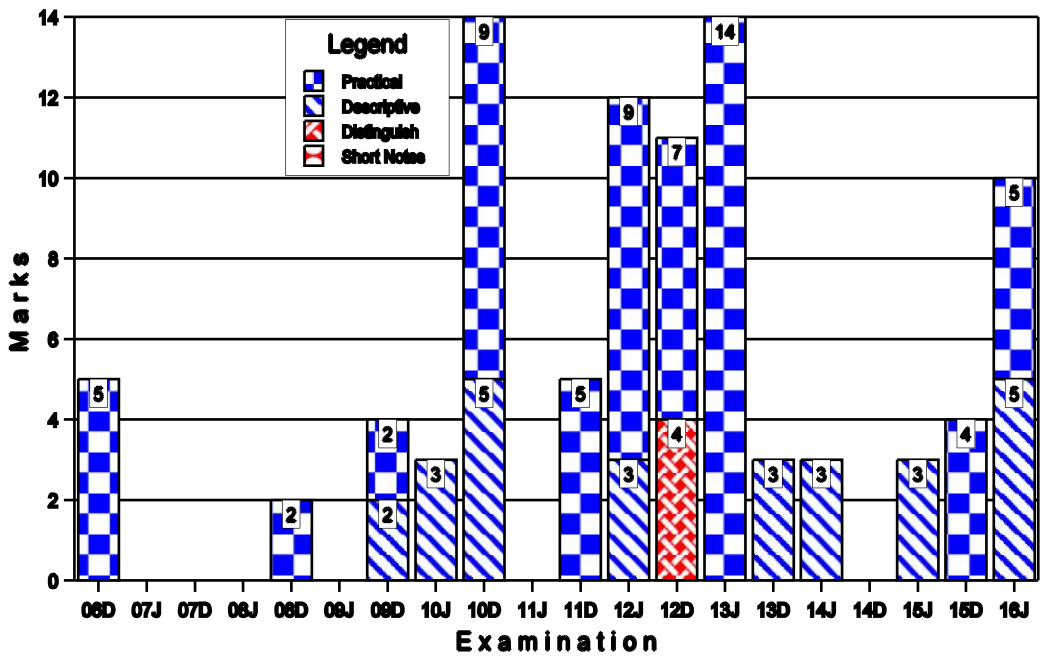
1 Basics of Income Tax Law and Residential Status

This Chapter Includes : Basics of Taxation; Direct Taxes & Indirect Taxes; Sources and Authority of Taxes in India; Seventh Schedule of the Constitution; Rates of Income Tax; Residential Status of : Individuals, HUF, Firm, AOP, LLP, Company, Others; Incidence of Tax; Income from Interest; Royalty; Fees for Technical Services.

Marks of Short Notes, Distinguish Between, Descriptive & Practical Questions



DISTINGUISH BETWEEN

2012 - Dec [2] (a) State the difference between residential status of a company and that of others. (2 marks)

(b) Explain the difference between 'Total Income' and 'Gross Total Income'. (2 marks)

Answer:

(a) Rules to determine residential status of Companies [Sec. 6(3)]

A person being a company shall be said to be resident in India in any previous year if:

1. It is an Indian Company, or
2. Its place of effective management at any time in that year, is in India.

Note:

1. A company cannot be "ordinarily" or "not ordinarily resident".
2. Place of Effective management to mean the place where key management and commercial decisions that are necessary for the conduct of the entity's business as a whole, are, in substance made.

Answer:

(b)

GTI Sec. 2(45)	Total Income Sec. 5
1. Sum total of all 5 heads [Salary, House Property, Business Profession, Capital Gain, Other Sources]	1. GTI (-)ded^{n} u/s chap. VI A
2. GTI is not rounded off	2. Rounded off u/s 288A
3. No tax is calculated on GTI	3. Tax is calculated on NI

DESCRIPTIVE QUESTIONS

2009 - Dec [1] {C} (d) (iv) A company which has its head office in India operated in Pakistan declared dividend subject to remittance from Pakistan. During the previous year relevant to the assessment year, the remittance could not be recovered from Pakistan. What is the tax liability in the hands of shareholder? Discuss. (2 marks)

Answer:

As head office of Company is in India. So register of members will also be maintained in India. Income from dividend will be considered as income deemed to accrue on arise in India and hence taxable.

As dividend from domestic company is exempt U/s 10(34). Hence this dividend will be exempt from tax.

2010 - June [8] (b) State the Elements/Sources of Income Tax Law. (3 marks)

Answer:

The elements/sources of Income Tax Law are:

(i) The Income Tax Act, 1961.
(ii) Finance Act.- Annual
(iii) The Income Tax Rules, 1962.
(iv) Circulars/notifications from CBDT.
(v) Judicial Decisions.

2010 - Dec [5] (b) One of the exceptions to the rule that the income of the previous year shall be assessed in the subsequent assessment year is the shipping business of non-resident. Discuss briefly the assessment aspect of such income from shipping business. (5 marks)

Answer:

Section 172-Shipping Business of Non Resident:

Where a ship, belonging to or chartered by a non-resident, carries passengers, livestock, mail or goods shipped at a port in India, the ship is allowed to leave the port only when the tax has been paid or satisfactory arrangement has been made for payment thereof, 7.5% of the freight paid or payable to the owner or the charterer or to any person on his behalf, whether in India or outside India on account of such carriage is deemed to be his income which is charged to tax in the same year in which it is earned.[Section- 44B]

Section 172 will not apply if time-charterer carries his own goods. When the time charterers carried their own cargo, they served their own interests and this kind of self service was not contemplated for the purpose of assessment, and Section 172 would not be attracted - Lima Leitao & Co. Ltd. v. Union of India.

2012 - June [3] (a) State how the residential status of a company is determined under the Income-tax Act, 1961. (3 marks)

Answer:

A company is a resident in India in any previous year in the following cases [Sec 6(3)]

(i) It is an Indian company as defined under section 2(26) of the Act;

(ii) during the relevant previous year, control and management of its affairs is situated wholly in India.

A company is said to be Non- resident in India in any previous year in the following cases-

(i) it is not an Indian company; and

(ii) during the relevant previous year, control and management of its affairs is situated wholly or partially outside India.

2013 - Dec [2] (a) What are the circumstances in which previous year and assessment year will be the same? (3 marks)

Answer:

Previous year and the assessment year will be same in the following cases:

1. Shipping business of non-resident (Section 172)
2. Persons leaving India (Section 174)
3. AOP or BOI or Artificial juridical person formed for a particular event or purpose (Section 174A)
4. Persons likely to transfer property to avoid tax (Section 175)
5. Discontinued Business (Section176)

2014 - June [5] (c) Explain the term "substantial interest" defined in Section 2(32) and its application in at least two situations. (3 marks)

Answer:

Substantial Interest

(a) For company- If individual along with relatives hold not less than 20% equity shares beneficially.

(b) For others- If individual along with relatives is entitled to atleast 20% of income.

Application

An individual is chargeable to tax in respect of any salary, commission, fees or any other remuneration received by the spouse from a concern in which the individual has substantial interest.

(i) But that portion of salary etc., of spouse which is due to application of technical or professional knowledge or experience shall not be clubbed.

(ii) If husband and wife both have substantial interest in the concern and
- both are receiving remuneration because of interest in the concern
- then the remuneration of both shall be clubbed in the hands of that spouse whose total income is greater, before clubbing such income.

2015 - June [4] (d) Mr. Bharat, an engineering graduate, born and brought up in India, got employment in USA in August, 2015. By what date he should leave India, in order to become a non-resident? By that, what tax advantage he will get? (3 marks)

Answer:

Planning for residential status:

A person who leaves India for employment if remains for less than 182 days during the financial year of leaving, he will be a non-resident.

Mr. Bharat must leave India before 29th September, 2015 to be non-resident for the financial year 2015-16.

When he plans his departure in such a way that he becomes non-resident, his income accruing or arising outside India will not be subjected to tax in India. His income accruing or arising in India alone will be liable to tax in India.

2016 - June [2] (a) State the situations in which the income of the assessee can be assessed in the previous year itself, instead of in the assessment year. (5 marks)

PRACTICAL QUESTIONS

2006 - Dec [4] (c) 'Y', a foreign citizen (not being a person of Indian origin), comes to India, for first time in the last thirty years on March 20, 2015. On September 1, 2015, he leaves India for Nepal on a business trip. He comes back on February 26, 2016. Determine his residential status under the Income- tax Act, 1961 for the assessment year 2016-2017. (5 marks)

Answer:

During the previous year Mr. Y is in India for 188 days (1st April 2015 to 1st Sept. 2015 and 26th Feb. 16 to 31st March 16). Hence, he satisfies the basic condition of 182 days or more during the previous year. So he is Resident in India.

Further to decide whether Mr. Y is Resident and Ordinarily Resident or Resident but not Ordinarily Resident. Additional conditions should be satisfied.

Additional conditions u/s 6(6)-

i. He is resident in India for any two years out of 10 years just preceding previous year.
ii. He must be in India for 730 days or more during 7 years just preceding previous year.

    As Mr. Y does not satisfy additional conditions. Hence, Mr. Y is resident but not ordinarily resident.

2008 - Dec [5] (a) Kamlesh was working as a crew member on an Indian ship plying in foreign waters. During the year ended 31.03.2016, the ship did not touch the Indian coast, except for 180 days. State the residential status for the assessment year 2016-17 and taxability of his salary. (2 marks)

Answer:

Any individual, who is a citizen of India, leaving India in any year for the purpose of employment or as a member of crew of an Indian ship, is considered as resident in India only when his stay in India during that previous year is 182 days or more.

But in the given situation Mr. Kamlesh stays in India only for 180 days during the previous year. Hence, he is non resident in India.

Income received from salary is considered as income received and accrue outside India. Hence, it is not taxable in India.

2009 - Dec [6] (d) X got an employment in Singapore during the previous year 2015-16. He left for Singapore on August 9, 2015. He is an Indian Citizen. Determine the residential status for the Assessment Year 2016-17. (2 marks)

Answer:

Any individual, who is a citizen of India, leaving India in any year for the purpose of employment or as a member of crew of an Indian ship, is considered as resident in India only when his stay in India during that previous year is 182 days or more.

But in the given situation Mr. X stays in India only for 131 days during the previous year. Hence, he is non resident in India.

2010 - Dec [4] (a) Following are the details of income of Mr. Subramani for the financial year 2015-2016:

Income from property in Sri Lanka remitted by the tenant to the assessee in India through SBI	₹ 2,10,000
Profit from business in India	₹ 1,00,000
Loss from business in Sri Lanka (whose control and management of business wholly remained in India)	₹ 80,000
Dividend from shares in foreign companies received outside India	₹ 60,000
Interest on deposits in Indian companies	₹ 1,20,000

Determine the total income in terms of the Income-tax Act, 1961 in the following situations:

(i) Resident and ordinarily resident of India;
(ii) Resident but not ordinarily resident of India;
(iii) Non-resident. (9 marks)

Answer:

Computation of Taxable Income under various Residential Status

Particulars	Resident and Ordinarily Resident	Resident but not Ordinarily Resident	Non Resident
Income from property in Sri Lanka	2,10,000	2,10,000	2,10,000
Profit from business in India	1,00,000	1,00,000	1,00,000
Loss from business in Sri Lanka(Control & Management wholly in India)	(80,000)	(80,000)	Not Taxable
Dividend from shares in foreign co. received outside India	60,000	Not Taxable	Not Taxable
Interest on deposits in Indian Companies	1,20,000	1,20,000	1,20,000
Total Income	**4,10,000**	**3,50,000**	**4,30,000**

2011 - Dec [4] (a) BIRLA Ltd., a cement manufacturing company, entered into an agreement with a supplier for purchase of additional cement plant. One of the conditions in the agreement was that if the supplier failed to supply the machinery within the stipulated time, the company would be compensated at 5% of the price of the respective portion of the machinery without proof of actual loss. The company received ₹ 8.50 lakhs from the supplier by way of liquidated damages on account of his failure to supply the machinery within the stipulated time. What is the nature of liquidated damages received by BIRLA Ltd. from the supplier of plant for failure to supply machinery to the company within the stipulated time-a capital receipt or a revenue receipt ? (5 marks)

Answer:

As per the decision of *Apex Court in CIT. v. Saurashtra Cement Ltd. (2010)*, it was decided that receipts for procuring the capital asset are of capital nature. The Apex Court affirmed the decision of the Gujarat High Court holding that the damages were directly and intimately linked with the procurement of a capital asset i.e., the cement plant, which leads to delay incoming into existence of the profit-making unit. It was not a receipt in the course of profit making. Therefore, the amount received by the assessee towards compensation for sterilization of the profit earning source, not in the ordinary course of business, is a capital receipt in the hands of the assessee. Therefore in this case, the liquidated damages of ₹ 8.50 lakhs received by Birla Ltd., from the supplier of plant for failure to supply machinery to the company within the stipulated time is a capital receipt.

2012 - June [2] (a) Following details are furnished by Mr. Appaji for the year ended 31.03.2016:

		₹
(i)	Profit on sale of shares in Indian company, sold in India but proceeds received in France	30,000
(ii)	Dividend from a Korean company received in France	50,000
(iii)	Rent from property in Sri Lanka deposited in Sri Lanka but later remitted to India through approved banking channel-Gross	1,00,000
(iv)	Dividend from ABC (P) Ltd.	20,000
(v)	Income from nursery in Gujarat	40,000

Compute the total income of Mr. Appaji if he is

(i) Resident and ordinarily resident;
(ii) Resident but not ordinarily resident;
(iii) Non-resident. (9 marks)

Answer:

Computation of total income of Mr. Appaji for the assessment year 2016-17

	ROR	**RNOR**	**NR**
Profit on sale of shares in Indian company, sold in India but proceeds received in France	30,000	30,000	30,000

Dividend from a Korean company received in France	50,000	Nil	Nil
Rent from property in Sri Lanka deposited in Sri Lanka but later remitted to India through approved banking channel	70,000*	Nil	Nil
Dividend from ABC (P) Ltd.	Exempt	Exempt	Exempt
Income from nursery in Gujarat	Agri income	Agri income	Agri income
Total Income	**1,50,000**	**30,000**	**30,000**

Note: * Taking ₹ 1,00,000 (Gross) as NAV, standard deduction u/s 24(a) is applicable.

2012 - Dec [2] (d) Mr. A furnishes the following particulars of his income during the previous year 2015-16:

(i) Income from agriculture in Bangladesh, received thereof ₹ 2,00,000 and sub-sequently remitted to India.

(ii) Gift of ₹ 52,000 received in foreign currency from a relative in India.

(iii) Arrears of salary ₹ 70,000 received in India from a former employer in England.

(iv) Income from property received abroad but later on remitted to India ₹ 3,20,000. (₹ 1 lakh used in Bahrain for educational expenses and ₹ 2 lakhs remitted in India later).

(v) Profit from business outside India managed from India ₹ 90,000 and received outside India.

Find out the gross total income of Mr. A for the assessment year 2016-17 if A is (i) Resident and ordinarily resident (ii) Resident but not ordinarily resident and (iii) Non-resident. (7 marks)

Answer:

Particulars	**Res. & ord. resident (ROR)**	**Res. but not ord. resident (NOR)**	**Non resident (NR)**

Income from agriculture in Bangladesh, received there but later on remitted to India	2,00,000	-	-
Gift received from a relative in India [exempt u/s 56(2)(VII)]	-	-	-
Arrears of salary received in India from a former employer in England	70,000	70,000	70,000
Income from property received outside India but later on remitted to India	3,20,000	-	-
Profit from business outside India, managed from India.	90,000	90,000	-
Gross Total Income	**6,80,000**	**1,60,000**	**70,000**

2013 - June [2] (a) Mr. Jeff, a citizen of USA came to India for 80 days, 90 days, 110 days and 130 days in the financial years 2012-13, 2013-14, 2014-15 and 2015-16 respectively. Determine his residential status for the Assessment Year 2016-17. (3 marks)

(b) Compute the total income of Mr. Taylor, UK citizen and a non-resident for the Assessment Year 2016-17 from the following details furnished by him.

		₹
(i)	Income from business carried out in Mumbai (60% received in USA)	5,00,000
(ii)	Capital gain from sale of shares of Zenith Private Limited, an Indian company. Sale proceeds were received in UK	3,50,000
(iii)	Rent from a house property in New Jersey collected there, but later remitted to India through normal banking channel	12,00,000
(iv)	Dividend received from MNO Limited, an Indian Company	2,50,000

(v) Royalty received in UK from PQR Limited, an Indian company for use of trade mark for its business operation in India	6,00,000
(vi) Interest on loan received in UK from S&T Limited, an Indian company. The loan was used by S&T Limited for its business carried on in Dubai.	3,00,000

(7 marks)

Answer:

(a) As per Section 6 an individual is a resident in India in any previous year, if he fulfils any of the following two conditions:

(i) He is present in India in that previous year for 182 days or more.

(ii) He was present in India within 4 years preceding that previous year for 365 days or more and for 60 days or more in that previous year.

In this case Jeff was physically present in India for less than 182 days in previous year 2015-16.

AY 2016 –17 – FY 2015-16 = 130 days

4 Previous Years

FY 2011 – 12	NIL
FY 2012 – 13	80
FY 2013 – 14	90
FY 2014 – 15	110
	280 days

Hence, non-resident. He was present in India for 130 days (more than 60 days in the previous year and he was physically present in India for 280 days (80+90+110) i.e. less than 365 days in 4 previous years preceding the previous year 2015 –16. Hence, he does not fulfill the second condition and Jeff is non-resident in India for the Assessment Year 2016–17.

Answer:

(b)

Particulars	₹
Income from business carried out in India is income from business connection in India and deemed to accrue or arise in	

India.	5,00,000
Capital gain is deemed to accrue or arise in India as shares of Indian company are capital assets situated in India. Place of receipt of consideration is immaterial.	3,50,000
Rent from house property situated in New Jersey being an income from source outside India is not taxable. Subsequent remittance of rent to India does not alter the position.	
Dividend from Indian company though an income deemed to accrue or arise In India is exempted under section 10(34)	---
Royalty received from the Indian company is deemed to accrue or arise in India, as the patent was used by the Indian company for its business in India.	---
Interest on loan received from the Indian company is not deemed to accrue or arise in India as the amount of loan was used by the Indian company for its business carried out outside India	6,00,000
Total Income	---
	14,50,000

2013 - June [3] (b) Mr. Rajput, aged 82 years gives you the following information for the previous year 2015-16:

		₹
(i)	Interest on fixed deposits with banks	4,80,000
(ii)	Long-term capital gain on sale of land	50,000
(iii)	Short-term capital gain on sale of shares (securities transactions tax paid)	20,000

Compute tax payable by Mr. Rajput for the Assessment year 2016-17 in cases (i) he is resident; (ii) he is non-resident. (4 marks)

Answer:

As per the proviso to Section 112(1)(a) if the following conditions are satisfied :

(i) The taxpayer is a resident individual or a resident HUF. He or it may be ordinarily resident or not ordinarily resident.

(ii) Taxable income - Long-term Capital Gain is less than the amount of basic exemption limit

The following shall be deducted from long-term capital gain :
Exemption limit – (Net Income or taxable income including Long-term Capital Gain – Long-term Capital Gain)

(i) As Mr. Rajput is a resident, the relief u/s 112 is available

	₹
Basic Exemption Limit	5,00,000
Taxable income including Long-term Capital Gain	5,30,000
Long-term Capital Gain	50,000
Relief u/s 112	20,000
Computation of tax payable :	₹
Tax on income other than capital gain ₹ 4,80,000	Nil
Tax on long-term capital gain on sale of land i.e., ₹ 50,000 – 20,000 i.e., ₹30,000 @ 20%.	6,000
Tax on short-term capital gain on sale of shares @ 15% as per Section 111A as STT is paid.	3,000
Tax	9,000
EC & SHEC @ 3% (2% EC, 1% SHEC)	270
Total Tax	9,270

(ii) As Mr. Rajput is a non-resident

Computation of tax payable :	₹
Tax on income other than capital gain ₹ 4,80,000	23,000
Tax on long-term capital gain on sale of land i.e., ₹ 50,000 @ 20%.	10,000
Tax on short-term capital gain on sale of shares @ 15% as per Section 111A as STT is paid.	3,000
Tax	36,000
EC & SHEC @ 3% (2% EC, 1+ SHEC)	1,080
Total Tax	37,080

2015 - Dec [1] {C} Answer the following questions with brief reasons/workings:

(c) Mr. David, a citizen of Spain came to India for the first time in previous year 2011-12 and stayed for 100 days in that year. During the previous years 2012-13, 2013-14, 2014-15 and 2015-16 he stayed in India for 120 days, 110 days, 80 days and 90 days respectively. What is the residential status of Mr. David for the assessment year 2016-17?

(2 marks)

(f) X. Limited is an Indian company. However, it carries on business in USA. All the shareholders are residents of USA. The Board Meetings and Annual General Meetings are held outside India. What is the residential status of X. Limited? (2 marks)

Answer:

(c) As per Section 6 an individual is a resident in India in any previous year if he fulfills any of the following two conditions:

(i) He is present in India in that previous year for 182 days or more.

(ii) He was present in India within 4 year preceding that previous year for 365 days or more and for 60 days or more in that previous year.

In case of Mr. David, he was physically present in India for less than 182 days in previous year - 2015-16 but, he is physically present in India for 410 days in 4 year preceding that previous year and he also present for more than 60 days (i.e. 90 days) in previous year. Hence, Mr. David is resident in India in A.Y. 2016-17.

(f) As per section 6(3), a company is said to be resident in India in any previous year if (i) it is an Indian Company, or (ii) in case of other company whose control and management of the affairs of the company is wholly in India.

X Limited is an Indian Company. Therefore, X Limited is a resident in India even if the business is carried on outside India and the meeting of the board and shareholders are held outside India.

2016 - June [4] (a) Following are the transactions related to Mr. Kiran Kumar, a resident but not ordinarily resident in India during the previous year 2015-16. Compute Gross Total Income of Mr. Kiran Kumar for the assessment year 2016-17.

Particulars	₹
Income from agriculture in Sri Lanka (received in Sri Lanka and subsequently remitted to India)	4,00,000
Arrears of salary received in India from a former employer in USA	2,50,000
Rent from house property located outside India and received outside India (₹ 2,00,000 is used in Bahrain for the educational expenses of his son studying there and the balance ₹ 30,00,000 subsequently remitted of India)	5,00,000
Income from business in Japan which is managed and controlled from India (₹ 90,000 received in India and balance ₹ 3,10,000 received outside India)	4,00,000

(5 marks)

Table Showing Marks of Compulsory Questions

Year	11 D	12 J	12 D	13 J	13 D	14 J	14 D	15 J	15 D	16 J
Practical									4	
Total									4	