.

Answer

**Computation of depreciation allowance under section 32 for the A.Y. 2020-21**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Normal Depreciation [u/s 32 (1) (ii)]</th>
<th>Additional Depreciation [u/s 32 (1) (iia)]</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>(A) Plant and Machinery (15% block) (Put to use for 180 days or more)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- New machinery installed on 01.05.2019</td>
<td>84.00</td>
<td>84.00</td>
</tr>
<tr>
<td>- Lorries for transporting goods to depots</td>
<td>3.00</td>
<td></td>
</tr>
<tr>
<td>Normal Depreciation @15% &amp; additional depreciation @20%</td>
<td>13.05</td>
<td>16.80</td>
</tr>
<tr>
<td><strong>(B) Plant and Machinery (15% block) (Put to use for less than 180 days – hence, depreciation is restricted to 7.5%, being 50% of 15%)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- Fork-lift trucks, used inside a factory</td>
<td>4.00</td>
<td>4.00</td>
</tr>
<tr>
<td>Normal Depreciation @ 7.5% &amp; additional depreciation @10%</td>
<td>0.30</td>
<td>0.40</td>
</tr>
<tr>
<td><strong>(C) Plant and Machinery (40% block) (Put to use for less than 180 days, hence depreciation restricted to 30%, i.e., 50% of 40%)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- Computers installed in office premises</td>
<td>1.00</td>
<td></td>
</tr>
<tr>
<td>- Computers installed in factory</td>
<td>2.00</td>
<td>2.00</td>
</tr>
<tr>
<td>Normal depreciation @20% &amp; additional depreciation @10%</td>
<td>0.60</td>
<td>0.20</td>
</tr>
<tr>
<td><strong>(D) Plant and Machinery (40% block) (Put to use for 180 days or more)</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

27.3
- New windmill purchased and installed on 18.06.2019  
  Normal Depreciation @ 40% & additional depreciation @ 20%  
  Total depreciation and additional depreciation  
  - Plant and Machinery (15% block) (A +B)  
  - Plant and Machinery (40% block) (C + D)  
  Depreciation available under section 32 = Rs.44.55 crores

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Plant &amp; Machinery</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>15%</td>
</tr>
<tr>
<td>WDV as on 01.04.2019 (The company was started during the year – as given in question)</td>
<td>Nil</td>
</tr>
<tr>
<td>Add: Plant and Machinery acquired during the year</td>
<td></td>
</tr>
<tr>
<td>- New Machinery installed on 01.05.2019</td>
<td>84.00</td>
</tr>
<tr>
<td>- Lorries for transporting goods to sales depots</td>
<td>3.00</td>
</tr>
<tr>
<td>- Fork-lift trucks, used inside factory</td>
<td>4.00</td>
</tr>
<tr>
<td>- New imported machinery</td>
<td>12.00</td>
</tr>
<tr>
<td>- New Windmill purchased and installed on 18.6. 2019</td>
<td></td>
</tr>
<tr>
<td>- Computers installed in office premises</td>
<td></td>
</tr>
<tr>
<td>- Computers installed in factory</td>
<td></td>
</tr>
<tr>
<td></td>
<td>103.00</td>
</tr>
<tr>
<td>Less: Asset sold during the year</td>
<td>Nil</td>
</tr>
<tr>
<td>WDV as on 31.3.2020 (before charging depreciation)</td>
<td>103.00</td>
</tr>
<tr>
<td>Less: Depreciation for the P.Y.2019-20</td>
<td></td>
</tr>
<tr>
<td>- Normal depreciation</td>
<td>13.35</td>
</tr>
<tr>
<td>- Additional depreciation</td>
<td>17.20</td>
</tr>
<tr>
<td>WDV as on 1.4.2020</td>
<td>72.45</td>
</tr>
</tbody>
</table>

Notes:

(1) Windmills and any specially designed devices which run on windmills installed on or after 1.4.2014 would be eligible for depreciation @ 40%.

(2) New imported machinery was not installed during the previous year 2019-20. Hence, it would not be eligible for additional depreciation for A.Y. 2020-21. It would also not be eligible for normal depreciation for A.Y 2020-21, since it was not put to use in the P.Y.2019-20 being the year of acquisition.

(3) It may be noted that investment in the following plant and machinery would not be eligible for additional depreciation under section 32(1)(iia):

(a) Lorries for transporting goods to sales depots, being vehicles/road transport vehicles; and

(b) Computers installed in office premises.

(4) As per section 2(28) of the Motor Vehicles Act, 1988, the definition of a “vehicle” excludes, *inter alia*, a vehicle of special type adopted for use only in a factory or in any enclosed premises. Therefore, fork-lift trucks used inside the factory would not fall within the definition of “vehicle”. Hence, it is eligible for additional depreciation under section 32(1)(iia).
Question 3

(A) Examine the taxability and/or allowability of the following receipts or expenditures under the provisions of the Income-tax Act, 1961, for the assessment year 2020-21:

(i) S Ltd. receives a sum of Rs. 10 lakhs from K Ltd. on 3rd January, 2020 for agreeing not to carry on any business relating to computer software in India for the next three years.

(ii) Secret commission was paid during the previous year 2019-20.

(iii) P Ltd. paid dollars equivalent to Rs. 50 lakhs as sales commission for the year ended 31.03.2020, without deducting tax at source, to Mr. Rodrigues, a citizen of UK and non-resident who acted as agent for booking orders, from various customers who are outside India.

(B) Can the following transactions be covered under section 43B for disallowance?

(i) A bank guarantee given by a company towards disputed tax liabilities.

(ii) Interest payable to Goods and Services Tax Department but not paid before the due date specified in section 139(1).

Answer

(A) (i) As per section 28(va), any sum received under an agreement for not carrying out any activity in relation to any business / profession (i.e., non-compete fee) is chargeable to income-tax under the head “Profits and gains of business or profession”.

Accordingly, Rs. 10 lakhs received by S Ltd. from K Ltd. for agreeing not to carry on any business relating to computer software in India for the next three years is chargeable to income-tax under the head “Profits and gains of business or profession”.

The amount shall be allowed as deduction in the hands of K Ltd. provided tax has been deducted at source under section 194J on the payment so made to S Ltd. If tax is not deducted at source, 30% of the expenditure shall be disallowed under section 40(a)(ia).

(ii) Secret commission is one of the forms of commission payment generally made by business organizations. Secret commission is a payment for obtaining business orders or contracts from parties and /or customers and paid to employees and / or officials of those parties and / or customers or companies from whom business orders are obtained by the assessee.

Explanation 1 below section 37(1) of Income-tax Act, 1961 provides that any expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law, shall not be deemed to have been incurred for the purpose of business and no deduction or allowance shall be made in respect of such expenditure. In view of the Explanation, any expenditure incurred for a purpose which is an offence and prohibited by law cannot be allowed as expenditure. Therefore, if secret commission payment could be established as a payment for an offence prohibited by law, the same cannot be allowed as deduction.

(iii) A foreign agent of an Indian exporter operates in his own country and no part of his income accrues or arises in India. His commission is usually remitted directly to him and is, therefore, not received by him or on his behalf in India. The commission paid to the non-resident agent for services rendered outside India is, thus, not chargeable to tax in India.
Since commission income for booking orders by non-resident who remains outside India is not subject to tax in India, disallowance under section 40(a)(i) is not attracted in respect of payment of commission to such non-resident outside India even though tax has not been deducted at source. Thus, the amount of Rs. 50 lakhs remitted to Mr. Rodrigues outside India in foreign currency towards commission would not attract disallowance under section 40(a)(i) for non-deduction of tax at source.

(B) (i) For claiming deduction of any expense enumerated under section 43B, the requirement is, the actual payment and not deemed payment. Furnishing of bank guarantee cannot be equated with actual payment. Actual payment requires that money must flow from the assessee to the public exchequer as specified in section 43B. Therefore, deduction of an expense covered under section 43B cannot be claimed by merely furnishing a bank guarantee [CIT v. McDowell & Co Ltd (2009) 314 ITR 167 (SC)]

(ii) Interest payable to Goods and Services Tax department is part of Goods and Services Tax. Therefore, interest payable to Goods and Services Tax department, which is not paid before the “due date” of filing of return of income, would attract disallowance under section 43B [Mewar Motors v. CIT (2003) 260 ITR 218 (Raj)]

Question 4

ILT Limited is engaged in manufacturing pipes and tubes. The profit and loss account of the company for the year ended 31st March, 2020 shows a net profit of Rs. 405 lacs. The following information and particulars are furnished to you. You are required to compute total income of the company for Assessment Year 2020-21 indicating reasons for treatment of each item.

(i) A group free air ticket was provided by a supplier for reaching a certain volume of purchase during the financial year 2019-20. The same is encashed by the company for Rs. 10 lacs in April 2019 and credited to General Reserve Account.

(ii) A regular supplier of raw materials agreed for settlement of Rs. 8 lacs instead of Rs. 10 lacs for poor quality of material supplied during the previous year which was not given effect in the running account of the supplier.

(iii) Andhra Bank sanctioned and disbursed a term loan in the financial year 2016-17 for a sum of Rs. 50 lacs. Interest of Rs. 8 lacs was in arrear. The bank has converted the arrear interest into a new loan repayable in 10 equal instalments. During the year, the company has paid 2 instalments and the amount so paid has been reduced from Funded Interest in the Balance Sheet.

(iv) The company remitted Rs. 5 lacs as interest to a company incorporated in USA on a loan taken 2 years ago. Tax deducted under section 195 from such interest has been deposited by the company on 15th July, 2020. The said interest was debited to profit and loss account.

(v) Sandeep, a sales executive stationed at HO at Delhi, was on official tour in Bangalore from 31st May, 2019 to 18th June, 2019 and 28th September, 2019 to 15th October, 2019 for the business development. The company has paid Sandeep's salary in cash, from its local office at Bangalore for the month of May, 2018 (payable on 1st June) and September 2018 (payable on 1st October), amounting to Rs. 45,000 and
Rs. 47,000 respectively (net of TDS and other deduction), as Sandeep has no bank account at Bangalore. These were included in the amount of “salary” debited to Profit and Loss Account.

(vi) The company has contributed Rs. 50,000 by cheque to an electoral trust and the same stands included under the head "General Expenses".

Answer

Computation of total income of ILT Ltd. for the A.Y.2020-21

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.(in lacs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profits and gains from business or profession</td>
<td></td>
</tr>
<tr>
<td>Net profit as per profit and loss account</td>
<td>405.00</td>
</tr>
<tr>
<td>Add : Items debited to profit and loss account, but to be disallowed and items not considered in accounts but to be taxed</td>
<td></td>
</tr>
<tr>
<td>Value of group free air ticket provided by a supplier is taxable as business income under section 28(iv), as the value of any benefit, whether convertible into money or not, arising from business is taxable as business income.</td>
<td>10</td>
</tr>
<tr>
<td>Amount waived by the supplier of raw materials is a deemed income under section 41(1), as the expenditure was allowed as deduction in the last year and there is a benefit by way of remission or cessation of a trading liability. The fact that effect was not given in the running account of supplier is not relevant.</td>
<td>2</td>
</tr>
<tr>
<td>Interest payable outside India to a foreign company is allowable (See Note 1 below)</td>
<td>-</td>
</tr>
<tr>
<td>Contribution to electoral trust is not an allowable expenditure while computing business income. Hence, the same has to be added back, since it is included in general expenses.</td>
<td>0.50</td>
</tr>
<tr>
<td>Salary paid to employee Sandeep is eligible for deduction. Disallowance under section 40A(3) will not apply [See Note 2 below]</td>
<td>NIL 12.50</td>
</tr>
<tr>
<td>Less: Amount of deduction allowable</td>
<td></td>
</tr>
<tr>
<td>Under section 43B, interest on loan due to any scheduled bank, etc. is allowed as deduction, if such interest is actually paid irrespective of the method of accounting followed by the assessee. Conversion of arrear interest into a fresh loan by a bank cannot be considered as actual payment of interest. However, the amount of funded interest (i.e., converted loan) actually paid is allowable as deduction. Hence, Rs. 1,60,000, being two installments of Rs. 80,000 each, actually paid is deductible.</td>
<td>1.60</td>
</tr>
<tr>
<td>Business Income</td>
<td>415.90</td>
</tr>
<tr>
<td>Gross total income</td>
<td>415.90</td>
</tr>
<tr>
<td>Less: Deduction under Chapter VI-A</td>
<td></td>
</tr>
<tr>
<td>Deduction under section 80GGB in respect of contribution by the assessee company to an electoral trust.</td>
<td>0.50</td>
</tr>
<tr>
<td>Total Income</td>
<td>415.40</td>
</tr>
</tbody>
</table>

Notes:
1. Since tax has been deducted on interest payable outside India to a foreign company during the previous year 2019-20 and the same has been deposited before the due date of filing return of income under section 139(1), disallowance under section
40(a)(i) is not attracted. Since the interest has already been debited to profit and loss account, no further adjustment is required.

2. In respect of payment of salary to sales executive in cash, no disallowance under section 40A(3) is to be made as the payments fall within the scope of Rule 6DD(i). Salary paid to him in cash is allowable as the executive was temporarily posted for a continuous period of more than 15 days in Bangalore which is not the place of his normal duty. Further tax was deducted from such salary under section 192 and he does not maintain any bank account in Bangalore. No disallowance under section 40A(3) is attracted in respect of such salary.

Question 5

G Ltd. is engaged in the business of growing and manufacturing tea in India. For the previous year ended 31.03.2019, its composite business profits before allowing deduction u/s 33AB is Rs. 60,00,000. On 01.09.2019, it deposited a sum of Rs. 11,00,000 in the Tea Development Account. During the previous year 2017-18, G Ltd. had incurred a business loss of Rs. 14,00,000 which has been carried forward. On 25.01.2020, it withdrew Rs. 10 lakhs, from deposit account which is utilized as under:

- Rs. 6,00,000 for purchase on non-depreciable asset as per the scheme specified.
- Rs. 3,00,000 for purchase of machinery to be installed in the office premises.
- Rs. 1,00,000 was spent for the purpose of scheme on 05.04.2020.

(i) You are required to determine business income of G Ltd. and the tax consequences that may arise from the above transactions in the relevant assessment year.

(ii) What will be the consequence if the asset which was purchased for Rs. 6,00,000 is sold for Rs. 8,00,000 in April, 2020.

Answer

(i) Computation of Business Income of G Ltd. for the A.Y. 2020-21

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs. 10,00,000 being the amount withdrawn from Tea Development Account has to be utilized in the prescribed manner, otherwise, the withdrawn amount would be chargeable to tax as business income. In the given case, the taxability of withdrawal amount based on their utilization is as follows:</td>
<td>Not taxable</td>
</tr>
<tr>
<td>- Rs. 6,00,000, out of the amount withdrawn from the deposit account, utilised for purchase of non-depreciable asset as per the specified scheme. [As per section 33AB(6), no deduction would be allowed under section 33AB since amount is spent out of Rs. 11 lakh deposited in Tea Development Account, which has already been allowed as deduction in A.Y.2019-20 (See Working Note below)].</td>
<td></td>
</tr>
<tr>
<td>- Rs. 3,00,000, being the amount utilized for purchase of machinery to be installed in the office premises is not a permissible utilization. Hence, the amount would be deemed as profits and gains of business of the previous year 2019-20 as per section 33AB(4).</td>
<td>3,00,000</td>
</tr>
<tr>
<td>- Rs. 1,00,000 was spent for the purpose of scheme on 05.04.2020. As per section 33AB(7), this amount would be taxable since the same is not utilized during the same previous year (i.e., P.Y. 2019-</td>
<td>1,00,000</td>
</tr>
</tbody>
</table>
(20) in which the amount is withdrawn from the deposit account.

When any part of withdrawal amount becomes taxable, the agricultural and non-agricultural portions of income must be segregated.

Accordingly, Rs. 1,60,000, being 40% of Rs. 4,00,000 (Rs. 3,00,000 + Rs. 1,00,000) would be chargeable to tax as business income and the balance Rs. 2,40,000, being 60% of Rs. 4,00,000 would be agricultural income exempt from tax.

Working Note:

**Computation of Business Income of G Ltd. for the A.Y. 2019-20**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Composite business profits before allowing deduction under section 33AB</td>
<td>60,00,000</td>
</tr>
<tr>
<td><strong>Less:</strong> Deduction under section 33AB(1) would be the lower of:</td>
<td></td>
</tr>
<tr>
<td>- Amount deposited in Tea Development Account on or before 30.9.2019 [i.e., Rs. 11,00,000]</td>
<td>11,00,000</td>
</tr>
<tr>
<td>- 40% of profits of such business [i.e., Rs. 24,00,000, being 40% of Rs. 60,00,000]</td>
<td></td>
</tr>
<tr>
<td><strong>Less:</strong> 60% of Rs. 49,00,000, being agricultural income [as per Rule 8]</td>
<td>29,40,000</td>
</tr>
<tr>
<td>Business income</td>
<td>19,60,000</td>
</tr>
<tr>
<td><strong>Less:</strong> Brought forward business loss of A.Y.2018-19 set-off as per section 72</td>
<td>14,00,000</td>
</tr>
<tr>
<td>Business income chargeable to tax</td>
<td>5,60,000</td>
</tr>
</tbody>
</table>

(ii) **Consequences, if asset purchased out of deposit account is sold during the previous year 2020-21**

As per section 33AB(8), if the asset is sold before the expiry of eight years from the end of the previous year in which it was acquired, then, the cost of such asset shall be deemed to be the profits and gains from business or profession of the previous year in which asset is sold.

Therefore, Rs. 6,00,000 would be deemed to be the business income (composite) for the A.Y.2021-22. However, since the full cost of the asset was deducted in the assessment year 2019-20 (being part of Rs. 11 lakh deposited in Tea Development Account) before segregation of agricultural income and non-agricultural income, the agricultural and non-agricultural portions of income should be segregated in the year in which such amount becomes taxable on account of sale of asset before the expiry of eight years. Therefore, Rs. 3,60,000, being 60% of Rs. 6,00,000 would represent agricultural income. The balance Rs. 2,40,000 being 40% of Rs. 6,00,000 would be chargeable to tax as business income.

Moreover, the difference between the sale consideration and purchase price of the asset would be chargeable to tax as “Short term capital gains”, which is computed as follows:

| Sales consideration                             | 8,00,000 |
| **Less:** Cost of acquisition                   | 6,00,000 |
| **Short term capital gain**                     | 2,00,000  |
Question 6

The trading and profit and loss account of Pingu Trading Pvt. Ltd. having business of agricultural produce, consumer items and other products for the year ended 31.03.2020 is as under:

**Trading Account**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Stock</td>
<td>3,75,000</td>
<td>Sales</td>
<td>1,55,50,000</td>
</tr>
<tr>
<td>Purchases</td>
<td>1,25,75,000</td>
<td>Closing Stock</td>
<td>4,50,000</td>
</tr>
<tr>
<td>Freight &amp; Cartage</td>
<td>1,26,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gross profit</td>
<td>29,24,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,60,00,000</td>
<td></td>
<td>1,60,00,000</td>
</tr>
</tbody>
</table>

**Profit and Loss Account**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bonus to staff</td>
<td>47,500</td>
<td>Gross profit</td>
<td>29,24,000</td>
</tr>
<tr>
<td>Rent of premises</td>
<td>53,500</td>
<td>Income-tax refund</td>
<td>20,000</td>
</tr>
<tr>
<td>Advertisement</td>
<td>5,000</td>
<td>Warehousing charges</td>
<td>15,00,000</td>
</tr>
<tr>
<td>Bad Debts</td>
<td>75,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest on loans</td>
<td>1,67,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depreciation</td>
<td>71,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Goods and Services tax demand paid</td>
<td>1,08,350</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Miscellaneous expenses</td>
<td>5,25,650</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net profit of the year</td>
<td>33,90,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>44,44,000</td>
<td></td>
<td>44,44,000</td>
</tr>
</tbody>
</table>

On scrutiny of records, the following further information and details were extracted/gathered:

(i) There was a survey under section 133A on the business premises on 31.3.2020 in which it was revealed that the value of closing stocks of 31.3.2019 was Rs. 8,75,000 and a sale of Rs. 75,000 made on 13.3.2020 was not recorded in the books. The value of closing stocks after considering these facts and on the basis of inventory prepared by the department as on 31.3.2020 worked out at Rs. 12,50,000, which was accepted to be correct and not disputed.

(ii) Income-tax refund includes amount of Rs. 4,570 of interest allowed thereon.

(iii) Bonus to staff includes an amount of Rs. 7,500 paid in the month of December 2019, which was provided in the books on 31.03.2019.

(iv) Rent of premises includes an amount of Rs. 5,500 incurred on repairs. The assessee was under no obligation to incur such expenses as per rent agreement.

(v) Advertisement expenses include an amount of Rs. 2,500 paid for advertisement published in the souvenir issued by a political party. The payment is made by way of an account payee cheque.

(vi) Miscellaneous expenses include:

(a) amount of Rs. 15,000 paid towards penalty for non-fulfillment of delivery conditions of a contract of sale for the reasons beyond control,

(b) amount of Rs. 1,00,000 paid to the wife of a director, who is working as junior lawyer for taking an opinion on a disputed matter. The junior advocate of High Courts normally charge only Rs. 25,000 for the same opinion,

(c) amount of Rs. 1,00,000 paid to an Electoral Trust by cheque.
(vii) Goods and Services Tax demand paid includes an amount of Rs. 5,300 charged as penalty for delayed filing of returns and Rs. 12,750 towards interest for delay in deposit of tax.

(viii) The company had made an investment of Rs. 25 lacs on the construction of a warehouse in rural area for the purpose of storage of agricultural produce. This was made available for use from 15.09.2019 and the income from this activity is credited in the Profit and Loss account under the head “Warehousing charges”.

(ix) Depreciation under the Income-tax Act, 1961 works out at Rs.65,000.

(x) Interest on loans includes an amount of Rs. 80,000 on which tax was not deducted.

Compute the income chargeable to tax for assessment year 2020-21 of Pingu Trading Pvt. Ltd, ignoring MAT. Support your answer with working notes.

**Answer**

Computation of Income of Pingu Trading Pvt. Ltd. chargeable to tax for the A.Y. 2020-21

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net profit as per profit and loss account</td>
<td>33,90,000</td>
</tr>
<tr>
<td><strong>Add:</strong> Difference in the value of stocks detected on survey under section 133A on 31.03.2020 chargeable as income <strong>(See Note 1)</strong></td>
<td>3,75,000</td>
</tr>
<tr>
<td><strong>Less:</strong> Income-tax refund credited in the profit and loss account, out of which interest is to be considered separately under the head “Income from other sources”</td>
<td>20,000</td>
</tr>
<tr>
<td><strong>Add:</strong> Expenses either not allowable or to be considered separately but charged in the profit &amp; loss account</td>
<td>37,45,000</td>
</tr>
<tr>
<td>Repair expenses on rented premises where assessee is under no obligation to incur such expenses are not allowable as per section 30(a)(i). However, if such expenses are required for carrying on the business efficiently, the same are allowable under section 37. In this case, assuming that such expenses are required for carrying on business efficiently, the same are allowable under section 37. Advertisement in the souvenir of political party not allowable as per section 37(2B) <strong>(See Note 3)</strong></td>
<td>2,500</td>
</tr>
<tr>
<td>Payment made to the wife of a director examined as per section 40A(2) and the excess payment made to be disallowed <strong>(See Note 5)</strong></td>
<td>75,000</td>
</tr>
<tr>
<td>Payment made to electoral trust by cheque <strong>(See Note 6)</strong></td>
<td>1,00,000</td>
</tr>
<tr>
<td>Penalty levied by the Goods and Services tax department for delayed filing of returns not allowable as being paid for infraction of law <strong>(See Note 7)</strong></td>
<td>5,300</td>
</tr>
<tr>
<td>Depreciation as per books</td>
<td>71,500</td>
</tr>
<tr>
<td>30% of interest paid on loan without deduction of tax at source not allowable as per section 40(a)(ia)</td>
<td>24,000</td>
</tr>
<tr>
<td><strong>Less:</strong> Depreciation allowable as per Income-tax Act, 1961</td>
<td>65,000</td>
</tr>
<tr>
<td><strong>Less:</strong> Income from specified business (warehousing charges) credited to profit and loss account, to be considered separately <strong>(See Note 8)</strong></td>
<td>15,00,000</td>
</tr>
<tr>
<td>Income from business (other than specified business)</td>
<td>24,58,300</td>
</tr>
</tbody>
</table>
Computation of income / loss from specified business (See Note 8)

Income from specified business \(Rs.\ 15,00,000\)

Less: Deduction under section 35AD @ 100\% of Rs. 25 lakhs \(Rs.\ 25,00,000\)

Loss from specified business to be carried forward as per section 73A \(10,00,000\)

Income from Other Sources

Interest on income-tax refund \(4,570\)

Gross Total Income \(24,62,870\)

Less: Deduction under section 80GGB

Contribution to political party (See Note 3) \(Rs.\ 2,500\)

Contribution to an Electoral trust (See Note 7) \(Rs.\ 1,00,000\)

1,02,500

Total Income \(23,60,370\)

Notes:

1) The business premises were surveyed and differences in the figures of opening and closing stocks and sales were found which have not been disputed and accepted by the assessee. Therefore, the trading account for the year is to be re-cast to arrive at the correct amount of the gross profit/ net profit for the purpose of return of income to be filed for the previous year ended on 31.3.2020.

Revised Trading Account

<table>
<thead>
<tr>
<th>Particular</th>
<th>Rs.</th>
<th>Particular</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Stock</td>
<td>8,75,000</td>
<td>Sales</td>
<td>1,56,25,000</td>
</tr>
<tr>
<td>(Rs. 1,55,50,000 + Rs. 75,000)</td>
<td></td>
<td>Closing Stock</td>
<td>12,50,000</td>
</tr>
<tr>
<td>Purchases</td>
<td>1,25,75,000</td>
<td>Freight and Cartage</td>
<td>1,26,000</td>
</tr>
<tr>
<td>Freight and Cartage</td>
<td>1,26,000</td>
<td>Gross Profit</td>
<td>32,99,000</td>
</tr>
<tr>
<td></td>
<td>1,68,75,000</td>
<td></td>
<td>1,68,75,000</td>
</tr>
</tbody>
</table>

The difference of gross profit of \(Rs.\ 32,99,000 - Rs.\ 29,24,000 = Rs.\ 3,75,000\) is to be added as income of the business for the year.

2) Bonus for the previous year 2018-19 paid after the due date for filing return for that year would have been disallowed under section 43B for the P.Y.2018-19. However, when the same has been paid in December 2019, it should be allowed as deduction in the P.Y.2019-20(A.Y. 2020-21). Since it is already included in the figure of bonus to staff debited to profit and loss account of this year, no further adjustment is required.

3) The amount of \(Rs.\ 2,500\) paid for advertisement in the souvenir issued by a political party attracts disallowance under section 37(2B). However, such expenditure falls within the meaning assigned to “contribute” under section 293A of the Companies Act, 1956, and is hence, eligible for deduction under section 80GGB. Any contribution to the political party or electoral trust made by way of cash is not allowed as deduction under section 80GGB. Since in the present case, the payment to the political party is made by way of an account payee cheque, it is allowed as deduction under section 80GGB.

4) The penalty of \(Rs.\ 15,000\) paid for non-fulfilment of delivery conditions of a contract for reasons beyond control is not for the breach of law but was paid for breach of contractual obligations and therefore, is an allowable expense.

5) It has been assumed that \(Rs.\ 25,000\) is the reasonable payment for the wife of Director, working as a junior lawyer, since junior advocates of High Courts normally
charge only Rs. 25,000 for the same opinion and therefore, the balance Rs. 75,000 has been disallowed.

(6) Payment to an electoral trust qualifies for deduction under section 80GGB since the payment is made by way of a cheque. However, since the amount has been debited to profit and loss account, the same has to be added back for computing business income.

(7) The interest of Rs. 12,750 paid on the delayed deposit of goods and services tax is for breach of contract and hence, is allowable as deduction. However, penalty of Rs. 5,300 for delay in filing of returns is not allowable since it is for breach of law.

(8) Deduction @ 100% of the capital expenditure is available under section 35AD in respect of specified business of setting up and operating a warehouse facility for storage of agricultural produce which commences operation on or after 1.04.2012. It is presumed that Rs. 25 lacs does not include expenditure on acquisition of any land.

The loss from specified business under section 35AD (warehousing) should be segregated from the income from other businesses, since, as per section 73A(1), any loss computed in respect of any specified business referred to in section 35AD shall not be set off except against profits and gains, if any, of any other specified business.

In view of the provisions of section 73A(1), the loss of Rs. 10 lacs from the specified business cannot be set-off against income from other businesses. Such loss has to be carried forward to be set-off against profit from specified business in the next assessment year. The return should be filed on or before the due date under section 139(1) for carry forward of such losses.

Question 7

(a) A Ltd. paid IDBI (a public financial institution) a lump sum pre-payment premium of Rs. 1.2 lacs on 7.4.2019 for restructuring its debts and reducing its rate of interest. It claimed the entire sum as business expenditure for the P.Y. 2019-20. The Assessing Officer, however, held that the pre-payment premium should be amortised over a period of 10 years (being the tenure of the restructured loan), and thus, allowed only 10% of the pre-payment premium in the P.Y.2019-20. Discuss, with reasons, whether the contention of A Ltd. is correct or that of the Assessing Officer.

(b) Explain the tax treatment of emergency spares (of plant and machinery) acquired during the year which, even though kept ready for use, have not actually been used during the relevant previous year.

Answer

(a) This issue came up before the Delhi High Court in CIT v. Gujarat Guardian Ltd (2009) 177 Taxman 434. The Court observed that the assesse company’s claim for deduction has to be allowed in one lump sum keeping in view the provisions of section 43B(d), which provide that any sum payable by the assessee as interest on any loan or borrowing from any financial institution shall be allowed to the assessee in the year in which the same is paid, irrespective of the periods, in which the liability to pay such sum is incurred by the assessee according to the method of accounting regularly followed by the assessee. The High Court concurred with the Tribunal’s view supporting the assessee that in terms of section 36(1)(iii) read with section 2(28A), the deduction for pre-payment
premium was allowable. Since there was no dispute that the pre-payment premium was nothing but interest and that it was paid to a public financial institution i.e. IDBI, the Court held that, in terms of section 43B(d), the assessee’s claim for deduction has to be allowed in the year in which the payment has actually been made.

Therefore, applying the ratio of the above case, the contention of A Ltd. is correct and not that of the Assessing Officer.

Note – Section 36(1)(iii) provides for deduction of interest paid in respect of capital borrowed for the purposes of business or profession. Section 2(28A) defines interest to include, inter alia, any other charge in respect of the moneys borrowed or debt incurred. Section 43B provides for certain deductions to be allowed only on actual payment. From a combined reading of these three sections, it can be inferred that –

(i) pre-payment premium represents interest as per section 2(28A);
(ii) such interest is deductible as business expenditure as per section 36(1)(iii);
(iii) such interest is deductible in one lump-sum on actual payment as per section 43B(d).

(b) As per ICDS V on Tangible Fixed Assets, machinery spares shall be charged to the revenue as and when consumed. When such spares can be used only in connection with an item of tangible fixed asset and their use is expected to be irregular, they shall be capitalised. Where the spares are capitalised as per the above requirement, the issue as to provision of depreciation arises – whether depreciation can be provided where such spares are kept ready for use or is it necessary that they are actually put to use. This issue was dealt with by the Delhi High Court in CIT v. Insilco Ltd (2010) 320ITR 322. The Court observed that the expression “used for the purposes of business” appearing in section 32 also takes into account emergency spares, which, even though ready for use, yet are not consumed or used during the relevant period. This is because these spares are specific to a fixed asset, namely plant and machinery, and form an integral part of the fixed asset. These spares will, in all probability, be useless once the asset is discarded and will also have to be disposed of. In this sense, the concept of passive use which applies to standby machinery will also apply to emergency spares. Therefore, once the spares are considered as emergency spares required for plant and machinery, the assessee would be entitled to capitalize the entire cost of such spares and claim depreciation thereon.

Note – One of the conditions for claim of depreciation is that the asset must be “used for the purpose of business or profession”. In the past, courts have held that, in certain circumstances, an asset can be said to be in use even when it is “kept ready for use”. For example, depreciation can be claimed by a transport company on spare engines kept in store in case of need, though they have not actually been used by the company. Hence, in such cases, the term “use” embraces both active use and passive use for business purposes.

Question 8

“Easy Call Ltd.”, to provide telecom services in Mumbai, obtained a licence on 1.4.2017 for a period of 10 years ending on 31.3.2027 against a fee of Rs. 27 lacs to be paid in 3 installments of Rs. 9 lacs each by April, 2017, April, 2018 and April, 2019, respectively. The company has commenced business on 1.5.2018.
Explain, how the payment made for licence fee shall be dealt with under the Income-tax Act, 1961 and the amount, if any, deductible for A.Y. 2020-21.

**Answer**
The payment made for acquiring the licence to operate telecom services in Mumbai shall be subject to deduction as per the scheme in section 35ABB. As per section 35ABB, any amount actually paid for obtaining licence to operate telecommunication services shall be allowed as deduction in equal instalments during the number of years for which the license is in force.

**If the payment is made before the commencement of business:** The deduction shall be allowed beginning with the year of commencement of business.

**In any other case:** It will be allowed commencing from the year of payment. Deduction shall be allowed up to the year in which the license shall cease to be in force.

The amount of deduction available for A.Y. 2020-21 is worked out below:-

<table>
<thead>
<tr>
<th>(1) Previous year of payment</th>
<th>(2) Unexpired period of license</th>
<th>(3) Instalment paid (Rs.)</th>
<th>(4) = (3)/(2) Deduction in respect of each instalment (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2017-18</td>
<td>9 years</td>
<td>9,00,000</td>
<td>1,00,000</td>
</tr>
<tr>
<td>2018-19</td>
<td>9 years</td>
<td>9,00,000</td>
<td>1,00,000</td>
</tr>
<tr>
<td>2019-20</td>
<td>8 years</td>
<td>9,00,000</td>
<td>1,12,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td><strong>27,00,000</strong></td>
<td><strong>3,12,500</strong></td>
</tr>
</tbody>
</table>

The deduction under section 35ABB from assessment year 2020-21 shall be Rs. 3,12,500.

**Question 9**
Alpha Ltd., a manufacturing company, has disclosed a net profit of Rs. 12.50 lacs for the year ended 31st March, 2020. You are required to compute the taxable income of the company for the Assessment year 2020-21, after considering the following information, duly explaining the reasons for each item of adjustment:

(i) Advertisement expenditure debited to profit and loss account includes the sum of Rs. 60,000 paid in cash to the sister concern of a director, the market value of which is Rs. 52,000.

(ii) Repairs of plant and machinery debited to profit and loss account includes Rs. 1.80 lacs towards replacement of worn out parts of machineries. Such expenditure does not increase the future benefit from the asset beyond its previously assessed standard of performance.

(iii) A sum of Rs. 6,000 on account of liability foregone by a creditor has been taken to general reserve. The original purchases was debited to the Profit & Loss Account in the A.Y. 2015-16.

(iv) Sale proceeds of import entitlements amounting to Rs. 1 lac has been credited to Profit & Loss Account, which the company claims as capital receipt not chargeable to income-tax.

(v) Being also engaged in the biotechnology business, the company incurred the following expenditure on in-house research and development as approved by the prescribed authority:

(a) Research equipments purchased Rs. 1,50,000.

(b) Remuneration paid to scientists Rs. 50,000.
The total amount of Rs. 2,00,000 is debited to the profit and loss account.

Answer

Computation of taxable income of Alpha Ltd. for the A.Y.2020-21

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net profit as per profit and loss account</td>
<td>12,50,000</td>
</tr>
<tr>
<td><strong>Add: Items debited to profit and loss A/c but not deductible or income to be taxed</strong></td>
<td></td>
</tr>
<tr>
<td>1. Payment of advertisement expenditure of Rs.60,000</td>
<td></td>
</tr>
<tr>
<td>(i) Rs. 8,000, being the excess payment to a relative disallowed under section 40A(2)</td>
<td>8,000</td>
</tr>
<tr>
<td>(ii) As the payment is made in cash and since the remaining amount of Rs. 52,000 exceeds Rs. 10,000, 100% shall be disallowed under section 40A(3)</td>
<td>52,000</td>
</tr>
<tr>
<td>2. Under section 31, expenditure relatable to current repairs regarding plant, machinery or furniture is allowed as deduction. The test to determine whether replacement of parts of machinery amounts to repair or renewal is whether the replacement is one which is in substance replacement of defective parts or replacement of the entire machinery or substantial part of the entire machinery [CIT v. Darbhanga Sugar Co. Ltd. [1956] 29 ITR 21 (Pat)]. Here expenditure on repairs does not bring in any new asset into existence. Such replacement can only be considered as current repairs. Hence, no adjustment is required. Further, as per ICDS V on Tangible Fixed Assets, only an expenditure that increases the future benefits from the existing asset beyond its previously assessed standard of performance has to be added to the actual cost.</td>
<td></td>
</tr>
<tr>
<td>3. Liability foregone by creditor chargeable as business income but not credited to profit and loss account [taxable under section 41(1)]</td>
<td>6,000</td>
</tr>
<tr>
<td>4. Sale proceeds of import entitlements. The sale of the rights gives rise to profits or gains taxable under section 28(iii.a). As the amount has already been credited to profit and loss account, no further adjustment is necessary.</td>
<td></td>
</tr>
<tr>
<td><strong>Less: Amount not debited to profit and loss account but allowable as deduction</strong></td>
<td></td>
</tr>
<tr>
<td>5. Expenditure on in-house research and development is entitled to a weighted deduction of 150% of the expenditure (both capital and revenue) so incurred under section 35(2AB)(1) = Rs. 2 lacs × 150% = Rs.3 lacs</td>
<td></td>
</tr>
<tr>
<td>Expenditure of Rs. 2,00,000 has already been debited to Profit &amp; Loss Account, therefore only additional deduction of Rs. 1 lacs further to be allowed</td>
<td>1,00,000</td>
</tr>
<tr>
<td><strong>Taxable Income</strong></td>
<td>12,16,000</td>
</tr>
</tbody>
</table>

Question 10

(i) A corporation was set up by the State Government transferring all the buses owned by it for a consideration of Rs. 75 lacs, which was discharged by the Corporation by issue of equity shares. The Corporation in its assessment claimed depreciation.
Can the depreciation be denied in the Corporation’s hands on the ground that there was no registration of the buses in favour of the Corporation?

(ii) Ravi succeeded to his father’s business in the year 2017. In the previous year ended 31.3.2020, Ravi has written off the balance in the name of ‘Y’ which relates to supply made by his father, when he carried on business. Ravi desires to know whether the write off could be eligible for deduction.

Answer

(i) The decision of the Supreme Court in Mysore Minerals Ltd v. CIT (1999) 239 ITR 775 is relevant in the context of the facts stated. The term “asset used” in section 32 must be assigned a wider meaning and anyone in possession of property in his own title, exercising dominion over the property, to the exclusion of others and having the right to use and enjoy it, must be taken to be the owner.

Registration of the buses is only a formality to perfect the title and does not bar enjoyment. The Corporation cannot, therefore, be denied depreciation on the buses. A similar decision was also taken in CIT v. J & K Tourism Development Corporation (2001) 114 Taxman 734 (J&K).

(ii) The deduction of bad debt is allowed if it is written off in the books of account of the assessee. In this case, Ravi has succeeded to the business carried on by his father. Under clause (vii) of section 36(1) the amount has been written off in the books of account as irrecoverable is eligible for deduction provided the debt has been taken into account in computing the income of the business in an earlier previous year [vide section 36(2)].

Therefore, Ravi is eligible for deduction in respect of the amount due in the name of Y which is written off in the books of account as bad debt, even though the debt represents the amount due for the supplies made by previous owner viz. deceased father of Ravi. [CIT v. T. Veerabhadra Rao, K. Koteswara Rao and Co (1985) 155 ITR 152 (SC)].

Question 11

Boat Club is an association governed by the provisions of Section 44A of the Income-tax Act, 1961. The subscription received from members for the year ended 31st March, 2020 was Rs. 2,00,000. The expenditures in the normal course of its activities were Rs. 3,85,000. Its other income taxable under the Act works out to Rs. 2,75,000. You are consulted as to how Boat Club’s income would be determined for assessment year 2020-21?

Answer

As per section 44A, the deficiency arising on account of income from members by way of, inter alia, subscriptions, falling short of the expenditure incurred solely for the protection or advancement of the interest of its members, shall first be set off against the association’s income under the head “Profits and gains of Business or Profession”. If there is no such income under this head, the deficiency shall be set off against income under any other head.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income from subscription</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Less: Expenses incurred in the course of its activities</td>
<td>3,85,000</td>
</tr>
<tr>
<td>Deficiency</td>
<td>(-)1,85,000</td>
</tr>
</tbody>
</table>
Past Questions                             AJ Education NeXt

| Other income | 2,75,000 |
| Less: Deficiency Rs.1,85,000 but limited to 50% of other income | 1,37,500 |
| **Income of the Association** | **1,37,500** |

There is a ceiling on the deduction admissible by way of deficiency being that it shall not exceed one-half of the total income of the association computed before making any allowance under this section. This ceiling has been exceeded above and the deficiency hence is limited to **Rs. 1,37,500** being one-half of **Rs. 2,75,000** [vide section 44A(3)].

**Question 12**

*X Ltd. set up a manufacturing unit in Warangal in the state of Telangana on 01.06.2019. It invested Rs. 30 crore in new plant and machinery on 1.6.2019. Further, it invested Rs. 25 crore in the plant and machinery on 01.11.2019, out of which Rs. 5 crore was second hand plant and machinery. Compute the depreciation allowable under section 32. Is X Ltd. entitled for any other benefit in respect of such investment? If so, what is the benefit available?*

**Solution**

(i) **Computation of depreciation under section 32 for X Ltd. for A.Y. 2020-21**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs. (in crores)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Plant and machinery acquired on 01.06.2019</td>
<td>30,000</td>
</tr>
<tr>
<td>Plant and machinery acquired on 01.11.2019</td>
<td>25,000</td>
</tr>
<tr>
<td><strong>WDV as on 31.03.2020</strong></td>
<td><strong>55,000</strong></td>
</tr>
<tr>
<td>Less: Depreciation @ 15% on Rs. 30 crore</td>
<td>4,500</td>
</tr>
<tr>
<td>Depreciation @ 7.5% (50% of 15%) on Rs. 25 crore</td>
<td>1,875</td>
</tr>
<tr>
<td>Additional Depreciation@35% on Rs. 30 crore</td>
<td>10,500</td>
</tr>
<tr>
<td>Additional Depreciation@17.5% (50% of 35%) on Rs. 20 crore</td>
<td>3,500</td>
</tr>
<tr>
<td><strong>WDV as on 01.04.2020</strong></td>
<td><strong>34,625</strong></td>
</tr>
</tbody>
</table>

(ii) **Computation of deduction under section 32AD for X Ltd. for A.Y. 2020-21**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs. (in crores)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deduction under section 32AD @ 15% on Rs. 50 crore</td>
<td>7.50</td>
</tr>
<tr>
<td><strong>Total benefit</strong></td>
<td><strong>7.50</strong></td>
</tr>
</tbody>
</table>

**Notes:**

1. As per the second proviso to section 32(1)(ii), where an asset acquired during the previous year is put to use for less than 180 days in that previous year, the amount deduction allowable as normal depreciation and additional depreciation would be restricted to 50% of amount computed in accordance with the prescribed percentage.

Therefore, normal depreciation on plant and machinery acquired and put to use on 1.11.2019 is restricted to 7.5% (being 50% of 15%) and additional depreciation is restricted to 17.5% (being 50% of 35%).

2. The balance additional depreciation of Rs. 3.5 crore, being 50% of Rs. 7 crore (35% of Rs. 20 crore) would be allowed as deduction in the A.Y.2021-22.

3. As per section 32(1)(iia), additional depreciation is allowable in the case of any new machinery or plant acquired and installed after 31.3.2005 by an assessee engaged, *inter alia*, in the business of manufacture or production of any article or thing. In this case, since new plant and machinery acquired was installed by a manufacturing unit set up in a notified backward area in the State of Telengana, the
rate of additional depreciation is 35% of actual cost of new plant and machinery. Since plant and machinery of Rs. 20 crore was put to use for less than 180 days, additional depreciation@17.5% (50% of 35%) is allowable as deduction. However, additional depreciation shall not be allowed in respect of second hand plant and machinery of Rs. 5 crore.

Likewise, the benefit available under sections 32AD would not be allowed in respect of second hand plant and machinery.

Accordingly, additional depreciation and investment allowance under section 32AD have not been provided on Rs. 5 crore, being the actual cost of second hand plant and machinery acquired and installed in the previous year.

**Question 13**

A Ltd., engaged in the business of manufacturing, furnishes the following particulars for the P.Y.2019-20. Compute the deduction allowable under section 35 for A.Y.2020-21, while computing its income under the head “Profits and gains of business or profession”.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Amount paid to Indian Institute of Science, Bangalore, for scientific research</td>
<td>1,00,000</td>
</tr>
<tr>
<td>2. Amount paid to IIT, Delhi for an approved scientific research programme</td>
<td>2,50,000</td>
</tr>
<tr>
<td>3. Amount paid to X Ltd., a company registered in India which has as its main object scientific research and development, as is approved by the prescribed authority</td>
<td>4,00,000</td>
</tr>
<tr>
<td>4. Expenditure incurred on in-house research and development facility as approved by the prescribed authority</td>
<td></td>
</tr>
<tr>
<td>(a) Revenue expenditure on scientific research</td>
<td>3,00,000</td>
</tr>
<tr>
<td>(b) Capital expenditure (including cost of acquisition of land Rs. 5,00,000) on scientific research</td>
<td>7,50,000</td>
</tr>
</tbody>
</table>

**Solution**

**Computation of deduction under section 35 for the A.Y.2020-21**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Section</th>
<th>% of weighted deduction</th>
<th>Amount of deduction (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payment for scientific research</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Indian Institute of Science</td>
<td>1,00,000</td>
<td>35(1)(ii)</td>
<td>150%</td>
<td>1,50,000</td>
</tr>
<tr>
<td>IIT, Delhi</td>
<td>2,50,000</td>
<td>35(2AA)</td>
<td>150%</td>
<td>3,75,000</td>
</tr>
<tr>
<td>X Ltd.</td>
<td>4,00,000</td>
<td>35(1)(iia)</td>
<td>100%</td>
<td>4,00,000</td>
</tr>
<tr>
<td>Expenditure incurred on in-house research and development facility</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue expenditure</td>
<td>3,00,000</td>
<td>35(2AB))</td>
<td>150%</td>
<td>4,50,000</td>
</tr>
<tr>
<td>Capital expenditure (including cost of acquisition of land Rs. 5,00,000)</td>
<td>2,50,000</td>
<td>35(2AB)</td>
<td>150%</td>
<td>3,75,000</td>
</tr>
<tr>
<td><strong>Deduction allowable under section 35</strong></td>
<td></td>
<td></td>
<td></td>
<td><strong>17,50,000</strong></td>
</tr>
</tbody>
</table>

**Question 14**

Mr. A commenced operations of the businesses of setting up a warehousing facility for storage of food grains, sugar and edible oil on 1.4.2019. He incurred capital expenditure of Rs. 80 lakh, Rs. 60 lakh and Rs. 50 lakh, respectively, on purchase of land and
building during the period January, 2019 to March, 2019 exclusively for the above businesses, and capitalized the same in its books of account as on 1st April, 2019. The cost of land included in the above figures are Rs. 50 lakh, Rs. 40 lakh and Rs. 30 lakh, respectively. Further, during the P.Y.2019-20, he incurred capital expenditure of Rs. 20 lakh, Rs. 15 lakh & Rs. 10 lakh, respectively, for extension/reconstruction of the building purchased and used exclusively for the above businesses.

The profits from the business of setting up a warehousing facility for storage of food grains, sugar and edible oil (before claiming deduction under section 35AD and section 32) for the A.Y. 2020-21 is Rs. 16 lakhs, Rs. 14 lakhs and Rs. 31 lakhs, respectively.

Compute the income under the head "Profits and gains of business or profession" for the A.Y.2020-21 and the loss to be carried forward, assuming that Mr. A has fulfilled all the conditions specified for claim of deduction under section 35AD and has not claimed any deduction under Chapter VI-A under the heading “C. – Deductions in respect of certain incomes”. Assume in respect of expenditure incurred, the payments are made by account payee cheque or use of ECS through bank account.

**Solution**

### Computation of profits and gains of business or profession for A.Y. 2020-21

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs. (in lakhs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit from business of setting up of warehouse for storage of edible oil (before providing for depreciation under section 32)</td>
<td>31</td>
</tr>
<tr>
<td>Less: Depreciation under section 32</td>
<td></td>
</tr>
<tr>
<td>10% of Rs. 30 lakh, being (Rs. 50 lakh – Rs. 30 lakh + Rs. 10 lakh)</td>
<td>3</td>
</tr>
<tr>
<td>Income chargeable under “Profits and gains from business or profession”</td>
<td>28</td>
</tr>
</tbody>
</table>

### Computation of income/loss from specified business under section 35AD

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Food Grains</th>
<th>Sugar</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>(A) Profits from the specified business of setting up a warehousing facility (before providing deduction under section 35AD)</td>
<td>16</td>
<td>14</td>
<td>30</td>
</tr>
<tr>
<td><strong>Less: Deduction under section 35AD</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(B) Capital expenditure incurred prior to 1.4.2017 (i.e., prior to commencement of business) and capitalized in the books of account as on 1.4.2017 (excluding the expenditure incurred on acquisition of land) = Rs. 30 lakh (Rs. 80 lakh – Rs. 50 lakh) and Rs. 20 lakh (Rs. 60 lakh – Rs. 40 lakh)</td>
<td>30</td>
<td>20</td>
<td>50</td>
</tr>
<tr>
<td>(C) Capital expenditure incurred during the P.Y. 2018-19</td>
<td>20</td>
<td>15</td>
<td>35</td>
</tr>
<tr>
<td>(D) Total capital expenditure (B + C)</td>
<td></td>
<td></td>
<td>85</td>
</tr>
<tr>
<td><strong>(E) Deduction under section 35AD</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>100% of capital expenditure</td>
<td>50</td>
<td>35</td>
<td>85</td>
</tr>
<tr>
<td><strong>Total deduction u/s 35AD for A.Y. 2020-21</strong></td>
<td>50</td>
<td>35</td>
<td>85</td>
</tr>
<tr>
<td>(F) Loss from the specified business of setting up and operating a warehousing facility (after providing for deduction under section 35AD) to be carried forward as per section 73A (A-E)</td>
<td>(34)</td>
<td>(21)</td>
<td>(55)</td>
</tr>
</tbody>
</table>
Notes:
(i) Deduction of 100% of the capital expenditure is available under section 35AD for A.Y.2020-21 in respect of specified business of setting up and operating a warehousing facility for storage of sugar and setting up and operating a warehousing facility for storage of agricultural produce where operations are commenced on or after 01.04.2012 or on or after 01.04.2009, respectively.
(ii) However, since setting up and operating a warehousing facility for storage of edible oils is not a specified business, Mr. A is not eligible for deduction under section 35AD in respect of capital expenditure incurred in respect of such business.
(iii) Mr. A can, however, claim depreciation@10% under section 32 in respect of the capital expenditure incurred on buildings. It is presumed that the buildings were put to use for more than 180 days during the P.Y. 2019-20.
(iv) Loss from a specified business can be set-off only against profits from another specified business. Therefore, the loss of Rs. 55 lakh from the specified businesses of setting up and operating a warehousing facility for storage of food grains and sugar cannot be set-off against the profits of Rs. 28 lakh from the business of setting and operating a warehousing facility for storage of edible oils, since the same is not a specified business. Such loss can, however, be carried forward indefinitely for set-off against profits of the same or any other specified business.

Question 15
XYZ Ltd. commenced operations of the business of a new three-star hotel in Madurai, Tamil Nadu on 1.4.2019. The company incurred capital expenditure of Rs. 50 lakh during the period January, 2019 to March, 2019 exclusively for the above business, and capitalized the same in his books of account as on 1st April, 2019. Further, during the P.Y. 2019-20, it incurred capital expenditure of Rs. 2 crore (out of which Rs. 1.50 crore was for acquisition of land) exclusively for the above business.

Compute the income under the head "Profits and gains of business or profession" for the A.Y.2021-21, assuming that XYZ Ltd. has fulfilled all the conditions specified for claim of deduction under section 35AD and has not claimed any deduction under Chapter VI-A under the heading "C. – Deductions in respect of certain incomes".

The profits from the business of running this hotel (before claiming deduction under section 35AD) for the A.Y.2020-21 is Rs. 25 lakhs. Assume that the company also have another existing business of running a four-star hotel in Coimbatore, which commenced operations ten years back, the profits from which are Rs. 120 lakhs for the A.Y.2020-21. Also, assume that expenditure incurred during the previous year 2019-20 were paid by account payee cheque or use of ECS through bank account.

Solution

Computation of profits and gains of business or profession for A.Y. 2020-21

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profits from the specified business of new hotel in Madurai (before providing deduction under section 35AD)</td>
<td>25 lakh</td>
</tr>
<tr>
<td>Less: Deduction under section 35AD</td>
<td></td>
</tr>
<tr>
<td>Capital expenditure incurred during the P.Y.2019-20(excluding the expenditure incurred on acquisition of land) = Rs. 200 lakh – Rs. 150 lakh</td>
<td>50 lakh</td>
</tr>
<tr>
<td>Capital expenditure incurred prior to 1.4.2019 (i.e., prior to commencement of business) and capitalized in the books of account</td>
<td>50 lakh</td>
</tr>
</tbody>
</table>
as on 1.4.2019
Total deduction under section 35AD for A.Y. 2020-21
Loss from the specified business of new hotel in Madurai
Profit from the existing business of running a hotel in Coimbatore
Net profit from business after set-off of loss of specified business against
profits of another specified business under section 73A

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deduction allowed under section 35AD for A.Y. 2019-20</td>
<td>50,00,000</td>
</tr>
<tr>
<td>Less: Depreciation allowable u/s 32 for A.Y. 2019-20 [10% of Rs. 50 lacs]</td>
<td>5,00,000</td>
</tr>
<tr>
<td>Deemed income under section 35AD(7B)</td>
<td>45,00,000</td>
</tr>
</tbody>
</table>

ABC Ltd., however, by virtue of proviso to Explanation 13 to section 43(1), can claim depreciation under section 32 on the building in Unit B for A.Y. 2020-21. For the purpose of claiming depreciation on building in Unit B, the actual cost of the building would be:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Actual cost to the assessee</td>
<td>50,00,000</td>
</tr>
<tr>
<td>Less: Depreciation allowable u/s 32 for A.Y. 2019-20 [10% of Rs. 50 lacs]</td>
<td>5,00,000</td>
</tr>
<tr>
<td>Actual cost in the hands of ABC Ltd. in respect of building in its Unit B</td>
<td>45,00,000</td>
</tr>
</tbody>
</table>

### Question 17

The following are the particulars in respect of a scheduled bank incorporated in India -

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs. in lakh</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Provision for bad and doubtful debts under section 36(1)(via) upto A.Y. 2019-20</td>
<td>100</td>
</tr>
<tr>
<td>(ii) Gross Total Income of A.Y. 2020-21 [before deduction under section 36(1)(via)]</td>
<td>800</td>
</tr>
<tr>
<td>(iii) Aggregate average advances made by rural branches of the bank</td>
<td>300</td>
</tr>
<tr>
<td>(iv) Bad debts written off (for the first time) in the books of account (in respect of urban advances only) during the previous year 2019-20</td>
<td>210</td>
</tr>
</tbody>
</table>

Compute the deduction allowable under section 36(1)(vii) for the A.Y. 2020-21.
Solution

Compute the deduction allowable under section 36(1)(vii) for the A.Y.2020-21.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs. in lakh</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bad debts written off (for the first time) in the books of account</td>
<td>210</td>
</tr>
<tr>
<td>Less: Credit balance in the “Provision for bad and doubtful debts” under</td>
<td></td>
</tr>
<tr>
<td>section 36(1)(viia) as on 31.3.20</td>
<td></td>
</tr>
<tr>
<td>(i) Provision for bad and doubtful debts u/s 36(1)(viia) upto A.Y.2019-20</td>
<td>100</td>
</tr>
<tr>
<td>(ii) Current year provision for bad and doubtful debts u/s 36(1)(viia)</td>
<td>98</td>
</tr>
<tr>
<td>[8.5% of Rs. 800 lakhs + 10% of Rs. 300 lakhs]</td>
<td>198</td>
</tr>
<tr>
<td>Deduction under section 36(1)(vii) in respect of bad debts written off for</td>
<td></td>
</tr>
<tr>
<td>A.Y.2020-21</td>
<td>12</td>
</tr>
</tbody>
</table>

Question 18

Isac Limited is a company engaged in the business of biotechnology. The net profit of the company for the financial year ended 31.03.2020 is Rs. 35,25,890 after debiting the following items:

<table>
<thead>
<tr>
<th>S. No</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Purchase price of raw material used for the purpose of in-house research and</td>
<td>11,80,000</td>
</tr>
<tr>
<td></td>
<td>development</td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Purchase price of asset used for in-house research and development</td>
<td></td>
</tr>
<tr>
<td></td>
<td>wrongly debited to profit and loss account:</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(1) Land</td>
<td>5,00,000</td>
</tr>
<tr>
<td></td>
<td>(2) Building</td>
<td>3,00,000</td>
</tr>
<tr>
<td>3.</td>
<td>Expenditure incurred on notified agricultural extension project</td>
<td>25,50,000</td>
</tr>
<tr>
<td>4.</td>
<td>Expenditure on notified skill development project:</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(1) Purchase of land</td>
<td>40,00,000</td>
</tr>
<tr>
<td></td>
<td>(2) Expenditure on training for skill development</td>
<td>32,50,000</td>
</tr>
<tr>
<td>5.</td>
<td>Expenditure incurred on advertisement in the souvenir published by a</td>
<td>75,000</td>
</tr>
<tr>
<td></td>
<td>political party</td>
<td></td>
</tr>
</tbody>
</table>

Compute the income under the head “Profits and gains of business or profession” for the A.Y.2020-21 of Isac Ltd.

Solution

Computation of income under the head “Profits and gains of business or profession” for the A.Y.2020-21

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net profit as per profit and loss account</td>
<td>35,25,890</td>
<td></td>
</tr>
<tr>
<td>Add: Items debited to profit and loss account, but to be disallowed</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchase price of Land used in in-house research and development - being</td>
<td></td>
<td>5,00,000</td>
</tr>
<tr>
<td>capital expenditure not allowable as deduction under section 35</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchase price of building used in in-house research and development -</td>
<td></td>
<td></td>
</tr>
<tr>
<td>being capital expenditure, 100% of which is allowable as deduction u/s</td>
<td></td>
<td></td>
</tr>
<tr>
<td>35(1)(iv) read with section 35(2)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Expenditure incurred on notified agricultural extension project (to be</td>
<td></td>
<td>25,50,000</td>
</tr>
<tr>
<td>treated separately)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Expenditure incurred on notified skill development</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### Question 19

Hari, an individual, carried on the business of purchase and sale of agricultural commodities like paddy, wheat, etc. He borrowed loans from Andhra Pradesh State Financial Corporation (APSFC) and Indian Bank and has not paid interest as detailed hereunder:

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i)</td>
<td>Andhra Pradesh State Financial Corporation (P.Y. 2018-19 &amp; 2019-20)</td>
</tr>
<tr>
<td>(ii)</td>
<td>Indian Bank (P.Y. 2019-20)</td>
</tr>
<tr>
<td></td>
<td><strong>Total</strong></td>
</tr>
</tbody>
</table>

Both APSFC and Indian Bank, while restructuring the loan facilities of Hari during the year 2019-20, converted the above interest payable by Hari to them as a loan repayable in 60 equal installments. During the year ended 31.3.2020, Hari paid 5 installments to APSFC and 3 installments to Indian Bank.

Hari claimed the entire interest of Rs. 45,00,000 as an expenditure while computing the income from business of purchase and sale of agricultural commodities. Discuss whether his claim is valid and if not what is the amount of interest, if any, allowable.

### Solution

According to section 43B, any interest payable on the term loans to specified financial institutions and any interest payable on any loans and advances to scheduled banks shall be allowed only in the year of payment of such interest irrespective of the method of accounting followed by the assessee. Where there is default in the payment of interest by...
the assessee, such unpaid interest may be converted into loan. Such conversion of unpaid interest into loan shall not be construed as payment of interest for the purpose of section 43B. The amount of unpaid interest so converted as loan shall be allowed as deduction only in the year in which the converted loan is actually paid.

In the given case of Hari, the unpaid interest of Rs. 15,00,000 due to APSFC and of Rs. 30,00,000 due to Indian Bank was converted into loan. Such conversion would not amount to payment of interest and would not, therefore, be eligible for deduction in the year of such conversion. Hence, claim of Hari that the entire interest of Rs. 45,00,000 is to be allowed as deduction in the year of conversion is not tenable. The deduction shall be allowed only to the extent of repayment made during the financial year. Accordingly, the amount of interest eligible for deduction for the A.Y.2020-21 shall be calculated as follows:

<table>
<thead>
<tr>
<th></th>
<th>Interest outstanding (Rs.)</th>
<th>Number of Installments</th>
<th>Amount per installment (Rs.)</th>
<th>Installments paid</th>
<th>Interest allowable (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>APSFC</td>
<td>15 lakh</td>
<td>60</td>
<td>25,000</td>
<td>5</td>
<td>1,25,000</td>
</tr>
<tr>
<td>Indian Bank</td>
<td>30 lakh</td>
<td>60</td>
<td>50,000</td>
<td>5</td>
<td>1,50,000</td>
</tr>
<tr>
<td><strong>Total amount eligible for deduction</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td><strong>2,75,000</strong></td>
</tr>
</tbody>
</table>

**Question 20**

Vinod is a person carrying on profession as film artist. His gross receipts from profession are as under:

<table>
<thead>
<tr>
<th>Financial year</th>
<th>Gross Receipts (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2016-17</td>
<td>1,15,000</td>
</tr>
<tr>
<td>2017-18</td>
<td>1,80,000</td>
</tr>
<tr>
<td>2018-19</td>
<td>2,10,000</td>
</tr>
</tbody>
</table>

What is his obligation regarding maintenance of books of accounts for Assessment Year 2020-21 under section 44AA of Income-tax Act, 1961?

**Solution**

Section 44AA(1) requires every person carrying on any profession, notified by the Board in the Official Gazette (in addition to the professions already specified therein), to maintain such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of the Income-tax Act, 1961.

A person carrying on a notified profession shall be required to maintain specified books of accounts, only if:

(i) his gross receipts in all the three years immediately preceding the relevant previous year has exceeded Rs. 1,50,000; or

(ii) it is a new profession which is setup in the relevant previous year, it is likely to exceed Rs. 1,50,000 in that previous year.

In the present case, Vinod is a person carrying on profession as film artist, which is a notified profession. Since his gross receipts have not exceeded Rs. 1,50,000 in financial year 2016-17, the requirement under section 44AA to compulsorily maintain the prescribed books of account is not applicable to him for A.Y. 2020-21.

Mr. Vinod, however, required to maintain such books of accounts as would enable the Assessing Officer to compute his total income.
Question 21

Mr. Praveen engaged in retail trade, reports a turnover of Rs. 1,98,50,000 for the financial year 2019-20. His income from the said business as per books of account is Rs. 11,20,000 computed as per the provisions of Chapter IV-D “Profits and gains from business or Profession” of the Income-tax Act, 1961. All transactions are carried out by way of A/c payee cheque/ECS through bank A/c. Retail trade is the only source of income for Mr. Praveen. A.Y. 2019-20 was the first year for which he declared his business income in accordance with the provisions of presumptive taxation under section 44AD.

(i) Is Mr. Praveen eligible to opt for presumptive taxation scheme in respect of his income from retail trade for the assessment year 2020-21?

(ii) If so, determine his income from retail trade as per the applicable presumptive provision.

(iii) In case Mr. Praveen does not opt for presumptive taxation of income from retail trade, what are his obligations under the Income-tax Act, 1961?

(iv) What is the due date for filing his return of income under both the options?

Solution:

(i) Yes. Since his total turnover for the F.Y 2019-20 is below Rs. 200 lakhs, he is eligible to opt for presumptive taxation scheme under section 44AD in respect of his retail trade business.

(ii) His income from retail trade, applying the presumptive tax provisions under section 44AD, would be Rs. 15,88,000, being 8% of Rs. 1,98,50,000.

(iii) Mr. Praveen had declared profit for the previous year 2018-19 in accordance with the presumptive provisions and if he does not opt for presumptive provisions for any of the five consecutive assessment years i.e., A.Y. 2020-21 to A.Y. 2024-25, he would not be eligible to claim the benefit of presumptive taxation for five assessment years subsequent to the assessment year relevant to the previous year in which the profit has not been declared in accordance the presumptive provisions i.e., if he does not opt for presumptive taxation in say P.Y. 2019-20, then he would not be eligible to claim the benefit of presumptive taxation for A.Y. 2021-22 to A.Y. 2025-26.

Consequently, Mr. Praveen is required to maintain the books of accounts and get them audited under section 44AB, since his income exceeds the basic exemption limit.

(iv) In case he opts for the presumptive taxation scheme under section 44AD, the due date would be 31st July, 2020.

In case he does not opt for the presumptive taxation scheme, he is required to get his books of account audited, in which case the due date for filing of return would be 30th September, 2020.

Question 22

Mr. X commenced the business of operating goods vehicles on 1.4.2019. He purchased the following vehicles during the P.Y.2019-20. Compute his income under section 44AE for A.Y. 2020-21.

<table>
<thead>
<tr>
<th>Gross Vehicle Weight (in kilograms)</th>
<th>Number</th>
<th>Date of purchase</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) 7,000</td>
<td>2</td>
<td>10.04.2019</td>
</tr>
<tr>
<td>(2) 6,500</td>
<td>1</td>
<td>15.03.2020</td>
</tr>
</tbody>
</table>
Would your answer change if the two goods vehicles purchased in April, 2019 were put to use only in July, 2019?

Solution

Since Mr. X does not own more than 10 vehicles at any time during the previous year 2019-20, he is eligible to opt for presumptive taxation scheme under section 44AE. Rs. 1,000 per ton of gross vehicle weight or unladen weight per month or part of the month for each heavy goods vehicle and Rs. 7,500 per month or part of month for each goods carriage other than heavy goods vehicle, owned by him would be deemed as his profits and gains from such goods carriage.

Heavy goods vehicle means any goods carriage, the gross vehicle weight of which exceeds 12,000 kg.

<p>| | | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>(1)</td>
<td>(2)</td>
<td>(3)</td>
<td>(4)</td>
</tr>
<tr>
<td></td>
<td>Number of Vehicles</td>
<td>Date of purchase</td>
<td>No. of months for which vehicle is owned</td>
</tr>
<tr>
<td>2</td>
<td>29.08.2019</td>
<td>8</td>
<td>16</td>
</tr>
<tr>
<td>1</td>
<td>23.02.2020</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>18</td>
</tr>
<tr>
<td></td>
<td>Goods vehicle other than heavy goods vehicle</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>10.4.2019</td>
<td>12</td>
<td>24</td>
</tr>
<tr>
<td>1</td>
<td>15.3.2020</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>3</td>
<td>16.7.2019</td>
<td>9</td>
<td>27</td>
</tr>
<tr>
<td>1</td>
<td>2.1.2020</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>55</td>
</tr>
</tbody>
</table>

The presumptive income of Mr. X under section 44AE for A.Y.2020-21 would be - Rs. 6,82,500, i.e., 55 × Rs. 7,500, being for other than heavy goods vehicle + 18 × Rs. 1,000 × 15 ton being for heavy goods vehicle.

The answer would remain the same even if the two vehicles purchased in April, 2019 were put to use only in July, 2019, since the presumptive income has to be calculated per month or part of the month for which the vehicle is owned by Mr. X.
QUESTIONS ON TAXATION OF VARIOUS ENTITIES

Question 23

Sona Ltd., a resident company, earned a profit of Rs. 15 lakhs after debit/credit of the following items to its Statement of Profit and Loss for the year ended on 31/03/2020.

(i) Items debited to Statement of Profit and Loss:

<table>
<thead>
<tr>
<th>No.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Provision for the loss of subsidiary</td>
<td>70,000</td>
</tr>
<tr>
<td>2.</td>
<td>Provision for doubtful debts</td>
<td>75,000</td>
</tr>
<tr>
<td>3.</td>
<td>Provision for income-tax</td>
<td>1,05,000</td>
</tr>
<tr>
<td>4.</td>
<td>Provision for gratuity based on actuarial valuation</td>
<td>2,00,000</td>
</tr>
<tr>
<td>5.</td>
<td>Depreciation</td>
<td>3,60,000</td>
</tr>
<tr>
<td>6.</td>
<td>Interest to financial institution (unpaid before filing of return)</td>
<td>1,00,000</td>
</tr>
<tr>
<td>7.</td>
<td>Penalty for infraction of law</td>
<td>50,000</td>
</tr>
</tbody>
</table>

(ii) Items credited to Statement of Profit and Loss:

<table>
<thead>
<tr>
<th>No.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Profit from unit established in special economic zone</td>
<td>5,00,000</td>
</tr>
<tr>
<td>2.</td>
<td>Share in income of an AOP as a member</td>
<td>1,00,000</td>
</tr>
<tr>
<td>3.</td>
<td>Income from units of UTI</td>
<td>75,000</td>
</tr>
<tr>
<td>4.</td>
<td>Long term capital gains</td>
<td>3,00,000</td>
</tr>
</tbody>
</table>

Other Information:

(i) Depreciation includes Rs. 1,50,000 on account of revaluation of fixed assets.
(ii) Depreciation as per Income-tax Rules is Rs. 2,80,000.
(iii) Brought forward loss of Rs. 10 lakhs which includes unabsorbed depreciation of Rs. 4 lakhs.
(iv) The capital gain has been invested in specified assets under section 54EC.
(v) The AOP, of which the company is a member, has paid tax at maximum marginal rate.
(vi) Provision for income-tax includes Rs. 45,000 of interest payable on income-tax.

Compute minimum alternate tax under section 115JB of the Income-tax Act, 1961, for A.Y. 2020-21, assuming that Sona Ltd. is not required to comply with the Indian Accounting Standards.

Solution

Computation of “Book Profit” for levy of MAT under section 115JB for A.Y.2020-21

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Profit as per Statement of Profit and Loss</td>
<td>15,00,000</td>
</tr>
<tr>
<td>Add: Net profit to be increased by the following amounts as per Explanation 1 to section 115JB:</td>
<td></td>
</tr>
<tr>
<td>- Provision for the loss of subsidiary</td>
<td>70,000</td>
</tr>
<tr>
<td>- Provision for doubtful debts, being the amount set aside as provision for diminution in the value of any asset</td>
<td>75,000</td>
</tr>
<tr>
<td>- Provision for income-tax</td>
<td>1,05,000</td>
</tr>
<tr>
<td>[As per Explanation 2 to section 115JB, income-tax shall include, inter alia, any interest charged under the Act, therefore, whole of the amount of provision for income-tax including Rs. 45,000 towards interest</td>
<td></td>
</tr>
</tbody>
</table>
payable has to be added]  
- Depreciation  

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Depreciation</td>
<td>3,60,000</td>
</tr>
</tbody>
</table>

Less: Net profit to be decreased by the following amounts as per Explanation 1 to section 115JB:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Share in income of an AOP as a member</td>
<td>1,00,000</td>
</tr>
<tr>
<td>[In a case, where AOP has paid tax on its total income at maximum marginal rate, no income-tax is payable by the company, being a member of AOP, in accordance with the provisions of section 86. Therefore, share in income of an AOP on which no income-tax is payable in accordance with the provisions of section 86, would be reduced while computing book profit, since the same has been credited to profit and loss account]</td>
<td></td>
</tr>
<tr>
<td>- Income from units in UTI</td>
<td>75,000</td>
</tr>
<tr>
<td>[Income from units in UTI shall be reduced while computing the book profits, since the same is exempt under section 10(35)]</td>
<td></td>
</tr>
<tr>
<td>- Depreciation other than depreciation on revaluation of assets (Rs. 3,60,000 – Rs. 1,50,000)</td>
<td>2,10,000</td>
</tr>
<tr>
<td>- Unabsorbed depreciation or brought forward business loss, whichever is less, as per the books of account. Lower of unabsorbed depreciation Rs. 4,00,000 and brought forward business loss Rs. 6,00,000 as per books of accounts has to be reduced while computing the book profit]</td>
<td>4,00,000</td>
</tr>
</tbody>
</table>

| Book Profit                                     | 13,25,000 |

### Computation of MAT liability under section 115JB

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>15% of book profit</td>
<td>1,98,750</td>
</tr>
<tr>
<td>Add: Held and Education cess@4%</td>
<td>7,950</td>
</tr>
<tr>
<td>Minimum Alternate Tax liability</td>
<td>2,06,700</td>
</tr>
</tbody>
</table>

**Notes:**

1. It is only the specific items mentioned under Explanation 1 to section 115JB, which can be adjusted from the net profit as per the Statement of Profit and Loss prepared as per the Companies Act for computing book profit for levy of MAT. Since the following items are not specified thereunder, the same cannot be adjusted for computing book profit:
   - Interest to financial institution (unpaid before filing of return) and
   - Penalty for infraction of law

2. Provision for gratuity based on actuarial valuation is an ascertained liability [CIT v. Echjay Forgings (P) Ltd. (2001) 251 ITR 15 (Bom.).] Hence, the same should not be added back to compute book profit.

3. As per proviso to section 115JB(6), the profits from unit established in special economic zone cannot be excluded while computing the book profit, and hence, such income would be liable for MAT.
(4) Long-term capital gains cannot be deducted while computing book profit even if such amount of capital gains is invested in specified assets under section 54EC, since book profit has to be computed by adding/deducting the items mentioned under Explanation 1 to section 115JB alone. Capital Gains reflected in the statement of profit and loss shall be part of book profit under section 115JB. Capital gains exempted under section 54EC cannot also be excluded for computing book profit. [CIT v. Veekaylal Investment Co. P. Ltd. (2001) 249 ITR 597 (Bom.) & N J Jose and Co. (P) Ltd. v. ACIT (2010) 321 ITR 132 (Ker.)]

Question 24

The following are the particulars of income of three investment funds for P.Y.2020-21:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>A</th>
<th>B</th>
<th>C</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business Income</td>
<td>Nil</td>
<td>2,00,000</td>
<td>Nil</td>
</tr>
<tr>
<td>Capital Gains</td>
<td>16</td>
<td>14</td>
<td>(6)</td>
</tr>
<tr>
<td>Income from other sources</td>
<td>4</td>
<td>4</td>
<td>8</td>
</tr>
</tbody>
</table>

Compute the total income of the investment funds and unit-holders for A.Y.2020-21, assuming that:
(i) each investment fund has 20 unit holders each having one unit; and
(ii) income from investment in the investment fund is the only income of the unit-holder.

If Investment Fund C has the following income components for A.Y.2021-22, what would be the total income of the fund and the unit holder for that year?

Business Income **Rs. 2 lakh**
Capital Gains **Rs. 9 lakh**
Income from other source **Rs. 8 lakh**

Solution

**Computation of total income of the investment fund for A.Y.2019-20**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>A</th>
<th>B</th>
<th>C</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business Income</td>
<td>Nil</td>
<td>2,00,000</td>
<td>Nil</td>
</tr>
<tr>
<td>Total Income</td>
<td>Nil</td>
<td>2,00,000</td>
<td>Nil</td>
</tr>
</tbody>
</table>

**Computation of total income of a unit holder of the following Investment funds for A.Y. 2019-20**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>A</th>
<th>B</th>
<th>C</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital Gains</td>
<td>80,000</td>
<td>70,000</td>
<td>-</td>
</tr>
<tr>
<td>Income from other sources</td>
<td>20,000</td>
<td>20,000</td>
<td>30,000</td>
</tr>
<tr>
<td>Total Income</td>
<td>1,00,000</td>
<td>90,000</td>
<td>30,000</td>
</tr>
</tbody>
</table>

Notes:
(i) The total income of Investment Fund B would be chargeable to tax@30% if the fund is a firm and @30%/25%, as the case may, if the fund is a company and at the maximum marginal rate, in any other case.
(ii) In case of Investment Fund C, the business loss of **Rs. 2 lakh** is set-off against income from other sources of **Rs. 8 lakh**. Loss of **Rs. 6 lakh** under the head capital
gains cannot be set-off. The same has to be carried forward by the Investment Fund for set-off in the subsequent years.

(iii) For A.Y.2020-21, the brought forward capital loss of Rs. 6 lakh can be set-off against capital gains of Rs. 9 lakh. Business income of Rs. 2 lakh would be taxable in the hands of the Investment Fund. Capital gains of Rs. 3 lakh (Rs. 9 lakh – Rs. 6 lakh) and Income from other sources of Rs. 8 lakh would be taxable in the hands of the unit-holders. The total income of each unit holder for A.Y.2020-21 would be Rs. 55,000, comprising of-

Capital gains = Rs.15,000 [i.e., Rs.3 lakh/20]
Income from other sources = Rs. 40,000 [i.e., Rs. 8 lakh / 20]

---

**Question 25**

**XYZ Ltd. is engaged in the manufacture of textile since 01-04-2009. Its Statement of Profit & Loss shows a profit of Rs. 700 lakhs after debit/credit of the following items:**

(1) Depreciation calculated on the basis of useful life of assets as per provisions of the Companies Act, 2013 is Rs. 50 lakhs.
(2) Employer's contribution to EPF of Rs. 2 lakhs and Employees' contribution of Rs. 2 lakhs for the month of March, 2020 were remitted on 8th May 2020.
(3) The company appended a note to its Income Statement that industrial power tariff concession of Rs. 2.5 lakhs was received from the State Government and credited the same to Statement of P & L.
(4) The company had provided an amount of Rs. 25 lakhs being sum estimated as payable to workers based on agreement to be entered with the workers union towards periodical wage revision once in 3 years. The provision is based on a fair estimation on wage and reasonable certainty of revision once in 3 years.
(5) The company had made a provision of 10% of its debtors towards bad and doubtful debts. Total sundry debtors of the company as on 31-03-2020 was Rs. 200 lakhs.
(6) A debtor who owed the company an amount of Rs. 40 lakhs was declared insolvent and hence, was written off by debit to Statement of Profit and loss.
(7) Sundry creditors include an amount of Rs. 50 lakhs payable to A & Co, towards supply of raw materials, which remained unpaid due to quality issues. An agreement has been made on 31-03-2020, to settle the amount at a discount of 75% of the outstanding. The amount waived is credited to Statement of Profit and Loss.
(8) The opening and closing stock for the year were Rs. 200 lakhs and Rs. 255 lakhs, respectively. They were overvalued by 10%.
(9) Provision for gratuity based on actuarial valuation was Rs. 500 lakhs. Actual gratuity paid debited to gratuity provision account was Rs. 300 lakhs.
(10) Commission of Rs. 1 lakhs paid to a recovery agent for realization of a debt. Tax has been deducted and remitted as per Chapter XViib of the Act.
(11) The company has purchased 500 tons of industrial paper as packing material at a price of Rs. 30,000/ton from PQR, a firm in which majority of the directors are partners. PQR's normal selling price in the market for the same material is Rs. 28,000/ton.

**Additional Information:**

(1) **There was an addition to Plant & Machinery amounting to Rs. 50 lakhs on 10-06-2019, which was used for more than 180 days during the year. Additional depreciation has not been adjusted in the books.**

(2) **Normal depreciation calculated as per income-tax rules is Rs. 80 lakhs.**

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27.31
(3) The company had credited a sub-contractor an amount of Rs. 10 lakhs on 31-03-2019 towards repairing a machinery component. The tax so deducted was remitted on 31-12-2019.

(4) The company has collected Rs. 7 lakhs as sales tax from its customers and paid the same on the due dates. However, on an appeal made, the High Court directed the Sales Tax Department to refund Rs. 3 lakhs to the company. The company in turn refunded Rs. 2 lakhs to the customers from whom the amount was collected and the balance of Rs. 1 lakh is still lying under the head “Current Liabilities”.

Compute total income and tax payable for A.Y. 2020-21. Ignore MAT provisions.

Note - The turnover of XYZ Ltd. for the P.Y.2017-18 was Rs. 405 crore.

**Answer**

**Computation of Total Income of XYZ Ltd. for the A.Y.2020-21**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profits and Gains from Business and Profession</td>
<td>7,00,00,000</td>
</tr>
<tr>
<td>Profit as per Statement of profit and loss account</td>
<td></td>
</tr>
</tbody>
</table>

**Add: Items debited but to be considered separately or to be disallowed**

(a) Depreciation as per Companies Act, 2013  | 50,00,000 |
(b) Employees’ contribution to EPF [See Note 1 below]  | 2,00,000 |
(c) Employers contribution to EPF | Nil |
(d) Provision for wages payable to workers | Nil |
(e) Provision for doubtful debts [10% of Rs. 200 lakhs] | 20,00,000 |
<table>
<thead>
<tr>
<th>(f)</th>
<th>Bad debts written off</th>
<th>Nil</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Bad debts write off in the book of account is allowable as deduction under section 36(1)(vii). Since the same has already been debited to profit and loss account, no further adjustment is required</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(g)</th>
<th>Provision for gratuity</th>
<th>2,00,00,000</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Provision of Rs. 500 lakhs for gratuity based on actuarial valuation is not allowable as deduction as per section 40A(7). However, actual gratuity of Rs. 300 lakhs paid is allowable as deduction. Hence, the difference has to be added back</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(h)</th>
<th>Commission paid to recovery agent for realization of a debt.</th>
<th>Nil</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Commission of Rs. 1 lakh paid to a recovery agent for realization of a debt is an allowable expense under section 37 as per DCIT v. Super Tannery (India) Ltd. (2005) 274 ITR 338 (All). Since the same has been debited to profit and loss account, no further adjustment is required</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(i)</th>
<th>Purchase of paper at a price higher than the fair market value</th>
<th>10,00,000</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>As per section 40A(2), the difference between the purchase price (Rs. 30,000 per ton) and the fair market value (Rs. 28,000 per ton) multiplied by the quantity purchased (500 tons) has to be added back since the purchase is from a related party, a firm in which majority of the directors are partners, at a price higher than the fair market value</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(j)</th>
<th>Sales tax not refunded to customers out of sales tax refund</th>
<th>1,00,000</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The amount of sales tax refunded to the company by the Government is a revenue receipt chargeable to tax under section 41(1). Deduction can be claimed of amount refunded to customers [CIT v. Thirumalaiswamy Naidu &amp; Sons (1998) 230 ITR 534 (SC)]. Hence, the net amount of Rs. 1,00,000 (i.e., Rs. 3,00,000 minus Rs. 2,00,000) would be chargeable to tax</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(k)</th>
<th>Industrial power tariff concession received from State Government</th>
<th>Nil</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Any assistance in the form of, inter alia, concession received from the Central or State Government would be treated as income as per section 2(24)(xviii). Since the same has been credited to Statement of profit and loss, no adjustment is required</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(l)</th>
<th>Discount given by Sundry Creditors for supply of raw materials</th>
<th>Nil</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Discount of 75% given by Sundry Creditors for supply of raw materials is taxable under section 41(1). Since the</td>
<td></td>
</tr>
</tbody>
</table>

**Less: Items credited but to be considered separately/ permissible expenditure and allowances**

<table>
<thead>
<tr>
<th>(k)</th>
<th>Industrial power tariff concession received from State Government</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Any assistance in the form of, inter alia, concession received from the Central or State Government would be treated as income as per section 2(24)(xviii). Since the same has been credited to Statement of profit and loss, no adjustment is required.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(l)</th>
<th>Discount given by Sundry Creditors for supply of raw materials</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Discount of 75% given by Sundry Creditors for supply of raw materials is taxable under section 41(1). Since the</td>
</tr>
</tbody>
</table>
same has already been credited to Statement of profit and loss, no further adjustment is required

(m) Depreciation as per Income-tax Act, 1961

Depreciation as per Income-tax Act, 1961

80,00,000

(n) Over-valuation of stock [Rs. 55 lakhs × 10/110]

Over-valuation of stock [Rs. 55 lakhs × 10/110]

5,00,000

The amount by which stock is over-valued has to be reduced for computing business income. Rs. 50 lakhs, being the difference between closing and opening stock, has to be adjusted to remove the effect of over-valuation.

(o) Additional Depreciation [See Note 2 below]

Additional Depreciation [See Note 2 below]

10,00,000

[Additional depreciation@20% is allowable on Rs. 50 lakhs, being actual cost of new plant & machinery acquired on 10.06.2019, as the same was put to use for more than 180 days in the P.Y.2019-20.]

(p) Payment to a sub-contractor where tax deducted last year was remitted after the due date of filing of return [See Note 3 below]

Payment to a sub-contractor where tax deducted last year was remitted after the due date of filing of return [See Note 3 below]

3,00,000

[30% of Rs. 10 lakhs, being payment to a sub-contractor, would have been disallowed under section 40(a)(ia) while computing the business income of A.Y.2019-20, since tax deducted was remitted after the due date of filing of return. However, the same is allowable in A.Y.2020-21, since the remittance has been made on 31.12.2019]

Total Income

Total Income

98,00,000

8,85,00,000

Computation of tax liability of XYZ Ltd. for A.Y.2020-21

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax @30% on the above total income (since the turnover exceeded Rs. 400 crore in the P.Y. 2017-18)</td>
<td>2,65,50,000</td>
</tr>
<tr>
<td>Add: Surcharge@7% (since total income exceeds Rs. 1 crore but less than Rs. 10 crore)</td>
<td>18,58,500</td>
</tr>
<tr>
<td>Add: Health and Education cess@4%</td>
<td>11,36,340</td>
</tr>
<tr>
<td>Total tax liability</td>
<td>2,95,44,840</td>
</tr>
</tbody>
</table>

Notes:

(1) Employees contribution to PF deposited after the due date mentioned under the PF Act is not allowable as deduction as per section 36(1)(va). The same has also been affirmed by the Gujarat High Court in CIT v. Gujarat State Road Transport Corporation (2014) 366 ITR 170. Hence, in the above solution, employees’ contribution to PF has been disallowed while computing business income.

The CBDT has, vide Circular No. 22/2015, dated 17.12.2015, clarified that the employer contribution to provident fund remitted on or before due date of filing of return under section 139(1), is allowable as deduction while computing Business Income. Further, it has also clarified that the circular does not apply to claim of deduction relating to employee’s contribution welfare funds which are governed by section 36(1)(va) of the Act.

27.34
Alternate View - An alternate view has, however, been expressed in CIT v. Kiccha Sugar Co. Ltd. (2013) 356 ITR 351 (Uttarakhund), CIT v. AIMIL Ltd (2010) 321 ITR 508 (Del) and CIT v. Nipso Polyfabriks Ltd (2013) 350 ITR 327 (HP) that employees' contribution to PF, deducted from the salaries of the employees of the assessee, shall be allowed as deduction from the income of the employer-assessee, if the same is deposited by the employer-assessee with the provident fund authority on or before the due date of filing of return for the relevant previous year. If this view is considered, then no disallowance would be attracted in this case, since the employees’ contribution has been remitted before the due date of filing of return of income.

(2) Rs. 50 lakhs, being the addition to plant and machinery on 10.6.2019 qualifies for additional depreciation@20% under section 32(1)(iia). Since only the normal depreciation as per Income-tax Rules, 1962, has been debited to profit and loss account, additional depreciation of Rs. 10 lakhs (being 20% of Rs. 50 lakhs) has to be deducted while computing business income.

(3) Since the tax deducted during the P.Y.2018-19 was remitted only on 31.12.2019, i.e., after the due date of filing of return for A.Y.2019-20, Rs. 3,00,000, being 30% of Rs. 10 lakh would have been disallowed while computing the business income of that year. Since the tax deducted has been remitted on 31.12.2019, Rs. 3,00,000 would be allowed as deduction while computing the business income of the A.Y.2020-21.

Question 26

PQR LLP, a limited liability partnership set up a unit in Special Economic Zone (SEZ) in the financial year 2015-16 for production of washing machines. The unit fulfills all the conditions of section 10AA of the Income-tax Act, 1961. During the financial year 2018-19, it has also set up a warehousing facility in a district of Tamil Nadu for storage of agricultural produce. It fulfills all the conditions of section 35AD. Capital expenditure in respect of warehouse amounted to Rs. 75 lakhs (including cost of land Rs. 10 lakhs). The warehouse became operational with effect from 1st April, 2019 and the expenditure of Rs. 75 lakhs was capitalized in the books on that date.

Relevant details for the financial year 2019-20 are as follows:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit of unit located in SEZ</td>
<td>40,00,000</td>
</tr>
<tr>
<td>Export sales of above unit</td>
<td>80,00,000</td>
</tr>
<tr>
<td>Domestic sales of above unit</td>
<td>20,00,000</td>
</tr>
<tr>
<td>Profit from operation of warehousing facility (before considering deduction under Section 35AD).</td>
<td>1,05,00,000</td>
</tr>
</tbody>
</table>

Compute income tax (including AMT under Section 115JC) payable by PQR LLP for Assessment Year 2020-21.

Answer

Computation of total income and tax liability of PQR LLP for A.Y.2020-21
(under the regular provisions of the Income-tax Act, 1961)

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profits and gains of business or profession</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unit in SEZ</td>
<td>40,00,000</td>
<td></td>
</tr>
<tr>
<td>Less: Deduction under section 10AA [See Note (1) below]</td>
<td>32,00,000</td>
<td>8,00,000</td>
</tr>
</tbody>
</table>

27.35
Profit from operation of warehousing facility | 1,05,00,000
Less: Deduction under section 35AD [See Note (2) below] | 65,00,000
Business income of warehousing facility chargeable to tax | 40,00,000
Total Income | 48,00,000

Computation of tax liability (under the normal/regular provisions)

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax@30% on Rs. 48,00,000</td>
<td>14,40,000</td>
</tr>
<tr>
<td>Add: Education cess@4%</td>
<td>57,600</td>
</tr>
<tr>
<td>Total tax liability</td>
<td>14,97,600</td>
</tr>
</tbody>
</table>

Computation of adjusted total income of PQR LLP for levy of Alternate Minimum Tax

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Income (as computed above)</td>
<td>48,00,000</td>
</tr>
<tr>
<td>Add: Deduction under section 10AA</td>
<td>32,00,000</td>
</tr>
<tr>
<td>Add: Deduction under section 35AD</td>
<td>65,00,000</td>
</tr>
<tr>
<td>Less: Depreciation under section 32</td>
<td></td>
</tr>
<tr>
<td>On building @10% of Rs. 65 lakhs</td>
<td>6,50,000</td>
</tr>
<tr>
<td>Adjusted Total Income</td>
<td>1,38,50,000</td>
</tr>
<tr>
<td>Alternate Minimum Tax@18.5%</td>
<td>25,62,250</td>
</tr>
<tr>
<td>Add: Surcharge@12% (since adjusted total income &gt; Rs. 1 crore)</td>
<td>3,07,470</td>
</tr>
<tr>
<td>Add: Health and Education cess @ 4%</td>
<td>1,14,789</td>
</tr>
<tr>
<td>Tax liability under section 115JC (rounded off)</td>
<td>29,84,510</td>
</tr>
</tbody>
</table>

Since the regular income-tax payable is less than the alternate minimum tax payable, the adjusted total income shall be deemed to be the total income and tax is leviable @18.5% thereof plus surcharge@12% and cess@4%. Therefore, the tax liability is Rs. 29,84,510.

AMT Credit to be carried forward under section 115JEE

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax liability under section 115JC</td>
<td>29,84,510</td>
</tr>
<tr>
<td>Less: Tax liability under the regular provisions of the Income-tax Act, 1961</td>
<td>14,97,600</td>
</tr>
<tr>
<td>AMT Credit to be carried forward under section 115JEE</td>
<td>14,86,910</td>
</tr>
</tbody>
</table>

Notes:

1. Deduction under section 10AA in respect of Unit in SEZ = 
   \[
   \text{Profit of the Unit in SEZ} \times \frac{\text{Export turnover of the Unit in SEZ}}{\text{Total turnover of the Unit in SEZ}} 
   \]
   \[
   = Rs. 40,00,000 \times \frac{\text{80,00,000}}{1,00,00,000} = Rs. 32,00,000 
   \]

2. Deduction @ 100% of the capital expenditure is available under section 35AD for A.Y.2020-21 in respect of specified business of setting up and operating a warehousing facility for storage of agricultural produce which commences operation on or after 01.04.2012.

   Further, the expenditure incurred, wholly and exclusively, for the purposes of such specified business, shall be allowed as deduction during the previous year in which
he commences operations of his specified business if the expenditure is incurred prior to the commencement of its operations and the amount is capitalized in the books of account of the assessee on the date of commencement of its operations. Deduction under section 35AD would, however, not be available on expenditure incurred on acquisition of land. In this case, since the capital expenditure of Rs. 65 lakhs (i.e., Rs. 75 lakhs – Rs. 10 lakhs, being expenditure on acquisition of land) has been incurred in the F.Y.2018-19 and capitalized in the books of account on 1.4.2019, being the date when the warehouse became operational, Rs. 65,00,000, being 100% of Rs. 65 lakhs would qualify for deduction under section 35AD.
QUESTIONS ON ASSESSMENT PROCEDURE

Question 27
Teachwell Education is a trust approved under section 10(23C)(vi) which runs various educational institutions. During the course of assessment under section 143(3), the Assessing Officer finds that the trust has carried out its activities in contravention of the section under which it was approved for exemption. Hence, the Assessing Officer wants to pass an order without giving exemption under section 10, which the assessee objects. You are required to examine the following with respect to the provisions of Income-tax Act, 1961.

(a) Whether the Assessing Officer can pass an order without giving exemption under section 10?
(b) Can the Assessing Officer get any additional time limit in completing this assessment?

Answer
(a) As per the first proviso to section 143(3), in the case of an institution approved under, inter alia, section 10(23C)(vi), which is required to furnish the return of income under section 139(4C), the Assessing Officer shall not pass an order of assessment under section 143(3) without giving effect to the provisions of section 10, unless he is of the view that the activities of the institution are being carried on in contravention to the provisions of that section and:

(1) he has intimated the Central Government or the prescribed authority, which had earlier approved the concerned institution, about the contravention of the relevant provisions by the institution; and
(2) the approval granted to such institution has been withdrawn or notification in that respect has been rescinded.

Therefore, in the aforesaid case, the Assessing Officer can pass an assessment order without giving exemption under section 10 to Teachwell Education, which is an educational institution approved under section 10(23C)(vi), only if he has intimated the contravention made by Teachwell Education to the Central Government or the prescribed authority, as the case may be, and its approval under section 10(23C)(vi) is withdrawn.

(b) As per Explanation 1 to section 153, in case the Assessing Officer intimates the contravention of provisions of section 10(23C)(vi) to the Central Government or the prescribed authority, the period commencing from the date of intimation of such contravention by the Assessing Officer and ending on the date on which the copy of the order of withdrawing the approval under section 10(23C)(vi) is received by the Assessing Officer, shall be excluded for computing the period of limitation for completing the assessment.

Further, in case the time limit available to the Assessing Officer for passing an assessment order, after such exclusion, is less than 60 days, such remaining period of assessment shall be deemed to have been extended to 60 days.

Therefore, the Assessing Officer will get the above mentioned additional time for completing the assessment of Teachwell Education.

Question 28
The Assessing Officer issued a notice under section 142(1) on the assessee on 24th December, 2019 calling upon him to file return of income for Assessment Year 2019-20. In response to the said notice, the assessee furnished a return of loss and claimed carry
forward of business loss and unabsorbed depreciation. State whether the assessee would be entitled to carry forward as claimed in the return.

**Answer**

As per the provisions of section 139(3), any person who has sustained loss under the head ‘Profit and gains of business or profession’ is allowed to carry forward such a loss under section 72(1) or section 73(2), only if he has filed the return of loss within the time allowed under section 139(1). Also, the provisions of section 80 specify that a loss which has not been determined as per the return filed under section 139(3) shall not be allowed to be carried forward and set-off under, inter alia, section 72(1) (relating to business loss) or section 73(2) (losses in speculation business) or section 74(1) (loss under the head “Capital gains”) or section 74A(3) (loss from the activity or owning and maintaining race horses) or section 73A (loss relating to a “specified business”). However, there is no such condition for carry forward of unabsorbed depreciation under section 32.

In the given case, the assessee has filed its return of loss in response to notice under section 142(1). As per the provisions stated above, the return filed by the assessee in response to notice under section 142(1) is a belated return and therefore, the benefit of carry forward of business loss under section 72(1) or section 73(2) or section 73A shall not be available. The assessee shall, however be entitled to carry forward the unabsorbed depreciation as per provisions of section 32(2).

**Question 29**

The regular assessment of MNO Ltd. for the Assessment Year 2018-19 was completed under section 143(3) on 13th March, 2020. There was an audit objection by the Revenue Audit team that interest on loan should be disallowed partly as there was diversion of borrowed fund to sister concern without charge of interest.

Based on the above facts:

(i) State, with reasons, whether the Assessing Officer can issue notice under section 148 on the basis of audit objection of the Revenue Audit team.

(ii) If the action stated in (i) above is not permitted, what is the option open to the Revenue Department to deal with the said audit objection?

**Answer**

(i) Section 147 states that if the Assessing Officer has **reason to believe that any income chargeable to tax has escaped assessment for any assessment year**, he may assess or reassess such income and also any other income chargeable to tax which has escaped assessment and which comes to his notice subsequently in the course of the proceedings under this section.

The Assessing Officer should, therefore, have reason to believe that income chargeable to tax has escaped assessment. The belief should be that of the Assessing Officer and not of the revenue audit team.

Further, the Income-tax Act, 1961 does not confer jurisdiction on the Assessing Officer to change its opinion on the interpretation of a particular provision earlier adopted by it. If the issue had already been considered earlier during the course of scrutiny assessment and the Assessing Officer had come to a conclusion that no disallowance of interest paid by the assessee is required, even though loans had been given to sister concern without any interest, the same issue cannot be the basis of reassessment, merely because the revenue audit team takes a different view.

The Supreme Court, in ACIT v. ICICI Securities Primary Dealership Ltd. (2012) 348 ITR 299, held that re-opening of the assessment by the Assessing Officer on the ground of change of opinion is not valid.
Therefore, the Assessing Officer cannot issue notice under section 148 on the basis of audit objection of the Revenue Audit team. If the Assessing Officer has acted only under compulsion of the audit party and not independently, the action of reopening would be invalid.

(ii) The option open to the Revenue is initiation of proceedings under 263, by the jurisdictional Commissioner. He has the power to call for and examine the records, if he is of the opinion that the order passed by the Assessing Officer under section 143(3) is erroneous in so far as it is prejudicial to the interests of the Revenue. However, where the Assessing Officer has considered the issue in the original assessment and come to a conclusion that no disallowance of interest is called for, the Commissioner cannot initiate revisionary proceedings, merely because he holds a different view. Only where the view taken by the Assessing Officer is unsustainable in law, the Commissioner will be justified in initiating the revisionary proceedings under section 263. It was so held in CIT vs. Sohana Woollen Mills (2008) 296 ITR 238 (P & H).

Mere audit objection and possibility of a different view are not sufficient to conclude that the order of the Assessing Officer is erroneous or prejudicial to the interest of revenue.

Question 30
State whether the following assesseees have to file return of income and if so, the due date for the assessment year 2020-21:

(i) A registered trade union having income from let out property of Rs. 1,00,000.
(ii) A public trust hospital having an aggregate annual receipt of Rs. 200 lacs and availing exemption under section 10(23C)(via) with total income of Rs. 1,10,000.

Answer
(i) A registered trade union is having income from house property, which is exempt under section 10(24). Section 139(4C) mandates filing of return only when the total income exceeds the maximum amount which is not chargeable to tax without giving effect to the provisions of section 10. In this case, even without giving effect to section 10(24), the total income of the registered trade union is below basic exemption limit and therefore, there is no mandatory requirement to file the return of income.

(ii) Since the total income without giving effect to the exemption under section 10(23C)(via) is Rs. 3,30,000, which exceeds Rs. 2,50,000, the trust has to file its return of income by 30th September, 2020.

Question 31
Dishant received a notice under section 148 from the Assessing Officer for A.Y. 2016-17 on the ground that depreciation on certain assets was allowed in excess. The Assessing Officer recorded the reason for reopening. The original assessment was completed under section 143(3). In course of reassessment proceeding, the Assessing Officer also disallowed certain sum under section 14A in respect of expenses purported to be in relation to dividend from companies and tax-free interest. However, the Assessing Officer did not record the reason for applying the provisions of section 147 in respect of the issue of disallowance under section 14A and passed the order disallowing the excess depreciation and also certain sum under section 14A. Is there any infirmity in the order passed by the Assessing Officer?
Answer

Explanation 3 to section 147 permits the Assessing Officer to assess or reassess the income in respect of any issue (which has escaped assessment) which comes to his notice subsequently in the course of proceedings under section 147, even though the reason for such issue does not form part of the reasons recorded under section 148(2). Therefore, in the instant case, the Assessing Officer has the power to disallow expenses under section 14A in addition to disallowing excess depreciation for which notice under section 148 was issued even though the reason for issue relating to disallowance under section 14A was not recorded under section 148(2).

Hence, there is no deficiency in the order passed by the Assessing Officer.

Question 32

In the proceedings initiated under section 153A, the assessment order passed in respect of Mr. Simbu pertaining to a particular assessment year was annulled by the Income-tax Appellate Tribunal in its order passed on 28.1.2019. The same was received on 28.2.2020 by the jurisdictional Commissioner of Income-tax. Does the Department have any power to complete the assessment subsequent to such annulment? If yes, within what time limit?

Answer

As per section 153A(2), if any proceedings initiated under section 153A or any order of assessment or reassessment made under section 153A(1) has been annulled in any appeal or other legal proceeding, the abated assessment or reassessment relating to any assessment year shall stand revived with effect from the date of receipt of the order of such annulment by the Principal Commissioner or Commissioner. If the order of annulment is set aside, such revival shall cease to have effect [Sub-section (2) of section 153A]. The time limit for completion of such assessment or reassessment shall be one year from the end of the month in which the abated assessment revives or within the period specified in section 153B(1) [i.e., 18 months from the end of the financial year in which the last of authorisations for search or requisition was executed], whichever is later.

Question 33

The assessment of CNK Associates, a partnership firm, for the assessment year 2017-18 was made under section 143(3) on 31st July, 2019. The Assessing Officer made two additions to the income of the assessee viz. (a) addition of Rs. 2 lacs under section 40(a)(ia) due to non-furnishing of evidence of payment of TDS and (ii) addition of Rs. 5 lacs on account of unexplained cash credit. The assessee contested addition on account of unexplained cash credit in appeal to the Commissioner (Appeals). The appeal was decided in January, 2020 against the assessee. The assessee approaches you for your suggestion as to whether it should apply for revision to the Commissioner under section 264 or rectification to the Assessing Officer under section 154 as regards disallowance under section 40(a)(ia). What should be your suggestion?

Answer

The Commissioner cannot exercise his power of revision under section 264 where the order sought to be revised has been made the subject of an appeal to the Commissioner (Appeals) or to the Appellate Tribunal [Section 264(4)], even if the relief claimed in the revision is different from the relief claimed in the appeal. This was the view of the Supreme Court in the case of Hindustan Aeronautics Limited vs. CIT (2000) 243 ITR 808. It is not open to the assessee to seek recourse to revision under section 264 after the appeal is decided. Therefore, although the matter of addition of Rs. 2 lacs under section 40(a)(ia)
was not taken before the Commissioner (Appeals), the assessee, CNK Associates cannot apply for revision under section 264 in respect of the same.

Under section 154(1A), where any matter had been considered and decided in any proceeding by way of appeal or revision, rectification of such matter cannot be done by the Assessing Officer. However, in respect of the matter which has not been considered and decided in the appeal or revision, the order of the Assessing Officer can be rectified under section 154. Thus, the assessee can apply to the Assessing Officer for rectification of the order in respect of addition under section 40(a)(ia), as this matter has not been considered and decided in any proceeding by way of appeal or revision.

In view of above, the assessee, CNK Associates should seek rectification under section 154.

**Question 34**
Examine critically in the context of provisions of the Act “Can the Assessing Officer issue notice under section 148 to reopen the same assessment order on the same grounds for which the CIT had issued notice under section 263 of the Act”?

**Answer**
The Assessing Officer cannot issue notice under section 148 to reopen the same assessment order on the same grounds for which the Commissioner had issued notice under section 263 of the Income-tax Act, 1961, since the third proviso to section 147 specifically provides that the Assessing Officer may assess or reassess an income which is chargeable to tax and has escaped assessment, other than the income involving matters which are the subject matter of any appeal, reference or revision. Therefore, if the income relates to a matter which is the subject matter of revision under section 263, then the Assessing Officer cannot issue notice under section 148 to reopen the assessment order.

**Question 35**
Is the Assessing Officer empowered to assess or reassess an income which is chargeable to tax and has escaped assessment, in a case which is pending before the Appellate Tribunal? Discuss.

**Answer**
As per third proviso to section 147, the Assessing Officer may assess or reassess an income which is chargeable to tax and which has escaped assessment, other than the income involving matters which are the subject matter of any appeal, reference or revision. Therefore, in respect of the matters which are the subject matter of an appeal before the Appellate Tribunal, it is not possible for the Assessing Officer to initiate proceeding under section 147. However, in respect of other matters, which are not the subject matter of the appeal, the Assessing Officer can initiate proceeding under section 147.

**Question 36**
A search was conducted under section 132 in the business premises of Harish on 15th December, 2019. At that time, assessments under section 143(3) for A.Y. 2017-18 and A.Y. 2018-19 and reassessment proceeding under section 147 for A.Y. 2016-17 were pending before the Assessing Officer.

(i) What are the assessment years for which notice can be issued for making post-search assessment?

(ii) What would be the fate of pending assessments and reassessment?

(iii) What would be the effect, if the post-search assessment orders are annulled by the Income-tax Appellate Tribunal?
Answer

(i) The notice under section 153A can be issued for six assessment years preceding the assessment year relevant to the previous year in which the search is conducted. In this case, the search is conducted in the previous year 2019-20, the relevant assessment year for which is A.Y.2020-21. Therefore, notice can be issued for the six preceding assessment years i.e. for assessment years 2014-15 to 2019-20. Further, notice for assessment or reassessment can be issued by Assessing Officer for the relevant assessment year or years (i.e. for A.Y.2010-11 to A.Y.2013-14) if the following conditions are satisfied:

(a) The Assessing Officer has in his possession, books of account or other documents or evidence which reveal that the income, represented in the form of asset, which has escaped assessment amounts to or is likely to amount Rs.50 lakhs or more in the relevant assessment year or in aggregate in the relevant assessment years.

(b) The income so referred above has escaped assessment for such year or years; and

(c) The search under section 132 is initiated or requisition under section 132A is made on or after 01.04.2017 (This condition is satisfied since the search has taken place in December, 2019).

Note - The expression "relevant assessment year" shall mean an assessment year preceding the assessment year relevant to the previous year in which search is conducted or requisition is made which falls beyond six assessment years but not later than ten assessment years from the end of the assessment year relevant to the previous year in which search is conducted or requisition is made. "Asset" shall include immovable property being land or building or both, shares and securities, loans and advances, deposits in bank account.

(ii) As per section 153A, the assessment or reassessment relating to any assessment year, falling within the above period of six assessment years and for the relevant assessment year or years, pending on the date of initiation of the search under section 132, shall abate. In other words, they will cease to be applicable. Therefore, the assessments under section 143(3) for assessment years 2017-18 and 2018-19 and the reassessment proceeding under section 147 for assessment year 2016-17 shall abate.

(iii) Section 153A provides that where the post-search assessment order is annulled in any appeal or any other legal proceeding, the abated assessment and reassessment proceedings shall stand revived. Therefore, the assessments under section 143(3) relating to assessment years 2017-18 and 2018-19 and the reassessment proceeding relating to assessment year 2016-17, which abated on initiation of search, shall stand revived with effect from the date of receipt of the order of such annulment by the Principal Commissioner or Commissioner.

Question 37
Tai Ltd. filed its return of income for assessment year 2019-20 on 6th June, 2019. The return is selected for regular assessment under section 143(3) for which notice under section 143(2) is served on the company on 3rd October, 2020. The company responded to the notice under section 143(2). Examine whether the service of the notice is within time and if not, whether the assessment order can be challenged by the assessee.
Answer
The time limit for service of notice under section 143(2) is six months from the end of the financial year in which the return of income was furnished by the assessee. The return of income for assessment year 2019-20 was filed by the assessee on 6th June, 2019. Therefore, the notice under section 143(2) has to be served by 30th September, 2020. However, the notice was served on the assessee only on 3rd October, 2020. Hence, the notice issued under section 143(2) is time-barred.

However, as per section 292BB, where an assessee had appeared in any proceedings or co-operated in any enquiry relating to an assessment or reassessment, it shall be deemed that any notice required to be served upon him, has been duly served upon him in time in accordance with the provisions of the Act and such assessee shall be precluded from raising any objection in any proceeding or enquiry that the notice was (a) not served upon him or (b) not served upon him in time or (c) served upon him in an improper manner.

The above provision shall not be applicable where the assessee has raised such objection before the completion of such assessment or reassessment. Therefore, in the instant case, if the assessee, Tai Limited, had raised an objection to the proceeding, on the ground of non-service of the notice under section 143(2) upon it on time, then, the validity of the assessment order can be challenged. In absence of such objection, the assessment order cannot be challenged.

Question 38
In the case of Mr. Rajesh, a summary assessment was made under section 143(1) for assessment year 2016-17 without calling him. Thereafter, Mr. Rajesh has received a notice under section 148 on 6th April, 2019 for reopening of assessment. Can Mr. Rajesh challenge the legality of the notice on the ground of change of opinion?

Answer
Under the scheme of section 143(1), only the adjustments relating to any arithmetical error in the return, incorrect claim which is apparent from any information in the return, disallowance of losses claimed where the relevant return of income was filed beyond the due date under section 139(1), disallowance of expenditure indicated in the audit report but not taken into account in computing total income in the return, disallowance of deduction claimed under section 10AA, sections 80-IA to 80-IE, where return is furnished beyond due date and addition of income appearing in Form 26AS or Form 16 or Form 16A which has not been included in computing the total income in the return are permitted. In short, what is permissible is only correction of errors apparent on the basis of the return and tax audit report filed as well as Form 26AS, Form 16 or Form 16A. Therefore, the intimation given under section 143(1) is only a preliminary assessment, commonly referred to as a summary assessment without calling the assessee. The same cannot be treated as an order of assessment under section 143(3). Since there has been no assessment under section 143(3) in this case, the question of change of opinion does not arise.

Therefore, the assessee cannot challenge the legality of the notice issued under section 148 reopening the assessment on the ground of change of opinion in a case where no assessment is made under section 143(3). This inference is supported by the Supreme Court ruling in ACIT vs. Rajesh Jhaveri Stock Brokers P. Ltd. (2007) 291 ITR 500.
Question 39
Discuss the correctness or otherwise of the following proposition in the context of the Income-tax Act, 1961:
A fresh claim before the Assessing Officer can be made only by filing a revised return and not otherwise.

Answer
This proposition is correct. A return of income filed within the due date under section 139(1) or a belated return filed under section 139(4) may be revised by filing a revised return under section 139(5) where the assessee finds any omission or wrong statement in the original return subject to satisfying other conditions. There is no provision in the Income-tax Act, 1961, to make changes or modification in the return of income by filing a letter. The revised return can be filed at any time before the end of the relevant assessment year or before completion of assessment, whichever is earlier. In a case where a return of income has been filed within the due date under section 139(1) or after the due date under section 139(4), the only option available to the assessee to make an amendment to such return is by way of filing a revised return under section 139(5). Therefore, a fresh claim can be made before the Assessing Officer only by filing a revised return and not otherwise. The Supreme Court in Goetze (India) Ltd. vs. CIT (2006) 284 ITR 323 has held that there is no provision in the Income-tax Act, 1961 to allow an amendment in the return of income except by way of filing a revised return.

Question 40
The Assessing Officer within the powers vested in him under section 142(2A), while examining the accounts of PNF Ltd., had ordered to get the same audited. The company challenges this order on the ground “that the opportunity was not provided to them by the Assessing Officer prior to passing of such an order”. Decide the correctness of the action of the Assessing Officer.

Answer
As per the proviso to section 142(2A), the Assessing Officer shall not direct the assessee to get the accounts so audited unless the assessee has been given a reasonable opportunity of being heard.
Therefore, in this case, the order of the Assessing Officer is not valid, since the assessee was not given an opportunity of being heard prior to passing of such order.

Question 41
Smt. Kanti engaged in the business of growing, curing, roasting and grounding of coffee after mixing chicory had a total income of Rs. 6,00,000 from this business which was her only source of income during the year ended on 31.3.2020. She consults you to have an opinion whether she is required to file return of income for the A.Y. 2020-21 as per provisions of section 139(1).

Answer
The clarification regarding filing of return of income by the coffee growers being individuals covered by Rule 7B of the Income-tax Rules, 1962 is given in Circular No.10/2006 dated 16.10.2006. According to the Circular, an individual deriving income from growing, curing, roasting and grounding of coffee with or without mixing chicory, would not be required to file the return of income if the aggregate of 40% of his or her income from growing, curing, roasting and grounding of coffee with or without mixing chicory and income from all other sources liable to tax in accordance with the
provisions of this Act, is equal to or less than the basic exemption limit prescribed in the First Schedule of the Finance Act of the relevant year.

In this case, Smt. Kanti has a total income of Rs. 6,00,000 from this business, which was her only source of income for P.Y.2018-19. 40% of her total income works out to Rs. 2,40,000, which is less than the basic exemption limit of Rs. 2,50,000 in respect of an individual assessee. Therefore, Smt. Kanti is not required to file a return of income for the A.Y.2019-20 as per the provisions of section 139(1).

**Question 42**

Ram, an individual, filed his return of income for the assessment year 2020-21 on 15.6.2020. He later discovered that he had not claimed deduction under section 80C in the said return. He claimed the said deduction through a letter addressed to the Assessing Officer. The Assessing Officer completed the assessment without allowing the deduction claimed by Ram. Is the Assessing Officer justified in doing so?

**Answer**

The Supreme Court has, in Goetze (India) Ltd. v. CIT (2006) 284 ITR 323, ruled that the assessing authority has no power to entertain a claim for deduction made after filing of the return of income otherwise than by way of a revised return. In the instant case, Ram has claimed the deduction under section 80C, which he omitted to claim in the original return of income, through a letter addressed to the Assessing Officer and not by filing a revised return under section 139(5). In view of the decision of the Supreme Court cited above, the Assessing Officer was justified in completing the assessment without allowing the deduction under section 80C.

**Question 43**

Examine the correctness or otherwise of the following statements in the context of provisions contained in the Income-tax Act, 1961 and the decided case laws:

“The Assessing Officer is bound to allow the set-off of brought forward losses under section 72 even if the assessee has not claimed the same in the return filed”.

**Answer**

The statement is correct.

The Supreme Court has, in CIT v. Mahalakshmi Sugar Mills Co. Ltd. (1986) 160 ITR 920, held that it is the duty of the Assessing Officer to apply the relevant provisions of the Act for the purpose of determining the true figure of the assessee’s total income and consequential tax liability. Merely because the assessee has not claimed the set-off in the return filed, it cannot relieve the Assessing Officer of his duty to apply section 72 in the appropriate case.

As per CBDT Circular No.14 (XL-35) of 1955 dated 11.04.1955, it is the duty of the Assessing Officer to assist a taxpayer in every reasonable way, particularly in the matter of claiming and securing reliefs and in this regard, they should take the initiative in guiding a taxpayer where proceedings or other particulars before them indicate that some refund or relief is due to him.

Therefore, on the basis of the above Supreme Court ruling and the CBDT Circular, the Assessing Officer is bound to allow the set-off of brought forward losses under section 72, even if the assessee has not claimed the same in the return filed, provided the loss was determined in pursuance of a return filed under section 139(3) in any earlier previous year. Moreover, the wording used in section 72 is “shall”, indicating that the provisions relating to set off of brought forward business loss are mandatory.
Therefore, the Assessing Officer is bound to allow the claim for set off of brought forward business losses even if the assessee has not claimed the same in the return filed.

**Question 44**

X, an individual, has got his books of account for the year ending 31.3.2020 audited under section 44AB. His total income for the assessment year 2020-21 is Rs. 5,20,000. He desires to know if he can furnish his return of income for the assessment year 2020-21 through a Tax Return Preparer.

**Answer**

Section 139B provides for submission of return of income through Tax Return Preparers. It empowers the Central Board of Direct Taxes (CBDT) to frame a scheme for the purpose of enabling any specified class or classes of persons to prepare and furnish their returns of income through Tax Return Preparers. Specified class or classes of persons have been defined to mean any person, other than a company or a person whose accounts are required to be audited under section 44AB or under any other existing law, who is required to furnish a return of income under the Act. Thus, companies and persons whose accounts are liable for tax audit under section 44AB do not fall within the definition of ‘specified class or classes of persons’ and consequently, cannot furnish their returns of income through Tax Return Preparers. In the instant case, the books of account of X for the year ending 31.3.2020 have been audited under section 44AB. As such, he cannot furnish his return of income for the assessment year 2020-21 through a Tax Return Preparer.

**Question 45**

In April, 2019, the business premises of Priyanka Ravi were searched under section 132 by the DDI, Delhi. The search was concluded on 30.04.2019 and following assets/documents were found which were not recorded in her books of accounts:

- Jewellery of Rs. 25 Lacs pertaining to P.Y. 2014-15
- Agreement for purchase of land which contains the payment of advance of Rs. 35 Lacs in cash in the P.Y.2013-14
- Shares purchased in the P.Y.2011-12 and in the P.Y.2012-13 totaling to Rs. 40 Lacs.
- Paper containing the payment of Rs. 15 Lacs in the P.Y.2009-10 and Rs. 10 Lacs in P.Y.2008-09 to a contractor for construction of residential house.

Accordingly, Assessing Officer has issued the notice for all the previous years from P.Y.2008-09 to P.Y.2018-19 under section 153A.

However, Miss Priyanka Ravi contented that the Assessing Officer cannot issue the notice under section 153A beyond six assessment years immediately preceding the assessment year relevant to the previous year in which the search was conducted under section 132 i.e. notice can be issued up to A.Y.2014-15 (P.Y. 2013-14).

Discuss about the correctness of action of Assessing Officer and the contention of Miss Priyanka Ravi.

**Answer**

As per section 153A(1), issuance of notice and assessment or reassessment under the said section can also be made for an assessment year preceding the assessment year relevant to the previous year in which search is conducted or requisition is made which falls **beyond six assessment years but not beyond ten assessment years** from the assessment year relevant to the previous year in which search is conducted or requisition is made, provided that -
(i) the Assessing Officer has in his possession books of account or other documents or evidence which reveal that the income which has escaped assessment amounts to or is likely to amount to **fifty lakh rupees or more in one year or in aggregate in the relevant assessment years**;
(ii) such income escaping assessment is represented in the form of asset which **shall include immovable property being land or building or both, shares and securities, deposits in bank account, loans and advances**;
(iii) the income escaping assessment or part thereof relates to such year or years; and
(iv) search under section 132 is initiated or requisition under section 132A is made on or after 1-4-2017.

In the light of the above amended provision, the Assessing Officer can issue the notice u/s 153A beyond six assessment years but not beyond ten assessment years from the assessment year relevant to the previous year in which search is conducted or requisition is made. Thus, in the given case, the Assessing Officer can issue notice under section 153A upto A.Y.2010-11 as she,
a. has in his possession, documents or evidence which reveals the escaped assessment amounts to **Rs. 55 lacs in aggregate during the relevant four assessment years i.e. from A.Y. 2010-11 to A.Y. 2013-14**

b. such income escaping assessment represents in the form of assets which includes **Rs. 40 lacs being Shares purchased in P.Y. 2011-12 and P.Y. 2012-13 plus Rs. 15 lacs being payment to contractor for construction of residential house in P.Y. 2009-10** (payment of **Rs. 10 lacs relevant to P.Y. 2008-09 cannot be included as it is beyond ten assessment years)

c. search was conducted after 01.04.2017.

Hence, the contention of Miss. Priyanka Ravi that the Assessing Officer cannot issue the notice under section 153A beyond six assessment years immediately preceding the assessment year relevant to the previous year in which the search was conducted under section 132 is incorrect.

The action of Assessing Officer is **partly correct** as it is possible to him to issue notice beyond six assessment years but not beyond ten assessment years from the assessment year relevant to the previous year in which search is conducted or requisition is made. Thus, he cannot issue the notice under section 153A for the A.Y.2009-10.

**Question 46**
The assessment of Mr. Hari for A.Y.2012-13 was made on 28.3.2014 making an addition of **Rs. 3,25,000** for a certain income received during the P.Y.2011-12. The assessee contested the addition before Commissioner (Appeals) but lost the case. The Appellate Tribunal passed an order on 26.2.2019 holding that the said income was not taxable in the P.Y.2011-12 but the same was taxable in the year of accrual, being P.Y.2006-07 relevant to A.Y.2007-08. The Assessing Officer issued notice under section 148 for A.Y.2007-08 in March 2019 bringing to tax the sum of **Rs. 3,25,000**. Is the notice valid?

Would your answer change if in the said case, the assessment order for A.Y.2012-13 was made on 4.4.2014 instead of 28.3.2014?

**Solution**
Section 149 requires issue of notice under section 148 within a period of 6 years from the end of the relevant assessment year, where income escaping assessment exceeds **Rs. 1 lakh**. Accordingly, in respect of A.Y.2012-13, notice can be issued upto 31.3.2019. Section
150(1) enables issue of notice at any time to give effect to a finding contained in an appellate order. However, this is subject to the provisions of section 150(2), which places a restriction that if on the date of passing of the order which was the subject-matter of appeal, no notice could have been issued, then, such notice cannot be issued by virtue of the enabling provision contained in section 150(1).

In this case, the income was taxable in the A.Y. 2007-08 as per the order of the Appellate Tribunal. The six year time limit, in this case, expires on 31.3.2014. Since the original assessment in respect of such income was made on 28.3.2014, the notice issued under section 148 consequent to the Appellate Tribunal order is valid.

Had the assessment order for A.Y. 2012-13 been made on 4.4.2014 (instead of 28.3.2014), then the same would have been outside the six year time limit from A.Y. 2007-08. Hence, since notice could not have been issued at that point of time, it cannot be now issued invoking the provisions of section 150(1).
QUESTIONS ON INCOME TAX AUTHORITY & THEIR POWERS

Question 47
The Director General of Income Tax after getting the information that Mr. Mogambo is in possession of unaccounted cash of Rs. 50 lacs, issued orders by invoking powers vested in him as per section 131(1A), for its seizure. Is the order for seizure of cash issued by the Director General of Income Tax correct? If not, does the Director General of Income Tax have any other power to seize such cash?

Answer
The powers under section 131(1A) deal with power of discovery and production of evidence. They do not confer the power of seizure of cash or any asset. The Director General, for the purposes of making an enquiry or investigation relating to any income concealed or likely to be concealed by any person or class of persons within his jurisdiction, shall be competent to exercise powers conferred under section 131(1), which confine to discovery and inspection, enforcing attendance, compelling the production of books of account and other documents and issuing commissions. Thus, the power of seizure of unaccounted cash is not one of the powers conferred on the Director General under section 131(1A).

However, under section 132(1), the Director General has the power to authorize any Additional Director or Additional Commissioner or Joint Director or Joint Commissioner etc. to seize money found as a result of search [Clause (iii) of section 132(1)], if he has reason to believe that any person is in possession of any money which represents wholly or partly income which has not been disclosed [Clause (c) of section 132(1)]. Therefore, the proper course open to the Director General is to exercise his power under section 132(1) and authorize the Officers concerned to enter the premises where the cash is kept by Mr. Mogambo and seize such unaccounted cash.

Question 48
The premises of Ganesh were subjected to a search under section 132 of the Act. The search was authorized and the warrant was signed by the Joint Commissioner of Income-tax having jurisdiction over the assessee, consequent to information in his possession. The assessee challenged the validity of search on the ground that section 132(1) does not empower Joint Commissioner to authorise a search under the Act. Decide the correctness of the contention raised by the assessee.

Answer
Under section 132(1), the income-tax authorities listed therein are empowered to authorise other income-tax authorities to conduct search and seizure operations. The authorities empowered to issue authorization include such Additional Director, Additional Commissioner, Joint Director and Joint Commissioner as are empowered by the CBDT to do so.

However, a Joint Commissioner can issue warrant of authorization only if he has been specifically empowered to do so by the CBDT. Therefore, only if the Joint Commissioner has not been specifically empowered by the CBDT to do so, the contention of the assessee would hold good.

Question 49
Examine whether the information regarding possession of unexplained assets and income received from the Central Bureau of Investigation, a Government agency, can constitute “information” for action under section 132. Discuss.
Answer
As per section 132(1)(c), authorization for search and seizure can take place if the authority, in consequence of information in his possession, has reason to believe that any person is in possession of money, bullion, jewellery or other valuable article or thing and these assets represent, either wholly or partly, income or property which has not been, or would not be disclosed by such person for the purposes of this Act. In the absence of such information, a search cannot be validly authorized.
The Apex Court in *UOI v Ajit Jain [2003] 260 ITR 80* has held that mere intimation by the CBI that money was found in the possession of the assessee, which according to the CBI was undisclosed, without something more, does not constitute “information” within the meaning of section 132, on the basis of which a search warrant could be issued. Consequently, the Supreme Court held that the search conducted on this basis and the assessment made pursuant to such search was not valid.

Question 50
In the course of search operations under section 132 in the month of July, 2019, a tax payer makes a declaration under section 132(4) on the earning of income not disclosed in respect of P.Y.2018-19. Can that statement save the tax payer from a levy of penalty, if he is yet to file his return of income for A.Y.2019-20?

Answer
Since the search is conducted on or after 15.12.2016, and return is yet to be filed for the P.Y. 2018-19, the penalty would be as follows

1. penalty@30%, if undisclosed income is admitted during the course of search in the statement furnished under section 132(4), and the assessee explains the manner in which such income was derived, pays the tax, together with interest if any, in respect of the undisclosed income, and furnishes the return of income for the specified previous year declaring such undisclosed income on or before the specified date (i.e., the due date of filing return of income or the date on which the period specified in the notice issued under section 153A expires, as the case may be).

2. penalty@60% in any other case.

Therefore, even if the tax payer furnishes the statement under section 132(4), penalty@30% of undisclosed income of the specified previous year would be attracted under section 271AAB.

Question 51
Cash of Rs. 25 lacs was seized on 12.9.2019 in a search conducted as per section 132 of the Act. The assessee moved an application on 27.10.2019 to release such cash after explaining the sources thereof, which was turned down by the department. The assessee seeks your opinion on, the following issues:

(i) Can the department withhold the explained money?
(ii) If yes, then to what extent and up to what period?

Answer
The proviso to section 132B(1)(i) provides that where the person concerned makes an application to the Assessing Officer, within 30 days from the end of the month in which the asset was seized, for release of the asset and the nature and source of acquisition of the asset is explained to the satisfaction of the Assessing Officer, then, the Assessing Officer may, with the prior approval of the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner, release the asset after recovering the existing liability under the Income-tax Act, 1961, etc. out of such asset.
‘Existing liability’, however, does not include advance tax payable. Such asset or portion thereof has to be released within 120 days from the date on which the last of the authorizations for search under section 132 was executed.

In this case, since the application was made to the Assessing Officer within the 30 day period the amount of existing liability may be recovered out of the asset and the balance may be released within 120 days from the date on which the last of the authorizations for search under section 132 was executed.

Note: It may be noted that one of the conditions mentioned above for release of an asset is that the nature and source of acquisition of the asset should be explained to the satisfaction of the Assessing Officer. However, in this case, it has been given that the assessee’s application for release of the asset, explaining the sources thereof, was turned down by the Department. If the application was turned down by the Department due to the reason that it was not satisfied with the explanation given by the assessee as to the nature and source of acquisition of the asset, then, the asset (in this case, cash) cannot be released, since the condition mentioned above is not satisfied.

Question 52
The business premises of Ram Bharose Ltd. and the residence of two of its directors at Delhi were searched under section 132 by the DDI, Delhi. The search was concluded on 9.8.2019 and following were also seized besides other papers and records:

(i) Papers found in the drawer of an accountant relating to Shri Krishna Ltd., Mumbai indicating details of various business transactions. However, Ram Bharose Ltd. is not having any direct or indirect connection of any nature with these transactions and Shri Krishna Ltd., Mumbai and its directors.

(ii) Jewellery worth Rs. 5 lacs from the bedroom of one of the director, which was claimed by him to be of his married daughter.

(iii) Papers recording certain transactions of income and expenses having direct nexus with the business of the company for the period from 16.4.2015 to date of search. It was admitted by the director that the transactions recorded in such papers have not been incorporated in the books.

You are required to answer on the basis of aforesaid and the provisions of Act, following questions:

(a) What action the DDI shall be taking in respect of the seized papers relating to Shri Krishna Ltd., Mumbai?

(b) Whether the contention raised by the director as to jewellery found from his bedroom will be acceptable?

(c) What presumption shall be drawn in respect of the papers which indicate transactions not recorded in the books?

(d) Can the company move an application for settlement of case as per Chapter XIX-A of the Act?

Answer

(a) The authorised officer being DDI, Delhi is not having any jurisdiction over Shri Krishna Ltd., Mumbai, and therefore as per section 132(9A), the papers seized relating to this company shall be handed over by him to the Assessing Officer having jurisdiction over Shri Krishna Ltd., Mumbai within a period of 60 days from the date on which the last of the authorisations for search was executed for taking further necessary action thereon.
(b) The contention raised by the Director will not be acceptable because as per the provisions of sub-section (4A)(i) of section 132, where any books of account, other documents, money, bullion, jewellery or other valuables are found in the possession or control of any person in the course of search, then, in respect thereof, it may be presumed that the same belongs to that person.

(c) As per section 132(4A), the presumptions in respect of the papers, indicating transactions not recorded in the books but having direct nexus with the business of the company, are that the same belong to the company, contents of such papers are true and the handwriting in which the same are written is/are of the persons(s) whose premises have been searched.

(d) As per clause (iiiia) in the Explanation to section 245A, the assessee can approach the Settlement Commission at any time after the date of issue of notice under section 153A or section 153C initiating the assessment proceedings. Therefore, an application can be made to the Settlement Commission where search has been initiated under section 132 followed by assessment under section 153A or section 153C.

The proviso to section 245C(1) specifies the monetary limit for making application for settlement of cases, in respect of search cases. Accordingly, the additional amount of income-tax payable on the income disclosed in the application must exceed Rs. 50 lacs so that application for settlement of the case is eligible for admission.

Question 53
In the course of search on 25.03.2019, assets were seized. Examine the procedure laid down to deal with such seized assets under the Act.

Answer
Section 132B of the Income-tax Act, 1961 deals with the application of assets seized under section 132. Such assets will be first applied towards the existing liability under the Income-tax Act, 1961, etc. ‘Existing liability’, however, does not include advance tax payable. Further, the amount of liability determined on completion of search assessment (including any penalty levied or interest payable in connection with such assessment) and in respect of which the assessee is in default or deemed to be in default, may be recovered out of such assets.

Where the nature and source of acquisition of such seized assets is explained to the satisfaction of the Assessing Officer, the amount of any existing liability mentioned in para 1 above may be recovered out of such asset and the remaining portion, if any, of the asset may be released, with the prior approval of the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner, as the case may be. The release must be made within 120 days from the date on which the last of the authorisations for search under section 132 or for requisition under section 132A was executed. The assets would be released to the person from whose custody they were seized.

When the assets consist of solely of money, or partly of money and partly of other assets, the Assessing Officer may apply such money in the discharge of the liabilities referred to in para 1 above and the assessee shall be discharged of such liability to the extent of the money so applied. However, the assets other than money may also be applied for the discharge of such liabilities if the complete recovery could not be made from the money seized or the money seized was not sufficient.

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27.53
QUESTIONS ON APPEAL & REVISION

Question 54
"SVS Propcon" did not make a claim of Rs. 20 lacs in the return of income filed for A.Y. 2020-21 which was disallowed in the previous assessment year under section 43B. However, the said claim was also not considered by the Assessing Officer during assessment proceedings on the ground that no revised return was filed. Can the assessee now make such claim before the appellate authority?

Answer
Yes, the assessee is entitled to raise additional claims before the appellate authorities. The restriction that an additional claim has to be made by filing a revised return applies only in respect of a claim made before the Assessing Officer. An assessee cannot make a claim before the Assessing Officer otherwise than by filing a revised return. It was so held by the Supreme Court in Goetze (India) Ltd v. CIT (2006) 284 ITR 323. However, this restriction does not apply to an additional claim made before an appellate authority. The appellate authorities have jurisdiction to permit additional claims before them, though, the exercise of such jurisdiction is entirely the authorities’ discretion. It was so held by the Bombay High Court in CIT v. Pruthvi Brokers & Shareholders (2012) 349 ITR 336.

Thus, an additional claim can be raised before the Appellate Authority even if no revised return is filed.

Question 55
Examine the correctness or otherwise of the following statements with reference to the provisions of the Income-tax Act, 1961:

(i) An appeal before Income-tax Appellate Tribunal cannot be decided in the event of difference of opinion between the Judicial Member and the Accountant Member on a particular ground.

(ii) A High Court does not have an inherent power to review an earlier order passed by it on merits.

Answer
(i) The statement given is not correct. As per the provisions of section 255, in the event of difference in opinion between the members of the Bench of the Income-tax Appellate Tribunal, the matter shall be decided on the basis of the opinion of the majority of the members. In case the members are equally divided, they shall state the point or points of difference and the case shall be referred by the President of the Tribunal for hearing on such points by one or more of the other members of the Tribunal. Such point or points shall be decided according to the opinion of majority of the members of the Tribunal who heard the case, including those who had first heard it.

(ii) The statement given is not correct. The Supreme Court, in CIT v. Meghalaya Steels Ltd. (2015) 377 ITR 112, observed that the power of review would inhere on High Courts, being courts of record under article 215 of the Constitution of India. There is nothing in article 226 of the Constitution to preclude a High Court from exercising the power of review which inhere in every court of plenary jurisdiction to prevent miscarriage of justice or to correct grave and palpable errors committed by it. The Supreme Court further observed that section 260A(7) does not purport in any manner to curtail or restrict the application of the provisions of the Code of Civil Procedure. Section 260A(7) only states that all the provisions that would
apply qua appeals in the Code of Civil Procedure would apply to appeals under section 260A. The Supreme Court opined that this does not in any manner suggest either that the other provisions of the Code of Civil Procedure are necessarily excluded or that the High Court’s inherent jurisdiction is in any manner affected.

**Question 56**
Does the Income-tax Appellate Tribunal have the following powers?

(i) Power to allow the assessee to urge any ground of appeal which was not raised by him before the Commissioner (Appeals);

(ii) Power to recall its own order.

**Answer**

(i) The Income-tax Appellate Tribunal has the power to entertain question raised for the first time. The Tribunal is not confined only to the issues arising out of the appeal before the Commissioner (Appeals). It has the power to allow the assessee to urge any ground not raised before the Commissioner (Appeals). However, the relevant facts in respect of such ground should be on record. The decision of the Supreme Court in the case of National Thermal Power Company Limited vs. CIT (1998) 229 ITR 383 (SC) supports this view.

(ii) The Delhi High Court, in Lachman Dass Bhatia Hingwala (P) Ltd. v. ACIT (2011) 330 ITR 243 (Delhi)(FB) observed that the justification of an order passed by the Tribunal recalling its own order is required to be tested on the basis of the law laid down by the Apex Court in Honda Siel Power Products Ltd. v. CIT (2007) 295 ITR 466, dealing with the Tribunal's power under section 254(2) to recall its order where prejudice has resulted to a party due to an apparent omission, mistake or error committed by the Tribunal while passing the order. Such recalling of order for correcting an apparent mistake committed by the Tribunal has nothing to do with the doctrine or concept of inherent power of review. It is a well settled provision of law that the Tribunal has no inherent power to review its own judgment or order on merits or reappreciate the correctness of its earlier decision on merits. However, the power to recall has to be distinguished from the power to review. While the Tribunal does not have the inherent power to review its order on merits, it can recall its order for the purpose of correcting a mistake apparent from the record.

When prejudice results from an order attributable to the Tribunal’s mistake, error or omission, then it is the duty of the Tribunal to set it right. The Delhi High Court observed that the Tribunal, while exercising the power of rectification under section 254(2), can recall its order in entirety if it is satisfied that prejudice has resulted to the party which is attributable to the Tribunal’s mistake, error or omission and the error committed is apparent.

**Question 57**
Can a rectification order under section 254 of the Income-tax Act, 1961 be passed by the Income-tax Appellate Tribunal beyond 6 months from the end of the month in which the order sought to be rectified was passed?

**Answer**

The issue as to whether a rectification order can be passed by the Income-tax Appellate Tribunal under section 254 beyond six months from the end of the month in which order sought to be rectified was passed, has been addressed in Sree Ayyanar Spinning and Weaving Mills Ltd. v. CIT (2008) 301 ITR 434 (SC). Section 254(2), dealing with the power of the Appellate Tribunal to pass an order of rectification of mistakes, is in two parts.
The first part refers to the suo motu exercise of the power of rectification by the Appellate Tribunal, whereas the second part refers to rectification on an application filed by the assessee or Assessing Officer bringing any mistake apparent from the record to the attention of the Appellate Tribunal.

If Income-tax Appellate Tribunal, suo moto, makes the rectification of its order, then the order has to be passed within 6 months from the end of the month in which the order sought to be rectified was passed. Where the application for rectification is made by the Assessing Officer or the assessee within 6 months from the end of the month in which the order sought to be rectified was passed, the Appellate Tribunal is bound to decide the application on merits and not on the ground of limitation i.e. order can be passed after expiry of 6 months from the end of the month in which the order sought to be rectified was passed. However, the application for rectification cannot be filed belatedly after 6 months from the end of the month in which the order sought to be rectified was passed. [Ajith Kumar Pitaliya vs ITO (2009) 318 ITR 182 (M.P.)]

Question 58
What do you mean by substantial question of law? Examine.
Answer
The expression “substantial question of law” has not been defined anywhere in the Act. However, it has acquired a definite meaning through various judicial pronouncements. The tests are:
(1) whether directly or indirectly it affects substantial rights of the parties; or
(2) the question is of general public importance; or
(3) whether it is an open question in the sense that issue is not settled by the pronouncement of the Supreme Court or Privy Council or by the Federal Court; or
(4) the issue is not free from difficulty; or
(5) it calls for a discussion for alternative view.

Question 59
Examine the correctness of the following statement:
“The Appellate Tribunal is empowered to grant indefinite stay for the demand disputed in appeals before it.”
Answer
Section 254(2A) provides that the Appellate Tribunal, where it is possible, may hear and decide an appeal within a period of four years from the end of the financial year in which such appeal is filed.
The Appellate Tribunal may, on merit, pass an order of stay in any proceedings relating to an appeal. However, such period of stay cannot exceed 180 days from the date of such order. The Appellate Tribunal has to dispose off the appeal within this period of stay.
Where the appeal has not been disposed of within this period and the delay in disposing the appeal is not attributable to the assessee, the Appellate Tribunal can further extend the period of stay originally allowed. However, the aggregate of period originally allowed and the period so extended should not exceed 365 days even if the delay in disposing of the appeal is not attributable to the assessee. The Appellate Tribunal is required to dispose off the appeal within this extended period. If the appeal is not disposed of within such period or periods, the order of stay shall stand vacated after the expiry of such period or periods. Therefore, the statement given in the question is not correct.
**Question 60**

Is Commissioner (Appeals) empowered to consider an appeal filed by an assessee challenging the order of assessment in respect of which the proceedings before the Settlement Commission abates? Examine.

**Answer**

Section 251(1) lists the powers of the Commissioner (Appeals) in disposing of an appeal. Clause (aa) of section 251(1) empowers the Commissioner (Appeals), in an appeal against the assessment order in respect of which the proceeding before the Settlement Commission abates under section 245HA, to confirm, reduce, enhance or annul the assessment after taking into consideration the following -

1. all the material and other information produced by the assessee before the Settlement Commission;
2. the results of the inquiry held by the Settlement Commission;
3. the evidence recorded by the Settlement Commission in the course of the proceeding before it; and
4. such other material as may be brought on his record.

**Question 61**

An Income-tax authority did not file an appeal to the Income-tax Appellate Tribunal against an order of the Commissioner (Appeals) decided against the Income-tax department on a particular issue in case of one assessee, Alpi for assessment year 2019-20 on the ground that the tax effect of such dispute was less than the monetary limit prescribed by CBDT. In assessment year 2020-21, similar issue arose in the assessments of Alpi and her sister Palki, which was decided by the Commissioner (Appeals) against the Department. Can the Income-tax department move an appeal to the Tribunal in respect of A.Y. 2020-21 against the orders of the Commissioner (Appeals) for Alpi and her sister Palki?

**Answer**

Under section 268A(1), the CBDT is empowered to issue orders, instructions or directions to the other income-tax authorities, fixing such monetary limits, as it may deem fit, to regulate filing of appeal or application for reference by any income-tax authority.

Under section 268A(2), where an income-tax authority has not filed any appeal or application for reference on any issue in the case of an assessee for any assessment year, due to above-mentioned order/instruction/direction of the CBDT, such authority shall not be precluded from filing an appeal or application for reference on the same issue in the case of the same assessee for any other assessment year or any other assessee for the same or any other assessment year. Further, in such a case, it shall not be lawful for an assessee to contend that the income-tax authority has acquiesced in the decision on the disputed issue by not filing an appeal or application for reference in any case.

In view of above provision, it would be in order for the Income-tax Department to move an appeal to the Tribunal against the orders of the CIT(A) in respect of A.Y. 2020-21 both for Alpi and Palki.

**Question 62**

A petition for stay of demand was filed before ITAT by XYZ Ltd. in respect of a disputed demand for which appeal was pending before it, on which stay was granted by the ITAT vide order dated 1.1.2019. The bench could not function thereafter till 1.2.2020 and therefore, the disputed matter could not be disposed off. The Assessing Officer attached the bank account on 16.2.2020 and recovered the amount of Rs. 15 lacs against
the arrear demand of Rs. 25 lacs. The assessee requested the Assessing Officer to refund back the amount as it holds stay over it. The Assessing Officer rejected the contention of the assessee. Now the assessee seeks your opinion.

**Answer**

The Appellate Tribunal may, on merit, pass an order of stay in any proceedings relating to an appeal. However, such period of stay cannot exceed 180 days from the date of such order. The Appellate Tribunal has to dispose off the appeal within this period of stay. Where the appeal has not been disposed off within this period and the delay in disposing the appeal is not attributable to the assessee, the Appellate Tribunal can further extend the period of stay originally allowed. Section 254(2A) provides that the aggregate of the period originally allowed and the period or periods so extended or allowed shall not, in any case, exceed 365 days, even if the delay in disposing of the appeal is not attributable to the assessee. If the appeal is not disposed of within such period or periods, the order of stay shall stand vacated after the expiry of such period or periods.

Accordingly, even if an appeal is not heard by the bench, say, due to the bench not functioning or due to the department seeking adjournment, the stay granted by the Appellate Tribunal shall stand vacated after the period of 365 days, inspite of the assessee having taken all steps to ensure speedy disposal of the appeal and having a good prima facie case.

In the present case, the period of 365 days has expired on 31.12.2019, after which date the order of stay stands vacated. Accordingly, the recovery of Rs. 15 lacs against the arrear demand of Rs. 25 lacs made by the Assessing Officer on 16.2.2020 is in order.

**Question 63**

An assessee who had been served with an order of assessment passed under section 143(3) on 1.1.2020 had filed an application against this order before the CIT as per section 264 on 11.1.2020. However, the CIT refused to entertain the application on the pretext of premature application. Assessee seeks your opinion.

**Answer**

An assessee, who is aggrieved by the order of the Assessing Officer under section 143(3) passed on 1.1.2020, had moved an application for revision of order under section 264 on 11.1.2020. The order passed by the Assessing Officer under section 143(3) is an order appealable before the Commissioner (Appeals). The time limit for filing an appeal is 30 days from the date of order i.e., upto 31.1.2020. This time limit had not expired on 11.1.2020 and the assessee had also not waived his right of appeal while filing the application for revision on 11.1.2020 before the Commissioner of Income-tax. The application filed before the Commissioner of Income-tax for revision under section 264 by the assessee will only be considered when the conditions specified under section 264(4) have been complied with. One of the conditions is that the Commissioner shall not revise any order where an appeal against the order lies to the Commissioner (Appeals) or Appellate Tribunal and the time within which such appeal may be made has not expired, unless the assessee has waived his right of appeal. In the present case, the time limit had not expired on 11.1.2020 and the assessee had also not waived the right of appeal while filing the application for revision before the Commissioner of Income-tax on 11.1.2020 under section 264. Therefore, the Commissioner’s refusal to entertain such application is correct.

**Note:** In practical situations, the Commissioner could have kept the proceedings in abeyance till the expiry of the time prescribed for filing appeal by the assessee and thereafter, could have assumed jurisdiction for making revision besides taking an undertaking from the assessee for waiving his right of appeal. In reality, taxpayers
usually will not prefer revision in such short time period nor would the Commissioner reject the application, the moment it is received by him.

**Question 64**

Answer the following in the context of provisions contained in the Income-tax Act, 1961:

The assessment for A.Y. 2016-17 was completed as per section 143(3) considering the various claims so made by the assessee on 23.12.2017. Subsequently, this was reopened under section 147 on certain issues, but excluding the claim of the assessee as to “Lease Equalisation Fund”. The order of reassessment was passed on 18.11.2018. The Commissioner within the powers vested under section 263 passed an order on 11.4.2020 rejecting the claim of assessee as to “Lease Equalisation Fund”. The assessee challenges that the action of the CIT is not sustainable because the same was barred by limitation.

**Answer**

This issue was settled by the Supreme Court in CIT v. Alagendran Finance Ltd. (2007) 293 ITR 1. The Supreme Court observed that though there was no doubt that once an order of assessment is reopened, the previous assessment will be held to be set aside and the whole proceedings would start afresh, however, it would not mean that even when the subject-matter of reassessment is distinct and different, the entire proceeding would be deemed to have been reopened. The doctrine of merger would apply only in a case where the subject-matter of reassessment and the subject-matter of assessment are the same. However, in this case, the revision proceedings related to Lease Equalisation Fund, which was not the subject matter of reassessment. Therefore, the doctrine of merger does not apply in this case.

Section 263(2) provides no order shall be made under section 263(1) after the expiry of two years from the end of the financial year in which the order sought to be revised was passed. The period of limitation as referred to in section 263(2) relates to the assessment in which the claim of the assessee as to Lease Equalisation Fund was considered by the Assessing Officer. This issue was not the subject matter of reassessment proceedings. Accordingly, the period of limitation shall be reckoned with reference to the original assessment order and not from the date of the order of reassessment. Therefore, in this case, the revision proceedings are barred by limitation since the original assessment order was made on 23.12.2017 and the revision should have been made by 31.3.2020.

**Question 65**

An assessee, who is aggrieved by all or any of the following orders, is desirous to know the available remedial recourse and the time limit against each under the Income-tax Act, 1961:

(i) passed under section 143(3) by the Assessing Officer.
(ii) passed under section 263 by the Commissioner of Income-tax.
(iii) passed under section 272A by the Director General.
(iv) passed under section 254 by the ITAT.

**Answer**

(i) An assessee, aggrieved by the order passed under section 143(3) by the Assessing Officer, can file an appeal before the Commissioner of Income-tax (Appeals) under section 246A(1) within 30 days of the date of service of the notice of demand relating to the assessment. However, where the assessee does not want to prefer an appeal, then he can move a revision petition before the Principal Commissioner or Commissioner of Income-tax under section 264 within a period of one year from the
date of on which the order was communicated to him or the date on which he otherwise came to know of it, whichever is earlier.

(ii) An assessee, aggrieved by the order passed under section 263 by the Commissioner of Income-tax, can file an appeal to Income-tax Appellate Tribunal under section 253(1)(c) within 60 days of the date on which the order sought to be appealed against is communicated to the assessee.

(iii) An assessee, aggrieved by the order passed under section 272A by the Director General, can file an appeal before the Income-tax Appellate Tribunal under section 253(1)(c) within 60 days of the date on which the order sought to be appealed against is communicated to the assessee.

(iv) An assessee, aggrieved by the order passed under section 254 by the Income-tax Appellate Tribunal, can file an appeal before the High Court under section 260A within 120 days from the date of receipt of order of Income-tax Appellate Tribunal, only where the order gives rise to a substantial question of law.

**Question 66**
Who can file memorandum of cross-objections before the Income-tax Appellate Tribunal? What is the time limit? What is the fee for filing memorandum of cross objections?

**Answer**
Section 253(4) of the Income-tax Act, 1961 gives the respondent (assessee or the Assessing Officer), in every appeal filed before the Income-tax Appellate Tribunal, a right to file a memorandum of cross-objections against any order of the Commissioner (Appeals). This right of filing a memorandum of cross-objections is an independent right given to the respondent in an appeal and is in addition to the right of appeal which may or may not be exercised by the assessee or the Assessing Officer under section 253(1) or section 253(2). The memorandum of cross-objections has to be in the prescribed form and verified in the prescribed manner and has to be filed within 30 days of the receipt of notice of the appeal. The Tribunal is empowered to permit filing of memorandum of cross-objections after the expiry of the prescribed period if sufficient cause is shown. Such memorandum of cross-objections will be disposed of by the Appellate Tribunal as if it were an appeal presented within the time specified in section 253(3). There is no fee for filing a memorandum of cross-objections.
QUESTIONS ON PENALTIES

Question 67
A search under section 132 was initiated in the premises of Mr. X on 30.4.2019 and undisclosed money and jewellery belonging to Mr. X was found in his premises. Examine the penal provisions under the Income-tax Act which are attracted in this case, assuming that the undisclosed assets were acquired out of his undisclosed income of previous year 2019-20.

Answer
In order to deter the practice of non-disclosure of income, section 271AAB(1A) provides for levy of penalty on undisclosed income found during the course of a search, which relates to specified previous year, i.e.-

- the previous year which has ended before the date of search, but the due date of filing return of income for the same has not expired before the date of search and the return has not yet been furnished (P.Y. 2018-19);
- the previous year in which search is conducted (P.Y. 2019-20).

Accordingly, under section 271AAB(1A), in respect of searches initiated on or after 15.12.2016,

- penalty@30% would be attracted, if undisclosed income is admitted during the course of search in the statement furnished under section 132(4), and the assessee explains the manner in which such income was derived, pays the tax, together with interest if any, in respect of the undisclosed income, and furnishes the return of income for the specified previous year declaring such undisclosed income on or before the specified date (i.e., the due date of filing return of income or the date on which the period specified in the notice issued under section 153A expires, as the case may be).
- In all other cases, penalty @60% of undisclosed income would be attracted.

Question 68
What is the quantum of penalty that could be levied in each of the following cases -
(i) Failure to get books of accounts audited as required under section 44AB within the time prescribed under the Act.
(ii) Failure to comply with a direction issued under section 142(2A).
(iii) Failure to furnish report from an accountant as required under section 92E.

Answer
The penalty that could be levied in each case is:
(i) **Failure to get books of accounts audited as required under section 44AB of the Income-tax Act, 1961** - a sum equal to ⅔% of the total sales, turnover or gross receipts, as the case may be, in business, or of the gross receipts in profession, in such previous year or years, or a sum of Rs. 1,50,000, whichever is less [Section 271B].
(ii) **Failure to comply with a direction issued under section 142(2A)** – a sum of Rs. 10,000 [Section 272A(1)(d)].
(iii) **Failure to furnish report from an accountant as required by section 92E** - a sum of Rs. 1,00,000 [Section 271BA].

Question 69
X, an individual whose total sales in the business of food grains for the year ending 31.3.2020 was Rs. 205 lakhs, did not maintain books of account for P.Y.2019-20, even
though his turnover exceeded Rs. 25 lakhs in the P.Y.2018-19. The Assessing Officer levied penalty of Rs. 25,000 under section 271A for non-maintenance of books of account and penalty of Rs. 1,02,500 under section 271B for not getting the books audited as required by section 44AB. Is the Assessing Officer justified in levying penalty under section 271B?

**Answer**

X is required to maintain books of account as per section 44AA for the P.Y.2019-20 since his turnover exceeded Rs. 25 lakhs in the P.Y.2018-19. He also has to get them audited under section 44AB, since his gross sales in the P.Y.2019-20 exceeds Rs. 1 crore. He is liable to pay penalty under section 271A for not maintaining his books of account as per section 44AA. Accordingly, the action of the Assessing Officer in levying penalty of Rs. 25,000 under section 271A is correct. However, where books of account have not been maintained, there cannot be a question of getting them audited. Audit of books of account presupposes maintenance of books of account. When admittedly X has not maintained books, he cannot obviously get the audit done.

In Surajmal Parsuram Todi v. CIT (1996) 222 ITR 691, the Gauhati High Court has held that when a person commits an offence by not maintaining books of accounts as contemplated by section 44AA, the offence is complete and after that there can be no possibility of any offence as contemplated by section 44AB and, therefore, the imposition of penalty under section 271B is erroneous.

Therefore, in this case, the Assessing Officer is not justified in levying penalty under section 271B.

**Question 70**

State the conditions, if any, to be satisfied by an assessee in order to get relief under section 273A(4) regarding the waiver of penalty. Can the Commissioner refuse to grant relief, when the conditions laid down in the section was complied with, by the assessee?

**Answer**

There are two conditions to be satisfied by an assessee in order to get relief in the form of a waiver or reduction of penalty by the Commissioner of Income-tax under section 273A(4) of the Act. These conditions are:

(i) The payment of penalty would cause "genuine hardship" to the assessee and the Commissioner is satisfied about the existence of genuine hardship having regard to the circumstances of the case. The existence of genuine hardship would entitle the assessee to relief. The CBDT in its Circular No 784 dated 22-11-1999 has clarified that "genuine hardship" referred to in the provisions of section 273A(4) should exist both at the time at which the application under section 273A(4) is made by the assessee before the Commissioner and at the time of passing of order under section 273A(4) by the Commissioner.

(ii) The assessee has co-operated in any enquiry relating to the assessment or any proceeding for the recovery of any amount due from him. As per the decision of Andhra Pradesh High Court in K.S.N. Murthy v. Chairman, CBDT (2001) 252 ITR 269, if the above conditions laid down for exercise of the discretion are satisfied, the Principal Commissioner or Commissioner cannot refuse to exercise the discretion. Though the power given to the Commissioner under section 273A is discretionary, the exercise of discretion cannot be either arbitrary or capricious and has to be judicious and objective, once the conditions required for exercise of discretion in any judicial or quasi-judicial proceedings are satisfied. Such discretion must be exercised taking into consideration all relevant facts.
The satisfaction for exercise of discretionary power under the section must be based on objective consideration and not on subjective satisfaction.

Also, as per the proviso to section 273A(4), in case the quantum of penalty exceeds Rs. 1 lakh, the Principal Commissioner or Commissioner can grant relief only with the previous approval of the Principal Chief Commissioner or Chief Commissioner or the Principal Director General or Director General, as the case may be.

Note - The Principal Commissioner or Commissioner has to pass an order under section 273A(4), either accepting or rejecting the application in full or in part, within a period of 12 months from the end of the month in which the application is received. Further, no order rejecting the application, either in full or in part, shall be passed unless the assessee has been given an opportunity of being heard.

**Question 71**

An assessee had credited a sum of Rs. 50,000 in cash in the account of Madan, said to represent a loan obtained from him. The Assessing Officer, having gone into the genuineness of the transaction, disbelieved the story of loan and treated the sum of Rs. 50,000 as the income of the assessee from undisclosed sources. He also started proceedings under section 271D and levied a penalty of Rs. 60,000 on the assessee for having accepted the loan in contravention of section 269SS. Examine the correctness of the levy.

**Answer**

There are several flaws in the penalty levied by the Assessing Officer. Firstly, the penalty leviable under section 271D cannot exceed the sum equal to the loan taken. Hence, the maximum penalty leviable would be Rs. 50,000. Secondly, any penalty imposable under section 271D shall be imposed by the Joint Commissioner. Hence, unless the Assessing Officer happens to be a Joint Commissioner the levy of penalty will be invalid. Thirdly, the Assessing Officer cannot, on the one hand, treat the loan as undisclosed income of the assessee and on the other, treat it as a loan for the purpose of section 269SS read with section 271D. Such a treatment will be self-contradictory. The moment the amount of Rs. 50,000 is treated as undisclosed income, it ceases to bear the character of loan and therefore, the foundation for the levy of penalty under section 271D disappears. [Diwan Enterprises v. CIT and Others (2000) 246 ITR 571].

**Question 72**

Examine the following cases and state whether the same are liable for penalty as per the provisions of the Income-tax Act, 1961.

(i) Raman & Associates had made payment in excess of the limits prescribed to the contractors for carrying out labour job work at various sites, but had not deducted tax at source as per section 194C. 

(ii) Hotels & Hotels were asked by Income-tax Officer (CIB) to furnish details of all such tourists who stayed in their hotels and had paid bill amount in excess of Rs. 10,000. They have not furnished the requisite information in spite of various reminders.

**Answer**

(i) Penalty under section 271C is attracted for failure to deduct tax at source. The penalty would be a sum equal to the amount of tax which such person has failed to deduct. Such penalty can be imposed only by the Joint Commissioner. Therefore, Raman & Associates shall be liable for penalty under section 271C equal to the amount of tax
which they have failed to deduct under section 194C from the payments made to the contractors. The penalty would be in addition to the disallowance of 30% of expenditure/payment under section 40(a)(ia).

(ii) Section 133(6) empowers the Income-tax authority to require any person to furnish information in relation to such points or matters which will be useful for or relevant to any enquiry or proceeding under the Act. Failure on the part of an assessee to furnish the information in relation to such points or matters as required makes him liable for penalty under section 272A(2) of Rs. 100 for every day during which the failure continues.

Note – In a case where no proceeding is pending, the Income-tax authority can exercise this power only after obtaining the approval of the Principal Director/Director or Principal Commissioner/Commissioner as the case may be. In this case, it is presumed that the Income-tax authority has obtained the approval of the Principal Director/Director or Principal Commissioner/Commissioner before exercising this power.

Question 73
Fox Limited failed to furnish information and documents sought by the Transfer Pricing Officer (TPO). Can TPO levy penalty for such failure? How much would be the quantum of penalty imposable for the said failure?

Answer
Under section 271G, if any person who has entered into an international transaction or specified domestic transaction fails to furnish any such information or document as required by section 92D(3) sought for by the Transfer Pricing Officer, then, such person shall be liable to a penalty which may be levied by the Assessing Officer or the Transfer Pricing Officer or the Commissioner (Appeals). Thus, the Transfer Pricing Officer is a competent authority to levy penalty.

Penalty would be a sum equal to 2% of the value of international transaction or specified domestic transaction for each such failure.

Question 74
What would be the penalty leviable under section 270A in case of the following assessees, if none of the additions or disallowances made in the assessment or reassessment qualify under section 270A(6) and the under-reported income is not on account of misreporting?

<table>
<thead>
<tr>
<th>Particulars of total income of A.Y.2020-21</th>
<th>M/s. Alpha, a resident firm</th>
<th>Beta Ltd., an Indian company</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) As per the return of income furnished u/s 139(1)</td>
<td>35,00,000</td>
<td>(12,00,000)</td>
</tr>
<tr>
<td>(2) Determined under section 143(1)(a)</td>
<td>45,00,000</td>
<td>(6,00,000)</td>
</tr>
<tr>
<td>(3) Assessed under section 143(3)</td>
<td>62,00,000</td>
<td>(2,00,000)</td>
</tr>
<tr>
<td>(4) Reassessed under section 147</td>
<td>81,00,000</td>
<td>6,00,000</td>
</tr>
</tbody>
</table>

Note – Beta Ltd. is a trading company. The total turnover of Beta Ltd. for the P.Y.2017-18 was Rs. 401 crore and the company has not exercised option under section 115BAA.

Answer
Penalty leviable under section 270A in case of M/s. Alpha, a resident firm
M/s. Alpha is deemed to have under-reported its income since:
(1) its income assessed under 143(3) exceeds its income determined in a return processed under section 143(1)(a); and
(2) the income reassessed under section 147 exceeds the income assessed under section 143(3).

Therefore, penalty is leviable under section 270A for under-reporting of income.

### Computation of penalty leviable under section 270A

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assessment under section 143(3)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Under-reported income:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total income assessed under section 143(3)</td>
<td>62,00,000</td>
<td></td>
</tr>
<tr>
<td>(-) Total income determined u/s 143(1)(a)</td>
<td>45,00,000</td>
<td>17,00,000</td>
</tr>
<tr>
<td><strong>Tax payable on under-reported income:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tax on under-reported income of Rs. 17 lakhs plus total income of Rs. 45 lakhs determined u/s 143(1)(a) [30% of Rs. 62 lakh + EC &amp; SHEC@4%]</td>
<td>19,34,400</td>
<td></td>
</tr>
<tr>
<td>Less: Tax on total income determined u/s 143(1)(a) [30% of Rs. 45 lakh + EC &amp; SHEC@4%]</td>
<td>14,04,000</td>
<td>5,30,400</td>
</tr>
<tr>
<td>Penalty leviable@50% of tax payable</td>
<td>2,62,200</td>
<td></td>
</tr>
</tbody>
</table>

**Reassessment under section 147 Under-reported income:**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assessment under section 143(3)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Under-reported income:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total income reassessed under section 147</td>
<td>81,00,000</td>
<td></td>
</tr>
<tr>
<td>(-) Total income assessed under section 143(3)</td>
<td>62,00,000</td>
<td>19,00,000</td>
</tr>
<tr>
<td><strong>Tax payable on under-reported income:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tax on under-reported income of Rs. 19 lakhs plus total income of Rs. 62 lakhs assessed u/s 143(3) [30% of Rs. 81 lakh + EC &amp; SHEC@4%]</td>
<td>25,27,200</td>
<td></td>
</tr>
<tr>
<td>Less: Tax on total income assessed u/s 143(3) [30% of Rs. 62 lakh + EC &amp; SHEC@4%]</td>
<td>19,34,400</td>
<td>5,92,800</td>
</tr>
<tr>
<td>Penalty leviable@50% of tax payable</td>
<td>2,96,400</td>
<td></td>
</tr>
</tbody>
</table>

**Penalty leviable under section 270A in the case of Beta Ltd., an Indian company**

Beta Ltd. is deemed to have under-reported its income since:
(1) the assessment under 143(3) has the effect of reducing the loss determined in a return processed under section 143(1)(a); and
(2) the reassessment under section 147 has the effect of converting the loss assessed under section 143(3) into income.

Therefore, penalty is leviable under section 270A for under-reporting of income.

### Computation of penalty leviable under section 270A

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assessment under section 143(3)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Under-reported income:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loss assessed u/s 143(3)</td>
<td>(2,00,000)</td>
<td></td>
</tr>
<tr>
<td>(-) Loss determined under section 143(1)(a)</td>
<td>(6,00,000)</td>
<td>4,00,000</td>
</tr>
</tbody>
</table>

27.65
Past Questions

### Question 75

M/s. XYZ is a firm liable to tax@30%. The following are the particulars furnished by the firm for A.Y.2020-21:

<table>
<thead>
<tr>
<th>Particulars of total income</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) As per the return of income furnished u/s 139(1)</td>
<td>50,00,000</td>
</tr>
<tr>
<td>(2) Determined under section 143(1)(a)</td>
<td>60,00,000</td>
</tr>
<tr>
<td>(3) Assessed under section 143(3)</td>
<td>75,00,000</td>
</tr>
<tr>
<td>(4) Reassessed under section 147</td>
<td>95,00,000</td>
</tr>
</tbody>
</table>

Can penalty be levied under section 270A on M/s. XYZ? If the answer is in the affirmative, compute the penalty leviable under section 270A.

### Solution

M/s. XYZ is deemed to have under-reported its income since:

1. its income assessed under 143(3) exceeds its income determined in a return processed under section 143(1)(a); and
2. the income reassessed under section 147 exceeds the income assessed under section 143(3).

Therefore, penalty is leviable under section 270A for under-reporting of income.

#### Computation of penalty leviable under section 270A

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assessment under section 143(3)</td>
<td></td>
</tr>
<tr>
<td>Under-reported income:</td>
<td></td>
</tr>
<tr>
<td>Total income assessed under section 143(3)</td>
<td>75,00,000</td>
</tr>
<tr>
<td>(-) Total income determined u/s 143(1)(a)</td>
<td>60,00,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>15,00,000</strong></td>
</tr>
<tr>
<td>Tax payable on under-reported income:</td>
<td></td>
</tr>
<tr>
<td>Tax on under-reported income of Rs. 15 lakhs plus tax on total income of Rs. 60 lakhs determined u/s 143(1)(a) [30% of Rs. 75 lakh + EC &amp; SHEC@4%]</td>
<td>23,40,000</td>
</tr>
<tr>
<td>Less: Tax on total income determined u/s 143(1)(a) [30% of Rs. 60 lakh]</td>
<td>18,72,000</td>
</tr>
</tbody>
</table>

Note – The applicable rate of tax for Beta Ltd. for A.Y.2020-21 is 30%, since its turnover for the P.Y.2017-18 exceeded Rs. 400 crore.
<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs. 60 lakh + EC &amp; SHEC@4%</th>
<th>4,68,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Penalty leviable@50% of tax payable</td>
<td></td>
<td>2,34,000</td>
</tr>
</tbody>
</table>

**Reassessment under section 147**

**Under-reported income:**

| Total income reassessed under section 147       | 95,00,000 |
| (-) Total income assessed under section 143(3) | 75,00,000 |
| **20,00,000**                                   |           |

**Tax payable on under-reported income:**

| Tax on under-reported income of Rs. 20 lakhs plus tax on total income of Rs. 75 lakhs assessed u/s 143(3) [30% of Rs. 95 lakh + EC & SHEC@4%] | 29,64,000 |
| Less: Tax on total income assessed u/s 143(3) [30% of Rs. 75 lakh + EC & SHEC@4%] | 23,40,000 |
| **6,24,000**                                    |           |

Penalty leviable@50% of tax payable

| 89,700 |

**Note** – The following assumptions have been made-

1. None of the additions or disallowances made in assessment or reassessment qualifies under section 270A(6); and
2. The under-reported income is not on account of misreporting.

**Question 76**

Mr. Ram, a resident individual of the age of 55 years, has not furnished his return of income for A.Y.2020-21. However, the total income assessed in respect of such year under section 144 is Rs. 12 lakh. Is penalty under section 270A attracted in this case, and if so, what is the quantum of penalty leviable?

**Solution**

Mr. Ram is deemed to have under-reported his income since he has not filed his return of income and his assessed income exceeds the basic exemption limit of Rs. 2,50,000. Hence, penalty under section 270A is leviable in his case.

**Computation of penalty leviable under section 270A**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assessment under section 143(3)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Under-reported income:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total income assessed under section 143(3)</td>
<td>12,00,000</td>
<td></td>
</tr>
<tr>
<td>(-) Basic exemption limit</td>
<td>2,50,000</td>
<td><strong>9,50,000</strong></td>
</tr>
<tr>
<td>Tax payable on under-reported income as increased by the basic exemption limit [30% of Rs.2 lakhs + Rs. 1,12,500]</td>
<td>1,72,500</td>
<td></td>
</tr>
<tr>
<td>Add: EC &amp; SHEC@4%</td>
<td>6,900</td>
<td>1,79,400</td>
</tr>
<tr>
<td>Penalty leviable@50% of tax payable</td>
<td>89,700</td>
<td></td>
</tr>
</tbody>
</table>

**Note** – It is assumed that the under-reported income is not on account of misreporting.
Question 77
ABC Ltd. is a domestic company liable to tax@25%. The following are the particulars furnished by the company for A.Y.2020-21:

<table>
<thead>
<tr>
<th>Particulars of total income</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>As per the return of income furnished u/s 139(1)</td>
<td>(15,00,000)</td>
</tr>
<tr>
<td>Determined under section 143(1)(a)</td>
<td>(8,00,000)</td>
</tr>
<tr>
<td>Assessed under section 143(3)</td>
<td>(5,00,000)</td>
</tr>
<tr>
<td>Reassessed under section 147</td>
<td>4,00,000</td>
</tr>
</tbody>
</table>

Is penalty leviable under section 270A on ABC Ltd., and if so, what is the quantum of penalty?

**Solution**
ABC Ltd. is deemed to have under-reported its income since:

1. The assessment under 143(3) has the effect of reducing the loss determined in a return processed under section 143(1)(a); and
2. The reassessment under section 147 has the effect of converting the loss assessed under section 143(3) into income.

Therefore, penalty is leviable under section 270A for under-reporting of income.

**Computation of penalty leviable under section 270A**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assessment under section 143(3)</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Under-reported income:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loss assessed u/s 143(3)</td>
<td>(5,00,000)</td>
<td></td>
</tr>
<tr>
<td>(-) Loss determined under section 143(1)(a)</td>
<td>(8,00,000)</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>3,00,000</td>
<td></td>
</tr>
<tr>
<td>Tax payable on under-reported income@25%</td>
<td>75,000</td>
<td></td>
</tr>
<tr>
<td>Add: EC &amp; SHEC@4%</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>78,000</td>
<td></td>
</tr>
<tr>
<td>Penalty leviable@50% of tax payable</td>
<td></td>
<td>39,000</td>
</tr>
</tbody>
</table>

**Reassessment under section 147**

| Under-reported income:                          |           |           |
| Total income reassessed under section 147       | 4,00,000  |           |
| (-) Loss assessed under section 143(3)          | (5,00,000) |           |
| **Total**                                        | 9,00,000  |           |
| Tax payable on under-reported income@25%        | 2,25,000  |           |
| Add: EC & SHEC@4%                               | 9,000     |           |
| **Total**                                        | 2,34,000  |           |
| Penalty leviable@50% of tax payable             |           | 1,17,000  |

**Note** – The following assumptions have been made -

1. None of the additions or disallowances made in assessment or reassessment qualifies under section 270A(6); and
2. The under-reported income is not on account of misreporting.

Question 78
A private bank has not filed its statement of financial transaction or reportable account in relation to the specified financial transactions for the financial year 2019-20. A notice was issued by the prescribed income-tax authority on 1st October, 2020 requiring the
bank to furnish the statement by 31st October, 2020. The bank, however, furnished the statement only on 15th November, 2020. What would be the penalty leviable under section 271FA?

Solution

<table>
<thead>
<tr>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-compliance of section</td>
<td>Penalty under section 271FA</td>
<td>Period</td>
<td>Quantum of penalty under section 271FA</td>
</tr>
<tr>
<td>285BA(1)</td>
<td>Rs. 500 per day of continuing default</td>
<td>1.6.2019 to 31.10.2019</td>
<td>153 days × Rs. 500</td>
</tr>
<tr>
<td>285BA(5)</td>
<td>Rs. 1,000 per day of continuing default</td>
<td>1.11.2019 to 15.11.2019</td>
<td>15 days × Rs. 1,000</td>
</tr>
</tbody>
</table>

91,500
QUESTIONS ON TDS/TCS & ADVANCE TAX

Question 79
Smt. Vijaya, proprietor of Lakshmi Enterprises, made turnover of Rs. 210 lakhs during the previous year 2017-18. Her turnover for the year ended 31-3-2020 was Rs. 90 lakhs.

Decide whether provisions relating to deduction of tax at source are attracted for the following payments made during the financial year 2019-20:
(i) Purchase commission paid to one agent Rs. 25,000 on 13.6.2019 towards purchases made during the year.
(ii) Payments to Civil engineer of Rs. 5,00,000 for construction of residential house for self use.

Answer
Since Smt. Vijaya’s turnover was Rs. 210 lakhs in the immediately preceding financial year (i.e., F.Y.2018-19), she is liable to deduct tax at source in the P.Y.2019-20, irrespective of her turnover being only Rs. 90 lakhs in the F.Y.2019-20.

(i) Tax@5% has to be deducted under section 194H in respect of purchase commission of Rs. 25,000 to an agent for purchases made during the year, since the same exceeds the threshold limit of Rs. 15,000 for non-deduction of tax at source thereunder.

(ii) Tax has to be deducted under section 194C in case of payment to resident contractors. The rate of tax is 1% if the payee is an individual or HUF and 2% in case of payees, other than individuals and HUFS.

However, as per section 194C(4), no individual or Hindu undivided family shall be liable to deduct income tax on the sum credited or paid to the account of the contractor where such sum is credited or paid exclusively for personal purposes of such individual or any member of the Hindu undivided family.

In this case, since Smt. Vijaya, an individual, makes payment of Rs. 5 lakh to a civil engineer for construction of residential house for self use, she is not liable to deduct tax at source under section 194C from such sum.

Question 80
What is the rate at which the tax is either to be deducted or collected under the provisions of the Act in the following cases?
(i) A partnership firm making sales of timber which was procured and obtained under a forest lease.
(ii) Payment of income of Rs.25 lakh on investments in the securities to the Foreign Institutional Investor.
(iii) A nationalized bank receiving professional services from a registered society made provision on 31-03-2020 of an amount of ` 25 lakh against the service charges bills to be received.
(iv) Payment of Rs. 5 lacs made to Mr. Phelps who is an athlete by a manufacturer of a swim wear for brand ambassador.
Answer

### Applicable Rate of TDS/TCS

<table>
<thead>
<tr>
<th>Situation</th>
<th>TCS/TDS</th>
<th>Rate</th>
<th>Note</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Partnership firm selling timber obtained under forest lease</td>
<td>TCS</td>
<td>2.5%</td>
<td>1</td>
</tr>
<tr>
<td>(ii) Payment of income on investments in the securities to the Foreign Institutional Investors</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In case the securities are Government securities</td>
<td>TDS</td>
<td>20.8% 5.20%</td>
<td>2</td>
</tr>
<tr>
<td>(iii) Professional services rendered by a registered society to a nationalised bank</td>
<td>TDS</td>
<td>10%</td>
<td>3</td>
</tr>
<tr>
<td>(iv) Payment by a manufacturer of swim wear to its brand ambassador Mr. Phelps, an athlete</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>If Mr. Phelps is a resident</td>
<td>TDS</td>
<td>10% 20.8%</td>
<td>4</td>
</tr>
<tr>
<td>If Mr. Phelps is a non-resident</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Notes:

1. As per section 206C(1), tax has to be collected at source@2½% by the partnership firm, being a seller, at the time of debiting of the amount payable by the buyer to the account of the buyer or at the time of receipt of such amount, whichever is earlier.

2. As per section 196D, tax has to be deducted at source @ 20.8% (20% plus cess@4%) by any person who is responsible for paying to a Foreign Institutional Investor, any income by way of interest on securities at the time of credit of such income to the account of the payee or at the time of payment of such income, whichever is earlier. Alternatively, if the said securities are assumed to be government securities, tax is deductible@5.20% (i.e., 5% plus cess@4%) under section 194LD.

3. Tax has to be deducted at source@10% under section 194J, by the nationalized bank at the time of credit of fees for professional services to the account of the registered society (i.e., on 31.3.2020), even though payment is to be made after that date.

4. Tax has to be deducted at source@10% under section 194J in respect of income of Rs. 5 lacs paid to Mr. Phelps, athlete, for advertisement, on the inherent presumption that Mr. Phelps is a resident. Alternatively, if Mr. Phelps is assumed to be a non-resident, who is not a citizen of India, tax has to be deducted at source@20.8% (20% plus cess 3%) under section 194E in respect of income of Rs. 5 lacs paid to Mr. Phelps, an athlete, for advertisement referred under section 115BBA.

**Question 81**

Examine the liability for tax deduction at source in the following cases for the assessment year 2020-21:

(i) Wings Ltd. has paid amount of Rs. 15 lacs during the year ended 31-3-2020 to Airports Authority of India towards landing and parking charges.

(ii) Omega Ltd., an event management company, organized a concert of international artists in India. In this connection, it engaged the services of an overseas agent Mr. John from UK to bring artists to India. He contacted the artists and negotiated
with them for performance in India in terms of the authority given by the company. He did not take part in event organized in India. The company made the payment of commission equivalent to Rs. 1 lac to the overseas agent.

(iii) Ramesh gave a building on sub-lease to Mac Ltd. with effect from 1-7-2019 on a rent of Rs. 20,000 per month. The company also took on hire machinery from Ramesh with effect from 1-11-2019 on hire charges of Rs. 15,000 per month. The rent of building and hire charges of machinery for the year 2019-20 were credited by the company to the account of Ramesh in its books of account on 31-3-2020.

(iv) Rs. 2,45,000 paid to Mr. X on 01-02-2020 by Karnataka State Government on compulsory acquisition of his urban land. What would be your answer if the land is agricultural land?

Answer

(i) **TDS on landing and parking charges:** The landing and parking charges which are fixed by the Airports Authority of India are not merely for the "use of the land". These charges are also for services and facilities offered in connection with the aircraft operation at the airport which include providing of air traffic services, ground safety services, aeronautical communication facilities, installation and maintenance of navigational aids and meteorological services at the airport [Japan Airlines Co. Ltd. v. CIT / CIT v. Singapore Airlines Ltd. (2015) 377 ITR 372 (SC)]. Thus, tax is not deductible under section 194I which provides deduction of tax for payment in the nature of rent.

Hence, tax is deductible @2% under section 194C by the airline company, Wings Ltd., on payment of Rs. 15 lacs made towards landing and parking charges to the Airports Authority of India for the previous year 2019-20.

(ii) **TDS on services of overseas agent outside India:** An overseas agent of an Indian company operates in his own country and no part of his income accrues or arises in India. His commission is usually remitted directly to him and is, therefore, not received by him or on his behalf in India. The commission paid to the non-resident agent for services rendered outside India is, thus, not chargeable to tax in India. Since commission income for contacting and negotiating with artists by Mr. John, a non-resident, who remains outside India is not subject to tax in India, consequently, there is no liability for deduction of tax at source. It is assumed that the commission equivalent to Rs. 1 lakh was remitted to Mr. John outside India.

(iii) **TDS on rent for building and machinery:** Tax is deductible on rent under section 194-I, if the aggregate amount of rental income paid or credited to a person exceeds Rs. 2,40,000. Rent includes payment for use of, inter alia, building and machinery.

The aggregate payment made by Mac Ltd. to Ramesh towards rent in P.Y.2019-20 is Rs. 2,55,000 (i.e., Rs. 1,80,000 for building and Rs. 75,000 for machinery). Hence, Mac Ltd. has to deduct tax@10% on rent paid for building and tax@2% on rent paid for machinery.

(iv) **TDS on compensation for compulsory acquisition:** Tax is deductible at source @10% under section 194LA, where payment is made to a resident as compensation or enhanced compensation on compulsory acquisition of any immovable property (other than agricultural land).

However, no tax deduction is required if the aggregate payments in a year does not exceed Rs. 2,50,000.
Therefore, no tax is required to be deducted at source on payment of Rs. 2,45,000 to Mr. X, since the aggregate payment does not exceed Rs. 2,50,000.

Since the definition of immovable property specifically excludes agricultural land, no tax is deductible at source on compensation paid for compulsory acquisition of agricultural land.

**Question 82**
Examine whether tax has to be deducted at source under the provisions of the Income-tax Act, 1961 in the following situations, which have taken place during the year ended 31-3-2020:

(i) M/s. Jiva & Co., a partnership firm, pays a sum of Rs. 43,000 as interest on loan borrowed from an Indian branch of a foreign bank.

(ii) Above firm has paid Rs. 42,000 as interest on capital to partner Mr. A, a resident in India, and Rs. 44,000 as interest on capital to partner Mr. B, a non-resident.

(iii) The above firm paid Rs. 50,000 being share of profit of partner Mr. B, a non-resident.

**Answer**

(i) Section 194A requires deduction of tax on any income by way of interest, other than interest on securities, credited or paid to a resident, at the rates in force. However, it specifically excludes from its scope, income credited or paid to any banking company to which the Banking Regulation Act, 1949 applies. An Indian branch of a foreign bank, transacting the business of banking in India, is a banking company to which the Banking Regulation Act, 1949 applies. Therefore, interest payment to such bank will not attract tax deduction under section 194A. Consequently, no tax is required to be deducted at source under section 194A on interest of Rs. 43,000 paid by M/s. Jiva & Co., a partnership firm, on loan borrowed from an Indian branch of a foreign bank.

(ii) Section 194A requiring deduction of tax at source on any income by way of interest, other than interest on securities, credited or paid to a resident, excludes from its scope, income credited or paid by a firm to its partner. Therefore, no tax is required to be deducted at source under section 194A on interest on capital of Rs. 42,000 paid by the firm to Mr. A, a resident partner. Section 195, which requires tax deduction at source on payments to non-residents, does not provide for any exclusion in respect of payment of interest by a firm to its non-resident partner. Therefore, tax has to be deducted under section 195 at the rates in force in respect of interest on capital of Rs. 44,000 paid to partner Mr. B, a non-resident.

(iii) As per section 10(2A), share of profit received by a partner from the total income of the firm is exempt from tax. Therefore, the share of profit paid to non-resident partner is not liable for tax deduction at source. However, section 195(6) provides that the person responsible for paying any sum, whether or not chargeable to tax, to a non-corporate non-resident or to a foreign company, shall be required to furnish the information relating to payment of such sum in the prescribed form and manner.
Question 83

"Come Air Ltd." has paid a sum of Rs. 12 lakhs during the year ended 31-3-2020 to Airports Authority of India towards landing and parking charges. The company has deducted tax at source@2% under section 194C on the said payment and remitted the tax deducted within the prescribed time. The Assessing Officer contended that landing and parking charges were levied for use of the land of the airport and hence, the payment was in the nature of rent attracting TDS@10% under section 194-I. Discuss the correctness or otherwise of the contention of the Assessing Officer.

Answer

The issue as to whether the charges fixed by the Airport Authority of India (AAI) for landing and take-off facilities and parking facility for the aircraft are for the “use of the land” by the airline company came up before the Supreme Court in Japan Airlines Co. Ltd. v. CIT / CIT v. Singapore Airlines Ltd. (2015) 377 ITR 372.

The Supreme Court observed that the charges which are fixed by the AAI for landing and take-off services as well as for parking of aircrafts are not for the "use of the land". These charges are for services and facilities offered in connection with the aircraft operation at the airport which include providing of air traffic services, ground safety services, aeronautical communication facilities, installation and maintenance of navigational aids and meteorological services at the airport.

There are various international protocols which mandate all authorities manning and managing these airports to construct the airport of desired standards which are stipulated in the protocols. The services which are required to be provided by these authorities, like AAI, are aimed at passengers' safety as well as for safe landing and parking of the aircrafts. Therefore, the services are not restricted to merely permitting "use of the land" of airport. On the contrary, it encompasses all the facilities that are to be compulsorily offered by the AAI in tune with the requirements of the protocol.

The Supreme Court observed that the charges levied on air-traffic includes landing charges, lighting charges, approach and aerodrome control charges, aircraft parking charges, aerobridge charges, hangar charges, passenger service charges, cargo charges, etc. Thus, when the airlines pay for these charges, treating such charges as charges for "use of the land" would tantamount to adopting a totally simplistic approach which is far away from reality.

The Supreme Court opined that the substance behind such charges has to be considered and when the issue is viewed from this angle, keeping the larger picture in mind, it becomes very clear that the charges are not for use of the land per se and, therefore, it cannot be treated as "rent" within the meaning of section 194-I. The Supreme Court, thus, concurred with the view taken by the Madras High Court in Singapore Airlines case and overruled the view taken by the Delhi High Court in United Airlines/Japan Airlines case.

Applying the rationale of the Supreme Court ruling to the facts of this case, the contention of the Assessing Officer that landing and parking charges are levied for use of the land of airport and hence, the charges are in the nature of rent to attract the provisions of tax deduction at source under section 194-I is not correct.
Question 84

Mr. Madhusudan is regular in deducting tax at source and depositing the same. In respect of the quarter ended 31st December, 2019 a sum of Rs. 80,000 was deducted at source from the contractors. The statement of tax deducted at source under section 200 was filed on 23rd March 2020 for the quarter ended 31.12.2019.

(i) Is there any delay on the part of Mr. Madhusudan in filing the statement of TDS?

(ii) If the answer to (i) above is in the affirmative, how much amount can be levied on Mr. Madhusudan for such default under section 234E?

(iii) Is there any remedy available to him for reduction/waiver of the levy?

Answer

(i) Yes, there has been a delay on the part of Mr. Madhusudan in filing the statement of TDS.

As per section 200(3) read with Rule 31A, the statement of tax deducted at source for the quarter ended 31st December, 2019 has to be filed on or before 31st January, 2020. However, the same has been filed only on 23rd March, 2020. Hence, there has been a 52 days delay on the part of Mr. Madhusudan in filing the statement of TDS.

(ii) As per section 234E of the Income-tax Act, 1961, where a person fails to file deliver or cause to be delivered the statement of tax deducted at source within the prescribed time, then, he shall be liable to pay, by way of fee, a sum of Rs. 200 for every day during which the failure continues.

The amount of fee shall not, however, exceed the amount of tax deductible.

In this case, since Mr. Madhusudhan has delayed filing the statement of TDS by 52 days, he would be liable to pay a fee of Rs. 10,400 (Rs. 200 × 52 days) under section 234E. The said fee does not exceed the tax deductible (Rs. 80,000, in this case).

(iii) The CBDT is empowered to issue general or special orders, whether by way of relaxation of any of the provisions of sections 139, 143, 144, 147 etc. or otherwise, in respect of any class of incomes or class of cases. The CBDT may issue such order(s) from time to time if it considers expedient so to do, for the purpose of proper and efficient management of the work of assessment and collection of revenue. Section 234E is included in the list of sections in respect of which the CBDT is empowered to issue order for relaxation of the provisions of the Act.

Hence, the remedy available to Mr. Madhusudhan is that he can file an application to the CBDT under section 119 and seek waiver/reduction of the penalty levied/leviable under section 234E.

Question 85

Siddharth Hospitals Pvt. Ltd. has recently been accorded recognition by several insurance companies to admit and treat patients on cashless hospitalization basis. Payment to the assessee hospital will be made by Third Party Administrators (TPA) who will process the claims of the patients admitted and make payments to the various hospitals including the assessee. All TPAs are corporate entities. The assessee wants to know whether the TPAs are bound to deduct tax at source under section 194J or under section 194C?
Past Questions

Answer
This issue has been clarified by the CBDT Circular No.8/2009 dated 24.11.2009. As per provisions of section 194J(1), any person, who is responsible for paying to a resident any sum by way of fees for professional services, shall, at the time of credit of such sum to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct an amount equal to 10% of such sum as TDS.

Further, as per clause (a) of Explanation to section 194J “professional services” includes services rendered by a person in the course of carrying on medical profession.

The services rendered by hospitals to various patients are primarily medical services and, therefore, the provisions of section 194J are applicable on payments made by TPAs to hospitals etc. Further, for invoking provisions of section 194J, there is no stipulation that the professional services have to be necessarily rendered to the person who makes payment to hospital. Therefore, TPAs who are making payment on behalf of insurance companies to hospitals for settlement of medical/ insurance claims etc. under various schemes including Cashless Schemes are liable to deduct tax at source under section 194J on all such payments to hospitals etc.

In view of the above, all such transactions between TPAs and hospitals would fall within the ambit of provisions of section 194J.

Question 86
Examine in the context of provisions contained in Chapter XVII of the Act and also work out the amount of tax to be deducted by the payer of income in the following cases:

(i) Payment of Rs. 5 lacs made by JCP & Co. to Pingu Events Co. Ltd. for organizing a debate competition on the subject "Preservation of Rural Heritage of Rajasthan".

(ii) "Profit Commission" of Rs. 1 lac paid on 10.6.2018 by a re-insurance company to the insurer company after the expiry of the term of insurance and where there was no claim during the treaty.

(iii) KD, a part time director of DAF Pvt. Ltd. was paid an amount of Rs. 2,25,000 as fees which was actually in the nature of commission on sales for the period 1.4.2019 to 30.6.2019.

Answer

(i) The services of Event Managers in relation to sports activities alone have been notified by the CBDT as “professional services” for the purpose of section 194J. In this case, payment of Rs. 5 lacs was made to an event management company for organization of a debate competition. Hence, the provisions of section 194J are not attracted.

However, TDS provisions under section 194C relating to contract payments would be attracted and consequently, tax has to be deducted @ 2% under section 194C. The tax deductible under section 194C would be Rs. 10,000, being 2% of Rs. 5 lacs.

(ii) Section 194D requires deduction of tax at source@5% from insurance commission, where the commission exceeds Rs. 15,000.

Reinsurance is different from insurance since there is no direct contractual relationship between the person insured and the re-insurer.
In order to attract section 194D, the commission or any other payment covered under the section should be a remuneration or reward for soliciting or procuring the insurance business. The insurance companies do not procure business for the reinsurance company nor does the reinsurer pay commission or other payment for soliciting the business from the insurance companies. Therefore, section 194D has no application.

Hence, when profit commission is paid by a reinsurance company to an insurance company, after the expiry of the term of insurance, in respect of cases where there is no claim during the operation of the reinsurance treaty, tax deduction under section 194D is not attracted.

(iii) Section 194J provides for deduction of tax at source @10% on any remuneration or fees or commission, by whatever name called, paid to a director, which is not in the nature of salary in respect of which tax is deductible at source under section 192.

Hence, tax is to be deducted at source under section 194J @10% by DAF Pvt. Ltd. on the commission of Rs. 2,25,000 paid to KD, a part-time director. The tax deductible under section 194J would be Rs. 22,500, being 10% of Rs. 2,25,000.

Question 87
Examine the applicability of the provisions relating to deduction of tax at source in the following transactions:

(i) Max Limited pays Rs. 1,02,000 to Mini Limited, a resident contractor who, under the contract dated 15th October, 2019, manufactures a product according to specification of Max Limited by using materials purchased from Max Limited.

(ii) A company operating a television channel makes payment of Rs. 5 lacs to a former cricketer for making running commentary of a one-day cricket match.

(iii) EL Ltd., a foreign company, pays outside India, salary to its employee, Mr. Raghavan, a foreign national and a non-resident, for services rendered in India.

Answer

(i) The definition of “work” under section 194C includes manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from such customer. In the instant case, Mini Limited manufactures the product as per the specification given by Max Limited by using the raw materials purchased from Max Limited. Therefore, it falls within the definition of “work” under section 194C. Consequently, tax is to be deducted on the invoice value excluding the value of material purchased from such customer if such value is mentioned separately in the invoice. If the material component is not mentioned separately in the invoice, tax is to be deducted on the whole of the invoice value.

(ii) Provisions for deduction of tax at source under section 194J are attracted in respect of payment of fees for professional services, if the amount of such fees exceeds Rs. 30,000 in the relevant financial year. The service rendered by a commentator in relation to sports activities has been notified by the CBDT as a professional service for the purposes of section 194J vide its Notification No. 88 dated 21st August, 2008. Therefore, tax is required to be deducted@10% from the fee of Rs. 5 lacs payable to the former cricketer.
(iii) Section 195 requires deduction of tax at source by any person responsible for making payment to a non-resident, any interest or any other sum chargeable under the provisions of the Income-tax Act, 1961 (other than income chargeable under the head "Salaries").

Section 192(1) requires “any person” responsible for paying income under the head “Salaries” to deduct tax at source. Therefore, even if the payer is a foreign company, section 192 would be applicable.

TDS provisions under section 192 are attracted, if the salary payable to a non-resident is chargeable to tax in India. Under section 9(1)(ii), income which falls under the head "Salaries" shall be deemed to accrue or arise in India, if it is earned in India. Salary payable for service rendered in India shall be regarded as income earned in India. Therefore, salary paid to Mr. Raghavan, a non-resident, attracts tax liability in India, as he has rendered services in India and the salary is attributable to such services.

Therefore, the foreign company, EL Limited, is liable to deduct tax at source under section 192 from the salary of Mr. Raghavan.

Question 88
Examine in the following cases the obligation of the person paying the income in respect of tax deduction at source and indicate the due date for payment of such tax, wherever applicable:

(i) MNO Ltd., the employer, credited salary due for the financial year 2019-20 amounting to Rs. 3,40,000 to the account of Q, an employee, in its books of account on 31.3.2020. Q has not furnished any information about his income/loss from any other head or proof of investments/payments qualifying for deduction under section 80C.

(ii) T, an individual whose total sales in business during the year ended 31.3.2019 was Rs. 2.20 crores, paid Rs. 9 lacs by cheque on 1.1.2020 to a contractor (an individual), for construction of his factory building. No amount was credited earlier to the account of the contractor in the books of T.

(iii) BCD Ltd. credited Rs. 28,000 towards fees for professional services and Rs. 27,000 towards fees for technical services to the account of HG in its books of account on 6.10.2019. The total sum of Rs. 55,000 was paid by cheque to HG on 18.12.2019.

Answer

(i) Section 192 requires deduction of tax from salary at the time of payment. Thus, the employer is not required to deduct tax at source when salary has not been paid but is merely credited to the account of the employee in its books of account. MNO Ltd. therefore, is not required to deduct tax at source in respect of the salary merely credited to the account of employee Q which is not paid.

If salary has been paid during the year to Q, then, MNO Ltd has to obtain from Q, the evidence-proof/particulars of prescribed claims (including claim for set-off of loss) under the provisions of the Act in such form and manner as may be prescribed.

If Q has not furnished any information about his income/loss under any other head or proof of investments/expenditure qualifying for deduction under section 80C, then,
the employer has to deduct tax without considering any claim for any expenditure or set-off of losses or deduction under section 80C.

(ii) An individual who is liable for tax audit under section 44AB in the immediately preceding financial year is liable to deduct tax at source under section 194C for the financial year 2018-19 in respect of the payment made to contractor exceeding Rs. 30,000 in a single contract and Rs. 1,00,000 in aggregate of contracts during the financial year. Turnover of the individual T is Rs. 2.20 crores in the financial year 2017-18. Therefore, T is liable to get his accounts for that year audited under section 44AB. As the payment during financial year 2018-19 to the contractor has exceeded the limits prescribed in section 194C, tax has to be deducted under section 194C.

The rate of tax deduction is 1% as the contractor is an individual.

(iii) The limit of Rs. 30,000 for non-deduction of tax under section 194J would apply separately for fees for professional services and fees for technical services. This means that if a person has rendered services falling under both the categories, tax need not be deducted if the fee for each category does not exceed Rs. 30,000 even though the aggregate of the amounts credited to the account of such person or paid to him for both the categories of services exceed Rs. 30,000. Therefore, BCD Ltd. is not required to deduct tax at source in respect of the fees either at the time of credit or at the time of payment.

Question 89
Examine the liability for tax deduction at source in the following cases for the assessment year 2020-21:

(i) Mr. Anand has been running a sole proprietary business whose accounts are audited under section 44AB with turnover of Rs. 202 lakhs for the A.Y. 2019-20. He pays a monthly rent of Rs. 10,000 for the office premises to Mr. R, the owner of building and an individual. Besides, he also pays service charges of Rs. 6,000 per month to Mr. R towards the use of furniture, fixtures and vacant land appurtenant thereto.

(ii) By virtue of an agreement with a nationalised bank, a catering organisation receives a sum of Rs. 50,000 per month towards supply of food, water, snacks etc. during office hours to the employees of the bank.

(iii) An Indian company pays gross salary including allowances and monetary perquisites amounting to Rs. 7,30,000 to its General Manager. Besides, the company provides non-monetary perquisites to him whose value is estimated at Rs. 1,20,000.

(iv) A notified infrastructure debt fund eligible for exemption under section 10(47) of the Income-tax Act, 1961 pays interest of Rs. 5 lakhs to a company incorporated in USA. The US Company incurred expenditure of Rs. 12,000 for earning such interest. The fund also pays interest of Rs. 3 lakhs to Mr. X, who is a resident of a notified jurisdictional area.

Answer
(i) Where the payer is an individual or HUF whose turnover exceeds the monetary limits specified in clause (a) of section 44AB, he has to deduct tax at source. Since the turnover of Mr. Anand was Rs. 202 lakhs for the A.Y.2018-19, he is liable to
deduct tax at source under section 194-I in respect of rental payments during the financial year 2019-20.

Accordingly, Mr. Anand is liable to deduct tax at source under section 194-I on the rental payments made. Section 194-I provides that rent includes any payment, by whatever name called, for the use of land or building together with furniture, fittings etc. Therefore, in the given case, apart from monthly rent of Rs. 15,000 p.m., service charge of Rs. 6,000 p.m. for use of furniture and fixtures would also attract TDS under section 194-I. Since the aggregate rental payments to Mr. R during the financial year 2019-20 exceeds Rs. 2,40,000, Mr. Anand is liable to deduct tax at source @10% under section 194-I from rent paid to Mr. R.

(ii) The definition of “work” under Explanation to section 194-C includes catering services and therefore, TDS provisions under section 194C are attracted in respect of payments to a caterer. As the payment exceeds Rs. 30,000, the nationalised bank is required to deduct tax at source at 2% on the payments made to catering organisation under 194-C. If the catering organization is an individual or HUF, then the tax deduction shall be @1%.

(iii) |
| Gross salary, allowances and monetary perquisites | Rs. 7,20,000 |
| Non-Monetary perquisites | 1,20,000 |
| Less: Standard deduction under section 16(1a) | 50,000 |
| **Tax Liability** | **Rs. 8,00,000** |
| Average rate of tax (Rs. 75,400 / Rs. 8,00,000 × 100) | 9.425% |

The company can deduct Rs. 75,400 at source from the salary of the General Manager. Alternatively, the company can pay tax on non-monetary perquisites as under –

Tax on non-monetary perquisites = 9.425% of Rs. 1,20,000 = Rs. 11,310

Balance to be deducted from salary = Rs. 64,090

If the company pays tax of Rs. 11,310 on non-monetary perquisites, the same is not a deductible expenditure as per section 40(a). The amount of tax paid towards non-monetary perquisite by the employer, however, is not chargeable to tax in the hands of the employee as per section 10(10CC).

(iv) As per section 194LB, tax would be deductible @ 5% on gross interest paid/credited by a notified infrastructure debt fund, eligible for exemption under section 10(47), to a foreign company.

In the first case, since the payment is to a foreign company, health and education cess @4% has to be added to the applicable rate of TDS. Therefore, the tax deductible under section 194LB would be Rs. 26,000 (i.e., 5.20% of Rs. 5 lakhs).

However, in case the notified infrastructure debt fund pays interest to a person who is a resident of a notified jurisdictional area, section 94A will apply. Accordingly, tax would be deductible @30% (plus health and education cess @4%) under section 94A, even though section 194LB provides for deduction of tax at a concessional rate of 5%. Therefore, the tax deductible in respect of payment of Rs. 3 lakh to Mr. X, who is a resident of a notified jurisdictional area, would be Rs. 93,600, being 31.2% of Rs. 3,00,000.
Question 90

The following issues arise in connection with the deduction of tax at source under Chapter XVII-B. Examine the liability for tax deduction in these cases:

(a) An employee of the Central Government receives arrears of salary for the earlier 3 years. He enquires whether he is liable for deduction of tax on the entire amount during the current year.

(b) A T.V. channel pays Rs. 10 lakh on 1.9.2019 as prize money to the winner of a quiz programme, “Who will be a Millionaire”?

(c) State Bank of India pays Rs. 50,000 per month as rent to the Central Government for a building in which one of its branches is situated.

(d) A television company pays Rs. 80,000 to a cameraman for shooting of a documentary film.

(e) A State Government pays Rs. 22,000 on 2.7.2019 as commission to one of its agents on sale of lottery tickets.

(f) A Turf Club awards a jack-pot of Rs. 5 lakh to the winner of one of its races on 1.2.2020.

Answer

(a) As per section 192, tax is deductible at source by any person who is responsible for paying any income chargeable under the head ‘Salaries’. However, as per subsection (2A) of that section, the employee will be entitled to relief under section 89 and consequently he will be required to furnish to the person responsible for making the payment, such particulars in the prescribed form (i.e., Form No.10E). The person responsible for making the payment shall compute the relief and take into account the same while deducting tax at source from salary.

(b) Under section 194B, the person responsible for paying by way of winnings from any card game and other game in an amount exceeding Rs. 10,000 shall at the time of payment deduct income-tax at 30%. Therefore, tax of Rs.3 lakh has to be deducted at source from the prize money of Rs. 10 lakh payable to the winner.

(c) Section 194-I, which governs the deduction of tax at source on payment of rent, exceeding Rs. 2,40,000 p.a., is applicable to all taxable entities except individuals and HUFs, whose turnover/gross receipts do not exceed the monetary limits specified under clause (a) of section 44AB. Section 196, however, provides exemption in respect of payments made to Government from application of the provisions of tax deduction at source. Therefore, no tax is required to be deducted at source by State Bank of India from rental payments to the Government.

(d) If the cameraman is an employee of the T.V. Company, the provisions of section 192 will apply. However, if he is a professional, TDS provisions under section 194-J will apply. Tax at 10% will have to be deducted at the time of credit of Rs. 80,000 or on its payment, whichever is earlier.

(e) Under section 194G, the person responsible for paying to any person stocking, distributing, purchasing or selling lottery tickets shall at the time of credit of the commission or payment thereof, whichever is earlier, amounting to more than Rs. 15,000, deduct income-tax at source @5%.
Accordingly, tax@5% under section 194G amounting to Rs. 1,100 has to be deducted from commission payment of Rs. 22,000 to the agent of the State Government.

(f) The payment by way of winnings from horse race is governed by section 194BB. Under this section, the person responsible for payment shall, at the time of payment, deduct tax at source @ 30%, if the payment exceeds Rs. 10,000. Accordingly, tax@30% amounting to Rs. 1,50,000 has to be deducted from the winnings of Rs. 5 lakh payable to the winner of the race.

Question 91
Examine and compute the liability for deduction of tax at source, if any, in the cases stated hereunder, for the financial year ended 31st March, 2020

(i) Mr. X, a resident, acquired a house property at Mumbai from Mr. Y for a consideration of Rs. 90 lakhs, on 20.6.2019. On the same day, Mr. X made two separate transactions, thereby acquiring an urban plot in Kolkata from Mr. C for a sum of Rs. 49,50,000 and rural agricultural land from Mr. D for a consideration of Rs. 60 lakhs.

(ii) On 17.6.2019, a commission of Rs. 50,000 was retained by the consignee 'ABC Packaging Ltd.' and not remitted to the consignor 'XYZ Developers', while remitting the sale consideration. Examine the obligation of the consignor to deduct tax at source.

(iii) Raj is working with AB Ltd. He is entitled to a salary of Rs. 55,000 per month w.e.f. 1.4.2019. He has a house property which is self-occupied. He paid an interest of Rs. 80,000 on loan, during the previous year 2019-20. The loan was taken for construction of house. He has notified his employer AB Ltd. that there will be a loss of Rs. 80,000 in respect of this house property for financial year ended 31.3.2020.

Answer

<table>
<thead>
<tr>
<th>Case</th>
<th>Amount of TDS (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i)</td>
<td>Since the consideration for transfer of house property at Mumbai exceeds Rs. 50 lakhs, Mr. X, being the transferee, is required to deduct tax @1% under section 194-IA on Rs. 90 lakhs, being the amount of consideration for transfer of property. Mr. X is not required to deduct tax as source under section 194-IA from the consideration of Rs. 49,50,000 paid to Mr. C for transfer of urban plot, since the consideration is less than Rs. 50 lakhs. Mr. X is also not required to deduct tax at source under section 194-IA from the consideration of Rs. 60 lakhs paid to Mr. D for transfer of rural agricultural land, since the same is specifically excluded from the scope of immovable property for the purpose of tax deduction under section 194-IA.</td>
</tr>
</tbody>
</table>

Note - Section 194-IA requires every transferee responsible for paying any sum as consideration for transfer of immovable property (land, other than agricultural land, or building or part of building) to deduct tax, at the rate of 1% of such sum, at the time of credit of such sum to the account of the resident transferor or at the time of...
payment of such sum to the resident transferor, whichever is earlier. However, no tax is required to be deducted where the consideration for transfer of an immovable property is less than **Rs. 50 lakhs**.

(ii) Section 194H requires deduction of tax at source@5% from commission and brokerage payments to a resident. However, no tax is to be deducted at source where the amount of such payment does not exceed **Rs. 15,000**.

In the given case, ‘ABC Packaging Ltd.’, the consignee, has not remitted the commission of **Rs. 50,000** to the consignor ‘XYZ Developers’ while remitting the sales consideration.

Since the retention of commission by the consignee/agent amounts to constructive payment of the same to him by the consignor/principal, deduction of tax at source is required to be made from the amount of commission [CBDT Circular No.619 dated 4/12/1991].

Therefore, XYZ Developers has to deduct tax at source on **Rs. 50,000** at the rate of 5%.

(iii) Section 192 provides that tax is required to be deducted on the payment made as salaries. Tax is to be deducted on the estimated income at the average of income tax computed on the basis of the rates in force for the financial year in which payment is made.

The employee may declare details of his other incomes (including loss under the head “Income from house property” but not any other loss) to his employer. In this case, since Mr. Raj has notified his employer AB Ltd. of loss from self-occupied house property, the employer has to take the same into consideration for deduction of tax at source.

Therefore, AB Ltd. is required to deduct tax at source on the salary of **Rs. 45,000** per month paid to Mr. Raj, in the following manner:

| Income under the head salaries (55,000 × 12) | 6,60,000 |
| Less: Standard deduction under section 16(ia) | 50,000 |
| | 6,10,000 |
| Income under the head “house property” | (80,000) |
| Gross total income | 5,30,000 |
| Less: Deduction under Chapter VI-A | Nil |
| **Total Income** | 5,30,000 |
| Tax@10% on **Rs. 1,70,000**, being the amount arrived at after reducing the basic exemption limit of **Rs. 2,50,000** from **Rs. 4,20,000** | 18,500 |
| Add: Health and Education cess @4% | 740 |
| Tax to be deducted at source | **19,240** |

**Question 92**

Mr. Sharma, an employee of M/s. ABC Ltd. since 10-04-2016 resigned on 31-03-2020 and withdrew **Rs. 60,000** being the balance in his EPF account. State with reasons whether the provisions of Chapter XVII-B are attracted and if so, what is the net amount receivable by the payee, Mr. Sharma?
Solution

As per section 192A, in a case where the accumulated balance due to an employee participating in a recognized provident fund is includible in his total income owing to the provisions of Rule 8 of Part A of the Fourth Schedule not being applicable, the trustees of the Employees Provident Fund Scheme, 1952 or any person authorised under the scheme to make payment of accumulated balance due to employees are required to deduct income-tax@10% at the time of payment of accumulated balance due to the employee. Tax deduction at source has to be made only if the amount of such payment or aggregate amount of such payment of the payee is Rs. 50,000 or more.

Rule 8 of Part A of the Fourth Schedule, inter alia, provides that only if an employee has rendered continuous service of five years or more with the employer, then accumulated balance in a recognized provident fund payable to an employee would be excluded from the total income of that employee.

In the present case, Mr. Sharma has withdrawn an amount exceeding Rs. 50,000 on his resignation after rendering a continuous service of four years with M/s. ABC Ltd. Therefore, tax has to be deducted at source@10% under section 192A on Rs. 60,000, being the amount withdrawn on his resignation without rendering continuous service of a period of five years with M/s. ABC Ltd.

The net amount receivable by Mr. Sharma is Rs. 54,000 [i.e., Rs. 60,000 – Rs. 6,000, being tax deducted at source].

Note – It is assumed that Mr. Sharma has furnished his permanent account number (PAN) to the person responsible for deducting tax at source. Otherwise, tax would be deductible at the maximum marginal rate. It may be noted that with effect from 1.6.2015 such employee can furnish declaration in Form No.15G for non-deduction of tax at source under section 192A by virtue of section 197A(1A).

Question 93

ABC Ltd. makes the following payments to Mr. X, a contractor, for contract work during the P.Y.2019-20–

- Rs. 20,000 on 1.5.2019
- Rs. 25,000 on 1.8.2019
- Rs. 28,000 on 1.12.2019

On 1.3.2020, a payment of Rs. 30,000 is due to Mr. X on account of a contract work.

Discuss whether ABC Ltd. is liable to deduct tax at source under section 194C from payments made to Mr. X.

Solution

In this case, the individual contract payments made to Mr. X does not exceed Rs. 30,000. However, since the aggregate amount paid to Mr. X during the P.Y.2019-20 exceeds Rs. 1,00,000 (on account of the last payment of Rs. 30,000, due on 1.3.2020, taking the total from Rs. 73,000 to Rs. 1,03,000), the TDS provisions under section 194C would get attracted. Tax has to be deducted@1% on the entire amount of Rs. 1,03,000 from the last payment of Rs. 30,000 and the balance of Rs. 28,970 (i.e., Rs. 30,000 – Rs. 1,030) has to be paid to Mr. X.
Question 94
Examine the applicability of the provisions for tax deduction at source under section 194DA in the following cases-

(i) Mr. X, a resident, is due to receive Rs. 4.50 lakhs on 31.3.2020, towards maturity proceeds of LIC policy taken on 1.4.2017, for which the sum assured is Rs. 4 lakhs and the annual premium is Rs. 1,10,000.

(ii) Mr. Y, a resident, is due to receive Rs. 3.25 lakhs on 31.3.2020 on LIC policy taken on 31.3.2012, for which the sum assured is Rs. 3 lakhs and the annual premium is Rs. 35,000.

(iii) Mr. Z, a resident, is due to receive Rs. 95,000 on 1.8.2019 towards maturity proceeds of LIC policy taken on 1.8.2013 for which the sum assured is Rs. 90,000 and the annual premium was Rs. 12,000.

Solution
(i) Since the annual premium exceeds 10% of sum assured in respect of a policy taken after 31.3.2012, the maturity proceeds of Rs. 4.50 lakhs due on 31.3.2020 are not exempt under section 10(10D) in the hands of Mr. X. Therefore, tax is required to be deducted at 5% under section 194DA on the amount of income comprised therein i.e., on Rs. 1,20,000 (Rs. 4,50,000, being maturity proceeds - Rs. 3,30,000, being the entire amount of insurance premium paid).

(ii) Since the annual premium is less than 20% of sum assured in respect of a policy taken before 1.4.2012, the sum of Rs. 3.25 lakhs due to Mr. Y would be exempt under section 10(10D) in his hands. Hence, no tax is required to be deducted at source under section 194DA on such sum payable to Mr. Y.

(iii) Even though the annual premium exceeds 10% of sum assured in respect of a policy taken after 31.3.2012, and consequently, the maturity proceeds of Rs. 95,000 due on 1.8.2019 would not be exempt under section 10(10D) in the hands of Mr. Z, the tax deduction provisions under section 194DA are not attracted since the maturity proceeds are less than Rs. 1 lakh.

******************************************************************
QUESTIONS ON TAXATION OF TRUST

Question 95
An institution operating for promotion of education claiming exemption under section 11 since 1994 furnishes the following data for the assessment year 2020-21:

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Particulars</th>
<th>Rs. in crores</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i)</td>
<td>Fees collected from students</td>
<td>14</td>
</tr>
<tr>
<td>(ii)</td>
<td>Construction of a new computer science laboratory</td>
<td>0.50</td>
</tr>
<tr>
<td>(iii)</td>
<td>Land acquired to be used as a cricket field for the students</td>
<td>2</td>
</tr>
<tr>
<td>(iv)</td>
<td>Amount earmarked and set apart for construction of an arts block within the next 4 years.</td>
<td>4</td>
</tr>
</tbody>
</table>

Compute the total income of the institution for the A.Y. 2020-21.

Answer

Computation of total income of the institution for the A.Y. 2020-21

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs. (in crores)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fees received</td>
<td>14.00</td>
</tr>
<tr>
<td>Less : 15% (exempt even if not spent for the objects of the institution)</td>
<td>2.10</td>
</tr>
<tr>
<td>Less : Accumulated for specified purpose (See Note 2)</td>
<td>11.90</td>
</tr>
<tr>
<td>Balance to be spent</td>
<td>4.00</td>
</tr>
<tr>
<td>Actual amount spent on construction of computer science lab (See Note 1)</td>
<td>0.50</td>
</tr>
<tr>
<td>Actual amount spent on purchase of land for cricket field (See Note 1)</td>
<td>2.00</td>
</tr>
<tr>
<td>Total Income</td>
<td>5.40</td>
</tr>
</tbody>
</table>

Notes:
(1) The institution must utilise 85% of its income within the previous year for the objects of the institution. The institution can apply its income either for revenue expenditure or for capital expenditure provided the expenditure is incurred for promoting the objects of the institution. Land acquired and meant for use as cricket field for students is a capital expenditure incurred for promoting the objects of the institution and hence, eligible for deduction. Likewise, the amount spent on construction of computer science laboratory is also eligible for deduction.

(2) Section 11(2) provides that a trust/institution can accumulate or set apart its income for a specified purpose by furnishing statement in prescribed format to the concerned Assessing Officer. However, the period for which the funds can be accumulated cannot exceed 5 years. The amount so accumulated should be invested in the specified forms and modes. In this case, the institution has to furnish statement in Form 10 on or before the due date of filing return of income to the Assessing Officer, stating the purpose for which the income is being accumulated or set apart and the period for which the income is being accumulated or set apart, which shall, in no case, exceed five years. Further, the institution has to invest Rs. 4 crore in the specified forms and modes.
Question 96
A public charitable trust registered under Section 12AA, for the previous year ending 31.3.2020, derived gross income of Rs. 21 Lacs, which consists of the following:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>(Rs. in Lacs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Income from properties held by trust (net)</td>
<td>10</td>
</tr>
<tr>
<td>(b) Income (net) from business (incidental to main objects)</td>
<td>4</td>
</tr>
<tr>
<td>(c) Voluntary contributions from public</td>
<td>7</td>
</tr>
</tbody>
</table>

The trust applied a sum of Rs. 11.60 lacs towards charitable purposes during the year which includes repayment of loan taken for construction of orphanage Rs. 3.60 lacs.

Determine the taxable income of the trust for the assessment year 2020-21.

**Answer**

**Computation of taxable income of public charitable trust**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Income from property held under trust (net)</td>
<td>10,00,000</td>
</tr>
<tr>
<td>(ii) Income (net) from business (incidental to main objects)</td>
<td>4,00,000</td>
</tr>
<tr>
<td>(iii) Voluntary contributions from public</td>
<td>7,00,000</td>
</tr>
</tbody>
</table>

Voluntary contribution made with a specific direction towards corpus are alone to be excluded under section 11(1)(d). In this case, there is no such direction and hence, included.

\[ 21,00,000 \]

Less: 15% of the income eligible for retention / accumulation without any conditions

\[ 3,15,000 \]

Less: Amount applied for the objects of the trust

(i) Amount spent for charitable purposes

\[ (Rs. 11,60,000 - Rs. 3,60,000) = 8,00,000 \]

(ii) Repayment of loan for construction of orphan home

\[ 3,60,000 \]

**Taxable Income**

\[ 6,25,000 \]

Question 97
An institution having its main object as “advancement of general public utility” received Rs. 30 lakhs in aggregate during the P.Y.2019-20 from an activity in the nature of trade. The total receipts of the institution, including donations, was Rs. 140 lakhs. It applied 85% of its total receipts from such activity during the same year for its main object i.e. advancement of general public utility.

(i) What would be the tax consequence of such receipt and application thereof by the institution?

(ii) Would your answer be different if the institution’s total receipts had been Rs. 150 lakhs (instead of Rs. 140 lakhs) in aggregate during the P.Y.2019-20?

(iii) What would be your answer if the main object of the institution is “relief of the poor” and the institution receives Rs. 30 lakhs from a trading activity, when its total receipts are Rs. 140 lakhs and applies 85% of the said receipts for its main object?

**Solution**

(i) As the main object of the institution is “advancement of object of general public utility”, the institution will lose its “charitable” status for the P.Y.2019-20, since it has received Rs. 30 lakhs from an activity in the nature of trade, which exceeds Rs. 28 lakhs, being 20% of the total receipts of the institution undertaking that activity.
for the previous year. The application of 85% of such receipt for its main object during the year would not help in retaining its “charitable” status for that year. The institution will lose its charitable status and consequently, the benefit of exemption of income for the P.Y.2019-20, irrespective of the fact that its approval is not withdrawn or its registration is not cancelled.

(ii) If the total receipts of the institution is Rs. 150 lakhs, and the institution receives Rs. 30 lakhs in aggregate from an activity in the nature of trade during the P.Y.2019-20, then it will not lose its “charitable” status since receipt of upto 20% of the total receipts of the institution in a year from such activity is permissible. The institution can claim exemption subject to fulfilment of other conditions under sections 11 to 13. Further, such activity should also be undertaken in the course of actual carrying out of such advancement of any other object of general public utility.

(iii) The restriction regarding carrying on of a trading activity for a cess, fee or other consideration will not apply if the main object of the institution is “relief of the poor”. Therefore, receipt of Rs. 30 lakhs from a trading activity by such an institution will not affect its “charitable” status, even if it exceeds 20% of the total receipts of the institution. The institution can claim exemption subject to fulfilment of other conditions under sections 11 to 13.

Question 98
A charitable trust, whose income can be exempt under section 11 of the Income-tax Act, 1961, was formed on 1st March, 2017. For the accounting year ended 31st March, 2020, it earned an income of Rs. 3,60,000. It filed with the Commissioner of Income-tax its application for registration on 31st August, 2019 explaining that for good and sufficient reasons, it was prevented from filing the application for so long.

Examine

(i) by which date the application for registration should have been filed;
(ii) whether such an application could have been filed before the formation of the trust;
(iii) in the absence of an order of registration from the Commissioner, can the trust be deemed to be registered;
(iv) the steps to be taken by the trust to secure exemption from income-tax;
(v) whether a certificate of registration once granted can be cancelled and if so, the conditions there for.

Solution

(i) The requirement of filing an application for registration under section 12A within one year of creation of the trust has been removed. The application can be filed at any time now. Accordingly, the provisions of sections 11 and 12 would apply from the assessment year relevant to the financial year in which the application is made i.e. the exemption would be available only with effect from the assessment year relevant to the previous year in which the application was filed.

However, where registration has been granted to the trust under section 12AA and on the said date, assessment proceedings relating to earlier assessment years are pending, then, the benefit of sections 11 and 12 shall be available in respect of income derived from property held under trust in those years, provided the objects and activities of the trust remain unchanged.
(ii) No. The application for registration under section 12A cannot be filed before the formation of the trust.

(iii) As per section 12AA(2), every order granting or refusing registration should be passed before the expiry of 6 months from the end of the month in which the application was received under section 12A. The Supreme Court, in CIT v. Society for Promotion of Education (2017) 382 ITR 6, held that the trust would be deemed as registered if the application under section 12AA is not disposed of within the stipulated period of six months. Therefore, in this case, the trust would be deemed as registered with effect from 1st March, 2020. The benefit of exemption under section 11 and 12 would be available from A.Y. 2020-21, being the assessment year relevant to the financial year in which the application is made.

(iv) The following are the steps to be taken by the trust to secure exemption from income-tax:

1. The trust should be registered with the Principal Commissioner or Commissioner of Income-tax under section 12AA.

2. The accounts of the trust for the previous year must be audited by a Chartered Accountant if its total income without giving effect to the provisions of section 11 and section 12 exceeds the maximum amount which is not chargeable to tax. The audit report in the prescribed form, duly signed and verified by the Chartered Accountant, should be furnished along with the return of income of the trust for the relevant assessment year.

3. At least 85% of the income is required to be applied for the approved purposes.

4. The unapplied income and the money accumulated or set apart should be invested or deposited in the specified forms or modes, after filing statement in Form 10 on or before the due date of filing return of income specified under section 139(1).

(v) Yes, the certificate of registration can be cancelled by the Commissioner. According to section 12AA, if the Commissioner is satisfied that the activities of the trust are not genuine or are not being carried out in accordance with the objects of the trust, he shall, after giving the trust a reasonable opportunity of being heard, pass an order in writing cancelling the registration of the trust.

Further, section 12AA(4) provides that where a trust or an institution has been granted registration, and subsequently it is noticed that its activities are being carried out in such a manner that,—

(i) its income does not enure for the benefit of general public;

(ii) it is for benefit of any particular religious community or caste;

(iii) any income or property of the trust is applied for benefit of specified persons like author of trust, trustees etc.; or

(iv) its funds are invested in prohibited modes,

then, the Commissioner may cancel the registration of such trust or institution. The Commissioner may also cancel the registration of such trust or institution, if it has not complied with the requirement of any other law and the order, direction or decree, by whatever name called, holding that such non-compliance has occurred, has either not been disputed or has attained finality. However, if the trust or institution proves that there was a reasonable cause for the activities to be carried out in the above manner, the registration shall not be cancelled.
QUESTIONS ON SET OFF AND CARRY FORWARD & SET OFF

Question 99

ABC Limited was amalgamated with XYZ Limited on 01.04.2019. All the conditions of section 2(1B) were satisfied.

ABC Limited has the following carried forward losses as assessed till the Assessment Year 2019-20:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs. (in lacs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Speculative Loss</td>
<td>4</td>
</tr>
<tr>
<td>(ii) Unabsorbed Depreciation</td>
<td>18</td>
</tr>
<tr>
<td>(iii) Unabsorbed expenditure of capital nature on scientific research</td>
<td>2</td>
</tr>
<tr>
<td>(iv) Business Loss</td>
<td>120</td>
</tr>
</tbody>
</table>

XYZ Limited has computed a profit of Rs. 140 lacs for the financial year 2019-20 before setting off the eligible losses of ABC Limited but after providing depreciation at 15% per annum on Rs. 150 lacs, being the consideration at which plant and machinery were transferred to XYZ Limited. The written down value as per income-tax record of ABC Limited as on 31st March, 2019 was Rs. 100 lacs.

The above profit of XYZ Limited includes speculative profit of Rs. 10 lacs.

Compute the total income of XYZ Limited for Assessment Year 2020-21 and indicate the losses/other allowances to be carried forward by it.

Answer

Computations of total income of XYZ Limited for the A.Y. 2020-21

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs. (in lacs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business income</td>
<td>7.50</td>
</tr>
</tbody>
</table>

Business income

- Business income before setting-off brought forward losses of ABC Ltd. 140.00
- Add: Excess depreciation claimed in the scheme of amalgamation of ABC Limited with XYZ Limited.
  - Value at which assets are transferred by ABC Ltd. 150
  - WDV in the books of ABC Ltd. 100
  - Excess accounted 50
  - Excess depreciation claimed in computing taxable income of XYZ Ltd. [Rs. 50 lacs × 15 %] [Explanation 2 to section 43(6)] 7.50

- Set-off of brought forward business loss of ABC Ltd. (See Notes 2 & 4) 120.00
- Set-off of unabsorbed depreciation under section 32(2) read with section 72A (See Notes 2 & 4) 18.00
- Set-off of unabsorbed capital expenditure under section 35(1)(iv) read with section 35(4) (See Note 5) 2.00

Business income 7.50
Notes:
1. It is presumed that the amalgamation is within the meaning of section 72A of the Income-tax Act, 1961.
2. In the case of amalgamation of companies, the unabsorbed losses and unabsorbed depreciation of the amalgamating company shall be deemed to be the loss or unabsorbed depreciation of the amalgamated company for the previous year in which the amalgamation was effected and such business loss and unabsorbed depreciation shall be carried forward and set-off by the amalgamated company for a period of 8 years and indefinitely, respectively.
3. As per section 72A(7), the accumulated loss to be carried forward specifically excludes loss sustained in a speculative business. Therefore, speculative loss of Rs. 4 lacs of ABC Ltd. cannot be carried forward by XYZ Ltd.
4. Section 72(2) provides that where any allowance or part thereof unabsorbed under section 32(2) (i.e., unabsorbed depreciation) or section 35(4) (i.e., unabsorbed scientific research capital expenditure) is to be carried forward, effect has to be first given to brought forward business losses under section 72.
5. Section 35(4) provides that the provisions of section 32(2) relating to unabsorbed depreciation shall apply in relation to deduction allowable under section 35(1)(iv) in respect of capital expenditure on scientific research related to the business carried on by the assessee. Therefore, unabsorbed capital expenditure on scientific research can be set-off and carried forward in the same manner as unabsorbed depreciation.
6. The restriction contained in section 73 is only regarding set-off of loss computed in respect of speculative business. Such a loss can be set-off only against profits of another speculation business and not non-speculation business. However, there is no restriction under the Income-tax Act, 1961 regarding set-off of normal business losses against speculative income. Therefore, normal business losses can be set-off against profits of a speculative business.

Consequently, there is no loss or allowance to be carried forward by XYZ Ltd. to the F.Y. 2020-21.

Question 100

X carrying on a business as sole proprietor, died on 31st March, 2019. On his death, the same business was continued by his legal heirs, by forming a firm. As on 31st March 2019, a determined business loss of Rs. 5 lacs is to be carried forward under the Income-tax Act, 1961.

Does the firm consisting of all legal heirs of Mr. X, get a right to have this loss adjusted against its current income?

Answer

Section 78(2) provides that where a person carrying on any business or profession has been succeeded in such capacity by another person, otherwise than by inheritance, then, the successor is not entitled to carry forward and set-off the loss of the predecessor against his income. This implies that generally, set-off of business losses should be claimed by the same person who suffered the loss and the only exception to this provison is when the business passes on to another person by inheritance.

The facts of case given in the question are similar to the case CIT v. Madhukant M. Mehta (2001) 247 ITR 805, where the Supreme Court has held that if the business is succeeded by inheritance, the legal heirs are entitled to the benefit of carry forward of
the loss of the predecessor. Even if the legal heirs constitute themselves as a partnership firm, the benefit of carry forward and set off of the loss of the predecessor would be available to the firm.

In this case, the business of X was continued by his legal heirs after his death by constituting a firm. Hence, the exception contained in section 78(2) along with the decision of the Apex Court discussed above, would apply in this case. Therefore, the firm is entitled to carry forward the business loss of Rs. 5 lacs of X.

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27.92