

Department of Commerce (CA)

CORE PAPER-XII-DIRECT TAX

**SEMESTER:V
B.COM(CA)**

SUB CODE:18BCA53C

UNIT3: Income from house property-profit and gains of business or profession-meaning-of business or profession-computation o profits and gains of business or profesion

REFERENCE BOOK:

- INCOME TAX LAW AND PRACTICE- GAUR AND NARANG
- DIRECT TAXES-B.B.LAL
- INCOME TAX LAW AND PRACTICE-DINKAR PAGARE
- INCOME TAX LAW AND PRACTICE -MALHOTRA

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1.3:INCOME FROM HOUSE PROPERTY.

According to Section 22 of the income tax act, "The annual value of property consisting of any buildings or lands appurtenant thereto of which the assessee is the owner,

other than such portions of such property as he may occupy for the purposes of any business or profession carried on by him, the profits of which are chargeable to incometax, shall be chargeable to income tax under the head Income from House Property".

ANNUAL VALUE.

The measure of charging income-tax under this head is the annual value of the property, i.e., the inherent capacity of a building to yield income. The expression 'annual value' has been defined in Section 23(1) of the Income-tax Act as:

- a) the sum for which the property might reasonably be expected to let from year to year; or
- b) where the property or any part of the property is let and the actual rent received or receivable by the owner in respect thereof is in excess of the sum referred to in clause (a), the amount so received or receivable; or
- c) where the property or any part of the property is let and was vacant during the whole or any part of the previous year and owing to such vacancy the actual rent received or receivable by the owner in respect thereof is less than the sum referred

Computation of Annual Value/Net Annual Value(NAV)

Net annual value shall be computed in the following manner:

Step1. Determine the Gross Annual Value(GAV)

Step2. Deduct municipal tax actually paid by the owner during the previous year from the Gross Annual Value.

For the purpose of computation of net annual value, properties can be classified into three categories:

A. Properties let out throughout the year.

B. Properties occupied by the owner for residential purposes or properties not selfoccupied owing to employment at any other place.

C. Partly let out and partly self-occupied property

(a) Tax is charged on income from the buildings or lands appurtenant thereto:

The buildings include residential buildings, buildings let out for business or profession or auditoriums for entertainment programmes. The location of the building is immaterial. It may be situated in India or abroad.

(b) Tax is charged on income from lands appurtenant to buildings:

Where the land is not appurtenant to a building the income from land can be charged as business income or “income from other sources”, as the case may be. The lands

appurtenant to buildings include approach roads to and from public streets, courtyards, motor garage, compound, play-ground and kitchen garden. In case of non-residential buildings, car-parking spaces, drying grounds or play-grounds shall be the lands appurtenant to buildings.

(c) Tax is charged from the owner of the buildings and land appurtenant thereto:

Where the recipient of the income from house property is not the owner of the building, the income is not chargeable under this head but under the head ‘Income from Business or Other Sources’. For example, the income to a lessee from sub-letting a house is not chargeable under the head ‘Income from House Property’. The owners may be of several types like:

- a) Real owner
- b) Legal owner
- c) Mortgagor in case of mortgaged property
- d) Lessee in case of leasehold property

Deemed owners: Sometimes there will be deemed owners as per the rule of income tax, like:

- i) Property transferred to spouse without adequate consideration- transferor will be the deemed owner
- ii) Self-acquired property converted into common pool of HUF- transferor will be the deemed owner
- iii) Impartible estate of HUF, the holder is its deemed owner.
- iv) Property acquired under power of attorney, its holder is the deemed owner.

(d) Utilised by the assessee for his own business or profession purpose

The annual value of such property or the portion thereof as is utilised by the assessee for the purposes of his own business, profession or vocation, the profits of which are assessable to tax, is not taxable under Section 22. The assessee is also not allowed to claim any deduction in respect of notional rent while computing income from any such business, profession or vocation.

Problem: 1

Mr. Harish owns two houses. The particulars of the two houses for the previous year are given below:

Particulars	House 1	House 2
Date of completion of the house	31 st March 2011	31 st December 2012
Use of house	Self occupied	Let out
Municipal value	30,000	60,000

Fair rent	35,000	90,000
Rent received -		1,20,000
Standard rent	25,000	65,000
Municipal taxes paid	4,000	8,000
Interest on loan for construction of house	30,000	40,000

Compute income from house property for the assessment year

Solution: 1

Computation of income from house property

a) Self – occupied house:

Annual value Nil

Less – Interest 30,000

Loss (a) (-) 30,000

b) Let out:

i. Municipal value 60,000

ii. Fair rent 90,000

iii. Standard rent 65,000 (a) Expected rent (i) or (ii), whichever is greater but not more than (iii) 65,000

(b) Actual rent 1,20,000

G. A.V. (a) or (b), whichever is greater 1,20,000

Less: municipal tax paid 8,000

Annual value 1,12,000

Less: 30% of A.V 33,600

Interest 40,000 73,600

Income from let out (b) 38,400.

Income from house property

Income from let out house = 38,400

Less: Loss from self-occupied house = 30,000

Income from house property = 8,400.



Income from Salary

Particulars	Amount
Basic Salary	—
Add:	—
1. Fees, Commission and Bonus	—
2. Allowances	—
3. Perquisites	—
4. Retirement Benefits	—
5. Fees, Commission and Bonus	—
Gross Salary	—
Less: Deductions from Salary	—
1. Entertainment Allowance u/s 16	—
2. Professional Tax u/s 16	—
Net Salary	—



Income from Salary

❖ Deduction/Exemption

What is the difference between Exemption and deduction?

- ✓ If an income is exempt from tax, then it is not included in the computation of income. However, the deduction is given from income chargeable to tax. Exempt income will never exceed the amount of income. However, the deduct may be less than or equal to or more than the amount of income.
- ✓ **Exemption** : Section 10 deals with exemptions
- ✓ **Deduction**: Section 80 C to 80 U deals with deduction



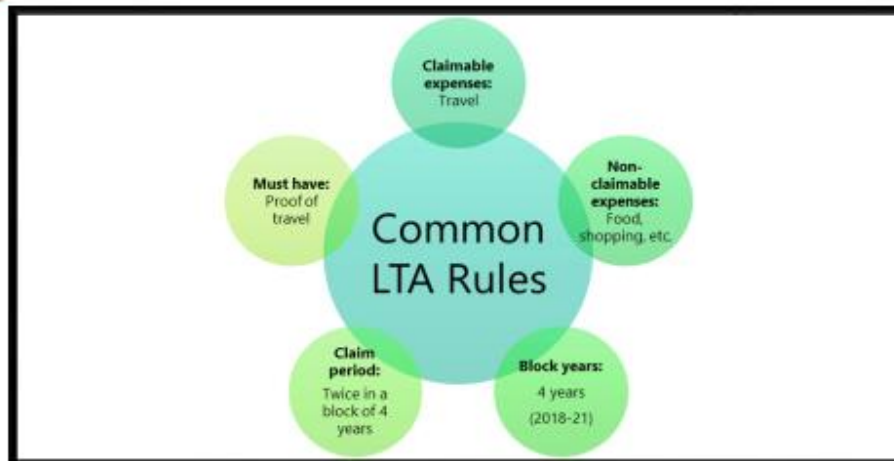
Deduction U/s (16)

There are basically two deduction

- 1.) Entertainment Allowance [Section 16(ii)] **-(Government Employees)**
- 2.) Professional Tax [Section 16(iii)] **-(KIPL- 2,350/-)**



Section 10(5)-Leave Travel Allowance



INCOME FROM BUSINESS OR PROFESSION

The meaning of the expression 'Business, has been defined in Section 2(13) of the Income-tax Act. According to this definition, business includes any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture.

According to the generally accepted principles, the meaning of the term 'profession' involves the concept of an occupation requiring either intellectual skill or manual skill controlled and directed by the intellectual skill of the operator.

Income chargeable to the head 'business or profession'.

The scope of income chargeable under the head 'Profits and Gains from business or Profession' is covered by Section 28 of the Act which lays down that the following items of

income must be charged to tax under this head:

- 1) **Income from business or profession:** The profits and gains of any business or profession which was carried on by the assessee at any time during the previous year.
- 2) **Compensations:**
 - a) Received on termination of a managing agency of Indian company.
 - b) Received on termination of a managing agency of foreign company
 - c) Received on termination of any agency or on modification of terms of agency,
 - d) Received from government or a corporation on taking over of management of property or business.
- 3) **Income from Trade associations:** Any income derived by a trade or professional or other similar association from the specific services performed by it for its members.
- 4) **Export Incentives:**
 - Profits on sale of a license granted under the Imports
 - Cash assistance (by whatever name called) received or receivable by any person against exports under any scheme of the Government of India;
 - Any duty of customs or excise re-paid or re-payable as drawback to any person against exports.
- 5) **The value of any benefit or perquisite**, whether convertible into money or not, which arises from the carrying on of a business or the exercise of a profession.
- 6) **Any interest, salary, bonus, commission or remuneration**, by whatever name called, due to or received by a partner of a firm from such firm.

7) Any sum, whether received or receivable in cash or kind, under an agreement for –
 (a) Not carrying out any activity in relation to any business or
 (b) not sharing any know-how, patent, copyright, trade mark, license, franchise or any other business or commercial right of similar nature or information or technique likely to assist in the manufacture or processing of goods or provision of services:

8) **keyman Insurance Policy:** Any sum received under a keyman Insurance Policy including the sum allocated by way of bonus on such policy.

9) any sum, whether received or receivable, in **cash or kind, on account of any capital asset** (other than land or goodwill or financial instrument) being demolished, destroyed, discarded or transferred, if the whole of the expenditure on such capital asset has been allowed as a deduction under section 35AD.

Computation of income from Business or Profession

Format for Computation of Business or Profession Income :

Computation of Income from Business

Net Profit as per Profit & Loss Account	
<i>Add</i> : Expenses disallowed/Inadmissible Expenses [i.e. items already debited in P & L A/c but not eligible for deduction]	-----
<i>Less</i> : Incomes Credited in P & L A/c to be treated separately under different heads of income	(-----)
<i>Less</i> : Expenses (not debited to P & L A/c) allowed as per Provisions	(-----)
Income from business	-----

Computation of Income from Profession

Receipts relating to Profession (on Cash Basis)	-----
<i>Less</i> : Payment relating to profession (both cash and accrual basis)	(-----)
Income from Profession	-----

Deductions allowable u/s: 30 to 36

Rent, Rates, Taxes, Repairs and Insurance for Buildings (Section 30)

2) **Repairs and Insurance of Machinery, Plant and Furniture** (Section 31)

3) Depreciation (Section 32)

Depreciation is the diminution in the value of an asset due to normal wear and tear or due to obsolescence. In order to allow depreciation the following conditions are to be fulfilled;

i. There must be an asset.

a) Tangible- building, machinery, plant.etc

b) Intangible- patent, copyright, trademark etc

ii. Such asset should be owned, wholly or partly, by the assessee

iii. Such asset should be used for purposes of Business or Profession.

iv. It should be used during the relevant Previous Years.

Depreciation will be charged on the 'Written Down Value'(WDV) of the 'Block of assets'.

Block of Assets:It means a group of assets falling within a class of assets

Written down value of block of asset:

Calculation of WDV



Written Down Value of the block of assets at the beginning of the current Previous Year.
Add: Actual cost of assets falling within that block, acquired during the Previous Year.
Less: Moneys Payable and scrap value if any, in respect of asset sold/discarded/ demolished/destroyed during the Previous Year
Written Down Value

Rate of depreciation for block of assets

Number	Nature of Asset	Rate of depreciation
Block 1	Residential building other than hotels and boarding houses	5%
Block 2	Building- Office, factory, godowns or buildings which are not used for residential purpose	10%
Block 3	Buildings temporary erection such as wooden structures	100%
Block 4	Any furniture/ fitting including electrical fittings	10%

Block 5	Any plant & machinery and motor cars	15%
Block 6	Ships, vessels, speed boatsetc	20%
Block 7	Buses, lorries and taxis used in the business of running them on hire.	30%
Block 8	Aero planes	40%
Block 9	Containers made of glass or plastic used as refills and plant and machinery.	50%
Block 10	Computers including software	60%
Block 11	Energy saving device	80%
Block 12	Air pollution control equipment; water pollution control equipment; solid water control equipment; recycling and resource recovery systems etc	100%
Block 13	Intangible assets- Know-how, patents, copyrights, trademarks, Licences, Franchises etc	25%

Rates of Depreciation:

a) First year of Acquisition.

a) If put to use for more than 180 days- full rate of depreciation

b) If put to use for less than 180 days- half rate of depreciation.

b) Subsequent years- full rate of depreciation.

c) Additional depreciation of 20% of actual cost for new plant and machinery if installed after 31.03.2005, if put to use less than 180 days, then the additional depreciation will be 10%. **Expenditure on Scientific Research** (Section 35)

The term “scientific research” means any activity for the extension of knowledge in the fields of natural or applied sciences including agriculture, animal husbandry or fisheries.

Particulars	Deduction	
Revenue Expenditure related to the business Incurred for own business	– Current year	100%
– Prior Period	100% upto 3 years prior to commencement	
Any sum paid to approved Scientific Research Association or University or College or Institution	For undertaking Scientific research	175% of amount paid
Any sum paid for scientific research, to a company, registered in India, having an object to carry out scientific research and development activities	For undertaking Scientific research	125% of amount paid

Any sum paid to an approved University, College or other Institution	For research in Social Science or Statistical research	125% of amount paid
Capital expenditure incurred for own Business (excluding cost of land)	related to Current year	100% reduction
Prior Period	100% upto 3 year prior to commencement	
Any sum paid to National Laboratory or University or IIT or a specified person	For undertaking a program approved by the prescribed Authority	200% of amount paid
In house research and development of Bio technology in the business of manufacture or production of any article or thing, not being an article or thing specified in list of Eleventh Schedule	Bio-technology or in housereseach	200% of expense incurred allowed upto 31.3.2017

Other deductions

- Insurance Premium
- Bonus
- Interest on Borrowings
- Discount on zero coupon bond
- Contributions to Recognised Provident Fund, Approved Superannuation Fund
- Contribution towards pension scheme
- Approved Gratuity Fund
- Deposit of the Employee's contribution by the Employer in relevant funds or or before date
- Bad Debts

- Expenditure on Family Planning
- Securities Transaction Tax
- Commodities Transaction Tax

Expenses Disallowed (Section 40)

The following amounts shall not be deducted in computing the income chargeable under the head "profits and gains of business or profession:

- i. Interest, royalty, fees for technical services payable outside India
- ii. TDS not deducted on certain payments:
- iii. Rate or Tax Paid on Profits:
- iv. Wealth Tax [Section 40a(ia)]:
- v. Amount paid by way royalty, licence fee, service fee, privilege fee, service charge by State Government undertaking to State Government.
- vi. Salaries [Section 40a(iii)]: Any payment which is chargeable under the head “salaries” if it is payable –
 - a) outside India; or
 - b) to a non-resident
- vii. Payment to Provident Funds etc: Any payment to a Provident Fund or other fund established for the benefit of employees of the assessee would be disallowed in cases where the assessee (employer) has not made effective arrangements to secure deduction of tax at source from any payment made from the fund which are chargeable to tax under the head ‘salaries’ in the hands of the employees.
- viii. Payment of tax on non-monetary perquisites [Section 40a(v)]:
- ix. Payment to Partners by a firm (Discussed under the chapter Assessment of firms).
- x. Payment by AOPs / BOIs (Discussed under the chapter assessment of AOP/BOI).

Problem: 1

From the following P&L. A/c of a merchant for the year ended 31st March, 2019 ascertain his taxable profit from business and house property:

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Profit & Loss Account

Office salary 4,800 Gross Profit 1,35,532
General expenses 2,550 Commission 1,205
Bad Debts written – off 2,100 Discount 751
Reserve for Bad Debts 3,000 Sundry Receipts 202
Fire Insurance Premium 450 Rent of Building 52,640
Advertisement 2,500 Capital gain 3,000
Interest on Capital 1,000
Interest on Bank Loan 1,550
Donations 3,875
Depreciation 1,200
Net profit 1,70,305
1,93,330 1,93,330

The amount of depreciation available is 1,000

Solution: 1

Taxable Profit from Business (For the assessment year 2016 - 17)

Net Profit as per Profit & Loss Account 1,70,305

Less: Items not taxable under the head of Business

Rent of building 52,640

Capital gain 3,000 55,640

1,14,665

Add: Items not allowed:

Reserve for Bad Debts 3,000

Interest on Capital 1,000

Donations 3,875

Excess Depreciation not allowed 200 8,075

Taxable Profits from Business 1,22,740

Income from **House Property:**

Rent Received (A. V.) 52,640

Less: 30% of A. V. 15,792 **36,488**

Note: Donations are eligible for deduction under section 80G.

Problem: 2

Mr. Ram purchased an old car on 10th July for 60,000. The car is used for business as well as for personal purposes of the assessee. Compute the amount of depreciation for the previous year. The rate of depreciation from A. Y. 14 15%.

Solution:

Assessment year 1

Cost of car 60,000 Less: Depreciation @ 15% 9,000

Less: 1/3 for personal use 3,000 6,000

W. D. V. 54,000

Assessment year 2

W. D. V. 54,000

Less: Depreciation @ 15% 8,100

Less: 1/3 for personal use 2,700 5,400

W. D. V. 48,600

Assessment year 3

W. D. V. 48,600

Less: Depreciation @ 15% 7,290

Less: 1/3 for personal use 2,430 4,860

43,740

Depreciation for the previous year would be 4,860

Note: when the ratio of the use of the car for business and private purposes is not known, usually 1/3 is taken as for personal use

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