

Issues in Taxation of Income (Non-Corporate)

By CA Mahavir Jain
B.Com.; DISA; FCA
Partner : JMT & Associates
Email: jmtca301@gmail.com

Issues in Taxation of Non-Corporate Income is a very vast subject. It covers issues in all heads of Income Viz. Salaries, Income from House Property, Profit & gains of Business or profession, Capital Gains and Income from Other Sources.

As it is very wide topic, we will discuss few common issues in each heads of Income.

Who are Non Corporate Assessee: Under Section 2(31) Non Corporate Assesses are (a) an Individual, (b) a Hindu Undivided Family (HUF), (c) a Firm, (d) an association of persons or body of individuals, (e) a local authority, and (f) every artificial juridical person not falling within any of preceding categories including a Company category. These are the categories of non corporate persons chargeable to tax under the Income tax Act.

These persons can be Resident and ordinary resident, Resident but not ordinary resident and Non Resident.

Which is Income to be taxed in above person's hand?

(a) Incidence of tax in the case of Resident & Ordinarily Resident

Assessee: Income which is accrues or arises (or is deemed to accrue or arise) in India and income which is accrues and arises outside India

(b) Incidence of tax in the case of Resident but not Ordinarily Resident

Assessee: The liability of tax in this case is same as in the case of a resident & ordinarily resident. However income which is not liable to tax in India is not taxable if (a) income is received or deemed to be received in India (b) income is accrued or deemed to be accrued in India or (c) business is controlled from a place within India or profession is set up in India.

(c) Incidence of tax in the case of a non-resident Assessee: A non-resident is liable to tax in respect of income received (or deemed to be received) in India by or on his behalf and income that accrues or arises (or deemed to accrue or arise) in India during the previous year.

1. SALARIES:- this includes all income earned by employee by way of salary, Wages, annuity or pension, fees, commission in lieu of Salary, advance salary etc.

ISSUES UNDER THE HEAD SALARIES:

Issue : When a person received Gratuity on Retirement, it is exempt to some limit U/s 10(10). If one received gratuity on resignation, whether it will be exempt upto given limit or is it taxable?

Issue : If employer also pays commission at a fixed percentage of turnover achieved by employee, whether it falls within the expression “Salary”?

Issue : My company does not provide me HRA and Conveyance Allowance. I pay house rent can I get deduction for the same. What about conveyance can I claim 1,600 p.m.?

2. **INCOME FROM HOUSE PROPERTY:** – this includes income from Building or land appurtenant thereto, whether self occupied property, income from having more than one house, rented property etc.

ISSUES UNDER THE HEAD INCOME FROM HOUSE PROPERTY

Issue : One has given on Rent his vacant plot or land on rent, whether he can claim deduction under section 24 such as 30% of Rent etc.?

Issue : If the tax payer constructed a house property by borrowing interest free loan; and he had to take interest bearing loan to repay the above interest free loan, whether interest paid on such loan is allowed ?

Issue : In case of builder if finished flats remain unsold as stock in trade, whether he should pay tax as notional income on such stock in trade flats?

Issue : Whether against Rent Income deduction for insurance, ground rent, land revenue, repairs, electricity, water supply, salary to lift man etc can be claimed?

Issue : When the owner of the building gets along-with the rent, rent or hire of other assets (furniture) or charges for different services provided in the building, then in which head these will be taxable?

3. **INCOME FROM BUSINESS OR PROFESSION:-** this includes income from all types of business may be retails, whole sale, Manufacturing, and all types of professions such as Doctors, Chartered Accountants, Lawyers etc.

ISSUES IN INCOME FROM BUSINESS OR PROFESSION

Issue : An assessee incurs expenditure for acquisition of a depreciable assets for Rs. 15,000/- after September and made payment otherwise than by an account payee cheque/draft or by NEFT - Lead to increase in the value of Asset, what % of depreciation shall be allowed to him?

Issue : An assessee has not deducted TDS on Rs. 50,000/- in the AY 2014-15 and hence the same 100% was disallowed in that year under section 40(a)(ia). The Section has been amended in next assessment year that if TDS not paid then 30% of such expenses will be disallowed and in the year of payment of TDS 30% of such expenses will be allowed. The Assessee paid TDS in the AY 2017-18, in such case whether 30% of expenses will be allowed in AY 2017-18 or 100% will be allowed?

Issue : Whether Assessee declaring Income under presumptive Taxation is required to explain each cash deposit in Bank related to gross receipt of trade ?

Issue : Whether AO after accepting the 8% profit under Presumptive taxes can asked to prove the cost of 92% to Assessee ?

Issue : In case of Assessee engaged in supply of labour and civil contracts offering income u/s 44AD , difference of turnover as per 26 AS can be added as a total Income of the Assessee ?

Issue : What would be the nature of the repair and maintenance expenditure incurred on a machine – Lead to increase in the economic life of Machinery, Revenue or Capital?

Issue : What would be the nature of the repair and reconditioning expenditure incurred on a Machine which broke down years ago – Revenue or Capital?

Issue : An individual who is a partner in a firm, that firm fall under tax audit so it has to filing return before 30-09 of Assessment year, then which date of filing return apply to a partner if he is not fall under tax audit?

4. **CAPITAL GAINS**: - this refers to income resulting from the appreciation of a capital asset (e.g., stocks, real estate, coins). Capital gains are not realized until the asset is sold. Capital gains are classified as either short- or long-term:

- Short-term – for assets being Equity Shares or Equity Oriented Mutual Funds is held for 12 months or less and is taxed at flat rate of 15%, (10% upto AY 2008-09) (+SC+EC+SHEC) for other assets held for 36 months or less is considered short-term capital gains and is taxed at ordinary income rates.

However if transfer takes place after 01-04-2017 than in case of Equity or Preference Shares in a unlisted company and immovable properties (being land or building or both) period of holding should be less than 24 months to be make the transfer as Short Term.

- Long-term – An asset other than short term capital assets is regarded as long term capital assets.

TAX ON SHORT-TERM CAPITAL GAINS [SECTION 111A]

(i) Any short term capital gain arising from the transfer of an equity share in a company or a unit of an equity oriented fund shall be liable to tax @15% (+SC +EC +SHEC) (10% up to A.Y. 2008-09) if the following conditions are satisfied:

- a) The transaction of sale should take place through a recognised Stock Exchange; and
- b) Such transaction is chargeable to securities transaction tax (STT)

If the total income of an assessee includes such short term capital gain and other income, the tax payable by the assessee in such a case shall be the aggregate of-

- a) The amount of income-tax calculated on such short term capital gains @15% and
 - b) The amount of income-tax payable on the balance amount of the total income as if such balance amount were the total income of the assessee.
- (ii) In the case of an individual or a HUF, being a resident, where the total income as reduced by such short term capital gain is below the basic exemption limit, then the short term capital gain shall be reduced by the amount of basic exemption limit not exhausted by any other income and only the balance short term capital gain shall be chargeable to tax @15%. For a non-resident assessee adjusting of basic exemption limit against short term capital gains not be applicable, hence the entire amount of short term capital gain shall be subject to tax @15%. Where assessee paying special rate of tax then he is not entitled to claim any deduction provided under Chapter VI-A in respect of such capital gain.
- (iii) The short term capital gain other than above shall be chargeable as per Normal Slab of Income of the Assessee.

TAX ON LONG -TERM CAPITAL GAINS [SECTION 112]

- (i) In case of long term gain taxpayers has to pay tax at a flat rate @ 20% (+SC+EC+SHEC) after taking benefit of indexation.
- (ii) If long term capital gain arises on transfer of equity shares or units of equity oriented mutual funds and the sale transactions is covered by STT, such gains is not chargeable to tax U/s 10(38). However w.e.f. AY 2018-19 the above exemption shall be available only in case of transfer of said shares or units which were acquired on or before 01-10-2004. If acquired after 01-10-2004 then exemption shall be available only if STT has been paid not

only on sale but also at the time of acquisition of such shares or units.

(iii) In case of listed shares/ securities are transfer and the assessee don't want to take benefit of indexation, than assessee shall pay long term gain @ 10% (+SC+EC+SHEC) only. Assessee at his discretion can choose benefit or Taxation.

Consistency in taxability of income/loss arising from transfer of unlisted shares under Income-tax Act, 1961-regd.-

1. Regarding characterisation of income from transactions in listed shares and securities, Central Board of Direct Taxes (CBDT) had issued a clarificatory Circular no.6/2016 dated 29th February, 2016, wherein with a view to reduce litigation and maintain consistency in approach in assessments, it was instructed that income arising from transfer of listed shares and securities, which are held for more than twelve months would be taxed under the head 'Capital Gain' unless the tax-payer itself treats these as its stock-in-trade and transfer thereof as its business income. It was further stated that in other situations, the issue was to be decided on the basis of existing Circulars issued by the CBDT on this subject.

2. Similarly, for determining the tax treatment of income arising from transfer of unlisted shares for which no formal market exists for trading, a need has been felt to have a consistent view in assessments pertaining to such income. It has, accordingly, been decided that the income arising from transfer of unlisted shares would be considered under the head 'Capital Gain', irrespective of period of holding, with a view to avoid disputes/litigation and to maintain uniform approach.

3. It is, however, clarified that the above would not be necessarily applied in the situations where:

- i. the genuineness of transactions in unlisted shares itself is questionable; or
- ii. the transfer of unlisted shares is related to an issue pertaining to lifting of corporate veil; or
- iii. the transfer of unlisted shares is made along with the control and management of underlying business and the Assessing Officer would take appropriate view in such situations.

Amendment to Section 50C

Section 50C has been amended where the date of an agreement fixing the value of consideration and the date of registration are not same, the stamp duty value may be taken as on the date of the agreement for transfer (and not as on the date of registration) for such transfer. However, this exception shall apply only in those cases where amount of consideration (or part thereof) has been received by way of an account payee cheque/draft or by use of electronic clearing system through a bank account, on or before the date of the agreement for transfer. This amendment is applicable from AY 2017-18 for earlier years one can take the shelter of different available judicial ruling.

ISSUES IN CAPITAL GAINS:-

Issue : What happens when business in shares was commenced by converting the shares into stock in trade of the business and subsequently the assessee sold these shares at profit?

Issue : What happens when there is a transfer of an immovable property comprising of land and building where land is held for more than 36 months but the super structure is held for not more than 36 months?

Issue : In Business of Professional for more than 36 months old where Books are treated as plant & Machinery and depreciation is charged, leaving WDV as Nil, if sold subsequently what will be profit and how taxable?

Issue : A share Broker sold shares which are held as personal investment and showed the same in his Wealth Tax return as investment, whether AO is justify to Assess the gain as Business Income ?

5. **INCOME FROM OTHER SOURCES:** – Section 56(1) of the Income Tax Act lays down that income of every kind which is not to be excluded from the total income and which is not chargeable under any of the above heads of Income shall be chargeable to income tax under residuary head ‘Income from other Sources’.

ISSUES IN INCOME FROM OTHER SOURCES:

Issue : What if the company issues of shares at a premium, i.e. the issue price is more than the FMV Based on the DCF ?

Issue : What if the Consideration was received from a non-resident who became a resident at the time of allotment ?

Issue : Whether consideration received in kind taxable under new clause 56 (viib)?

Issue : Whether Dividend Income are to be included in total taxable income chargeable to tax?

ADVANCE TAX PAYMENT : Due Dates and Interest on Late Payment

Section 208 makes it obligatory to pay advance tax in every case if the Income Tax Liability of any taxpayer is more than Rs. 10,000 in a financial year, than tax payer is liable to pay such tax in installments during the year itself rather than paying this tax at the end of the year. This tax which is payable during the year is called “Advance Tax” or “pay as you earn tax” as tax is liable to be paid at the time the income is earned i.e. during the year rather than paying this tax at the end of the year.

A senior citizen (above 60 years of age) not having any income from Business or Profession is not liable to pay advance tax w.e.f. AY 2013-14.

Payment of Advance Tax With effect from 1st June 2016, Advance Tax is liable to be paid as per the following schedule in case of All Assesseees

Advance Tax Payment: Due Dates and Interest on Late Payment

Due Date of Installment Amount Payable (w.e.f. AY 2016-17)

1. On or before 15th June Not less than 15% of the Advance Tax Liability
2. On or before 15th Sep Not less than 45% of the Advance Tax Liability as reduced by the amount, if any, paid in earlier installment
3. On or before 15th Dec Not less than 75% of the Advance Tax Liability as reduced by the amount, if any, paid in earlier installments
4. On or before 15th Mar 100% of the Advance Tax Liability as reduced by the amount, if any, paid in earlier installments

In case of default or short fall in advance tax interest @1% will be levied U/s 234B and/ or 234C as the case may be.

Presumptive Tax Scheme for Business and Profession

The Finance Act, 2016 includes various amendments that aim at helping professionals and small businesses. One of them is about presumptive taxation, the required paperwork for which was a matter of concern for many professionals such as doctors, lawyers, chartered accountants and others.

The Finance Act has made things simpler for professionals by reducing the amount of effort needed to estimate the income for the year and also to file the return on this.

For taxation purpose, most businesses and professionals have to maintain books of accounts, which are then evaluated at end of each financial year. A profit and loss statement is prepared and tax on income, if any, is paid accordingly. However, there is a special scheme— Presumptive Taxation Scheme (PTS)— under which one can file the return and pay tax on the basis of ‘presumed’ income.

Under PTS, eligible professionals and businesses can compute income on an estimated basis under section 44ADA and 44AD of the Income Tax Act, 1961, respectively, at a minimum prescribed rate. Businesses already had this provision, but from the current financial year, the threshold under PTS for eligible businesses has been raised from Rs.1 crore to Rs.2 crore. Professionals with less than Rs.50 lakh of gross receipts in a financial year are also now under the umbrella of PTS.

Eligible businesses

The scheme can be adopted by an eligible resident individual, a resident Hindu undivided family (HUF) and resident partnership firm. However, limited liability partnership (LLP) firms are not allowed to adopt this scheme. Also, those who claim benefits for their businesses on the basis of those being in free or special economic zones or in backward areas can’t avail of PTS. Even those who are earning income in the nature of commission or brokerage (such as insurance agents or mutual fund advisers) cannot adopt the scheme.

From the assessment year 2017-18, the scheme will cover businesses having a total turnover of less than Rs.2 crore during the financial year. “However, business of plying, hiring or leasing goods carriages referred to in another PTS under section 44AE, are not allowed to adopt this scheme,”.

Under PTS, if the above mentioned conditions are satisfied, the eligible businesses can estimate their income at the rate of 8% of the total turnover. For instance, if the turnover of the business is Rs.1.75 crore in the financial year and the owner decides to compute income on an estimated basis for filing income tax returns, business income chargeable to tax so calculated would be Rs.14

lakh (8% of Rs.1.75 crore). However, the assessee is allowed to willingly declare income at a higher rate than the minimum of 8% of the total turnover. So, it is on the business owner's discretion to declare that the profit margin in the business is more than the mandatory 8%. Tax will be paid accordingly. So, in the above example, an income of more than Rs.14 lakh on a total turnover of Rs.1.75 crore can be declared.

From AY 2017-18, instead of tax @8%, assessee will pay tax @6% only in respect of total Turnover or gross receipts received by an account payee cheque, Bank Draft or by use of electronic system through bank during the previous year or before the due date of submission of Return of Income U/s 139(1).

Eligible professionals

PTS has now been extended to professionals by inserting a new section—44ADA—in the Act. “Those who are governed or regulated by an institute or body such as doctors, lawyers, architects, interior designers and others can file returns under the scheme.”

According to the new section, eligible professionals, whose gross receipts are below Rs.50 lakh against the rendered services in a financial year, can file tax returns under PTS. For this, 50% of the total receipts during the fiscal will be considered as profit and will get taxed under the income tax head of “profits and gains of business or profession”. For instance, if the receipts of a professional during the year amount to Rs.40 lakh, and she chooses to file her tax return under PTS, her taxable income will be considered at a minimum of Rs.20 lakh. But she can voluntarily declare an income that's more than the mandatory 50% of the total receipts.

What is considered turnover or receipt?

Under PTS, you can only take into consideration gross turnover or receipts. But it is not clear as to what should be considered as receipts and what should not be. “It depends more on what kind of accounting method you use.”

“If you operate under the accrual system, take only those sales where you delivered the goods or completed the service within the specified time period you are considering. If you operate on cash basis, recognise only the sales where you received payment within the time period.”

That means that you can either take into account only the amount of goods or services delivered during the year, irrespective of whether the related payment has been received or not. In other case you can take into account only cash sales, accrued income (income earned but not received) can be taken into consideration in the year it is received.

Implication of Service tax and cess : Along with the fee charged for the service provided, professionals also collect service tax and cess as part of the bill. But will the service tax and cess components, which the professional has to pass on to the government, also be considered as receipts?

“Since gross receipts are not defined, there is not enough clarity on this. (But) as a matter of principle, service tax and cess should not be included in the gross receipts.”.

The argument here is that since service tax and applicable cess are payable to the government by the service provider, only the service fee should be treated as receipt.

Not allowed to claim : Professionals and businesses availing the benefits of PTS can't claim tax deduction under sections 30 to 38 of the Act, which would include deduction on expenses such as rent of the shop or office, insurance premium of goods and machines, interest on borrowed capital, employer's contribution to provident fund, depreciation on assets and machinery, and so on. Under PTS, it is deemed that deductions for such expenses have been factored in. From AY 2017-18 and onwards interest/salary paid to any partner/ working partner by a firm will also not be allowed.

No Advance Tax Payment :All professionals and businesses generally have to adhere to advance tax payment rules. According to section 208 of the Act, if the total estimated tax on their incomes for the relevant financial year is expected to be more than Rs.10,000 per annum, advance tax has to be paid. One has to pay 15% of the estimated income tax by 15 June, 45% by 15 September, 75% by 15 December and the rest by 15 March of the relevant financial year.

However, with PTS, the assessee is exempt from paying advance tax (upto AY 2016-17). From the AY 2017-18 an assessee (who opts for above scheme) is required to pay advance tax related to such business. However advance tax can be paid during the financial year on or before 15th March. This means that he/ she does not have to estimate his/ her income four times a year and pay advance tax accordingly. Instead, he/ she have to go through the exercise only once.

The main aim of PTS is to reduce tax compliance burden and cost of maintaining books of account for professionals and small businesses. While some points are still to be clarified, the scheme is a move forward.

THE INCOME COMPUTATION & DISCLOSURE STANDARDS

In exercise of the powers conferred by the amended sub-section (2) of Section 145, CBDT notified 10 Income Computation and disclosure Standards (ICDs) vide Notification S.O. 892(E), dated 31-03-2015. The said Notification came into force w.e.f. 01-04-2015 and became applicable from AY 2016-17.

CBDT has vide Notification No. S.O. 3079(E), dated 29-09-2016 come out with New revised version of the 10 ICDs which shall apply for AY 2017-18 and subsequent AY.

The 10 ICDs are as follows:

ICDs No.	Related Items
ICDS I	Accounting Policies
ICDS II	Inventories
ICDS III	Construction Contracts
ICDS IV	Revenue Recognition
ICDS V	Tangible Fixed Assets
ICDS VI	Effects of Changes in Foreign Exchange Rates
ICDS VII	Government Grants
ICDS VIII	Securities
ICDS IX	Borrowing Cost
ICDS X	Provisions, Contingent Liabilities and Contingent Assets

A. Applicability

- These are applicable to all assesses following mercantile system of accounting except an Individual or HUF who is not required to get his accounts audited under section 44AB of the Act.

B. How & Where Disclosures to be made for ICDs

- Disclosures as required by ICDs to be made in new Item Nos. 13(d) and 13(e) of Form No. 3CD in Tabular format-ICDS-wise.

Issue : Certain ICDS provisions are inconsistent with judicial precedents. Whether these judicial precedents would prevail over ICDS?

Issue : Does ICDS apply to non-corporate taxpayers who are not required to maintain books of account an/or who are covered by presumptive scheme of taxation like 44AD, 44AE, 44ADA, 44B, 44BB, 44BBA etc?

Issue : If there is conflict between ICDS and other specific provisions of the Rules governing taxation of income like rules 9A, 9B etc., which provisions, shall prevail?

Issue : Whether ICDS shall apply to computation of Minimum Alternate Tax (MAT) under section 115JB or Alternate Minimum Tax (AMT) under section 115JC of the Act?

Issue : Whether ICDS is applicable to revenues which are liable to tax on gross basis like interest, royalty and fees for technical services for non-residents under section 115A of the Act?

Issue : Whether bill discounting charges and other similar charges would fall under the definition of borrowing cost?

===== **T H A N K S** =====