

# Roots Institute of Financial Markets RIFM



## *Study Notes-Part 2* *Advanced Financial Planning*

## Forward

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We Are Constantly Engaged In Providing A Unique Educational Solution Through Continuous Innovation.

Wish You Luck.....

Faculty and Content Team, RIFM

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## Exam Pattern

Pattern of Questions in a Case Study											
		Module I		Module II		Module III		Module IV		Module V	
		No_Items	Marks	No_Items	Marks	No_Items	Marks	No_Items	Marks	No_Items	Marks
<b>Marks Category</b>	2	2	4	1	2	0	0	1	2	1	2
	3	1	3	1	3	1	3	0	0	1	3
	4	0	0	1	4	0	0	1	4	0	0
	5	0	0	0	0	1	5	2	10	1	5
<b>Total</b>		<b>3</b>	<b>7</b>	<b>3</b>	<b>9</b>	<b>2</b>	<b>8</b>	<b>4</b>	<b>16</b>	<b>3</b>	<b>10</b>

- A student who scores 50% or more will pass the examination and anyone who scores below 50% (exclusive) will fail the examination.
- There is no negative marking in the Examination.
- Successful students in the CFP<sup>CM</sup> Certification examination are not given their scores or ranks as practiced in most international professional certification examinations. However, given the aspiration needs of the students, grades will be provided to the successful students. Unsuccessful students shall get their marks in percentage terms along with the result.
- The following grading system will be used to provide grades.

Grade	Score (Percentage)
A	Equal and above 75%
B	Equal and above 60% and less than 75%
C	Equal and above 50% and less than 60%
Fail	Less than 50%

## Syllabus

### Advanced Financial Planning

**COURSE DESCRIPTION:** This module builds upon the foundations in Financial Planning and the knowledge requirements in Modules 2 to 5 to enable the CFP professional to construct a comprehensive Financial Plan for a client. Miscellaneous topics are also covered in this module.

**LEARNING OBJECTIVES:** At the end of this module, a student should be able to:

1. Determining the client's financial status by analyzing and evaluating the client's information.
2. Developing and preparing a client-specific Financial Plan tailored to meet the goals and objectives of client, commensurate with client's value, temperament, and risk tolerance.
3. Implement and monitor the Financial Plan.

### DETAILED CLASS OUTLINE:

#### Financial Planning Process

1. Establishing client- planner relationships
  - a. Explain issues and concepts related to overall Financial Planning process, as appropriate to the client
  - b. Explain services provided, the process of planning, documentation required
  - c. Clarify client's and certificant's responsibilities
2. Gathering client data and determining goals and expectations
  - a. Obtain information from client through interview/ questionnaire about financial resources and obligations
  - b. Determine client's personal and financial goals, needs and priorities
  - c. Assess client's values, attitudes and expectations
  - d. Determine client's time horizons
  - e. Determine client's risk tolerance level
  - f. Collect applicable client records and documents
3. Determining the client's financial status by analyzing and evaluating the client's information
  - A. General
    - a. Current financial status (e.g., assets, liabilities, cash flow, debt management)

- b. Capital needs
- c. Attitudes and expectations
- d. Risk tolerance
- e. Risk management
- f. Risk exposure

B. General Needs

- a. Emergency funds
- b. Children's education
- c. Children's marriage
- d. Buying real assets like home, car, durables, etc.
- e. Future lifestyle needs

C. Special needs

- a. Divorce / remarriage considerations
- b. Charitable planning
- c. Adult dependent needs
- d. Disabled child needs
- e. Education needs
- f. Terminal illness planning
- g. Entrepreneurial needs planning

D. Risk management

- a. Life insurance needs and current coverage
- b. Disability insurance needs and current coverage
- c. Medical insurance needs and current coverage
- d. Long – term care insurance needs and current coverage
- e. Homeowners insurance needs and current coverage
- f. Auto insurance needs and current coverage
- g. Commercial insurance needs and current coverage
- h. Other liability insurance needs and current coverage (e.g., umbrella, professional, errors and omissions, directors and officers)

E. Retirement

- a. Current retirement plan tax exposures
- b. Current retirement plans
- c. Retirement strategies

F. Employee benefits

- a. Available employee benefits

- b. Current participation in employee benefits

#### G. Investments

- a. Current investments
- b. Current investment strategies and policies

#### H. Taxation

- a. Tax returns
- b. Current Tax strategies
- c. Tax compliance status (e.g., estimated tax )
- d. Current tax liabilities

#### I. Estate planning

- a. Estate planning documents
- b. Estate planning strategies

#### 4. Analyze Client Objectives, Needs and Financial Situation

- a. Analysis of relevant information
- b. Need for specialist advice
- c. Issues that require further clarification

#### 5. Developing and presenting the Financial Plan

A. Developing and preparing a client-specific Financial Plan tailored to meet the goals and objectives of client, commensurate with client's value, temperament, and risk tolerance, covering:

##### 1. Financial position

- a. Current statement
- b. Projected statement
- c. Projected statement with recommendations

##### 2. Cash flow

- a. Projections
- b. Recommendations
- c. Projections with recommendations

3. Capital needs at retirement
  - a. Projections
  - b. Recommendations
  - c. Projections with recommendations
  
4. Capital needs projections at death
  - a. Recommendations
  - b. Projections with recommendations
  
5. Capital needs: disability
  - a. Recommendations
  - b. Projections with recommendations
  
6. Capital needs: General needs
  - a. Recommendations
  - b. Projections with recommendations
  
7. Capital needs: special needs
  - a. Recommendations
  - b. Projections with recommendations
  
8. Income tax
  - a. Projections
  - b. Recommendations
  - c. Projections with strategy recommendations
  
9. Employee benefits
  - a. Projections
  
10. Asset allocation
  - a. Statement
  - b. Strategy recommendations
  - c. Statement with recommendations



11. Investment

- a. Recommendations
- b. Policy statement
- c. Policy statement with recommendations

12. Risk

- a. Assessment
- b. Recommendations

13. List of prioritized action items

- a. Presenting and reviewing the plan with the client
- b. Collaborating with the client to ensure that plan meets the goals and objectives of the client, and revising as appropriate

6. Implementing the Financial Plan

- a. Assist the client in implementing and recommendations
- b. Coordinate as necessary with other professionals, such as accountants, attorneys, real estate agents, investment advisors, stock brokers and insurance agents

7. Monitoring the Financial Plan

- a. Monitor and evaluate soundness of recommendations
- b. Review the progress of the plan with the client
- c. Discuss and evaluate changes in client's personal circumstances, (e.g., birth/ death, age, illness, divorce, retirement)
- d. Review and evaluate changing tax law and economic circumstances
- e. Make recommendations to accommodate new or changing circumstances

**Miscellaneous Topics**

8. Internet Resources

- a. Internet usage and application
- b. Transactions over the net
- c. Issues of security
- d. Financial Planning using the Internet

9. Foreign exchange issues for individuals

- a. Foreign Exchange Management Act (FEMA)

- b. Currency risk management

10. Financial Planning for special needs and clients

- a. Individual life cycle
- b. Financial Planning for unmarried clients, single parents, widows/widowers, etc.
- c. Financial Planning for returning Non Resident Indians
- d. Other special needs and options (e.g., divorce, bankruptcy)

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# UNIT

## 3

### RETIREMENT PLANNING

- A. Employee benefit scheme*
- B. Defined contribution plans*
- C. Retirement need analysis*
- D. Annuity*

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## A. Defined contribution plan

### Introduction

Defined contribution plans are benefit plans, wherein the contribution of employer and employees are defined rather than the defined benefit payable to the employee. The plan thus seeks and runs on the contribution as per agreement and makes available the accumulated balance at the end of the period or at the time of withdrawal.

These benefit plans have evolved over the period taking cue from the disadvantages offered in the Defined Benefit Plan. These plans have offered greater transparency and portability to employees and employer and are designed to meet the changing need of the corporate world and employees. Though defined contribution plans have the characteristics of defined contribution, but the administration and characteristics of the plans have been changing and in the process we today have a number of plans in the market, which are bases on different characteristics of contribution.

These are some clear differences in the defined benefits and the defined contributions routes:

Defined Benefits	Defined Contributions
The kind of benefits to be received at the time of retirement is fixed based on a certain working.	The kind of benefits to be received at the time of retirement is not fixed on any calculations.
This figure is calculated using the way in which benefits are defined.	The amount received depends upon the earning of the investment.
There is an element of comfort and surety with this method.	There is no element of surety with this method.
This is beneficial to the employee.	This is beneficial to the employee.
The employee does not have to worry about how the earnings are going to managed once they know the amount to be received.	The employee has to worry about how the earning come because this determines the amount received.
If there is inadequate earning then the employer makes up the shortfall against the amount due.	If there is inadequate earning then the employer gets to enjoy a lesser amount of benefit
There is no definite relation between the contribution and the amount received in all cases.	There is no direct relation between the amount contributed and the amount received as a benefit.
Example is a Gratuity and voluntary retirement amounts.	Example is a Provident fund and public provident fund.

### Provident Fund

Provident fund is the most common type of Defined Contribution Plans in Operation in India; we have much type of plans, which are designed for all categories on individual.

Some type of Provident Funds:

#### **[a] STATUTORY PROVIDENT FUND**

Statutory Provident Fund under the provident fund Act, 1925 are maintained by government and semi-government organizations, local authorities, recognized educational institutions, railways, airlines etc. This is a blue-eyed baby. Everything is exempt from tax, without any ifs and buts, including the employer's contribution and the interest paid, even it is over 12%.

#### **Contribution**

An employee can make a contribution subject to a minimum of 6% of emoluments; however he can make contributions more than the minimum prescribed subject to the maximum of total emoluments received by the employee.

#### **Taxability**

Employee's contribution: eligible for deduction u/s 80C

Employee's contribution: Fully exempt from tax

Interest on PF: Fully exempt from tax

Repayment: Fully exempt from tax u/s 10(11)

#### **[b] RECOGNIZED PROVIDENT FUND**

Recognized Provident Fund (RPF) covered by Employee's Provident fund and miscellaneous Provisions Act, 1952 is applicable to establishments with 20 or more employees. Those with fewer employees are also allowed to opt for it. The PF Commissioner manages the funds. However, if the establishment desires to manage its own funds, a trust approved by the IT commissioner, has to be created which will invest the funds in accordance with the PF rules. Employee's contributions are covered by Sec 80C and there is no ceiling on his voluntary contribution. Employer's contribution in excess of 12% of employee's salary as well as interest paid exceeding 9.5% p.a. is charged to tax. Payment of accumulated balance in RPF is taxable under Rule 9(1) of Schedule IV (A) to the ITA, unless the employee renders continuous services with his employer for 5 years of the discontinuance is due to causes beyond control of the employee. This balance is also exempt if it is transferred to the employee's individual account in any RPF maintained by the new employer or by the PF commissioner. Service under his former employer or employers shall be included in computing the total period of continuous service.

#### **Employees' Provident Funds & Miscellaneous Provisions Act, 1952**

#### **Objective**

- Promoting and securing the well being of the employees by way of provident fund, family pension and insurance to them.
- Promoting a habit of saving amongst workers.
- Providing a steady workforce to the employers.
- Assisting the government by providing funds of considerable magnitude for utilization on various projects meant for promoting economic and social development of the country and the well being of its people.

#### **Applicability:** The Act shall apply to

- Every establishment which is a factory.
- Engaged in any industry mentioned in schedule I of the Act and employing 20 or more persons.

- Any other establishment employing twenty or more persons.
- Such other establishment as the central Government may notify.

All employees in such factory or establishment including contract labour, but excluding casual labour and receiving wages up to Rs. 6,500/- per month will be regulated by the provisions of the Act. Trainee and the apprentices are also not included in determination of the numerical strength.

Once the Act applies to any establishment, it shall continue to be governed by the Act, irrespective of the fact that the number of employees working therein falls below 20, subsequently.

### Contributions

Employees Provident Fund scheme takes care of the members at the time of retirement, medical care, housing, family obligations, education of children, finance of children policies. Etc. In terms of section 6 of the Act, the employee may contribute 12 or 10%, as the case may be, of the basic wages, dearness allowance including the cash value of any food concession and retaining allowance. An allowance paid to the employee for retaining his services when the establishment is not working is retaining allowance. The rate of contribution shall be 10% in the case of certain establishments.

- Any covered establishment with less than 20 employees.
- Any sick industrial company within the meaning of SICA.
- Any establishment which has at the end of the financial year accumulated losses equal to or exceeding its entire net worth.
- Any establishment in the business of jute, beedi, brick, coir.

If the employee so desire, he may opt to contribute a higher rate also. However, employer does not have to match the voluntary contribution over and above the statutory rate. The employer's contribution of 12% or 10% shall be up to 8.33% of the basic wages, dearness allowance and retaining allowance towards employees' pension scheme and the balance 1.67%/3.67% towards the provident fund. The employee does not have to make any contribution to the pension fund account. These amounts must be paid within 15 days from close of every month with the PF Commissioner in to the respective accounts maintained with the state bank of India. If the amount is not paid, employer is liable to pay "damages". In addition, criminal prosecution can also be launched.

### Taxability:

Employees' contribution: deduction u/s 80C is available. Employer's contribution: exempt up to 12% of salary, excess of 12% to be included in gross salary. Interest on PF: exempt u/s 10 up to 9.5% p.a. Interest credited in excess of 9.5% to be included in gross salary.

**Repayment:** Exempt in the following cases.

- In the case of an employee who has rendered continuous service with his employer for a period of 5 years or more.
- In the case of the employee whose service has been terminated by reason of ill health of the employee or due to the discontinuance of the employer's business or other cause beyond the control of the employee.
- In the case of an employee who obtains employment with another employer who maintain any RPF which the accumulated balance becoming due and payable is transferred.

In all other cases, where repayment is made, an employee will be liable to be taxed on the earlier exempted amount. Even the employer contribution and interest accumulated on the entire amount shall be taxed to income under the respective heads of income.

## **D. Annuity**

### **IMMEDIATE ANNUITY**

If the successive payments of the annuity are made at the end of the successive periods, then the annuity is called an immediate annuity. In case of immediate annuity certain of Rs. 10000 for 8 years, there would be 8 yearly payments in all; the first payment of Rs. 10000 being made at the end of the first year and the last at the end of the 8<sup>th</sup> year. Immediate annuity starts the first benefit payment from the payment interval (i.e. annually, half yearly, quarterly, and monthly-as the case may be) immediately after the date of the contract. The person who opts for 'Immediate annuity plan' has to pay a lump sum investment to the financial institution or has to pay a single premium to the insurance company. If the annuity starts after a gap of more than 1 year, then it will not be known as immediate annuity.

### **[C] Deferred Annuity**

The payments to be made under such an annuity are postponed for a given period called deferment period. The annuity will vest for payment at the end of the deferment period. In Deferred Annuity, pension is payable after a 'specific period' which would be a period between the date of contract and a future date beyond or more than one year. This period is called 'Deferment Period' In case of Deferred Annuity plans of insurance companies, the premiums can be paid as one lump sum (single premium) or as regular premium (premium payment either monthly, quarterly, half-yearly, yearly).

If death occurs to an annuitant during the deferred period, premiums paid are returned to the nominee or legal heir/s.

### **Further illustrations of types of Annuities**

- a) **Immediate Annuity Certain:** If the successive payments of the annuity are made at the end of the successive periods and or a definite number of years, then the annuity is called an immediate annuity certain. Also, these annuities commence immediately after the contract is concluded with the financial institution, providing the annuity scheme.
- b) **Immediate Annuity Due:** If these successive payments are made at the beginning of each successive period, then the annuity is called an annuity due.
- c) **Deferred Annuities certain:** It is an annuity certain postponed for a given period called deferment period. Deferred Annuity can again be either a deferred immediate annuity or a Deferred Annuity due. For example, a Deferred immediate Annuity certain for 15 years with deferment period of 5 years is one in which the first payment is to be made at the end of 6<sup>th</sup> year and the fifteenth payments at the end of 20<sup>th</sup> year. Again it is Deferred Annuity certain due for 15 years, with a deferment period of 5 years, the first payment is made at the beginning of the 6<sup>th</sup> year i.e. immediately at the end of deferment period of 5 years, the 15<sup>th</sup> payment will be made at the beginning of the 20<sup>th</sup> year i.e. at the end of 19<sup>th</sup> year.



- d) **Increasing Annuities:** In this type of annuities, the amount of annuity payment increase every year. The amount of increase is predefined as a fixed percentage per annum. This type of plans helps in mitigating the effects of inflation.

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# UNIT

## 5

### TAX & ESTATE PLANNING

- A. Basic concepts***
- B. Tax calculations and special rule***
- C. Total income & tax payment***
- D. Residential status of individual***
- E. Heads of income***
- F. Tax free income***
- G. Clubbing of income***
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- I. Deductions***
- J. Gift***
- K. Tax characteristics of business firms***
- L. Taxation of NRI***
- M. Penalty***
- N. Estate Planning***

**A. Tax calculations and special rules****Income Tax Rates for AY 2010-2011****Individuals and HUFs:****I. In case of individual (other than II and III below) and HUF:-**

Income Level / Slabs		Income Tax Rate
i.	Where the total income does not exceed Rs.1,60,000/-.	NIL
ii.	Where the total income exceeds Rs.1,60,000/- but does not exceed Rs.3,00,000/-.	10% of amount by which the total income exceeds Rs. 1,60,000/-
iii.	Where the total income exceeds Rs.3,00,000/- but does not exceed Rs.5,00,000/-.	Rs. 14,000/- + 20% of the amount by which the total income exceeds Rs.3,00,000/-.
iv.	Where the total income exceeds Rs.5,00,000/-.	Rs 54,000/- + 30% of the amount by which the total income exceeds Rs.5,00,000/-.

**II. In case of individual being a woman resident in India and below the age of 65 years at any time during the previous year:-**

Income Level / Slabs		Income Tax Rate
i.	Where the total income does not exceed Rs.1,90,000/-	NIL
ii.	Where total income exceeds Rs.1,90,000/- but does not exceed Rs.3,00,000/-	10% of the amount by which the total income exceeds Rs.1,90,000/-.
iii.	Where the total income exceeds Rs.3,00,000/- but does not exceed Rs.5,00,000/-.	Rs. 11,000/- + 20% of the amount by which the total income exceeds Rs.3,00,000/-.
iv.	Where the total income exceeds Rs.5,00,000/-	Rs.51,000/- + 30% of the amount by which the total income exceeds Rs.5,00,000/-.

**III. In case of an individual resident who is of the age of 65 (Called Senior Citizen) years or more at any time during the previous year:-**

Income Level / Slabs		Income Tax Rate
i.	Where the total income does not exceed Rs.2,40,000/-.	NIL

ii.	Where the total income exceeds Rs.2,40,000/- but does not exceed Rs.3,00,000/-	10% of the amount by which the total income exceeds Rs.2,40,000/-.
iii.	Where the total income exceeds Rs.3,00,000/- but does not exceed Rs.5,00,000/-	Rs.6,000/- + 20% of the amount by which the total income exceeds Rs.3,00,000/-.
iv.	Where the total income exceeds Rs.5,00,000/-	Rs.46,000/- + 30% of the amount by which the total income exceeds Rs.5,00,000/-.

Surcharge: NIL

Education Cess: 2% of the Income-tax.

Secondary and Higher Education Cess: 1% of the Income-tax.

**Firms:**

A Firm is taxable at the rate of 30 per cent for the assessment years 2010-11.

Surcharge: Nil

Education cess: It is 2 per cent of income tax and surcharge.

Secondary and higher education cess: It is 1 per cent of income tax and surcharge.

**Companies:**

For the assessment year 2010-11 the following rates of income tax are applicable.

Company	Rate of income tax (per cent)
In the case of a domestic company	30
In the case of a foreign company	
<ul style="list-style-type: none"> <li>Royalty received from government or an Indian concern in purchase of an agreement made by it with the Indian concern after March 31, 1961, but before April 1, 1976, or fees for rendering technical services in pursuance of an agreement made by it after February 29, 1964 but before April 1, 1976 and where such agreement has, in either case, been approved by the central Government.</li> </ul>	50
<ul style="list-style-type: none"> <li>Other income</li> </ul>	40

Surcharge-Surcharge is applicable at the rates given below-----

In Net income does not exceed Rs. 1 crore	If net income exceeds Rs. 1 core
---	----------------------------------

Domestic Company	Nil	10% (for assessment year 2010-11)
Foreign company	Nil	2.5%

**Marginal relief is available which is given below:**

Marginal relief – In the case of a company having a net income of exceeding Rs. 1 crore, the net amount payable as income-tax and surcharge shall not exceed the total amount payable as income-tax on total income of Rs. 1 crore by more than the amount of income that exceeds Rs. 1 crore.

Education cess- It is 2 per cent of income tax and surcharge.

Secondary and higher education cess- it is 1 per cent of income tax and surcharge.

**CO-OPERATIVE SOCIETIES:**

**THE FOLLOWING RATES ARE APPLICABLE TO A CO-OPERATIVE SOCIETY FOR THE ASSESSMENT YEAR 2010-11**

<i>NET INCOME RANGE</i>	<i>RATE OF INCOME TAX (%)</i>
<i>UP TO RS. 10,000</i>	<i>10</i>
<i>RS. 10,000- RS. 20,000</i>	<i>20</i>
<i>RS. 20,000 AND ABOVE</i>	<i>30</i>

**SURCHARGE: NIL**

**EDUCATION CESS-** It is 2 per cent of income tax and surcharge

Secondary and higher education cess- it is 1 per cent of income tax and surcharge.

**LOCAL AUTHORITIES:**

**LOCAL AUTHORITIES ARE TAXABLE AT THE RATE OF 30 PERCENT.**

**SURCHARGE: NIL**

**EDUCATION CESS-** It is 2 per cent of income tax and surcharge

Secondary and higher education cess- it is 1 per cent of income tax and surcharge.

## B. Heads of income

### Income from salaries

Section [15 to 17]

#### **Important concepts**

Employer & employee relationship

- For the income to be taxable under this head, relation of employer and employee must exist between the payer and payee.
- Any payment received by an individual from a person other than his employer cannot be termed as salary.
- Examples:
  - ✓ Remuneration received by a lecturer from his college is salary but remuneration received from another university is not salary. Hence it will be taxable under the head "Income from other sources", not under the head "salaries". (E.g. remuneration for setting question paper of another university).
  - ✓ If director is working in a company in the capacity of employee, then commission or director's sitting fee or any other amount received by him from that company should be taxable as a "Salary income", otherwise as a "Income from other sources",

1. MLAs or MPs are not treated as an employee of the Government; therefore remuneration received by these people is not taxable under the head "Salaries", but taxable under the head "Income from other sources",
2. Salary received by a partner from a partnership firm is taxable under the head "Business and profession"

There should be an intention to pay and receive salary. Likewise, there should be intention to render services.

Surrender of salary

- Salaries are taxable on due basis and once accrued to an employee, its subsequent waiver by the employee does not relieve him from tax liability.
- But if an employee surrenders his salary to Central Government u/s 2 of Voluntary Surrender of Salaries Act, 1961, the salary so surrendered will be excluded while computing his taxable income.

#### **Tax- free salary**

Amount of tax paid by the employer on behalf of the employee shall be included in the taxable income of the employee.

### Arrear of salary

Arrear will be taxed in the previous year in which these are paid or allowed to employee (i.e. receipts basis).

### Salary due or received in foreign currency

If the salary is earned in foreign currency, it will be converted into rupees.

- Conversion rate - T.T. buying rate on specified date.
- Specified date - Last date of the month immediately preceding the month in which the salary is Due /paid in advance /paid in arrears.

### How to compute salary in the grade system

#### Example

If any employee joins the service on 1-5-97 and is placed in the grade of Rs. 32,500 – 500 – 38,000 – 800 – 44,400.

This means that –

- He will get a basic salary of Rs. 32,500 w.e.f. 1-5-97
- He will get annual increment of Rs. 500 w.e.f. 1-5-98 and on wards till his salary reaches Rs. 38,000.
- Thereafter, he will get on annual incremental of Rs. 800 till his salary reaches 44,400.
- No further increment will be given thereafter till he is placed in other grade

#### Basis of charge (Sec.15)

Salary is chargeable either on

1. Due basis ; or
2. Receipt basis

(Whichever is earlier)

1. If salary is due at the end of the month - in this case, salary from April to March is taxable
2. If salary is due on 1<sup>st</sup> day of the next - In the case, salary from march to feb. Month is taxable.

Note – in case of Government employee, the salary become due on the 1<sup>st</sup> day of the next month whereas in case of none – Government employee (including bank employees.), the salary become due on the last day of the same month.

### METHOD OF ACCOUNTING

Method of accounting is irrelevant. It cannot vary the basis of charge fixed by sec.15.

**Salary earned & received outside India.**

Since salary earned and received outside India is not taxable in the hands of NOR & NR. Therefore perquisites received outside India for rendering services outside India is not chargeable to tax.

**MEANING OF SALARY [SEC. 17(1)]**

Salary includes: -

1. Wages
2. Any annuity or pension;
3. Any gratuity;
4. Any fees, commission or perquisites or profit in lieu of or in addition to any salary /wages;
5. Any advance of salary;
6. Leave encashment;
7. Employer contribution to Recognized provident fund (RPF).
8. Interest credited in RPF A/c
9. Transferred balance from URPF to RPF
10. The contribution made by the Central Government to the account of an employee under Pension Scheme referred to in Sec 80CCD.



Performa of computing taxable income

Basic salary	Rs.	Rs.
Dearness allowance		XXX
Bonus		XXX
Commission		XXX
Pension		XXX
Employer's contribution in excess of 12% to RPF.		XXX
Interest in excess of 9.5 % on RPF		XXX
Taxable allowance		XXX
Taxable perquisites (after proper valuation)		XXX
Taxable part of gratuity		XXX
Taxable part of computation of pension		XXX
Lump sum received from URPF to the extant employer's contribution and interest thereon		XXX
Taxable part of compensation received		XXXX
Gross salary		
Less : Deduction u/s 16	XXX	
(i) Entertainment allowance	XXX	
(ii) Employment tax		XXXX
<u>TAXABLE SALARY /NET SALARY</u>		

Meaning of Government employees for different purpose

S. No.	PURPOSE	GOVERNMENT EMPLOYEES
1.	Leave encashment/entertainment allowance Rent free House.	Central & State Govt.
2.	Gratuity	Central & State Govt. & Local authorities.
3.	Pension	Central & State Govt. & Local authorities & Statutory corporation & Judges of H.C./ S.C.

Meaning of salary for Computation

S. No.	Purpose of computation	Salary includes
1.	Entertainment allowance	Basic salary
2.	Gratuity [if gratuity Act, 1972 is applicable]	Basic salary + DA (whether forming part of retirement benefit or not)
3.	Leave encashment / HRA /	Basic salary + DA (whether forming

	RPF / Gratuity [it Act not applicable]	part of retirement benefit or not)+ fixed commission on turnover.
4.	Retirement compensation	Basic+ All allowance + Value of all benefit [excluding Bonus, Gratuity, Employer's contribution to any retirement benefits scheme.]
5.	Rent free accommodation or at concessional rate.	Basic + Allowance + Bonus + Commission + DA (If forming part of retirement benefit)+ Any money payment ( which is chargeable to tax) But does not include – 1. Employer's contribution to P.F. A/c. 2. Value of perquisite specified in sec. 17(2)

**Notes****Dearness allowance (DA)**

If in question DA is given, then it will not be treated as forming part of salary unless question specifically says that –

- If forming part of retirement benefit /
- Under the terms of employment /
- Consider for retirement benefit.

**Dearness pays (DP)**

It means it is forming part of retirement benefit unless question says otherwise.

**Computation of income under the head Salary****Following are fully taxable**

1. Basic salary
2. Dearness allowance (Whether forming part of salary or not)
3. Advance salary - Taxable on receipt basis (Relief U/s 89 can be claimed)
4. Arrear of salary – Taxable on receipts basis, if not taxable earlier on due basis (Relief u/s 89 can be claimed)
5. Bonus – Taxable on receipt basis,  
Note – if bonus is received in arrears, relief u/s 89 can be claimed.
6. Annuity received from employer.

7. Salary in lieu of notice period – Taxable on receipts basis.
8. Fee and commission.
9. Overtime payment.

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## **INCOME FROM HOUSE PROPERTY**

### **CHARGEABILITY [SECTION 22]**

1. The process of computation of income under the head “Income from house property” starts with the determination of annual value of the property. The concept of annual value and the method of determination is laid down in section 23.
2. The annual value of any property comprising of building or land appurtenant thereto, of which the assessee is the owner, is chargeable to tax under the head “Income from house property”.

### **CONDITIONS FOR CHARGEABILITY**

#### **(i) Property should consist of any building or land appurtenant thereto.**

- a. Buildings include not only residential buildings, but also factory buildings, offices, shops, godowns and other commercial premises.
- b. Land appurtenant means land connected with the building like garden, garage etc.
- c. Income from letting out of vacant land is, however, taxable under the head “Income from other sources”.

#### **(ii) Assessee must be the owner of the property**

1. Owner is the person who is entitled to receive income from the property in his own right.
2. The requirement of registration of the sale deed is not warranted.
3. Ownership includes both free-hold and lease-hold rights.
4. Ownership includes deemed ownership (discussed later in para 2.12)
5. The person who owns the building need not also be the owner of the land upon which it stands.
6. The assessee must be the owner of the house property during the previous year. It is not material whether he is the owner in the assessment year.
7. If the title of the ownership of the property is under dispute in a court of law, the decision as to who will be the owner chargeable to income-tax under section 22 will be of the Income-tax Department till the court gives its decision to the suit filed in respect of such property.

**(iii)** The property may be used for any purpose, but it should not be used by the owner for the purpose of any business or profession carried on by him, the profit of which is chargeable to tax.

#### **(iv) Property held as stock-in-trade etc.**

Annual value of house property will be charged under the head “Income from house property” in the following cases also –

- a. Where it is held by the assessee as stock-in-trade of a business;
- b. Where the assessee is engaged in the business of letting out of property on rent;

### **Exceptions**

#### **(a) Letting out is supplementary to the main business**

1. Where the property is let out with the object of carrying on the business of the assessee in an efficient manner, then the rental income is taxable as business income, provided letting is not the main business but it is supplementary to the main business.

2. In such a case, the letting out of the property is supplementary to the main business of the assessee and deductions/allowances have to be calculated as relating to profits/gains of business and not relating to house property.

**(b) Letting out of building along with other facilities**

1. Where income is derived from letting out of building along with other facilities like furniture, the income cannot be said to be derived from mere ownership of house property but also because of facilities and services rendered and hence assessable as income from business.
2. Where a commercial property is let out along with machinery e.g. a cotton mill including the building and the two lettings are inseparable, the income will either be assessed as business income or as income from other sources, as the case may be.

**DEEMED OWNERSHIP [SECTION 27]**

As per section 27, the following persons, though not legal owners of a property are deemed to be the owners for the purposes of section 22 to 26.

**(i) Transfer to a spouse [Section 27(i)]** – In case of transfer of house property by an individual to his or her spouse otherwise than for adequate consideration, the transferor is deemed to be the owner of the transferred property.

**Exception** – In case of transfer to spouse in connection with an agreement to live apart, the transferor will not be deemed to be the owner. The transferee will be the owner of the house property.

**(ii) Transfer to a minor child [Section 27(ii)]** – In case of transfer of house property by an individual to his or her minor child otherwise than for adequate consideration, the transferor would be deemed to be owner of the house property transferred.

**Exception** – In case of transfer to a minor married daughter, the transferor is not deemed to be the owner.

**Note** - Where cash is transferred to spouse/minor child and the transferee acquires property out of such cash, then the transferor shall not be treated as deemed owner of the house property. However, clubbing provisions will be attracted.

**(iii) Holder of an impartible estate [Section 27(ii)]** – The impartible estate is a property which is not legally divisible. The holder of an impartible estate shall be deemed to be the individual owner of all properties comprised in the estate. After enactment of the Hindu Succession Act, 1956, all the properties comprised in an Impartible estate by custom is to be assessed in the status of a HUF. However, section 27(ii) will continue to be applicable in relation to impartible estates by grant or covenant,.

**(iv) Member of a co-operative society etc. [Section 27(iii)]** – A member of a cooperative society, company or other association of persons to whom a building or part thereof is allotted or leased under a House Building Scheme of a society/company/association, shall be deemed to be owner of that building or part

thereof allotted to him although the co-operative society/company/ association is the legal owner of that building.

**(v) Person in possession of a property [Section 27(iia)]** – A person who is allowed to take or retain the possession of any building or part thereof in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act shall be the deemed owner of that house property. This would include cases where the –

- (1) possession of property has been handed over to the buyer
- (2) sale consideration has been paid or promised to be paid to the seller by the buyer
- (3) sale deed has not been executed in favour of the buyer, although certain other documents like power of attorney/agreement to sell/will etc. have been executed. In all the above cases, the buyer would be deemed to be the owner of the property although it is not registered in his name.

**(vi) Person having right in a property for a period not less than 12 years [Section 27(iib)]** – A person who acquires any rights in or with respect to any building or part thereof, by virtue of any transaction as is referred to in section 269UA (f) i.e. transfer by way of lease for not less than 12 years, shall be deemed to be the owner of that building or part thereof.

**Exception** – Any rights by way of lease from month to month or for a period not exceeding one year.

## COMPOSITE RENT

### (i) Meaning of composite rent

The owner of a property may sometimes receive rent in respect of building as well as –

1. other assets like say, furniture, plant and machinery.
2. for different services provided in the building, for eg. –
  - (1) Lifts;
  - (2) Security;
  - (3) Power backup;

The amount so received is known as “composite rent”.

### (ii) Tax treatment of composite rent

- (1) Where composite rent includes rent of building and charges for different services (lifts, security etc.), the composite rent is has to be split up in the following manner -
  - a. the sum attributable to use of property is to be assessed under section 22 as income from house property;
  - b. the sum attributable to use of services is to charged to tax under the head “Profits and gains of business or profession” or under the head “Income from other sources”.
- (2) Where composite rent is received from letting out of building and other assets (like furniture) and the two lettings are not separable –

- a. If the letting out of building and other assets are not separable i.e. the other party does not accept letting out of buildings without other assets, then the rent is taxable either as business income or income from other sources;
  - b. This is applicable even if sum receivable for the two lettings is fixed separately.
- (3) Where composite rent is received from letting out of buildings and other assets and the two lettings are separable –
- a. If building is let out along with other assets, but the two lettings are separable i.e. letting out of one is acceptable to the other party without letting out of the other, then income from letting out of building is taxable under “Income from house property”;
  - b. Income from letting out of other assets is taxable as business income or income from other sources;
  - c. This is applicable even if a composite rent is received by the assessee from his tenant for the two lettings.

### INCOME FROM HOUSE PROPERTY SITUATED OUTSIDE INDIA

1. In case of a resident in India (resident and ordinarily resident in case of individuals and HUF), income from property situated outside India is taxable, whether such income is brought into India or not.
2. In case of a non-resident or resident but not ordinarily resident in India, income from a property situated outside India is taxable only if it is received in India.

### WHEN PROPERTY INCOME IS NOT CHARGEABLE TO TAX

1. Income from Farm house Sec.10(1)
2. Property held for Charitable purpose Sec.11
3. Property income of an Education Institution and Hospital Sec.10(23)C
4. Property income of an approved Scientific research association Sec.10(21)
5. One place of an ex-ruler. Sec.10(19)A
6. Property income of a local authority Sec.10(20)
7. Property income of a Trade Union. Sec.10(24)
8. Property income of a Political party Sec.13A

### Computing income from house property

<b>Gross Annual Value</b>	.....
<b>Less: Municipal Taxes</b>	.....
<b>Net Annual Value</b>	.....
<b>Less: Deduction under Sec.24</b>	.....
<b>Standard Deduction</b>	.....
<b>Interest on borrowed capital</b>	.....
	=====
<b>Income from house property</b>	=====

### How to calculate Gross Annual Value

Tax under the head “incomes from house property” is not tax upon rent of a property. It is taxed on inherent capacity of a building to yield income. The standard selected as a measure of the income to be taxed is “annual value”.

- Step I Find out reasonable expected rent of the property.
- Step II Find out rent actually received or receivable after excluding unrealized rent before deducting loss due to vacancy.
- Step III Find out which one is higher - amount computed in Step I and Step II
- Step IV Find out loss because of vacancy
- Step Step III minus Step IV is gross annual value

**Step I - Find Out Reasonable Expected Rent [See. 23(1)(0)]** - Reasonable expected rent is deemed to be the sum for which the property might reasonably be expected to be let out from year to year.

In determining reasonable rent, several factors have to be taken into consideration, such as, location of the property, annual rateable value of the property fixed by municipalities, rents of similar properties in neighbourhood, rent which the property is likely to fetch having regard to demand and supply, cost of construction of the property and nature and kind of a house property. In a majority of cases, however, reasonable expected rent can be determined by taking into consideration the following factors:

- a. municipal valuation of the property; or
- b. fair rent of the property.

The higher of (a) or (b) is taken as reasonable expected rent.

If, however, a property is covered by a Rent Control Act, then the amount so computed cannot exceed the standard rent determinable under the Rent Control Act.

**Municipal valuation** - For collecting municipal taxes, local authorities make a periodical survey of all buildings in their jurisdiction. Such valuation may be taken as a strong evidence representing the earning capacity of a building. It cannot, however, be considered to be a conclusive evidence. Moreover, in some 'big cities (like Delhi, Mumbai, Chennai, Kolkata) municipal authorities determine net rateable value after deducting 10 per cent of the gross rateable value, on account of repairs, and an allowance for service taxes (such as sewerage tax and water tax). The net municipal valuation, therefore, requires an adjustment for determining reasonable expected rent for income tax purposes.

**Fair rent of the property** - Fair rent of the property can be determined on the basis of a rent fetched by a similar property in the same or similar locality.

**Standard rent under the rent control acts** - Standard rent is the maximum rent which a person can legally recover from his tenant under a Rent Control Act. If a property is covered under the Rent Control Act, its reasonable expected rent cannot exceed the standard rent (fixed or determinable) under the Rent Control Act.

**Provision illustrated** - As mentioned earlier, the reasonable expected rent under computation will be computed on the basis of three factors, namely.



- municipal valuation (MV),
- fair rent of the property (FR); and
- standard rent of the property (SR)

The higher of (MV) and (FR), subject to maximum of (SR), is expected rent under Step 1.

The example given below illustrates the aforesaid propositions-

(Rs. in thousand)

	A	B	C	D	E
Municipal Value (MV)	40	40	40	40	40
Fair Rent (FR)	48	48	48	50	55
Standard Rent (SR)	NA	45	35	45	63
Reasonable expected rent under step 1 [MV or FR, whichever is higher, subject to maximum of (SR)]	48	45	35	45	55**

\*\* Reasonable expected rent cannot exceed the amount of standard rent. Reasonable expected rent can however, be lower than standard rent-. In other words, standard rent is the maximum amount of reasonable expected rent. In the case of E, Rs. 55,000 (being higher of municipal valuation and 'fair rent) is the reasonable expected rent. Since this amount is lower than the maximum ceiling (i.e., standard rent'; Rs. 63(000), it is taken as reasonable expected rent.

**Step ii-Find out rent actually received or receivable** - For the purpose of Step II rent received or receivable shall be calculated as follows.

Rent of the Previous year (or that part of the previous year) for which the property is available for letting out	XXXX
Less: Unrealised rent if a few conditions are satisfied	XXXX
Rent recived/ receivable before deducting loss due to vacancy	XXXX

The Following points should be noted –

- Loss due to vacancy shall not be deducted from the computation of rent received/receivable as given above. It shall be deducted under Step IV
- Sometimes a tenant pays a composite rent of property as well as certain benefits provided by the landlored. To determine rent received/receivable, composite rent must be disintegrated and it is only that part of it attributable to the let out of property which would from the basis fro the aforesaid calculations.
- Occupier's (ie., tenant's) share of municipal tax realised from the tenant cannot be added to actual rent as it is the occupier's duty to pay municipal tax.
- If the tenant has undertaken to bear the cost of repairs, the amount spent by the tenant cannot be added to rent received to arrive at the annual value. A non-refundable deposit will be included in rent received or receivable on pro rata basis.
- Commission paid by the assessee-owner of property to a broker for rental income is not deductible.
- Amount spent by an assessee towards stamp duty for drawing up lease deed and registration thereof, would not be deducted from rent received.

7. An assessee had taken a property on sub-lease for a period of 99 years. Since period of lease was not less than 12years, rental income received by assessee shall to be assessed as 'Income from house property' by virtue of provisions of section 27(iiiB), read with section 269UA(f). lease rent paid by the assessee cannot be deducted from lease rental income received by it.
8. Payment to a municipal corporation for regularizing unauthorized construction is not deductible.
9. A refundable deposit cannot be included in rent received or receivable. To find out whether notional interest on refundable deposit can form part of rent received or the receivable, one has to examine the purpose for which refundable deposit/ security is taken from a tenant. Such deposit/security is taken from a tenant generally for any of the following purposes -
  - To ensure that tenant will vacate the property after the expiry of lease period.
  - To ensure proper payment of rent on due dates.
  - To check that the tenant will not misuse the property.
  - To check that tenant will not damage the property, .or will not make any unauthorized alteration.
  - To compensate short payment or non-payment of rent (in such case it is paid in lieu of rent).

Only in the last case, notional interest on refundable deposit/ security may form part of rent received or receivable.

10. Advance rent cannot be rent received/receivable of the year of receipt.

**When unrealised rent shall be excluded [explan. To see. 23(1)j] – Unrealised rent (which the owner could not realise) shall be excluded from rent received/receivable only if the following conditions are satisfied-**

✓ The tenancy is bona fide.
✓ The defaulting tenant has vacated, or steps have been taken to compel him to vacate the property.
✓ The defaulting tenant is not in occupation of any other property of the assessee
✓ The assessee has taken all reasonable steps to institute legal proceedings for the recovery of the unpaid rent or satisfies the Assessing Officer that legal proceedings would be useless.

**Q.1.** Find out the gross annual value in the following cases for the assessment year 2010-2011 (There is no unrealized rent)-

	X(Rs)	Y(Rs.)
Municipal value (per annum) (MV)	61,000	61,000
Fair rent (per annum) (FR)	1, 08,000	30,000
Standard rent under the	60,000	60,000

Rent Control act (per annum) (SR)		
Rate of rent		
- Old tenant (from April 1, 2009 to June 30, 2009) (Per month)	5,000	2,000
- New tenant (from July 1, 2009 to December 31, 2009) (Per month)	9,000	2,500
Period when the property remains unoccupied because suitable tenant was not available	January 1, 2010 to March 31, 2010	January 1, 2010 to March 31, 2010
Actual rent received/receivable (if there is no vacancy)	96,000	28,500
Loss due to vacancy	27,000	7,500

**Solution: Computation of gross annual value**

	X(Rs.)	Y(Rs.)
Step 1-Reasonable expected rent of the property [MV or FR, whichever is higher, but subject to maximum of SR]	60,000	60,000
Step II-Rent received/receivable after deducting unrealized rent but before adjusting loss due to vacancy	96,000	28,500
Step-III Amount computed in Step I or Step II, whichever is higher	96,000	60,000
Step-IV Loss due to vacancy	27,000	7,500
Step-V-Gross annual value is Step III minus Step IV	69,000	52,500

**Q.2.** Find out the gross annual value in respect of the following properties for the assessment year 2010-11-

(Rs. In

thousand)

	X	Y	Z	A	B
Municipal value (MV)	140	180	180	140	231
Fair rent (FR)	145	185	185	145	262
Standard rent (SR)	142	175	175	142	241
Actual rent if property is let out throughout the previous year 2009-10	168	168	168	168	252
Unrealized rent of the previous year 2009-10	14	42	1	70	42
Unrealized rent of the previous year 2008-09	3	4	5	6	7
Period when the property remains vacant (in number of months)	[1/2]	[1]	[1]	[3]	[5]
Loss due to vacancy	7	14	14	42	105

**Solution: Computation of gross annual value**

	X(Rs.)	Y(Rs.)	Z	A	B
Step 1-Reasonable expected rent of the property [MV or FR, whichever is higher, but subject to maximum of SR]	142	175	175	142	241
Step II-Rent received/receivable after deducting unrealized rent of the current previous year but before adjusting loss due to vacancy(unrealized of earlier years is not considered)	154	126	167	98	210
Step-III Amount computed in Step I or Step II, whichever is higher	154	175	175	142	241
Step-IV Loss due to vacancy	7	14	14	42	105
Step-V-Gross annual value is Step III minus Step IV	147	161	161	100	136

**Property taxes (Municipal taxes)**

1. Property taxes are allowable as deduction from the Gross Annual Value subject to the following two conditions:
  - a. It should be borne by the assessee (owner); and
  - b. It should be actually paid during the previous year
2. If property taxes levied by a local authority for a particular previous year are not paid during that year, no deduction shall be allowed in the computation of income from house property for that year.
3. However, if in any subsequent year the arrears are paid, then the amount so paid is allowed as deduction in computation of income from house property for that year.
4. Thus, we find that irrespective of the previous year in which the liability to pay such taxes arise according to the method of accounting regularly employed by the owner, the deduction in respect of such taxes will be allowed only in the year of actual payment.
5. In case of property situated outside India, taxes levied by local authority of the country in which the property is situated is deductible.
6. If municipal tax paid in percentage we will calculate on municipal value.
7. If property situated in foreign country Municipal tax levied by foreign authority are deductible.

**Statutory Deduction/Standard Deduction u/s 24(a):-**

- a) **30%** of net annual value is deductible irrespective of any expenditure incurred by the tax payer.
- b) If net annual value is negative than standard deduction shall be NIL.**

**Note:-**

- (i) Liabilities payable by tenant paid by owner is deductible in rent.
- (ii) Liabilities payable by owner paid by tenant added in rent.
- (iii) Repair & Maintenance & Municipal tax is not apart of rent if bear by tenant.
- (iv) Non-refundable deposit will include in rent received on prorated basis but refundable deposit can not be including in rent received.
- (v) Advance rent is not a part of rent received.

**Q.3.** Find out the income from property chargeable to tax for the assessment year 2010-11 in the following cases-

	<b>X(Rs.)</b>	<b>Y(Rs.)</b>
Municipal value (MV)	1,20,000	1,20,000
Fair rent (FR)	1,30,000	1,30,000
Standard rent under the Rent Control Act (SR)	1,10,000	1,10,000

Actual rent if property is let out throughout the previous year	1,26,000	1,26,000
Unrealized rent of the previous year 2009-10	10,500	Nil
Period when the property remains vacant (in number of month)	(1)	(Nil)
Loss due to vacancy	10,500	Nil
Municipal taxes- Tax of the year 2009-10	18,000	18,000
- Paid by X and Y during 2009-10	17,000	8,000
- Paid by X and Y after March 31,2010	1,000	1,000
- Paid by tenants during 2009-10	-	9,000

**Solution: Computation of income under the head “Income from house property”**

	X(Rs.)	Y(Rs.)
Gross annual value	1,10,000	1,10,000
Step 1-Reasonable expected rent of the property [MV or FR, whichever is higher, but subject to maximum of SR]		
Step II-Rent received/receivable after deducting unrealized rent but before adjusting loss due to vacancy	1,15,500	1,26,000
Step-III Amount computed in Step I or Step II, whichever is higher	1,15,500	1,26,000
Step-IV Loss due to vacancy	10,500	Nil
Step-V-Gross annual value is Step III minus Step IV	1,05,000	1,26,000
Less: Municipal tax paid by X or Y during the previous	17,000	8,000

year 2009-10		
Net annual value	88,000	1,18,000
Less: Standard deduction under section 24(a) [30% of net annual value]	26,400	35,400
Income from house property	61,600	82,600

### **Interest on borrowing capital u/s 24(b)**

i) Interest on pre-construction period/Capital interest:-

- a) Date of borrowing to date of repayment of loan.
- b) Date of borrowing to 31<sup>st</sup> March immediately prior to the date of completion of construction or date of acquisition.

“Pre-construction period mean (a) or (b) whichever is short period.

“Interest will be calculated on this period, and deduction will be available in 5 equal installments continuously from constructed or acquisition year.

ii) **Revenue interest:-** Interest on loan of previous year deduction will be available in previous year either paid or not.

- a) Interest is deductible on accrual basis.
- b) Interest on unpaid interest is not deductible.
- c) Brokerage on unpaid interest is not part of interest.
- d) If interest paid outside India than TDS must be deductible by payer of Interest.
- e) Loan for the purpose of purchases, construction, repair, renew reconstruction of the house property.
- (f) Interest on a fresh loan taken to repay the original loan for the aforesaid purpose is allowable as a deduction.

### **Deduction of interest**

- i) If let out property: - Capital as well as revenue int. is deductible.
- ii) If Partially let out and Partially Self Occupied. :- Capital as well as revenue interest. is deductible.
- iii) If self occupied:-
  - a) If loan taken before the date of 1.4.1999 for the purpose of purchase, construction, repair, renew than maximum allowable deduction Rs.30000/- (Capital+ Revenue)
  - b) If loan taken on or after 1<sup>st</sup> April 1999 for the purpose of purchase or construction and construction should be completed with in three years from the end of financial year in which the loan taken. Than deduction will be maximum Rs.1,50,000/- (Capital+Revenue)
  - (a) If loan is taken on or after 1<sup>st</sup> April 1999 for the purpose of **repair** and **renew** than deduction will be available only Rs.30000/-

### Type of House Property

1. Fully let out property in previous year:- As per above computation.
2. Partly let out and partly self occupied in previous year:- As per above computation.
3. Fully self occupied in previous year:- Only one house assessee can take for purpose of self occupied. It depends on assessee. If more than one house than other house deemed to be as a let out. (Only applicable on Individual & HUF)
4. Fully utilised in Business or Profession:- Not part of house property income. It will be covered in B & P Income Head.
5. If any house which is not completed and not ready for purpose of use in previous year:-  
Than it will not covered under income from House property. If we have received any sum than it will be cover in Income from other sources head.
6. If house is ready for rent but tenant is not available for rent:-  
Than GAV is NIL, Municipal tax will be deductible, statutory deduction NIL, **Interest on loan will be deductible.**
7. If house is vacant due to service on another place:-
  - a) He has to reside at the other place in a building not owned by him.
  - b) This property not actually let out during whole previous year and no other benefit is derived from the above property.
  - (c) GAV will NIL, Municipal tax will be NIL, statutory deduction will be NIL and **Interest on loan will be deductible.**

### Unrelised Rent

Rent is due but not received from tenant in previous year

- a) Unrealized rent was allowed as deduction in the **P/Y 2000-01 or earlier (U/S 25A)**
  - Amount recovered is taxable in the P/Y in which it is recovered.
  - If is taxable even if house is not owned, or deemed owned, by the assessee in the year of recovery.
  - Expenses of recovery are not deductible.
  - Amount recovered Minus (Bad Debts-Bad debts allowed by AO)
- b) Unrealised rent of the P/Y 2001-02 or subsequent year is collected subsequently (25AA)
  - Amount recovered is taxable in the P/Y in which it is recovered.
  - It is taxable even if house is not owned or deemed owned by the assessee in the year of recovery.
  - Expenses of recovery are not deductible.
  - Re-computation of the P/Y (in which unrealized rent related)

### Arrears of Rent Received (U/S 25B)

- Assessee has let out any building or land appurtenant thereto.
- Received any amount by way of arrears of rent from such property, not charge to income tax for any previous year.
- Deemed to be income of the P/Y in which such rent is received.
- Statutory deduction applicable (30%)
- If is taxable even if house is not owned, or deemed owned, by the assessee in the year of recovery.



- Recomputation of the P/Y (in which unrealised rent related)

**Q.4.** X owns a property, it is given on rent (rent being Rs.11,000 per month) to a bank. Municipal value of the property is Rs.1,30,000, fair rent is Rs.1,40,000 and standard rent is Rs.1,34,000. Municipal tax paid by X is as follows-Rs.26,000 on March 3,2009 and Rs.30,000 on May 10,2009. On May 1,2009,rent is increase from Rs.11,000 per month to Rs.14,000 per month with retrospective effect from April 1,2008.Arrears of rent of 2008-09 are paid on May 1,2009.Find out the income chargeable to tax for the assessment years 2009-10 and 2010-11.

**Solution:**

Gross annual value (on the assumption that rent is Rs.11,000 per month for the previous year 2008-09 and Rs.14,000 per month for the previous year 2009-10)	2009-10(Rs.)	2010-11(Rs.)
Municipal value (MV)	1,30,000	1,30,000
Fair rent (FR)	1,40,000	1,40,000
Standard rent (SR)	1,34,000	1,34,000
Step 1-Reasonable expected rent of the property [MV or FR, whichever is higher, but subject to maximum of SR]	1,34,000	1,34,000
Step II-Rent received/receivable after deducting unrealized rent but before adjusting loss due to vacancy	1,32,000	1,68,000
Step-III Amount computed in Step I or Step II, whichever is higher	1,34,000	1,68,000
Step-IV Loss due to vacancy	Nil	Nil
Step-V-Gross annual value is Step III minus Step IV	1,34,000	1,68,000
Less: Municipal tax	26,000	30,000
Net annual value	1,08,000	1,38,000
Less: Standard deduction under section 34(i.e.,30% of net annual value)	32,400	41,400
Income from property	75,600	96,600

Arrears of rent of the previous year 2008-09 paid on May 1, 2009

Gross annual value of previous year 2008-09 if rent is Rs.14, 000 per month	1, 68,000
Less: Gross annual value considered earlier	<u>1,</u>
<u>34,000</u>	
Arrear of rent	34,000
Less: 30% of Rs.34, 000	—
<u>10,200</u>	
Amount taxable	—
<u>23,800</u>	
Income from house property Assessment year 2009-10	75,600
Assessment year 2010-11 (i.e., Rs.96, 600+Rs.23, 800)	1,
20,400	

### TREATMENT OF INCOME FROM CO-OWNED PROPERTY [SECTION 26]

- 1) Where property is owned by two or more persons, whose shares are definite and ascertainable, then the income from such property cannot be taxed as income of an AOP.
- 2) The share income of each such co-owner should be determined in accordance with sections 22 to 25 and included in his individual assessment.
- 3) Where the house property owned by co-owners is self occupied by each of the co owners, the annual value of the property of each co-owner will be Nil and each co-owner shall be entitled to a deduction of Rs.30,000/Rs.1,50,000, as the case may be, under section 24(b) on account of interest on borrowed capital.
- 4) Where the house property owned by co-owners is let out, the income from such property shall be computed as if the property is owned by one owner and thereafter the income so computed shall be apportioned amongst each co-owner as per their specific share.

### TREATMENT OF INCOME FROM PROPERTY OWNED BY A PARTNERSHIP FIRM

- 1) Where an immovable property or properties is included in the assets of a firm, the income from such property should be assessed in the hands of the firm only.
- 2) Hence, the property income cannot be assessed as income of the individual partner in respect of his share in the firm.

## A. **Tax Free Incomes**

The following are 14 important items of income, which are fully exempt from income tax and which a resident individual Indian assessee can use with profit for the purpose of tax planning.

### 1. **Agricultural income**

Under the provisions of Section 10(1) of the Income Tax Act, agricultural income is fully exempt from income tax.

However, for individuals or HUFs when agricultural income is in excess of Rs 5,000, it is aggregated with the total income for the purposes of computing tax on the total income in a manner which results into "no" tax on agricultural income but an increased income tax on the other income.

### 2. **Receipts from Hindu Undivided Family (HUF)**

Any sum received by an individual as a member of a Hindu Undivided Family, where the said sum has been paid out of the income of the family, or, in the case of an impartible estate, where such sum has been paid out of the income of the estate belonging to the family, is completely exempt from income tax in the hands of an individual member of the family under Section 10(2).

### 3. **Share from a partnership firm**

Under the provisions of Section 10(2A), in the case of a person being a partner of a firm which is separately assessed as such, his share in the total income of the firm is completely exempt from income tax since AY 1993-94.

For this purpose, the share of a partner in the total income of a firm separately assessed as such would be an amount which bears to the total income of the firm the same share as the amount of the share in the profits of the firm in accordance with the partnership deed bears to such profits.

### 4. **Allowance for foreign service**

Any allowances or perquisites paid or allowed as such outside India by the Government to a citizen of India, rendering service outside India, are completely exempt from tax under Section 10(7). This provision can be taken advantage of by the citizens of India who are in government service so that they can accumulate tax-free perquisites and allowances received outside India.

### 5. **Commutation of pension**

The entire amount of any payment in commutation of pension by a government servant or any payment in commutation of pension from LIC pension fund is exempt from income tax under Section 10(10A) of IT Act.

However, in respect of private sector employees, only the following amount of commuted pension is exempt, namely:

(a) Where the employee received any gratuity, the commuted value of one-third of the pension which he is normally entitled to receive; and (b) In any other case, the commuted value of half of such pension.

It may be noted here that the monthly pension receivable by a pensioner is liable to full income tax like any other item of salary or income and no standard deduction is now available in respect of pension received by a tax payer.

### 6. **Life insurance receipts**

Under Section 10(10D), any sum received under a Life Insurance Policy (LIP), including the sum allocated by way of bonus on such policy, other than (1) u/s 80DDA or (2) under a Keyman Insurance Policy, or (3) under an insurance policy issued on or after 1.4.2003 in respect of which the premium payable for any of the

years during the term of the policy exceeds 20 per cent of the actual capital sum assured, is fully exempt from tax.

However, all moneys received on death of the insured are fully exempt from tax. Thus, generally moneys received from life insurance policies whether from the Life Insurance Corporation or any other private insurance company would be exempt from income tax.

### **7. Payment received from provident funds**

Under the provisions of Sections 10(11), (12) and (13) any payment from a government or recognised provident fund (PF) or approved superannuation fund, or PPF is exempt from income tax.

### **8. Certain types of interest payment**

There are certain types of interest payments which are fully exempt from income tax u/s 10 (15). These are described below:

**(i)** Income by way of interest, premium on redemption or other payment on such securities, bonds, annuity certificates, savings certificates, other certificates issued by the Central Government and deposits as the Central Government may, by notification in the Official Gazette, specify in this behalf.

**li(a)** In the case of an individual or a Hindu Undivided Family, interest on such capital investment bonds as the Central Government may, by notification in the Official Gazette, specify in this behalf (i.e. 7 Capital Investment Bonds);

**ii(b)** In the case of an individual or a Hindu Undivided Family, interest on such Relief Bonds as the Central Government may, by notification in the Official Gazette, specify in this behalf (i.e., 9 per cent or 8.5 per cent or 8 per cent or 7 per cent Relief Bonds); (iid) Interest on NRI bonds;

**iii(a)** Interest on securities held by the issue department of the Central Bank of Ceylon constituted under the Ceylon Monetary Law Act, 1949;

**iii(b)** Interest payable to any bank incorporated in a country outside India and authorised to perform central banking functions in that country on any deposits made by it, with the approval of the Reserve Bank of India or with any scheduled bank;

**(iv)** Certain interest payable by Government or a local authority on moneys borrowed by it, including hedging charges on currency fluctuation (from the AY 2000-2001), etc.;

**(v)** Interest on Gold Deposit Bonds;

**(vi)** Interest on certain deposits are: Bhopal Gas victims;

**(vii)** Interest on bonds of local authorities as notified,

**(viii)** Interest on 6.5 per cent Savings Bonds [Exempt] issued by the RBI, and

**(ix)** Stipulated new tax free bonds to be notified from time to time.

### **9. Scholarship and awards, etc**

Any kind of scholarship granted to meet the cost of education is exempt from tax under Section 10(16). Similarly, certain awards and rewards, etc. are completely exempt from tax under Section 10(17A), for example, Lakhota Puraskar of Rs 100,000 awarded to the best Rajasthani author, every year under Notification No. 199/28/95-IT (A-I) dated 22-4-1996.

Any daily allowance received by a Member of Parliament or by an MLA or any member of any Committee of Parliament or State legislature is also exempt from tax under Section 10(17).

### **10. Gallantry awards, etc. -- Section 10(18)**

The Finance Act, 1999 has, with effect from AY 2000-2001, provided for complete exemption for the pension and family pension of Gallantry Award Winners like

Paramvir Chakra, Mahavir Chakra, and Vir Chakra and also other Gallantry Award winners notified by the Central Government.

**11. Dividends on shares and units -- Section 10(34) & (35)**

With effect from the Assessment Year 2004-05, the dividend income and income of units of mutual funds received by the assessee completely exempt from income tax.

**12. Long-term capital gains of transfer of securities -- Section 10(38)**

With effect from FY 2004-05, any income arising to a taxpayer on account of sale of long-term capital asset being securities is completely outside the purview of tax liability especially when the transaction has been subjected to Securities Transaction Tax (STT). Thus, if the shares of any company listed in the stock exchange are sold after holding it for a minimum period of one year then there will be no liability to payment of capital gains. This provision would even apply for the old shares which are held by an assessee and are sold after the Finance (No.2) Act, 2004 came into force.

**14. Tax exemption regarding reverse mortgage scheme -- sections 2(47) and 47(x)**

Any transfer of a capital asset in a transaction of reverse mortgage for senior citizens under a scheme made and notified by the Central Government would not be regarded as a transfer and therefore would not attract capital gains tax. The loan amount would also be exempt from tax. These amendments by the Finance Bill, 2008 apply from FY 2007-08 onwards.

### C. **Tax ation of business forms**

#### **ASSESSMENT OF INDIVIDUALS**

The term “individual” as such has nowhere been defined in the Income-tax Act. Section 2(31), however, states that “person” *inter alia*, includes an individual. In the commonly understood sense of the term, an individual means a human being or a single person. The person may be major, minor, married or unmarried, possessing sound or unsound mind. All the same, he is assessable as an ‘individual’ and is liable to pay tax, if the total income earned by him during any previous year exceeds the prescribed limit exempted from tax. If an individual who is liable to pay tax for any year dies before he is assessed to tax, his executor, administrator or legal representative is treated as the individual assessee for purposes of assessment of the income of the deceased person. In the case of an individual who is a minor or a lunatic, the assessment of his income will be made on his guardian or the trustee. However, if the incapacitated person has no trustee or guardian or trustee or guardian is a non-resident and cannot be traced, the assessment can be made directly on the minor or lunatic. The rights and duties of all representative assesseees are the same as those of the persons they are representing.

**Total income of an individual:** The total income of an individual for any previous year, which is liable to tax, is to be computed under the various heads discussed earlier. Further, sections 60 to 65 of the Income-tax Act provide for clubbing of income arising to minor children, spouse, daughter-in-law etc. with the income of the individual under certain circumstances. These provisions must be strictly construed inasmuch as they create an artificial liability to tax.

A married woman, being an individual, is liable to income tax in respect of the total income of any previous year arising to her in her own right, including the income from assets inherited by her or gifted to her by a person other than her husband or her father-in-law or mother-in-law.

**Exemptions and reliefs available to individuals:** The tax exemptions and reliefs available under the Act to individuals in respect of income chargeable to tax fall under the following categories:

1. Income altogether excluded from the total income, and on which in consequence, no income-tax is payable [Section 10].
2. Deductions from gross total income both in respect of income, a part of which is not chargeable to income-tax and payments made by the assessee, a part and the whole of which is deductible from the gross total income.
3. Relief in tax when salary is paid in arrears [Section 89].
4. Special treatment for certain kinds of income [Section 180 and 180A].

#### **Rebate of tax and relief in certain cases**

##### **◆ Share of profit from firm**

Under the provisions of Section 10(2A), in the case of a person being a partner of a firm which is separately assessed as such, his share in the total income of the firm is completely exempt from income tax since AY 1993-94.

For this purpose, the share of a partner in the total income of a firm separately assessed as such would be an amount which bears to the total income of the firm the same share as the amount of the share in the profits of the firm in accordance with the partnership deed bears to such profits.

◆**Income from association of persons or bodies of individuals:** If the assessee is a member of an association of persons or a body of individuals (other than a H.U.F., a company or a firm) income-tax shall not be payable by him in respect of any portion of the amount receivable by him from the association or body on which tax has already been paid by the association or body [Section 86]. For the purposes of this provision in the case of an association of persons which is assessable under section 67A, the members of the AOP whose shares in the income are indeterminate or unknown, will be entitled to receive equal shares in the income of the AOP and the individual share of such member will be determined accordingly.

◆**Relief when salary etc. is paid in arrears or in advance [Section 89]:** It has already been explained in the Chapter relating to salaries that arrears or advances of salaries are assessable in the hands of the recipients in the year in which these are received. Consequently, in a financial year, an employee may become chargeable to tax in respect of salary for more than 12 months. Likewise any payment in the nature of profit in lieu of salary (within the meaning of section 17(3) of the Act) is also chargeable in the year of receipt in addition to the normal salary received by the employee. In consequence, the aggregate salary income may become liable to tax at a rate higher than that at which it would otherwise have been assessed. To obviate such a hardship, the Assessing Officer has been empowered to grant relief in appropriate cases, on the employee making an application, in accordance with Rule 21A of the Income-tax Rules.

In appropriate cases coming under section 192(2A), where the employer is the Government or a public sector undertaking, co-operative society, local authority, university, institution or body, such employer himself is entitled to take into account the relief under section 89(1).

**D. Taxation of non resident Indian (NRI)****Special provisions relating to certain incomes of non-residents - Chapter XII A:**

This Chapter seeks to lay down a concessional method of taxation of certain specified income of non-residents. For this purpose,

A non-resident Indian means a non-resident individual who may either be an Indian citizen or a person of Indian origin.

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

'Foreign exchange asset' means any 'specified asset' which the assessee has acquired, purchased with or subscribed to in convertible foreign exchange. Such 'specified assets' are as follows:

1. shares in an Indian company.
2. debentures issued by an Indian company which is not a private company as defined in the Companies Act, 1956.
3. deposits with a non-private Indian company.
4. any specified securities of Central Government.
5. units of the Unit Trust of India.
6. such other assets as may be notified by the Central Government.

The income derived from such a foreign exchange asset is called investment income. "Investment income" means any income derived (other than dividends referred to in section 115-O) from a foreign exchange asset.

"Long-term capital gains" means income chargeable under the head "Capital Gains" relating to a capital asset, being a foreign exchange asset which is not a short-term capital asset.

**Flat rate for investment income and long-term capital gains [Section 115E]:**

Where the total income of a non-resident Indian consists only of investment income and capital gains arising out of the transfer of long-term foreign exchange assets, tax payable by him shall be the aggregate of :

1. income-tax on investment income at the rate of 20%;
2. income-tax on long-term capital gains at the rate of 10%; and
3. income-tax on his other total income.

**Exemption on capital gains arising from transfer of long-term foreign exchange asset [Section 115F]:**

Where the non-resident Indian transfers the original foreign exchange asset and within a period of six months of such a transfer deposits or invests the whole or part of the net consideration in:

1. any specified asset or
2. any notified savings certificates referred to in section 10(4B) then,

the capital gains arising on such a transfer will be dealt with as follows :

If the cost of the new asset, referred to in (a) or (b) above, is not less than the net consideration in respect of the original asset the whole of such capital gain shall be



exempt. If such cost is less than the net consideration, the exemption will be limited to:

Total capital gain \* Cost of new asset /Net Consideration

**Note:**

1. When the new asset consists of deposits, the cost means the amount of such deposits.
2. Net consideration means the full value of the consideration received or accruing as a result of the transfer as reduced by any expenditure incurred wholly and exclusively in connection with such transfer.
3. Where the new asset is transferred or converted (otherwise than by transfer) into money, within a period of three years from the date of its acquisition, the capital gain, exempted as above, shall be chargeable as long term capital gain of the previous year in which the new asset is transferred or converted.

**Short Term Capital Gains**

1. Referred to in section 111A @ 15% - No slab benefit is available
2. Other short term capital gains taxable at the normal applicable rates non-residents at normal rates applicable to an individual.

**Flat rate of tax on winnings from lotteries, crossword puzzles etc. [Section 115BB]** : Under section 115BB, gross winnings from lotteries, crossword puzzles, races including horse races (other than income from the activity of owning and maintaining race horses), card games and other games of any sort or from gambling or betting of any nature whatsoever shall be chargeable to income-tax at a flat rate of 30% on the gross winnings.

**Tax on non-resident sportsmen or sports associations [Section 115BBA]:** This section is applicable where the total income of an assessee,

- a) being a sportsman (including an athlete), who is not a citizen of India and is a nonresident, Includes any income received or receivable by way of participation in any game or sport or advertisement or contribution of articles in relation to any game or sport in India in newspapers, magazines, journals
- b) being a non-resident sports association or institution, includes any amount guaranteed to be paid or payable to such association or institution in relation to any game or sport played in India.

The income-tax payable shall be the aggregate of -

- I. the amount of income-tax calculated on the income referred to in clause (a) or clause (b) at the rate of 10%;
- II. the amount of income-tax with which the assessee would have been chargeable had the total income of the assessee been reduced by the amount of income in clause (a) and (b).

No deduction in respect of any expenditure or allowance shall be allowed under any provision of this Act in computing the income referred to in clause (a) or clause (b).

**Return need not be filed [Section 115G]:** Where the total assessable income of the non-resident during the previous year consisted only of investment income and

long term capital gains relating to foreign exchange assets and tax on such income has been deducted at source then he need not file a return of income under section 139(1).

**Benefits available even after the assessee becomes a resident [Section 115H]:**

Where a person, who is a non-resident Indian in any previous year, becomes assessable as resident in India in respect of the total income in any subsequent year, he may furnish a declaration along with such a return to the effect that the provisions of this chapter shall continue to apply to him in relation to the investment income derived from

any foreign exchange asset being debentures, deposits, securities of Central Government and such other notified assets. If he does so, then these provisions will continue to apply to him till such assets are transferred or otherwise converted into money.

**Option to the assessee [Section 115-I] :** A non-resident Indian may elect not to be governed by these provisions. For this purpose he has to declare in the return regarding his option not to be governed by these provisions. In such a case the total income and tax payable there on will be computed in accordance with the other provisions of this Act and consequently, the provisions of this chapter will not apply to such nonresident assessees.

**Special concessions in the case of individuals not being citizens of India:**

Although basically the law of income-tax is applicable alike to both citizens and noncitizens of India, and there is no difference in the general principles for computing the total income under the Income-tax Act, however, on a consideration of the peculiar circumstances in which a foreigner might come to or live in India, certain concessions and reliefs are granted to them. These have been discussed in detail in Chapter 3 under the head 'Incomes not includible in the total income' [Section 10(6)].

**Shipping business of non-residents [Section 172]:** For the assessment of freight earned in India by ships belonging to or chartered by a non-resident, a special mode of assessment is prescribed under the Act. Under this section, no vessel owned by a non-resident can leave any port in India, unless the port authorities grant a tax clearance certificate. Such a certificate shall not be granted unless the master of the vessel produces a certificate from the Income-tax Authorities showing that the taxes payable have been paid or satisfactory arrangements for their payment have been made.

Where the non-resident owner has an agent in India from whom tax is recoverable on a regular assessment, the Assessing Officer in such cases, may grant a port clearance certificate, valid for one year on receipt of an application in his behalf. If the Assessing Officer is not satisfied that there is an agent in India who can be assessed on behalf of non-resident, he shall make a separate assessment in respect of the income of each vessel, before it leaves the port.

In such cases, 7½% of the amount paid or payable in or out of India on account of carriage of passengers or goods to the owner or charterer, is deemed to be his

income accruing in India in respect of the carriage. The income of the non-residents from shipping business must be computed under section 44B.

It is the responsibility of the master of the ship to prepare and furnish to the Assessing Officer return of the full amounts paid or payable to the owner or the charterer, on account of the carriage of goods or passengers. On receipt of such a return the Assessing Officer assesses the income and determines the amount of tax payable thereon, at the rates applicable to a company which has not made prescribed arrangement for the declaration and payment of dividends within India. This sum is payable by the master of the ship.

The time limit for completing such assessments is 9 months from the end of the financial year in which the return under section 172(3) is furnished. However, in respect of returns filed on or before 1.4.2007, assessments are required to be completed on or before 31.12.2008.

After the close of the previous year, it is permissible for a non-resident person on whom tax has been charged on an adhoc basis in respect of the income of a vessel to apply along with a return of his income that he may be assessed on the basis of the business income that actually arose to him in the previous year. On completion of the regular assessment the tax paid towards the adhoc assessment shall be adjusted against the amount due from the assessee and the excess or deficiency if any, shall be refunded to or recovered from the non-resident.

**Recovery of tax in respect of the income of a non-resident [Section 173]:** In the case of the non-resident the tax on the income which is deemed under section (9)(l)(i) to accrue or arise in India and is taxable as such may be recovered - (i) by deduction of tax at source; or (ii) by an assessment on the non-resident directly or (iii) by an assessment on the non-resident's agent in his representative capacity. Any arrears of such tax may also be recovered from any of the assets which may at any time come within India. But the arrears cannot be recovered by filing a suit in the foreign country where the non-resident principal resides since the Courts of one country have no authority to enforce the revenue laws of another.

Generally the proceedings for the recovery of tax cannot be commenced after the expiry of one year from the last day of the financial year in which the demand is made. But section 231 specifically provides that this one year period of limitation does not apply to recovery of tax under this section from the non-residents' assets in India. This section applies only where the income is covered by section (9)(1)(i); it cannot be made to apply for the recovery of taxes in respect of the income which is not deemed to accrue in India.

## Succession

The Succession Act came into operation on 30th September 1925 and it seeks to consolidate all Indian Laws relating to succession. It has no retrospective operation and is applicable to intestate and testamentary succession. .

A person is deemed to have died intestate in respect of the properties of which he has not made will which is capable of taking effect or he has made a Will, but the Will is not capable of taking effect. For example, the person has bequeathed his own property for an illegal purpose or if the subject of the bequest is not existing. Intestacy is of two kinds, total or partial. The property of an intestate devolves upon the wife or husband or' upon those who are related by blood or marriage of the deceased. The distribution of the property takes place as per personal law applicable to the deceased.

The law of succession in India falls within the realm of personal law. Because of this, we have so many different succession laws, each purporting to reflect the diverse and differing aspirations, customs and mores of the community to which the statute in question applies.

We have the Hindu Succession Act, the Parsi Succession Act, the Indian Succession act (which applies to Christians for the purposes with which we are now concerned), and even a Jaina Succession Act (which has of course now fallen into disuse, since Buddhists, Jains, and Sikhs are all now governed the Hindu Succession Act). As far as Muslims are concerned, the law of succession falls in to two broad streams, the Shia law of Succession and the Hanafi law of succession. Both these laws of succession form part of the common law of India and are recognized as having the force of law by virtue of the Shariat Laws Application) Act.

The Hindu Succession Act is a striking departure from the pre-existing ancient Hindu law as had been codified by Manu. It provides a very just and equitable set of rules which cover the issues to a Hindu male or a Hindu female who has died intestate, that is to say, without leaving behind a will. There are of course certain points where the pre-existing Hindu law has been codified without abrogation.

The Indian Succession Act is largely a reflection of the British law as was in vogue at the time.

### The Hindu Succession Law

The basic rules of succession as set out in the Hindu Succession act: The Act applies to Hindus (and this includes Buddhists, Jains and Sikhs as well). It includes also cults and sub-sects such as Arya Samaj, Ramakrishna Mission and the like. The Act deals with succession to a Hindu male separately and succession to Hindu females separately.

The coparcenary property of a Hindu male who dies after the commencement of the act without leaving behind any female heirs (or male heirs who claim through certain

female relatives) will devolve upon the remaining male coparceners equally. This is called Survivorship. It is an exception to the general rule succession.

The female heirs whose presence would result in survivorship not taking place are the widow, the mother, the daughter, the daughter of a predeceased son, the widow of a predeceased son, the daughter of a predeceased son of a predeceased son and the widow of a predeceased son of a predeceased son. The existence of certain specified male heirs who claim through such female heirs would also result in the non application of the rule of survivorship.

The female heirs who have been listed above are known as 'Class 1 female heirs'. There are certain male heirs who also fall into this category known as 'Class 1'. They are the son, the son of a predeceased son, the son of a predeceased daughter, and the son of a predeceased son of a predeceased son.

Clubbed together, all these heirs are known as 'Class 1 heirs'.

If one or more Class 1 heirs survive a Hindu male, such heir or heirs would succeed to the property to the exclusion of all other relatives.

### **Some interesting facts about the law of succession to Hindus.**

The Hindu law recognizes the right to succession of a child, which is en ventre, which is, not as yet born. Such a child succeeds to the estate of a person who died during the period of its gestation, upon its being born alive.

The second interesting rule is that when two people die simultaneously, the younger is, by an artificial rule, presumed to die subsequent to the elder.

The third interesting rule is that a murderer (or an abettor of a murder) will not succeed to the estate of the person who was murdered. Thus, spouses who plan to do away with each other as frequently as they seem to in the movies, would stand to gain little in reality, due to application of this rule. This brings us to the end of our very brief outline of the law of succession insofar as it pertains to Hindus.

### **Another Explanation of Hindu Succession Law**

#### **The Hindu Succession Act, 1956**

Succession in the Hindus is governed by the Hindu Succession Act, 1956, which bases its rule of succession on the basic principle of propinquity, i.e., preference to heirs on the basis of proximity of relationship. Earlier females were excluded; however this rule of exclusion of females has been done away with.

**The law of Intestate Succession is concerned with matters as to who are the Heirs, what are the rules of preference among the various relations, in what manner is the property distributed in case there is more than one heir and so on.**

**Intestate Succession** - A person who dies without making a Will is known as intestate. A heir is a person entitled to inherit property after the death of the intestate. The Hindu Succession Act applies to the whole of India except the f Jammu and

Kashmir. The Act applies to all Hindus, Buddhists, Jainas, Sikhs and to any other person who is not a Muslim, Christian, Parsi or Jew.

### **Special Marriage Act**

If a Hindu marries a non-Hindu under the Special Marriage Act, he shall be severed from the undivided family. However, if two persons who are Hindus get married under the Special Marriage Act, no such severance takes place.

If a Hindu marries a non-Hindu under the Special Marriage Act, succession to the property of such person whose marriage is solemnized under this Act and to the property of the issue of such marriage shall be regulated by the provisions of the Indian Succession Act. However, if two persons who are Hindus get married under the Special Marriage Act, the above provision does not apply and they are governed by the Hindu Succession Act.

### **Joint Family Property-**

Under the Mitakshara School, the joint family property devolves by survivorship. When a male Hindu dies after the commencement of this Act, having at the time of his death an interest in a Mitakshara coparcenary property, his interest in the property shall devolve by survivorship upon the surviving members of the coparcenary and not in accordance with this Act. However, if the Mitakshara dies leaving behind a female relative or male relative claiming through Class I, this undivided interest will not devolve survivorship but by succession as provided under the Act.

### **General rules of succession - Male Hindus**

The property of the male Hindu dying intestate shall devolve in the following manner:

Firstly upon all the heirs, being the relatives specified in Class i.

Secondly, if there is no heir of Class I, then upon heirs being the relatives specified in Class ii

Thirdly, if there is no heir of any of the classes, then upon the agnates of the deceased (one person is said to be agnate of another if the two are related by blood or adoption wholly through males)

Lastly, if there is no agnate, then upon the cognates of the deceased. (One person is said to cognate of another if the two are related by blood or adoption but not wholly through male)

Class 1<sup>st</sup> heirs:

- Son
- Daughter
- Widow

- Mother
- Son of a predeceased son
- Daughter of predeceased son
- Widow of predeceased son
- Son of a predeceased daughter
- Daughter of predeceased daughter
- Son of predeceased son of predeceased son
- Daughter of predeceased son of a predeceased son
- Widow' of predeceased son of a predeceased son

CLASS II<sup>nd</sup> heirs:

- Father
- Son's daughter's son, (2) son's daughter's daughter, (3) brother, (4) sister
- Daughter's son's son, (2) daughter's son's daughter, (3) daughter' daughter's son, (4) Daughter's daughter.
- Brother's son, (2) sister's son, (3) brother's daughter, (4) sister's daughter.
- Father's father; father's mother.
- Father's widow; brother's widow.
- Father's brother; father's sister.
- Mother's father; mother's mother.
- Mother's brother; mother's sister.

Class I heirs take simultaneously to the exclusion of all other heirs. Heirs in the first entry of Class II shall be preferred to those in the second entry; those in the second entry shall be preferred to those in the third entry; and so on in succession.

### General rules of succession - Female Hindus

The property of a female Hindu dying intestate shall devolve:

- Upon the sons and daughters (including the children of any predeceased son or daughter) and the husband;
- Upon the heirs of the husband;
- Upon the mother and father;
- Upon the heirs of the father; and;
- Upon the heirs of the mother

However, if any property is inherited by a female Hindu from her father or mother, it shall devolve in the absence of any son or daughter of the deceased (including the children of any predeceased son or daughter) not upon the heirs referred to above but upon the heirs of the father; and any property inherited by a female Hindu from her Husband or from her father-in-law shall devolve, in the absence of any son or daughter of the deceased (including the children of any predeceased son or daughter) not upon their referred to above, but upon the heirs of the husband.

### The Muslim Succession Law

The Muslim law of succession is a codification of the four sources of Islamic law, which are (1) The Holy Koran itself, (2) The Sunna - that is, the practice of the Prophet, (3) The Ijma - that is, the consensus of the learned men of the community on what should be the decision on a particular point, and (4) The Qiya - that is, an analogical deduction of what is right and just in accordance with the good principles laid down by God.

The Muslim law recognizes two types of heirs, the first being Sharers, and the second being Residuaries.

A relative who is a Sharer will take a specified portion of the deceased's estate irrespective of anything else.

A relative who is a Residuary will take whatever is left over, once the Sharers have taken their specified shares.

The Holy Book in Sura 4 Verse 7 says, "From what is left by parents and close relatives, there is a share for men and a share for women, whether the property left behind be small or large and this share shall be fixed."

The Sharers are 12 in number and are as follows:

(1) Husband, (2) Wife, (3) Daughter, (4) Daughter of a son (or son's son or son's son's son and so on) (5) Father, (6) Paternal Grandfather, (7) Mother, (8) Grandmother on the male line, (9) Full Sister (10) Consanguine sister, (11) Uterine sister, and (12) Uterine brother.

Any attempt to set out the exact share of each such Sharer and its fluctuation depends on various factors. The share taken by each sharer will fluctuate in certain circumstances:

A wife takes a one-fourth share in a case where the couple is without lineal descendants, a one eighth share otherwise. A husband (in the case of succession to the wife's estate) takes a half share in a case where the couple is without lineal descendants, and a one-fourth share otherwise.

A sole daughter takes a half share. Where the deceased has left behind more than one daughter, all daughters jointly take two-thirds. However, these two rules apply only in cases where the deceased has left behind no sons.

If the deceased had left behind son(s) and daughter(s), then, the daughters cease to be shares and become Residuaries instead, with the residue being so distributed as to ensure that each son gets double of what each daughter gets.

Lineal descendants (such as sons) exclude brothers and sisters, and therefore, the share of brothers and sisters (whether full, consanguine or uterine) will become nil in the presence of such descendants.



Residuaries are those who are entitled to the estate, if any, left after the sharers have received their respective shares. Of course, this is only a broad rule and there are several just and equitable exceptions to this rule. For instance, the existence of certain relations who fall under the category of residuaries has the effect of totally excluding certain other relations who fall under the category of Sharers.

### Example

If a Muslim gentleman dies, leaving behind his widow, a sister and a son, one would expect that the widow and the sister, being Sharers, would first take their specified share (one eighth and one half respectively) and that the son would take the balance (A son is a residuary, as we shall presently see). However, this does not happen. What happens instead is that though the sister is sharer, the existence of a son, totally excludes her, leaving her with no share at all. The effect of this is that the widow takes an eighth and the son takes the residue, that is to say, seven eighths.

The list of Residuaries is quite lengthy. At the head of the list are the sons. Then, come their sons, and further lineal descendants in the pure male line, all of whom are Residuaries. Next in the list are the fathers, their fathers, and further lineal ascendants in the pure male line in that orders. The next two entries in the list of Residuaries are full brothers and consanguine brothers. Then come those brothers' sons, and the sons of those sons and further lineal descendants. Then come the full and consanguine brothers of the deceased's father (that is to say, paternal uncles). Then come the sons of those paternal uncles, the sons of the sons of those paternal uncles and so on. Then, come paternal grand uncles who are related either fully or consanguinely.

Now, the order of priority given in this list is very important. The reason for this is that a residuary higher up in the order, excludes all others below him in the order.

Please also note that when there are certain corresponding female heirs for certain of the Residuaries (such as daughter-son, granddaughter-grandson and so on), then those female heirs succeed as Residuaries (giving up their share as sharers) and succeeding to the residue of the estate along with the listed Residuary, but only receiving half of what the male receives.

### Example

For instance, a Muslim gentleman dies leaving behind his widow, a son, a daughter and a brother. From the table of Sharers, one would assume that his wife would take one-eighth, his daughter would take one half and that the residue would go to the son and brother. This does not happen. The widow takes the one eighth that she is entitled to. The daughter, in the presence of the son, ceases to be a sharer, and becomes a residuary, entitled to half of the extent of the residue that the son succeeds to. The son and daughter, being higher up in the table of Residuaries than the brother, exclude the gentleman's brother altogether. Thus, of the residue of seven-eighths, the son and daughter succeed in a 2:1 ratio, taking thereby, 7/12 and 7/24 respectively.

Failing any Sharers or Residuaries, the next level of relations who would succeed to the estate of a deceased Muslim male or female, are a class of persons known as

Distant Kindred. We do not propose to go into this at all, since this would only serve to lengthen what is already a long column.

This is the law of succession to Muslim men and women who die intestate. Please note that there is no concept of ancestral property or rights by birth in the case of Muslim succession, as we had seen in the case of Hindu succession. The rights that a Muslim's heirs acquire upon his death are fixed and determined with certainty on that date and do not fluctuate.

### **Indian Succession Act**

The Indian Succession Act (which applies to Christians for the purposes with which we are now concerned), is largely a reflection of the British law as was in vogue at the time.

### **Intestate succession**

Intestate means when person dies without making a Will, which is capable of taking effect. The property devolves upon the wife or husband or upon the relatives of the deceased in the following manner:

If 'A' has left no Will - He has died intestate in respect of the whole of his property.

'A' has left a Will, whereby he has appointed 'B' his executor; but the will contains no other provisions -

'A' has died intestate in respect of the distribution of his property.

'A' has bequeathed his whole property for an illegal purpose - 'A' has died intestate in respect of the distribution of his property.

When a Will is partially incapable of being operative:

'A' has bequeathed Rs. 1000 to 'B' and Rs. 1000 to the eldest son of 'C', and has made no other bequest; and has died leaving the sum of Rs. 2000 and no other property. 'C' died before 'A' without having ever had a son. 'A' has died intestate in respect of the distribution of Rs.1000.

### **Application**

Hindus, Muslims, Buddhist, Sikh, Jaina - This part does not apply to the property of any Hindu, Mohammedan, Buddhist, Sikh or Jaina. Muhammadans are governed by Mohammeda law of Inheritance and the Hindus, Buddhists, Sikhs and Jainas by the Hindu Succession Act, 1956.

Parsis - The following provisions do not apply to Parsis:

Special Marriage Act - Notwithstanding anything contained in the Indian Succession Act with respect to its application to members of certain communities, succession to the property of any person whose marriage is solemnized under the Special Marriage Act and to the property of the issue of such marriage shall be regulated by the provisions of the Indian Succession Act.

However, if two persons who are Hindus get married under the Special Marriage Act, the above provision does not apply and they are governed by the Hindu Succession Act.

### **Distribution of property - Widow / Widower**

The property of an intestate devolves upon the wife or husband, or upon those who are of the kindred of the deceased, in the order and according to the rules given below. However, remember that a widow is not entitled to the provision hereby made for her if, by a valid contract made before her marriage. She has been excluded from her distributive share of her husband's estate.

**Where intestate has left widow and lineal descendants ( a person who is in direct line to an ancestor, such as child, grandchild, great-grandchild and on forever), or widow and kindred only, or widow and no kindred, the following rules are applicable:**

#### **Where the intestate has a widow-**

If he has also left any lineal descendants, one third of his property shall belong to his widow, and the remaining two-thirds shall go to his lineal descendants, according to the rules hereinafter contained;

If he left no lineal descendant, but has left persons who are of kindred to him, one-half of his property shall belong to his widow, and the other half shall go to those who are of kindred to him, in the order and according to the rules hereinafter contained;

If he has left none who are of kindred to him, the whole of his property shall belong to his widow.

Lineal descendants mean descendants born in lawful wedlock only.

#### **Where intestate has left no widow, and where he has left no kindred-**

Where the intestate has left no widow, his property shall go to his lineal descendants or to those who are of kindred to him, not being lineal descendants, according to the rules hereinafter contained; and if he has left none who are of kindred to him, it shall go to the Government.

### **Rights of a Widower.**

A husband surviving his wife has the same rights in respect of her property, if she dies intestate as a widow has in respect of her husband's property, if he dies intestate.

### **Rules of distribution - Children, Grandchildren Etc.**

The rules for the distribution of the intestate's property (after deducting the widow's share, if he has left a widow) amongst his lineal descendants (descendants born in lawful wedlock only) are as follows:

### **Where intestate has left child or children only**

Where the intestate has left surviving him a child or children, but no more remote lineal descendant through a deceased child, the property shall belong to his surviving child, if there is only one, or shall be equally divided among all his surviving children.

Child or children - The word 'child' does not include an illegitimate child, but must be one born out of lawful wedlock. The words 'any child' mean and include 'children' as well.

### **Where intestate has left no child, but grandchild or grandchildren**

Where the intestate has not left surviving him any child, but has left a grandchild or grandchildren and no more remote descendant through a deceased grandchild, the property shall belong to his surviving grandchild if there is only one, or shall be equally divided among all his surviving grandchildren.

### **Where intestate has left only great-grandchildren or remoter lineal descendants**

In like manner, the property shall go to the surviving lineal descendants who are nearest in degree to the intestate, where they are all in the degree of great-grandchildren to him, or are all in a more remote degree.

### **Where intestate leaves lineal descendants not all in same degree of kindred to him, and those through whom the more remote are descended are dead.**

If the intestate has left lineal descendants who do not all stand in the same degree of kindred to him, and the persons through whom the more remote are descended from him are dead, the property shall be divided into such a number of equal shares as may correspond with the number of the lineal descendants of the intestate who either stood in the nearest degree of kindred to him at his decease, or, having been of the like degree of kindred to him, died before him, leaving lineal descendants who survived him.

One of such shares shall be allotted to each of the lineal descendants who stood in the nearest degree of kindred to the intestate at his decease; and one of such shares shall be allotted in respect of each of such deceased lineal descendants; and the share allotted in respect of each of such deceased lineal descendants shall belong to his surviving child or children or more remote lineal descendants, as the case may be; such surviving child or children or more remote lineal descendants always taking the share which his or their parent or parents would have been entitled to, respectively if such parent or parents had survived the intestate.

**Where an intestate has left no lineal descendants, the rules for the distribution of his property (after deducting the widow's share, if he has left a widow) are as follows-**

If the intestate's father is living, he shall succeed to the property.

If the intestate's father is dead, but the intestate's mother is living, and if any brother or sister and the child or children of any brother or sister who may have died in the intestate's lifetime are also living, then the mother and each living brother or sister, shall be entitled to the property in equal shares, such children (if more than one) taking in equal shares - only the shares which their respective parents would have taken if living at the intestate's death.

If the intestate's father is dead, but the intestate's mother is living, and the brothers and sisters are all dead, but all or any of them have left children who survived the intestate, the mother and the child or children of each deceased brother or sister shall be entitled to the property in equal shares, such children (if more than one) taking in equal shares - only the shares which their respective parents would have taken if living at the intestate's death.

If the intestate's father is dead, but the intestate's mother is living, and there is neither brother, nor sister, nor child of any brother or sister of the intestate, the property shall belong to the mother.

Where the intestate has left neither lineal descendants, nor father, nor mother, the property shall be divided equally between his brothers and sisters and the child or children of such of them as may have died before him, such children (if more than one) taking in equal shares - only the shares which their respective parents would have taken if living at the intestate's death.

Where the intestate has left neither lineal descendants, nor parent, nor brother, nor sister, his property shall be divided equally among those of his relatives who are in the nearest degree of kindred to him.

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