Auditing Course Material

Part 37 of 61 (Chapters 3601-3700)

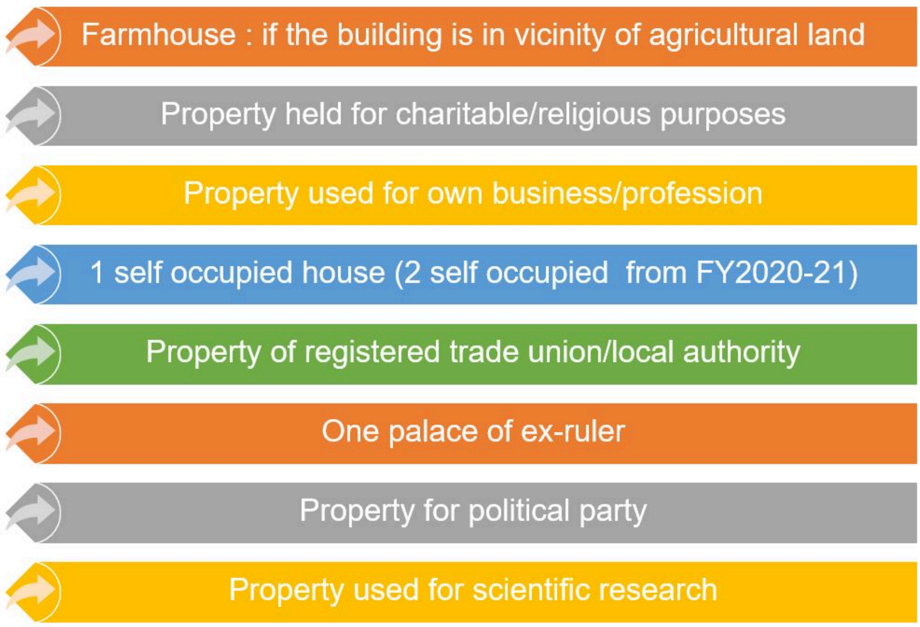
3. Basic Terms

In some cases, the owner obtains rent of other assets (like furniture) or he charges for different services provided in the building (for instance, charges for lift, security, air conditioning, etc.), apart from obtaining the rent of the building. The amount, so recovered, is known as *composite rent*.

If the owner of a house property gets a composite rent for the property as well as for services rendered to the tenants, composite rent is to be split up and the sum which is attributable to the use of property is to be assessed under Section 22 as income from house property.

The amount which relates to rendition of the services (such as electricity supply, provisions of lifts, supply of water, watch and ward facilities, etc.) is charged to tax under the head ‘Profits and gains of business or profession’ or under the head ‘Income from other sources’, as the case may be.

4. Property Incomes exempt from Tax



Some incomes from house property are exempt from tax. They are neither taxable nor included in the total income of the assessee.

Such Incomes are as follows:
1) Income from a farmhouse
2) Annual value of one palace in the occupation of an ex-ruler
3) Property income of a local authority
4) Property income of an approved scientific research association
5) Property income of an educational institution and hospital
6) Property income of a registered trade union
7) Income from property held for charitable purposes
8) Property income of a political party
9) Income from property used for own business or profession
10) One self-occupied property (two self-occupied properties w.e.f. AY 2020-21)

5. Basis of computing ‘Income from let out House Property’

Income from a let out house property is determined as under:

Gross Annual Value	XXX
Less: Municipal Taxes	(XXX)
Net Annual Value	XXX
Less: Deduction under Section 24 Standard Deduction (Sec. 24(a)) Interest on borrowed capital (Sec. 24(b))	 (XX) (XX)
Income from House Property	XXX

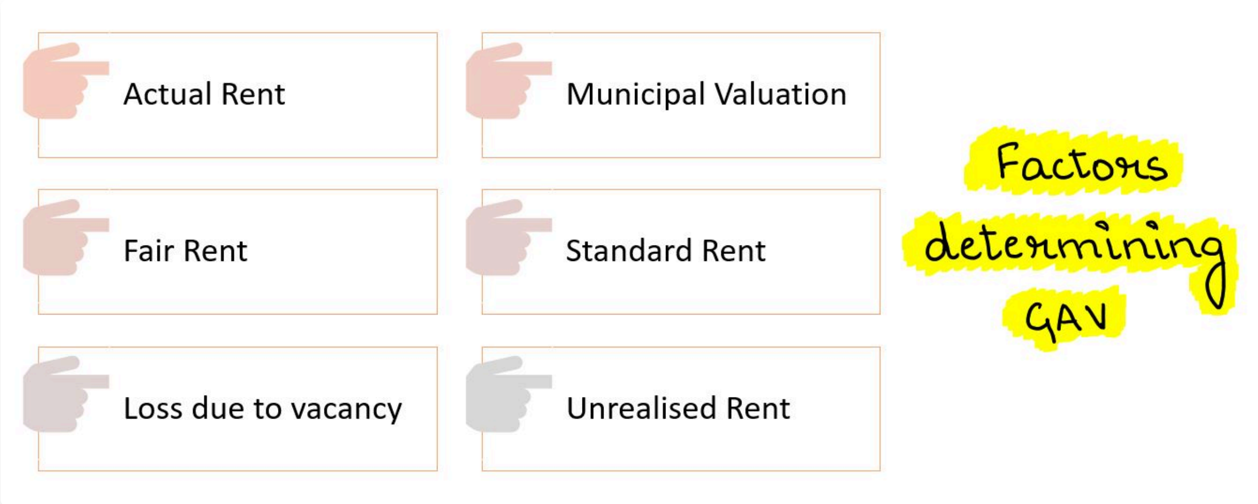
6. Determination of Annual Value

Tax under the head ‘Income from House Property’ is not a tax on rent of a property. The basis of calculating ‘Income from House property’ is the ‘Annual Value’. Annual Value is the inherent capacity of the property to earn income and it has been defined, as the amount for which the property may reasonably be expected to be let out from year to year.

Annual value is determined for following different types of house properties.
(1) Where the property is let out throughout the previous year
(2) Where let out property is vacant for part of the year
(3) In case of self-occupied property or unoccupied property
(4) Where a house property is let-out for part of the year and self-occupied for part of the year
(5) In case of deemed to be let out property
(6) In case of a house property held as stock-in-trade
(7) In case of a house property, a portion let out and a portion self-occupied.

These cases are discussed next one by one.

6. Determination of Annual Value



The following factors have to be taken into consideration while determining the Gross Annual Value of the property:

1) Rent payable by the tenant (Actual Rent): It is the most important factor in determining the annual value of a let-out house property. It does not include rent for the period during which the property remains vacant. Moreover, it does not include the rent that the taxpayer is unable to realize, if certain conditions are satisfied.

2) Municipal valuation of the property: Municipal or local authorities charge house tax on properties situated in the urban areas. For this purpose, they have to determine the income earning capacity of the property so as to calculate the amount of house tax to be paid by the owner of the property.

3) Fair rental value (market value of a similar property in the same area): It is the rent normally charged for similar house properties in the same locality. Although, two properties cannot be alike in every respect, the evidence provided by transactions of other parties, in the matter of other properties in the neighbourhood, more or less comparable to the property in question, is relevant in arriving at reasonable expected rent.

4) Standard rent payable under the 'Rent Control Act': Standard Rent is the maximum rent which a person can legally recover from his tenant under a 'Rent Control Act'. This rule is applicable, even if a tenant has lost his right to apply for fixation of the standard rent. This means that if a property is covered under the Rent Control Act, its reasonable expected rent cannot exceed the standard rent.

5) Loss Due to Vacancy: Where let out property is vacant for part of the year and owing to vacancy, the actual rent is lower than the Expected Rent, then the actual rent received or receivable will be the GAV of the property.

In the case of let-out property which is vacant for part of the year, if the actual rent received or receivable for let out period is less than the Expected rent (ER) for whole year not owing to vacancy, then Expected Rent (ER) is taken as the GAV.

6) Unrealized Rent: The actual rent received/ receivable should not include any amount of rent which is not capable of being realized. However, the following conditions should be satisfied.

(a) the tenancy is bona fide.

(b) the defaulting tenant has vacated, or steps have been taken to compel him to vacate the property.

(c) the defaulting tenant is not in occupation of any other property of the assessee.

(d) the assessee has taken all reasonable steps to institute legal proceeding for the recovery of unpaid rent or satisfies the Assessing officer that legal proceedings would be useless.

6. Determination of Annual Value

Following are the steps to determine Gross Annual Value (GAV), where the property is let out through out the year.

Step 1:Find out Reasonable Expected Rent

It will be computed on the basis of *3* factors, namely:
1) Municipal Valuation (MV)
2) Fair Rent of the property (FR)
3) Standard Rent (SR) under the Rent Control Act

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

Illustration (to explain Step 1)

					(Rs. in thousand)
Cases	**A**	**B**	**C**	**D**	**E**
Municipal Value (MV)	40	40	40	40	40
Fair Rent (FR)	46	46	46	48	51
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)	**46**	**45**	**35**	**45**	**51**

Step 2: Find out Rent actually received/ receivable

It may be calculated as under:

Rent of the previous year for which the property is available for letting out	XXX
Less: Unrealised Rent (subject to satisfaction of few conditions)	XXX
Rent Received / Receivable	XXX

Note: Loss due to vacancy shall not be deducted from the aforesaid computation. It shall be deducted under Step 5.

Thus, the Gross Annual Value (GAV) is determined as follows:

Step 1	Find out *reasonable expected rent* of the property.
Step 2	Find out *rent actually received/ receivable,* after excluding Unrealized Rent but before deducting loss due to vacancy.
Step 3	Determine *which one is higher*: Amount computed in Step 1 or Step 2.
Step 4	Find out loss because of vacancy.
Step 5	GAV = Step 3 minus Step 4
Note: If there is no loss because of vacancy, then value arrived at Step 3 will be considered as GAV.	

Annual Value

From the GAV computed above, municipal taxes paid by the owner during the previous year are to be deducted to arrive at the NAV.

6. Determination of Annual Value

X, Y, Z, A and B separately owns the following properties. Compute the Gross Annual Value for the AY 2025-26 will be computed as under:

					(Rs. in thousand)
Houses	**H1 X**	**H2 Y**	**H3 Z**	**H4 A**	**H5 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 (AR)	168	168	168	168	252
Unrealized Rent (UR) of Current Previous year (Conditions satisfied)	14	42	1	70	42
Loss due to Vacancy	7	14	14	42	105

Solution:

Computation of Gross Annual Value:

					(Rs. in thousand)
Houses	**H1 X**	**H2 Y**	**H3 Z**	**H4 A**	**H5 B**
Step 1: Reasonable expected rent (MV or FR, whichever is higher, subject to maximum of SR)	142	175	175	142	241
Step 2: Rent Received / Receivable after deducting unrealized rent (AR less UR)	154	126	167	98	210
Step 3: **Higher** of the amount computed in Step 1 and Step 2	154	175	175	142	241
Step 4: Loss due to Vacancy	7	14	14	42	105
Step 5: GAV (Step 3 minus Step 4)	**147**	**161**	**161**	**100**	**136**

6. Determination of Annual Value

Mr. X is the owner of three houses, which are all let out and not governed by the Rent Control Act. From the following particulars find out the gross annual value in each case (Amt. in Rs.):

Particulars	I	II	III
Municipal Value	30,000	20,000	35,000
Actual (De facto) Rent	32,000	28,000	30,000
Fair Rent	36,000	24,000	32,000

Solution:

Gross Annual Value (GAV): Higher of Expected or Actual Rent

Expected Rent: Higher of Municipal Valuation or Fair Rent

House I: Rs. 36,000

House II: Rs. 24,000

House III: Rs. 35,000

Actual Rent (given)

GAV: House I: Rs. 36,000 House II: Rs. 28,000 House III: Rs. 35,000

6. Determination of Annual Value

From the following information provided by Mr. Raja in respect of 3 properties rented out by him, compute the gross annual value of all the properties.

Particulars	**Property A (in Rs.)**	**Property B (in Rs.)**	**Property C (in Rs.)**
Municipal Value	8,48,484	8,48,484	2,52,252
Fair Rent	2,52,252	2,52,252	8,48,484
Standard Rent	Not Applicable	84,252	9,84,000
Actual Rent for the entire year	9,60,000	60,000	9,60,000
Unrealised Rent	1,60,000	NIL	80,000

Solution:

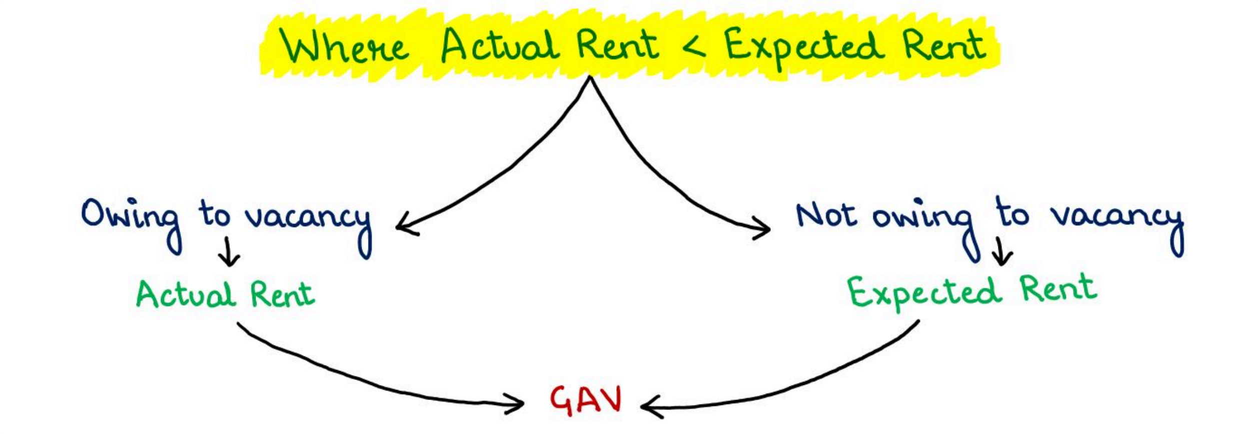
Gross annual value will be computed as follows:
Step 1: Compute reasonable expected rent of the property.
Step 2: Compute actual rent of the property.
Step 3: Compute gross annual value.

Based on these steps the computation will be as follows:

Particulars	**Property A (in Rs.)**	**Property B (in Rs.)**	**Property C (in Rs.)**
Amount at Step 1 *(See Note 1)*	8,48,484	84,252	8,48,484
Amount at Step 2 *(See Note 2)*	8,00,000	60,000	8,80,000
Amount at Step 3 i.e., Gross Annual Value *(See Note 3)*	8,48,484	84,252	8,80,000

Note 1: Amount at Step 1 (i.e., Reasonable expected rent) is higher of municipal value or fair rent (subject to standard rent).
Note 2: Amount at Step 2 is actual rent after deducting unrealised rent., i.e., Rs. 8,00,000 (9,60,000 – Rs. 1,60,000) in case of property A; Rs. 60,000 in case of property B; and Rs. 8,80,000 (Rs. 9,60,000 – Rs. 80,000) in case of property C.
Note 3: Gross annual value will be higher of amount at Step 1 or Step 2 (as there is no loss due to vacancy).

6. Determination of Annual Value



Where let out property is vacant for part of the year and **owing to vacancy**, the actual rent is lower than the Expected Rent, then the actual rent received or receivable will be the GAV of the property.

In the case of let-out property which is vacant for part of the year, if the actual rent received or receivable for let out period is less than the Expected rent (ER) for whole year **not owing to vacancy**, then Expected Rent (ER) is taken as the GAV.

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6. Determination of Annual Value

Where the property is self occupied for own residence or unoccupied throughout the previous year, its Annual value will be NIL, provided no other benefit is derived by the owner from such property.

'Unoccupied property' refers to a property which cannot be occupied by the owner by reason of his employment, business or profession at a different place and he resides at such other place in a building not belonging to him.

The benefit of NIL annual value is available only for upto 2 self-occupied or unoccupied house properties.

The benefit of NIL annual value in respect of upto 2 occupied house properties is available only to an individual or HUF.

No deduction for muncipal taxes is allowed in respect of such property/ properties as annual value means value determined after deduction of municipal taxes.

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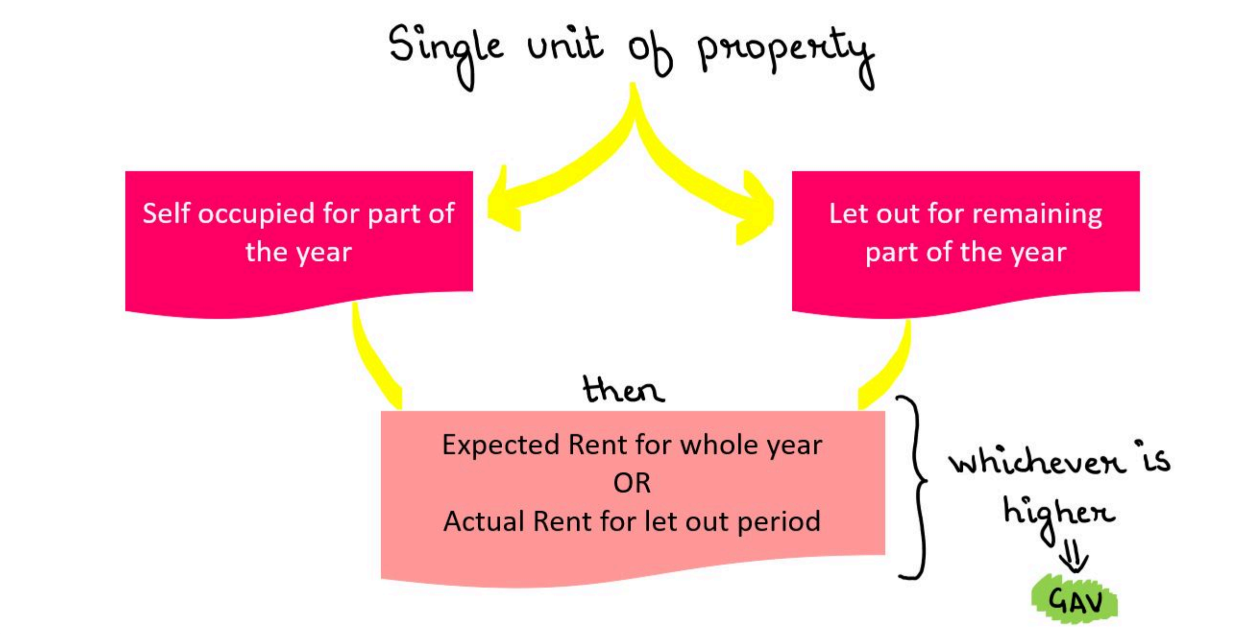
6. Determination of Annual Value

If a single unit of a property is self-occupied for part of the year and let-out for the remaining part of the year, the Expected Rent (ER) for the whole year shall be taken into account for determining GAV.



The ER for the whole year shall be compared to actual rent for the let out period and whichever is higher shall be adopted as the GAV.

However municipal tax for the whole year is allowed as deduction provided it is paid by the owner during the previous year.

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6. Determination of Annual Value

Where the assessee owns more than 2 properties for self occupation, then the income from any 2 properties, at the option of the assessee, shall be computed under the self occupied property category and their annual value will be NIL.

The other self-occupied/ unoccupied properties shall be treated as "deemed let out properties."

This option can be changed year after year in a manner beneficial to the assessee.

In case of deemed let-out property, the ER shall be taken as GAV.

The question of considering actual rent received/ receivable does not arise.

Municipal taxes actually paid by the owner during the previous year, in respect of the deemed let out properties, can be claimed as deduction.

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6. Determination of Annual Value

In some cases, property consisting of any buildings or lands appurtenant thereto may be held as stock-in-trade and the whole or any part of the property may not be let out during the whole or any part of the previous year.

In such cases, the annual value of such property or part of the property shall be NIL.

This benefit would be available for the period upto 2 years from the end of the financial year in which certificate of completion of construction of the property is obtained from the competent authority.

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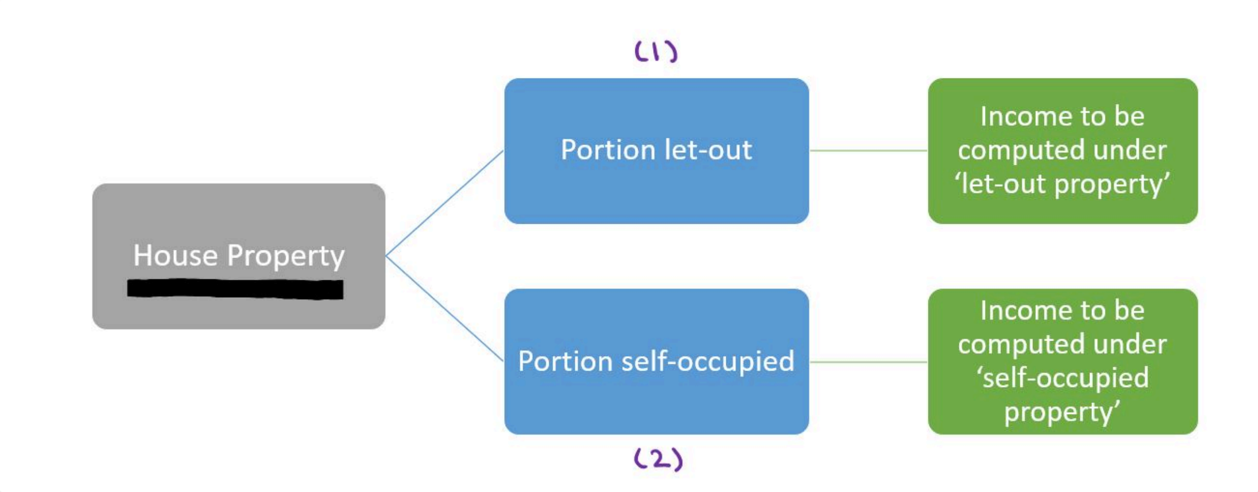
6. Determination of Annual Value



Income from any portion or part of a property which is let out shall be computed separately under the 'let out property' category and the other portion or part which is self-occupied shall be computed under the 'self-occupied property' category.

There is no need to treat the whole property as a single unit for computation of income from house property.

Municipal valuation/ fair rent/ standard rent, if not given separately, shall be apportioned between the let-out portion and self occupied portion either on plinth area or built-up floor space or on such other reasonable basis.

Property taxes, if given on a consolidated basis, can be bifurcated as attributable to each portion or floor or on a reasonable basis.

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6. Determination of Annual Value

From the Gross Annual Value, municipal taxes (including service taxes) are to be deducted, if the following conditions are fulfilled:

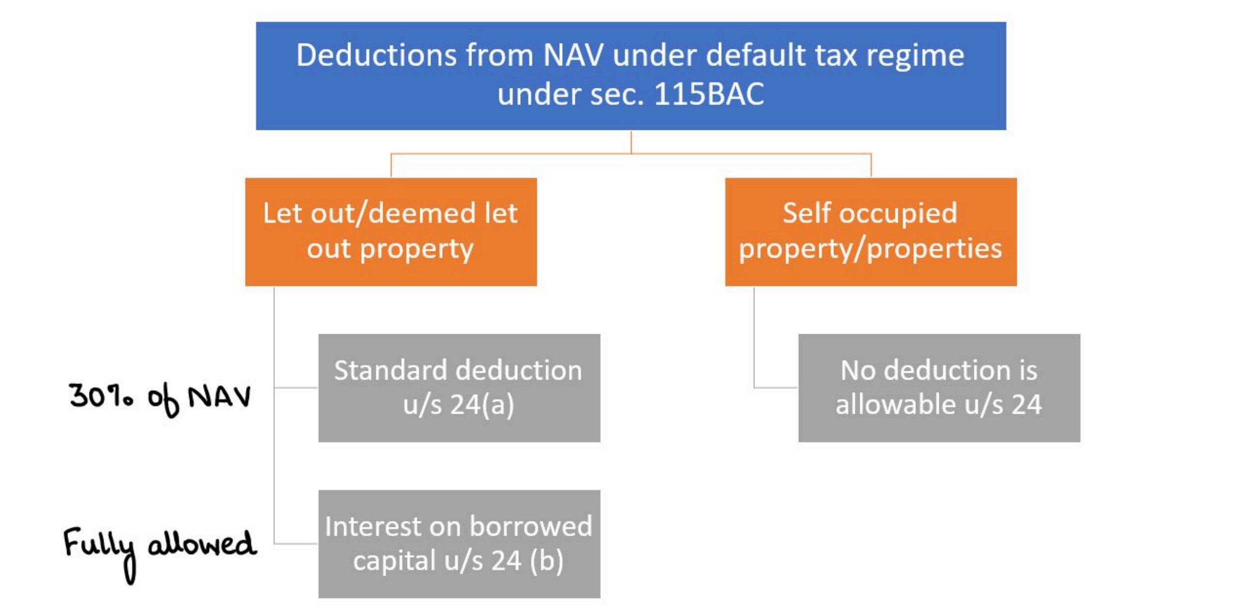
1) The property is let out during the whole or any part of the previous year.

2) The Municipal taxes must be borne by the landlord (if the Municipal taxes or any part, thereof, are borne by the tenant, it will not be allowed).

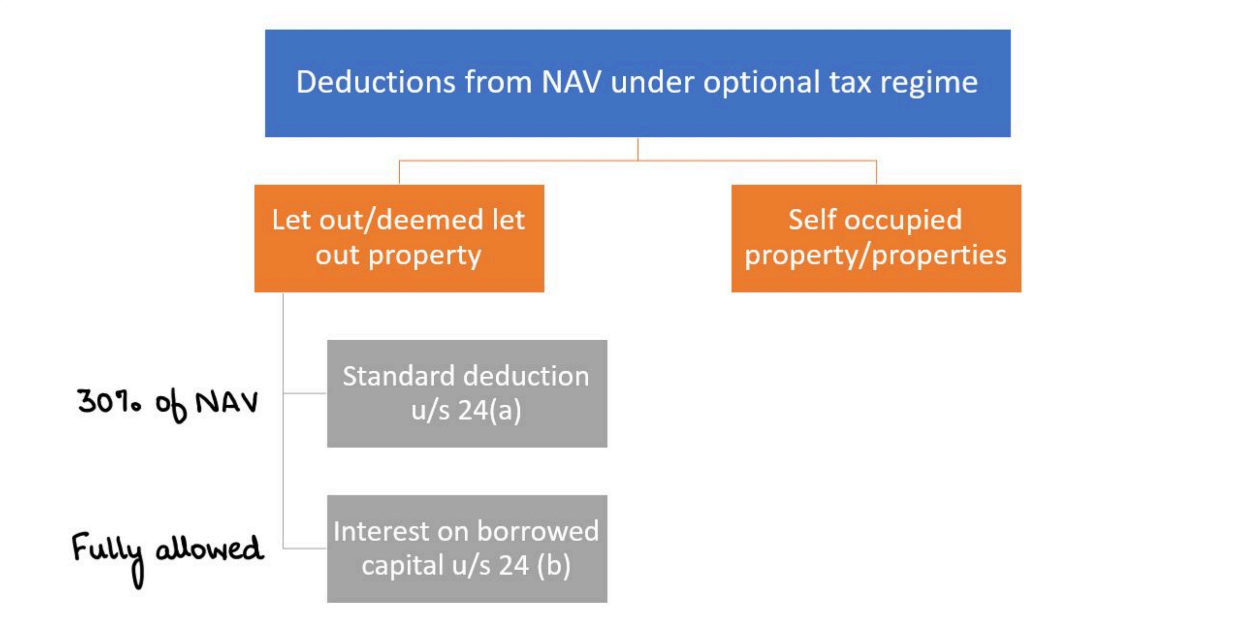
3) The Municipal taxes must be paid during the previous year (where the municipal taxes become due but have not been actually paid, it will not be allowed).

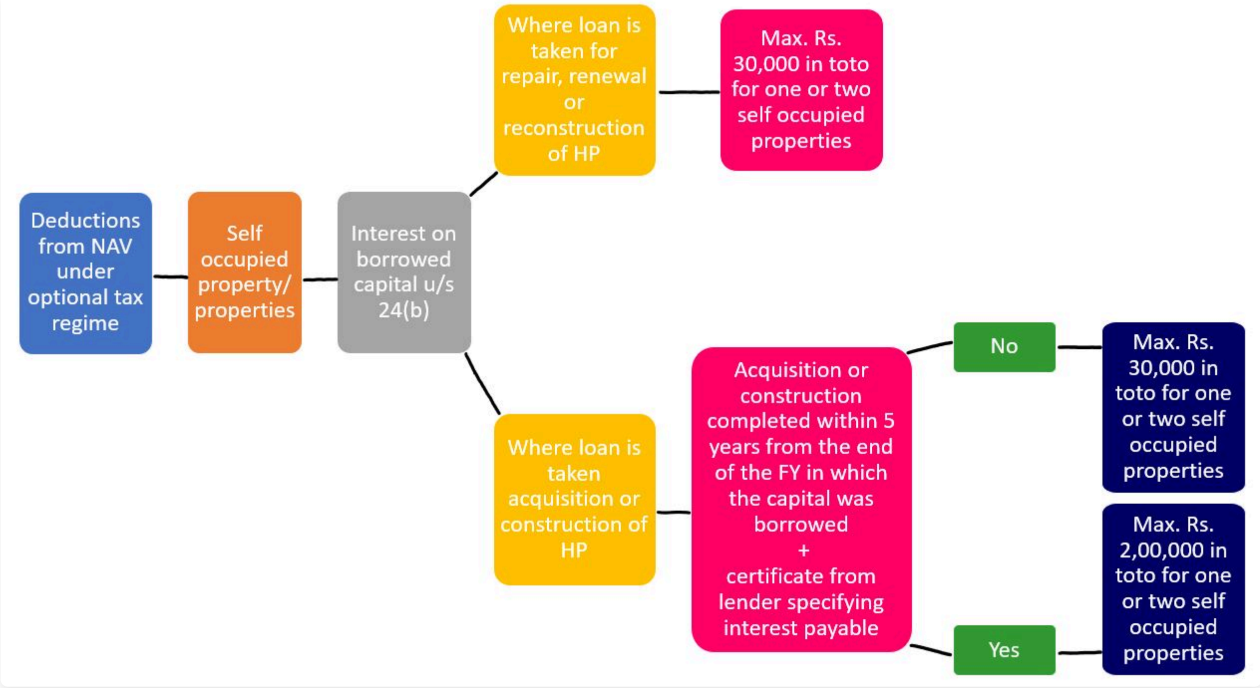
The value arrived at, after deducting municipal taxes, if any, may be referred to as **Net Annual Value.**

7. Deductions from NAV (Section 24)



Two deductions will be allowed from the net annual value (which is gross annual value less municipal taxes) to arrive at the taxable income under the head 'income from house property'. It has to be kept in mind that the deductions mentioned here (Section 24) are exhaustive and no other deductions are allowed.





The deductions admissible are as under:

1. Statutory deduction (Sec. 24(a))
30% of the net annual value will be allowed as a deduction towards repairs and collection of rent for the property, irrespective of the actual expenditure incurred.

The assessee *will not be entitled to deduction of 30%* in the following cases, as the annual value itself is NIL:
(a) In case of self-occupied properites, or
(b) In case of property held as stock-in-trade and the whole or any part of the property is not let out during the whole or any part of the previous year, upto 2 years from the end of the financial year in which certificate of completion of construction of the property is obtained from the competent authority.

2. Interest on borrowed capital (Sec. 24(b))
The interest on borrowed capital will be allowable as a deduction on an accrual basis if the capital has been borrowed for the purpose of purchase, construction, repairs, renewals or reconstruction of property.

The following points are to be kept in mind while claiming deduction on account of interest on borrowed capital:

a) In respect of let-out property, actual interest incurred on capital borrowed for the purpose of acquisition, construction, repairing, re-construction shall be allowed as deduction.
b) In respect of self-occupied residential house property, interest incurred on capital borrowed for the purpose of acquisition or construction of house property shall be allowed as deduction up to Rs. 2 lakhs. The deduction shall be allowed if capital is borrowed on or after 01-04-1999 and acquisition or construction of house property is completed within 5 years.
c) In respect of self-occupied residential house property, interest incurred on capital borrowed for the purpose of reconstruction, repairs or renewals of a house property shall be allowed as deduction up to Rs. 30,000.
d) Any interest pertaining to the period prior to the year of acquisition/ construction of the house property shall be allowed as deduction in 5 equal instalments, beginning with the year in which the property was acquired/ constructed. However, this is not allowed in case of the loan for repairs or reconstruction.
e) Deduction for interest on borrowed capital shall be limited to Rs. 30,000 in following circumstances:
1) If capital is borrowed before 01-04-1999 for the purpose of purchase or construction of a house property;
2) If capital is borrowed on or after 01-04-1999 for the purpose of re-construction, repairs or renewals of a house property;
3) If capital is borrowed on or after 01-04-1999 but construction of house property is not completed within 5 years from end of the previous year in which capital was borrowed.

Note: W.e.f. AY 2020-21, deduction for interest paid or payable on borrowed capital shall be allowed in respect of 2 (two) self-occupied house properties. However, the aggregate amount of deduction under this provision shall remain same i.e., Rs. 30,000 or Rs. 2,00,000, as the case may be.

7. Deductions from NAV (Section 24)

Mr. X has a house property in Delhi whose particulars are as under:

	(Amt. in Rs.)
Municipal Value	3,00,000
Standard Rent	3,12,000
Municipal Taxes paid	50,000
Interest on money borrowed for acquiring the house after 01.04.2020	1,60,000
Period of occupation for own residence	2 months
Actual rent for 10 months (per month)	35,000

Compute the income from house property for the AY 2025-26.

Solution:

Computation of Income from House Property	**(Amt. in Rs.)**	
GAV shall be higher of following two: (a) Expected Rent (municipal value Rs. 3,00,000 or FV Rs. 4,20,000, whichever is higher, i.e. Rs. 4,20,000 but restricted to standard rent i.e. Rs. 3,12,000) (b) Actual Rent received or receivable (35000 × 10)	3,12,000 3,50,000	**3,50,000**
Less: Municipal taxes paid		50,000
Net annual value		**3,00,000**
Less: Deduction u/s 24 (a) Statutory Deduction @ 30% (b) Interest on money borrowed for acquisition of house	90,000 1,60,000	2,50,000
Income from House Property		**50,000**

8. Property owned by Co-owners (Section 26)

The co-owned property may be self-occupied property or a let out property.

(i) Self-occupied property

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 2,00,000, as the case may be, on account of interest on borrowed capital, if they exercise the option of shifting out of the default tax regime provided under Section 115BAC(1A).

However, aggregate deduction of interest to each co-owner in respect of co-owned self-occupied property and any other self-occupied house property, if any, cannot exceed Rs.30,000/ Rs. 2,00,000, as the case may be.

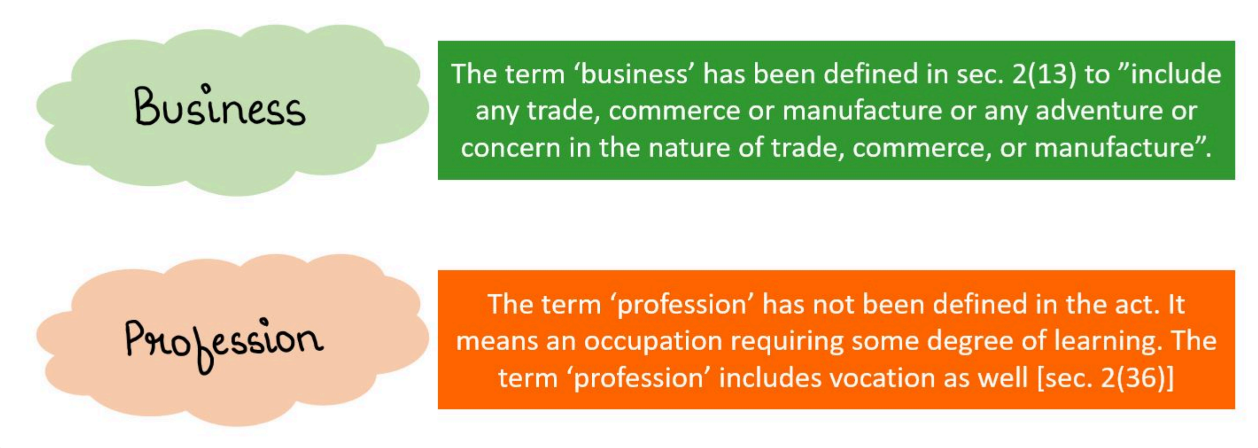
No deduction would be allowed in respect of interest on loan taken for purchase/ construction/ reconstruction/ repairs of self-occupied property where teh assessee pays tax under the default tax regime.

(ii) Let-out property

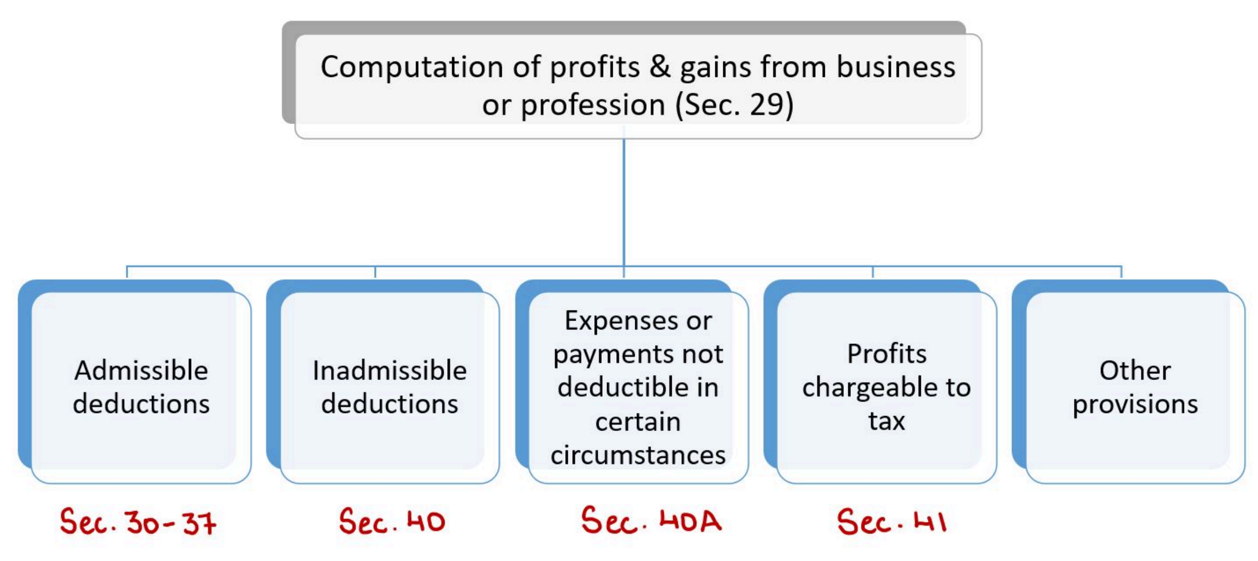
The incme from such property shall be computed as if the property is owned by one owner and thereafter the income so computed shall be apportioned amongst each co-owner as per their specific share.

1. Introduction

The Profits and Gains of Business or Profession (PGBP) is the largest head of income. The income from business and profession is known as profits and gains.



While calculating the profits and gains, we deduct various expenses from it. The expenses to be deducted for calculating the gains are defined in the 'Income Tax Act, 1961'. Sections 30 to 37 cover expenses, which are expressly allowed as deduction while computing business income. However, Sections 40, 40A and 43B cover expenses, which are not deductible (inadmissible deductions). Section 40 of the Act provides for inadmissible deductions and Section 40A provides for Expenses or payments not deductible in certain circumstances.



The expenses to be allowed as deduction, under Sections 30 to 37, are of two types. The first is 'Specific deductions', which are covered under Section 30 to 35, and second is 'General deductions', which are covered under Section 36 and 37. Specific deductions are allowed only to some of the businesses while general deductions are allowed to all the businesses.

The relevant sections from PGBP are discussed next one by one.

2. Chargeability of Tax

Under Section 28, the following income is chargeable to tax under the head *Profits and Gains of Business or Profession (PGBP)*:

1) Profits and gains of any business or profession;

2) Any compensation or other payments due to or received by any person specified in Section 28(ii);

3) Income derived by a trade, professional or similar association from specific services performed for its members;

4) The value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession; [Note that **vide Finance Act 2023**, the provisions of this clause also applies to cases where benefit or perquisite provided is in cash or in kind or partly in cash and partly in kind, w.e.f. 01.04.2024]

5) Any profit on transfer of the Duty Entitlement Pass Book Scheme;

6) Any profit on the transfer of the duty free replenishment certificate;

7) Export incentive available to exporters;

8) Any interest, salary, bonus, commission or remuneration received by a partner from firm;

9) Any sum received for not carrying out any activity in relation to any business or not to share any know-how, patent, copyright, trademark, etc.;

10) Fair market value of inventory as on the date on which it is converted into, or treated as, a capital asset determined in prescribed manner;

11) Any sum received under a key man insurance policy including bonus;

12) Any sum received/ receivable on account of capital asset (other than land or goodwill or financial instrument) being demolished, destroyed, discarded or transferred;

13) Income from speculative transaction.

3. Business Income not taxable under PGBP

Business includes (i) trade, (ii) commerce, (iii) manufacture, or (iv) any adventure or concern in the nature of trade, commerce or manufacture.

The profits derived from the following business activities **are not taxable** under Sec 28.
a) Rental income in the case of dealer in property, is taxable under the head 'Income from house Property', even if property constitutes stock-in-trade of recipient of rent or the recipient of rent is engaged in the business of letting properties on rent.
b) Dividend on shares in the case of a dealer-in-shares is taxable under the head 'Income from other sources', even if they are derived from shares held as stock-in-trade or the recipient of dividends is a dealer-in-shares.
c) Winning from lotteries, races, etc., are taxable under the head 'Income from other sources'.
d) Interest received on compensation or enhanced compensation is taxable in the year of receipt under the head 'Income from other sources', even if it pertains to a regular business activity. A deduction of 50% is allowed and, effectively, only 50% of such interest is taxable under the said head of income.

Illegal Business
Income from illegal business or profession is not exempt from tax.

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4. Business Loss

A trading loss is deductible in computing the profit earned by a business if the following conditions are satisfied:
(a) The loss should be a real loss and not notional or fictitious.
(b) The loss should be a loss on revenue account and not on the capital account.
(c) The loss must have actually arisen and been incurred, not merely anticipated or certain to occur in the future.
(d) The loss should be one that is incidental to the carrying on of the business and must arise or spring directly from or be incidental to the carrying out of an operation of the business.
(e) There should be no prohibition in the Income Tax Act, against its deductibility.

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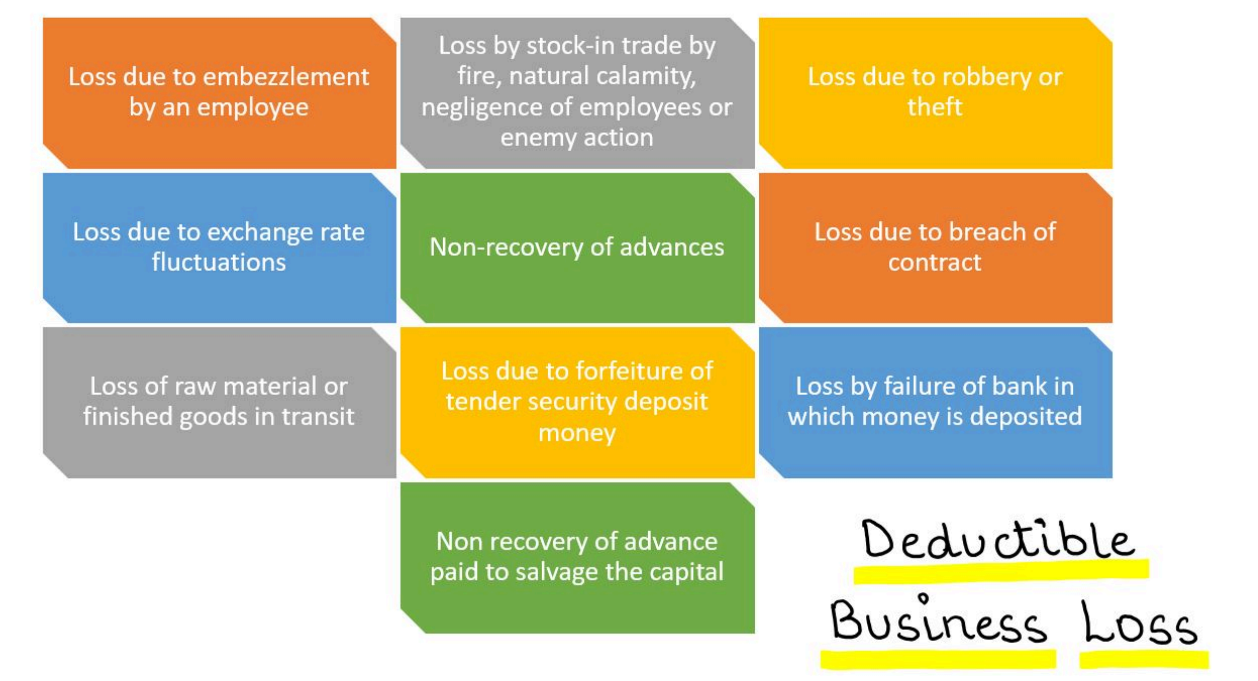
4. Business Loss

Trading losses of revenue nature incurred in carrying out the business are deductible, if they are incidental to the operation of business. This rule is applicable even if it is not specially coded anywhere under the Act.

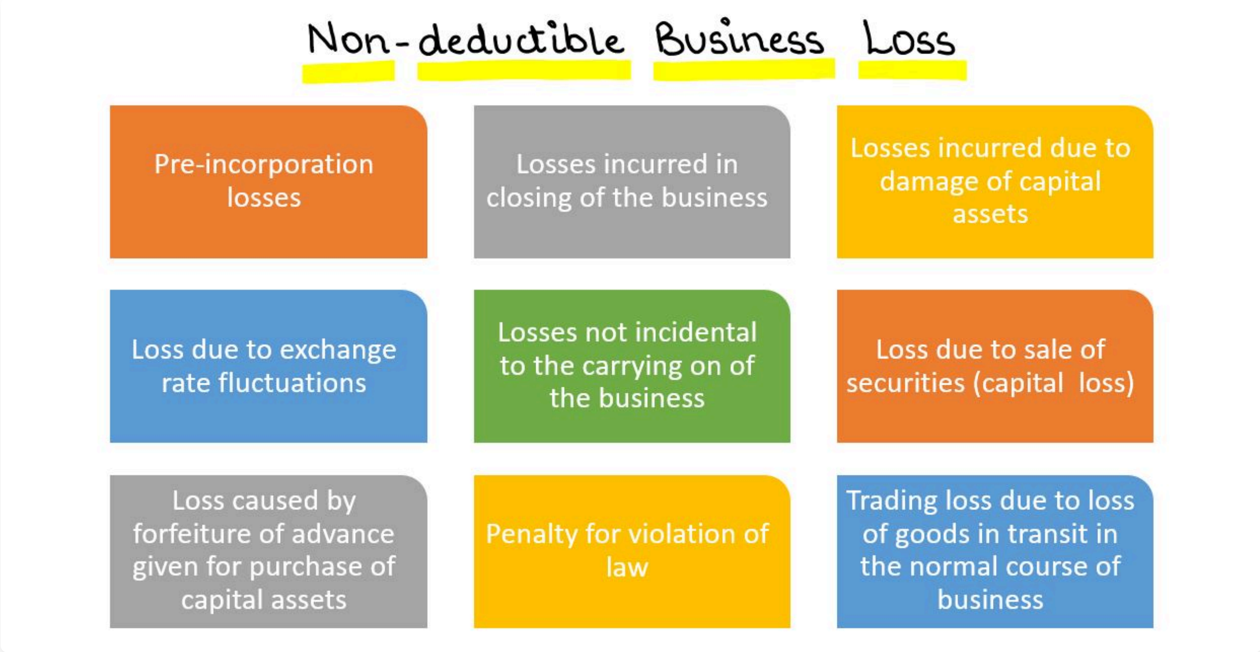
Deductible Business Loss



Instances of losses deductible from business income are as follows.

a) Loss of stock-in-trade as a result of enemy action or arising under similar circumstances.
b) Loss of stock-in-trade due to destruction by an act of God.
c) Loss arising on account of failure on the part of the assessee to accept delivery of goods.
d) Depreciation in funds kept in foreign country for purchase of stock-in-trade.
e) Loss due exchange rate fluctuations of foreign currency held on revenue account.
f) Loss arising from sale of securities held in the regular course of business.
g) Loss of cash and securities in a banking company on account of dacoity (maybe after banking hours).
h) Loss incurred on realization of amount advanced in connection with business.
i) Loss of security deposited for the purposes of acquisition of stock-in-trade.
j) Loss due to forfeiture of a deposit made by the assessee for properly carrying out of contract for supply of commodities.
k) Loss on account of embezzlement by an employee.
l) Loss incurred due to theft or burglary in factory premises during or after working hours.
m) Loss of precious stones or watches of a dealer while bringing them from business premises to his house.
n) Loss arising from negligence or dishonesty of employees.
o) Loss incurred on account of insolvency of banker with which current account is maintained by the assessee.
p) Loss incurred due to freezing of the stock-in-trade by enemy action.
q) Loss incurred by a sugar manufacturing company by foregoing advance made to sugarcane growers who used to sell sugarcane crop exclusively to the company.
r) Loss on account of non-recovery of advances given by the assessee-company (engaged in the business of financing its subsidiaries) to its 100% subsidiary company.
s) Loss incurred by a holding company which has guaranteed a loan taken by its subsidiary company.
t) Loss arising as a result of seizure and confiscation of illegal stock-in-trade is allowable as a business loss against income from illegal business.
u) Loss arising as a result of rejection of goods by the importer (as goods are unfit for human consumption).

Non-deductible Business Loss

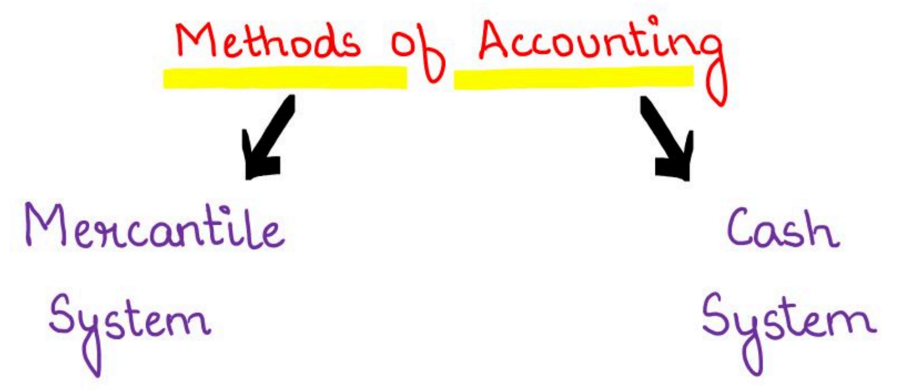


Instances of losses not deductible from business income are as follows.

a) Loss which is not incidental to trade or profession, carried on by the assessee.
b) Loss incurred due to damage, destruction etc., of capital assets.
c) Loss incurred due to sale of shares held as investment.
d) Loss of advances made for setting up of a new business which ultimately could not be started.
e) Depreciation of funds kept in foreign currency for capital purposes.
f) Loss arising from non-recovery of tax paid by an agent on behalf of the non-resident.
g) Anticipated future losses.
h) Provision made by the assessee in respect of non-performing assets.
i) Loss relating to any business or profession discontinued before the commencement of previous year.

5. Method of Accounting

Income under the heads *Profits and gains of business or profession* and *Income from other sources* shall be computed in accordance with 'method of accounting' regularly employed by the assessee.



There are two main methods of accounting—mercantile system and cash system.
a) In the case of **mercantile system**, net profit or loss is calculated after taking into consideration all income and expenditure of a particular accounting year irrespective of the fact, whether income is not received or expenditure is not actually paid during the accounting period.
b) In the case of **cash system** of accounting, on the other hand, a record is kept of actual receipts and actual payments of a particular year.

6. Tax Accounting Standards

The Central Board of Direct Taxes has notified the Income Computation and Disclosure Standards (ICDS) in September 2016, applicable from AY 2017-18. These standards are applicable for computation of income chargeable under the head 'Profits and gains of business or profession' or 'Income from other sources' and not for the purpose of maintenance of books of accounts.

The 10 notified Income Computation and Disclosure Standards (ICDS) are listed below.

ICDS I	Accounting Policies
ICDS II	Valuation of Inventories
ICDS III	Construction Contracts
ICDS IV	Revenue Recognition
ICDS V	Tangible Fixed Assets
ICDS VI	The Effect of Changes in Foreign Exchange Rate
ICDS VII	Government Grants
ICDS VIII	Securities
ICDS IX	Borrowing Cost
ICDS X	Provisions, Contingent Liabilities and Contingent Assets

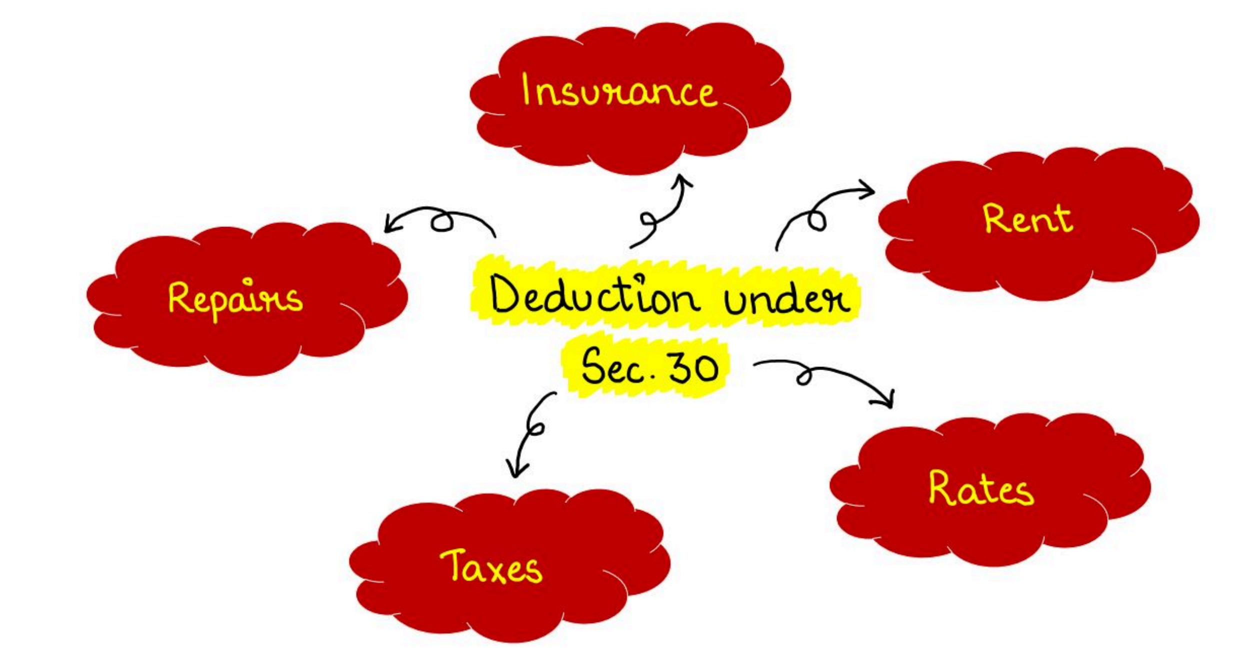
7. Specific Deductions under the Act

Sections 30 to 37 cover expenses, which are expressly allowed as deduction, while computing business income. Sections 40, 40A and 43B cover expenses which are not deductible.

Following deductions are discussed next one by one.

1. Rent, rates, taxes, repairs and insurance for building (Sec. 30)
2. Repairs and insurance of machinery, plant and furniture (Sec. 31)
3. Depreciation Allowance (Sec. 32)
4. Expenditure on scientific research (Sec. 35)
5. Amortisation of preliminary expenses (Sec. 35D)
6. Amortisation of expenditure incurred under Voluntary Retirement Scheme, VRS (Sec. 35DDA)
7. Insurance Premium (Sec. 36(1))
8. Bonus or commission to employees (Sec. 36(1)(ii))
9. Interest on borrowed capital (Sec. 36(1)(iii))
10. Employer's contribution to RPF and approved superannuation fund (Sec. 36(1)(iv))
11. Employer's contribution to National Pension Scheme (NPS) (Sec. 36(1) (iva))
12. Employer's contribution towards approved gratuity fund (Sec. 36(1)(v))
13. Employees' contribution towards staff welfare scheme (Sec. 36(1)(va))
14. Deduction on account of Bad debts (Sec. 36(1)(vii))
15. Expenses on family planning (Sec. 36(1)(ix))
16. General Deduction (Sec. 37(1))
17. Disallowance of CSR (Corporate Social Responsibility) expenditure
18. Advertisement Expenses (Sec. 37(2B)).

8. Rent, rates, taxes, repairs and insurance for building (Sec. 30)



Section 30 allows following deduction in respect of the rent, rates, taxes, repairs and insurance of buildings used by the assessee for the purposes of his business or profession.

1) the rent of premises, the amount of repairs (not being capital expenditure), if assessee has undertaken to bear the cost of repairs (this is applicable, if the assessee has occupied the property as a tenant);

2) the amount of current repairs (not being capital expenditure) (if the assessee has occupied the premises otherwise than as a tenant);

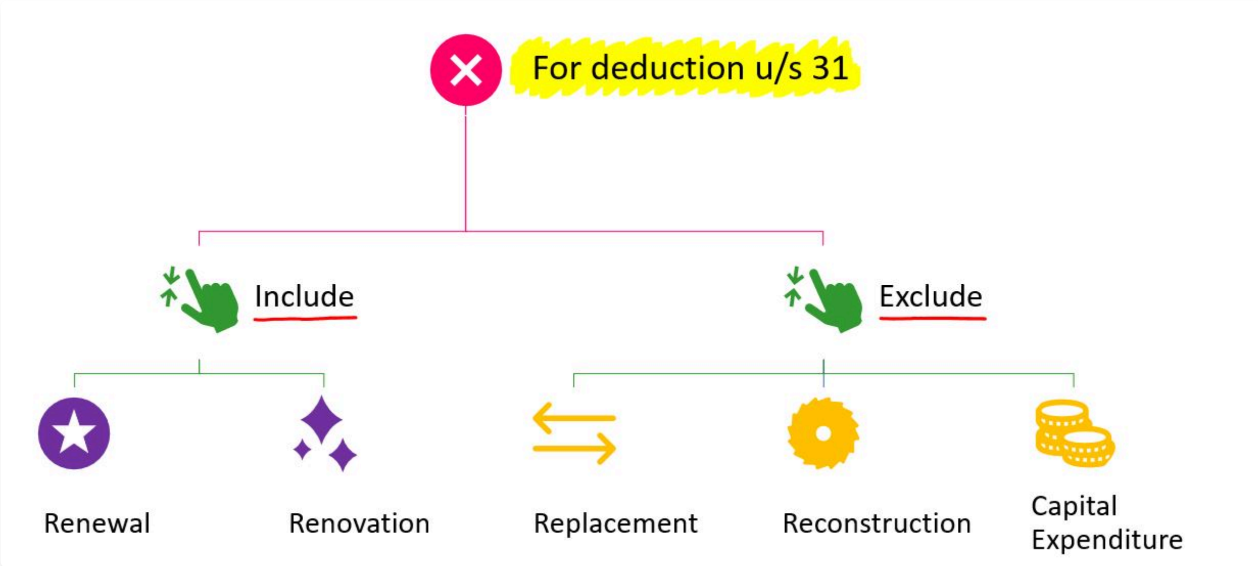
3) any sum on account of land revenue, local rates or municipal taxes; and

4) amount of any premium in respect of insurance against risk of damage or destruction of the premises.

5) Where the premises are used partly for business and partly for other purposes, only a proportionate part of the expenses attributable to that part of the premises used for purposes of business will be allowed as a deduction.

Land revenue, local rates or municipal taxes are deductible subject to the conditions as specified under Section 43B.

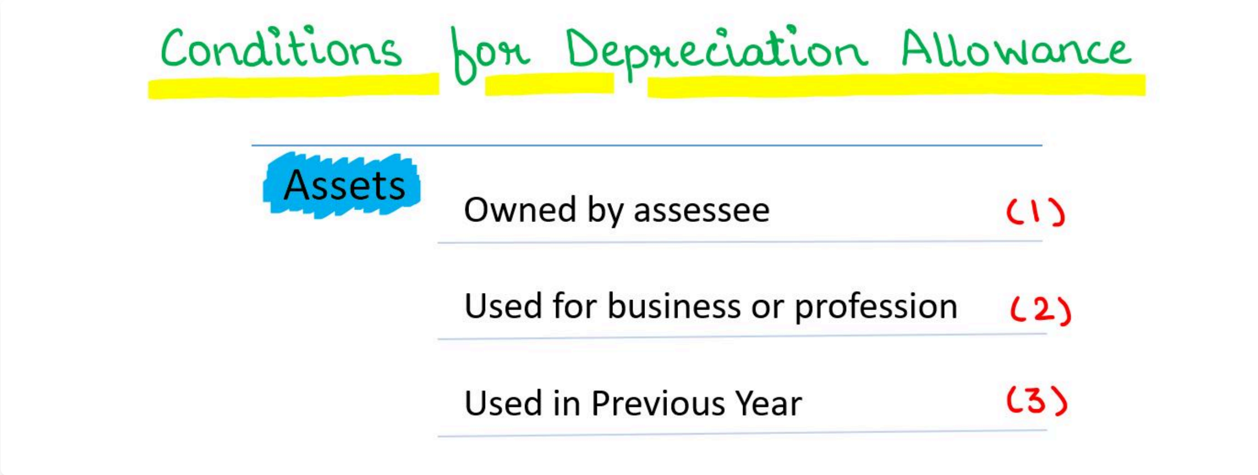
9. Repairs and insurance of machinery, plant and furniture (Sec. 31)



The expenditure incurred on current repairs (not being capital expenditure) and insurance in respect of plant, machinery and furniture used for business purposes is allowable as deduction under Section 31.

The term 'repairs' will include renewal or renovation of an asset but not its replacement or reconstruction. The expenditure should not be a capital expenditure.

10. Depreciation Allowance (Sec. 32)



Depreciation shall be determined according to the provisions of Section 32. It is allowed on block of assets. In order to avail depreciation, one should satisfy the following conditions:

1) Asset should be owned by the assessee.
2) Asset must be used for the purpose of business or profession.
3) Use of the asset in the previous year.
4) Depreciation is available on tangible as well as intangible assets.

Block of Assets

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

(a) being **tangible assets** such as buildings, machinery, plant or furniture and

(b) **intangible assets**, being know-how, patents, copyrights, trademarks, licences, Franchises or any other business or commercial rights of similar nature, in respect of which the same percentage of depreciation is prescribed.

Class of Assets

Assets eligible for depreciation have been classified into *four* classes:

(1) building;
(2) plant and machinery;
(3) furniture;
(4) intangible assets of the type discussed above.

Each class of assets, other than intangible assets, may have different blocks or groups, on which separate rates of depreciation are prescribed and for each such rate, separate block will be formed. In the case of intangible assets, there will be only one block as only one rate, i.e., 25% has been prescribed for all such intangible assets.

The other provisions related to depreciation allowance are discussed next.

10. Depreciation Allowance (Sec. 32)

WDV of block of assets, for the purpose of charging depreciation, for current year means:

In case of assets acquired before the previous year	**In case of assets acquired in the previous year**
The actual cost to the assessee of all the assets falling within the block *less* all depreciation actually allowed.	The actual cost to the assessee.

However, if any asset of the block is sold during the year, the WDV of a block of asset shall be computed as follows:

Step 1	Determine WDV of the entire block at the beginning of the previous year which will be WDV of that block of assets in the immediately preceding previous year as reduced by the depreciation actually allowed in respect of that block of assets in relation to said preceding previous year.
Step 2	Add the actual cost of any asset falling within the block, acquired during the previous year.
Step 3	Deduct the money received/ receivable, in respect of the asset of the same block, which is sold/ discarded/ demolished/ destroyed during the previous year, together with the amount of scrap value, if any.
Step 4	The resultant figure, will be the WDV of the block, at the end of the year, for the purpose of charging depreciation for the current year.
Note: The deduction under Step 3 cannot exceed the aggregate amount of Step 1 and Step 2. If it exceeds such amount, there will be no WDV for the purpose of charging depreciation. The excess amount is subject to the provisions of capital gain as per Sec. 50, i.e., it will be short-term capital gain.	

10. Depreciation Allowance (Sec. 32)

The assets should be actually used by the assessee for purposes of his business during the previous year. The asset must be put to use at any time during the previous year. The amount of depreciation allowance is not proportionate to the period of use during the previous year. *However, where the asset is used for less than 180 days in a year, the depreciation is allowed at 50% of the allowable depreciation according to the prescribed percentage in respect of the block of assets comprising such asset.*

For example, X Ltd. purchases an old plant (rate of depreciation: 15%) on May 10, 2022. It is put to use on January 10, 2025. In this case, the plant is acquired during 2024-25 and in 2024-25, it is put to use for less than 180 days. It is, therefore, qualified for half of the usual depreciation (i.e. 7.5%).

It is significant to note that this restriction applies only to the year of acquisition and not for subsequent years.

The following table highlights these provisions:

Whether the asset is put to use during the year	**For how many days the asset is put to use**	**Depreciation for 1st year (in which the asset is acquired)**	**Depreciation (of Subsequent year)**
No	-	No Depreciation	No depreciation
Yes	Less than 180 days	Half of usual depreciation	Usual Depreciation
Yes	180 days or more	Usual Depreciation	Usual Depreciation
Note: If any newly acquired asset is put to use for less than 180 days in a year and sold off in the same year, then the depreciation will be charged at full rate and not at half rate.			

10. Depreciation Allowance (Sec. 32)

WDV of the block having two machines namely X and Y as on 01.04.2024 is Rs. 6,00,000. Machine Z was acquired on 05.11.2024 for Rs. 3,00,000 and put to use on the same date. Machine X was sold on 28.03.2025 for Rs. 4,00,000. Compute the depreciation allowable for the AY 2025-26. (Normal rate of Depreciation 15%).

Solution:

		(Amt. in Rs.)
WDV of the block as on 01.04.2024		6,00,000
Addition during the year of Machine Z for less than 180 days		3,00,000
		9,00,000
Less: Sale price of X sold during the year		4,00,000
WDV as on 31.03.2025 for the purpose of charging depreciation		**5,00,000**
Depreciation @ 7.5% on Rs. 3,00,000 (acquisition price of Machine Z, which is put to use for less than 180 days) Depreciation @ 15% on balance Rs. 2,00,000 (Rs. 5,00,000 – Rs. 3,00,000)	22,500 30,000	52,500
WDV as on 01.04.2025		**4,47,500**

10. Depreciation Allowance (Sec. 32)

In such case, no depreciation will be allowed, as WDV of the block at the end of the year shall be reduced to *Nil*. Thus, if all the assets of the block are sold during the year, and (a) Sale price is greater than WDV + asset purchased during the year or (b) Sale price is less than WDV + asset purchased during the year, then, such excess or deficit shall be treated as short-term capital gain or short-term capital loss, as the case may be.

These cases are illustrated next.

10. Depreciation Allowance (Sec. 32)

The WDV of a block of asset as on 01.04.2024 was Rs. 8,00,000. An asset of the same block was acquired during the year for Rs. 2,00,000. Thereafter, all the assets of the block were sold for Rs. 13,00,000. Compute the depreciation for the AY 2025-26 and also indicate, if there is any short-term capital gain/loss.

Solution:

As the entire block of assets is sold, the block ceases to exist at the end of previous year, hence section 32 is not applicable.

Computation of short-term capital gain/loss

	(Amt. in Rs.)
Consideration price of block sold	13,00,000
Less: Cost of acquisition WDV of block plus asset purchased during the previous year (Rs. 8,00,000 + Rs. 2,00,000)	10,00,000
Short-term capital gain	**3,00,000**

10. Depreciation Allowance (Sec. 32)

The WDV of a block of asset as on 01.04.2024 was Rs. 8,00,000. An asset of the same block was acquired during the year for Rs. 2,00,000. Thereafter, all the assets of the block were sold for Rs. 9,00,000. Compute the depreciation for the AY 2025-26 and also indicate, if there is any short-term capital gain/loss.

Solution:

As the entire block of assets is sold, the block ceases to exist at the end of previous year, hence section 32 is not applicable.

Computation of short-term capital gain/loss

	(Amt. in Rs.)
Consideration price of block sold	9,00,000
Less: Cost of acquisition WDV of block plus asset purchased during the previous year (Rs. 8,00,000 + Rs. 2,00,000)	10,00,000
Short-term capital loss	**1,00,000**

Where a part of block is sold and the sale consideration of the asset sold exceeds the value of the block (or opening WDV of the block and the cost of any asset acquired during the previous year) although certain assets exist in the block, then the WDV of the block shall be reduced to Nil and no deprecation will be allowable on the block. Further, such excess shall be taxed as short-term capital gain.

For example, where a block consists of two buildings, A and B, whose WDV as on 01.04.2024 is Rs. 2,20,000 and later building A is sold during the previous year for Rs. 2,50,000. In this case, as the sale proceeds exceeds the total value of the block, the workings will be shown as under.

Particulars	**Amt. in Rs.**
WDV of block as on 01.04.2024	2,20,000
Addition during the previous year	Nil
	2,20,000
Less: Building A sold during the previous year but limited to WDV	2,20,000
WDV as on 31.03.2025	Nil
Depreciation during the year	Nil
WDV as on 01.04.2025	Nil
Note: In the above case, part of the block of asset is sold and building B exists in the block, hence, block will continue in the next previous year, but, at Nil value.	

10. Depreciation Allowance (Sec. 32)

The assessee can also claim additional depreciation at the rate of 20% of the actual cost of new plant and machinery acquired and installed after March 31, 2005, if following conditions are satisfied:
1) The assessee must be engaged in manufacture/ production of any article or thing or generation, transmission or distribution of power.
2) New Plant and Machinery (not available with respect to building & furniture etc.) should be acquired and installed after March 31, 2005.
3) It should be an eligible plant and machinery.

In case, the asset is put to use for less than 180 days in the year in which it is acquired, the rate of additional depreciation will be 10% (the remaining 10% shall be allowed as deduction in the next year). However, an industrial undertaking established in the notified backward area in the state of Andhra Pradesh, Bihar, Telangana and West Bengal, the rate of additional depreciation is 35% instead of 20%.

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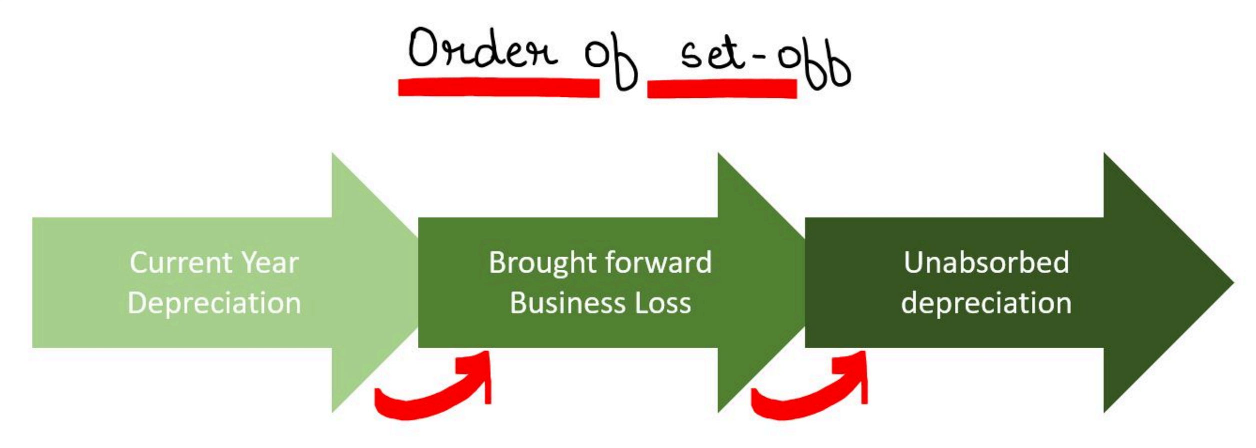
10. Depreciation Allowance (Sec. 32)

It is the depreciation that couldn't be consumed fully, that is, the profits were not sufficient to absorb it. It can be carried forward indefinitely. The current year depreciation and the brought forward business losses get priority in the set off over the unabsorbed depreciation, in that order.



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11. Expenditure on scientific research (Sec. 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. With a view to accelerate scientific research, Section 35 provides tax incentives.

The deduction allowable under this section consists of:

(a) Expenditure incurred by assessee himself

(i) *Revenue Expenditure*: Any revenue expenditure incurred by the assessee on scientific research related to his business within 3 years immediately preceding the commencement of the business on payment of salary to research personnel engaged in scientific research related to his business or on material inputs for such scientific research will be allowed as deduction in the year in which the business is commenced. The deduction will be limited to the amount certified by the prescribed authority.

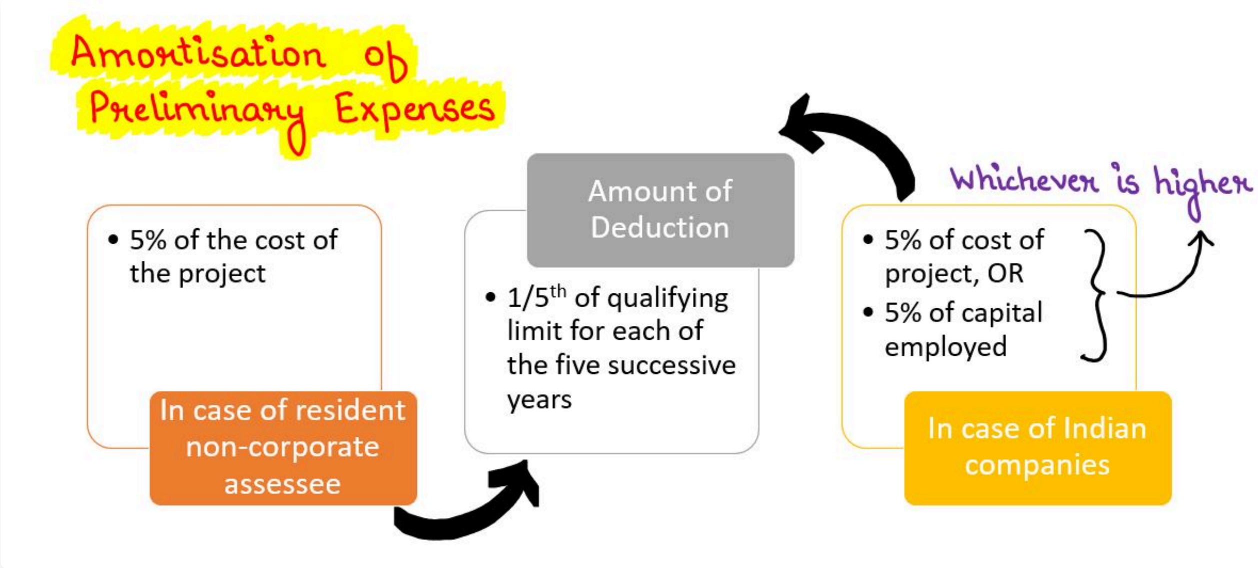
(ii) *Capital Expenditure*: Any expenditure of a capital nature (except expenditure incurred on acquisition of land) related to the business carried on by the assessee would be deductible in full in the previous year in which it is incurred. The deduction is allowed to the extent of 100% of such expenditure incurred in any previous year.

(b) Amount contributed or paid to certain specified /approved institutions (outsiders)

Where the assessee does not himself carry on research but makes contributions to the following institutions for this purpose, a deduction is allowed as follows:

Expenditure incurred/ contribution made to	**Deduction (as a % of expenditure incurred/ contribution made)**	
	For AY 2018-19 to AY 2020-21	**From AY 2021-22 onwards**
Any sum paid to notified approved research association/ university/ college/ other institution for scientific research	150%	100%
Any sum paid to a notified Indian Company for Scientific research	100%	100%
Any sum paid to notified approved research association/ university/ college/ other institutions for research in social science or statistical research	100%	100%
Any sum paid to an approved National Laboratory/ University/ IIT/ specified person for scientific research undertaken under an approved programme	150%	100%
Inhouse Expenditure (other than cost of land & building) by a company engaged in the business of Bio-technology or any business of production or manufacture of article or thing, not being an article or thing listed in Eleventh Schedule, on scientific research on approved in-house R & D facility	150%	100%

12. Amortisation of preliminary expenses (Sec. 35D)



Certain preliminary expenses are deductible under Section 35D. Deduction under Section 35D is available in case of an Indian company or a resident non-corporate assessee. A foreign company even if it is resident in India, cannot claim any deduction under section 35D.

The heads of qualifying expenditure are as follows:
1) Expenditure in connection with preparation of feasibility report, preparation of project report, conducting a market survey (or any other survey necessary for the business of the assessee), etc.
2) Legal charges for drafting any agreement.
3) Legal charges for drafting the memorandum and articles of association.
4) Printing expenses of the memorandum and articles of association.
5) Registration fees of a company under the provisions of the Companies Act.
6) Expenses in connection with the public issue of shares or debentures of a company, underwriting commission, brokerage and charges for drafting, typing, printing and advertisement of the prospectus.
7) Any other expenditure, which is prescribed.

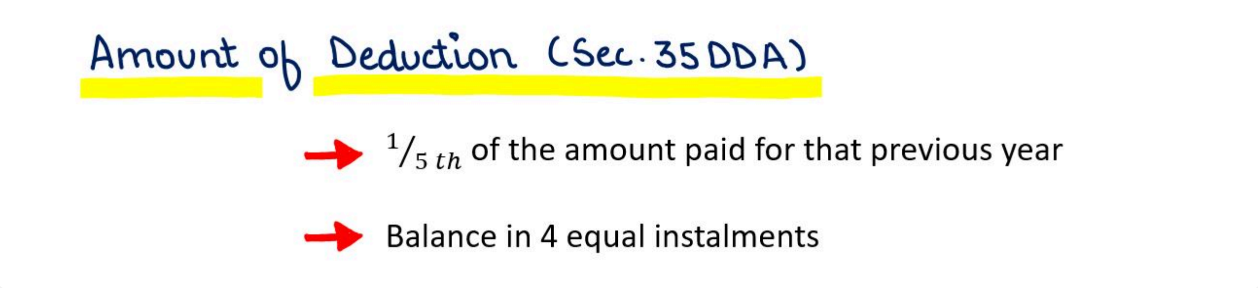
Qualifying Expenditure - Maximum ceiling
The aggregate expenditure cannot exceed the following:

In case of a corporate assesse	In case of a non-corporate assessee
a. 5% of cost of project; or b. 5% of capital employed, whichever is more	a. 5% of cost of project

Amount eligible for deduction
1/5th of the qualifying expenditure is allowable as deduction in each of the 5 successive years, beginning with the year in which the business commences, or as the case may be, the previous year in which extension of the industrial undertaking is completed or the new industrial unit commences production or operation.

13. Amortisation of expenditure incurred under Voluntary Retirement Scheme, VRS (Sec. 35DDA)

This section applies to an assessee, who has incurred expenditure in any previous year, in the form of payment to any employee in connection with his voluntary retirement. The amount of deduction allowable is $1/5^{th}$ of the amount paid for that previous year, and the balance in 4 equal instalments in the 4 immediately succeeding previous years.



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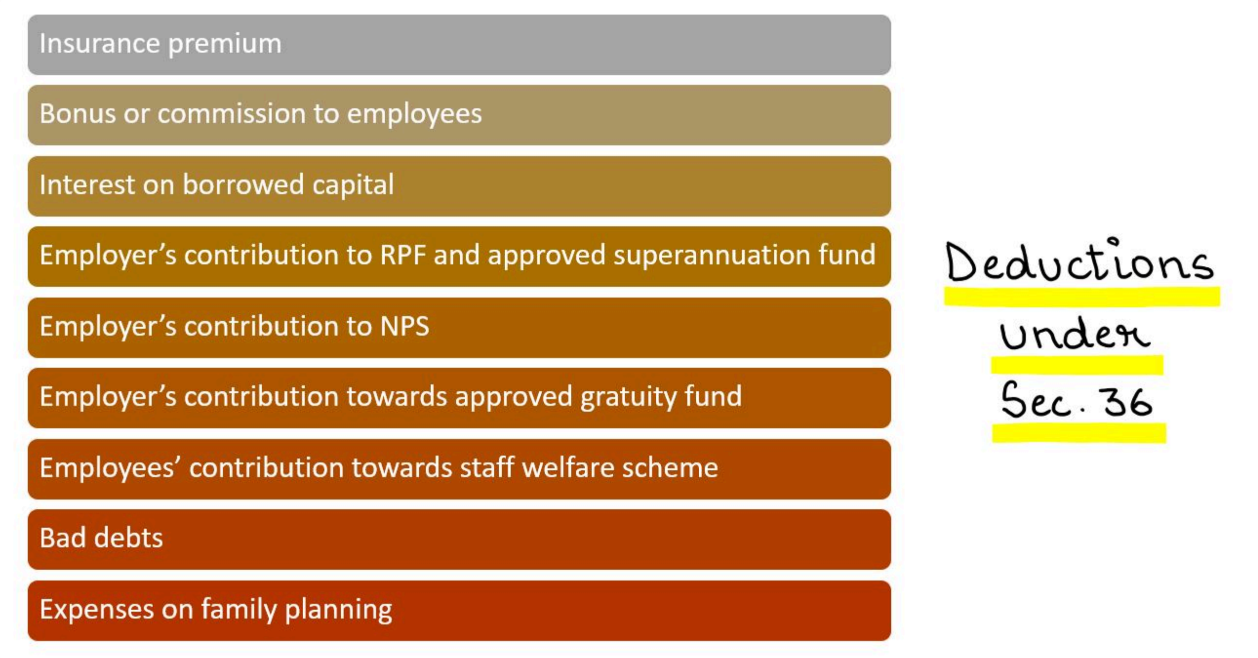
14. Deductions under Section 36

Section 36 of the Income Tax Act illustrates various expenses that are allowed as a deduction from the income earned from business and profession.

Following deductions under Section 36 are covered next.



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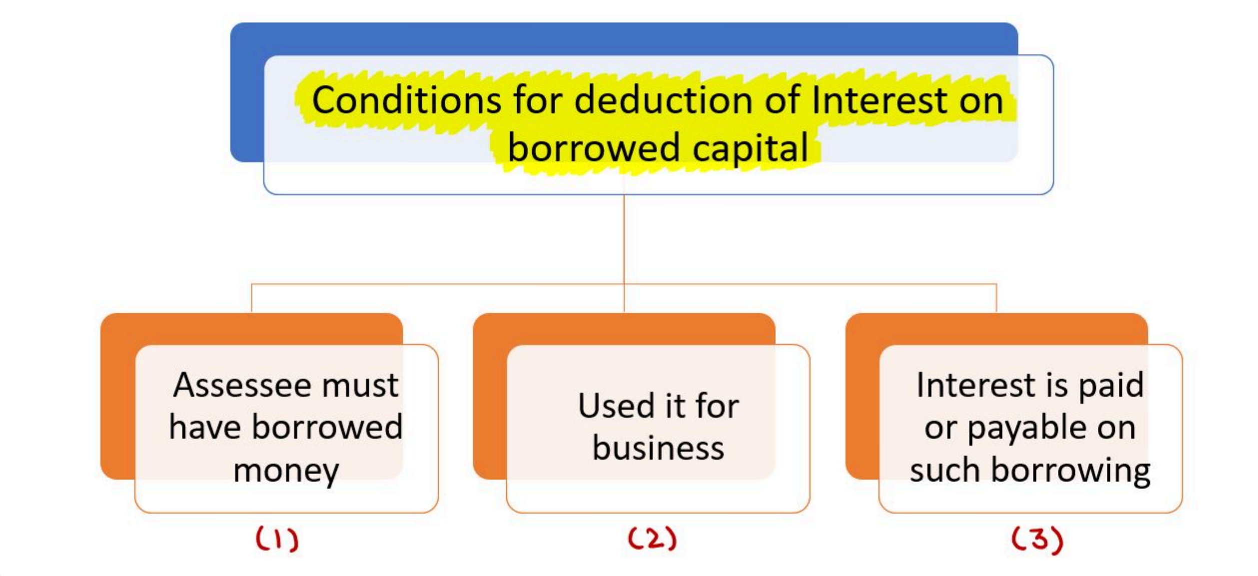
14. Deductions under Section 36

Insurance premium is deductible in the following cases:
a) Any premium paid in respect of insurance against risk of damage or destruction of stocks or stores, used for the purposes of business or profession.
b) Insurance premium paid by a federal milk co-operative society on the lives of cattle.
c) Health insurance premium of employees paid by employer by any mode, other than cash.

14. Deductions under Section 36

Bonus or commission paid to an employee is allowable as deduction subject to certain conditions. Bonus or commission is admissible only if, it is not payable as profit or dividend. Bonus or commission is allowed as deduction only where payment is made during the previous year, on or before the due date of furnishing return of income under Section 139.

14. Deductions under Section 36



Interest on capital borrowed is allowed as deduction, if the following conditions are satisfied:
a) The assessee must have borrowed money.
b) The money so borrowed must have been used for the purpose of business.
c) Interest is paid or payable on such borrowing.

However, following points are worth noting in this regard:
a) Interest on own capital is not deductible. In other words, interest shall be paid to another person. Interest paid by one unit of the assessee to another unit is not deductible.
b) Deduction of interest on borrowed capital cannot be denied only because the borrowed capital produces non-taxable income.
c) Interest paid to wife and daughters on money allotted to them, on partition, is deductible.
d) Interest paid by a firm to partners is deductible according to the provisions of Sec. 40(b) [i.e. @ 12% per annum simple interest]. However, interest paid by an AOP to its members is not deductible.

14. Deductions under Section 36

Any such contribution is allowable as deduction subject to the limits laid down for the purpose of recognizing the PF and approving superannuation fund.

14. Deductions under Section 36

Any such contribution is deductible to the extent of 10% of salary of employees.

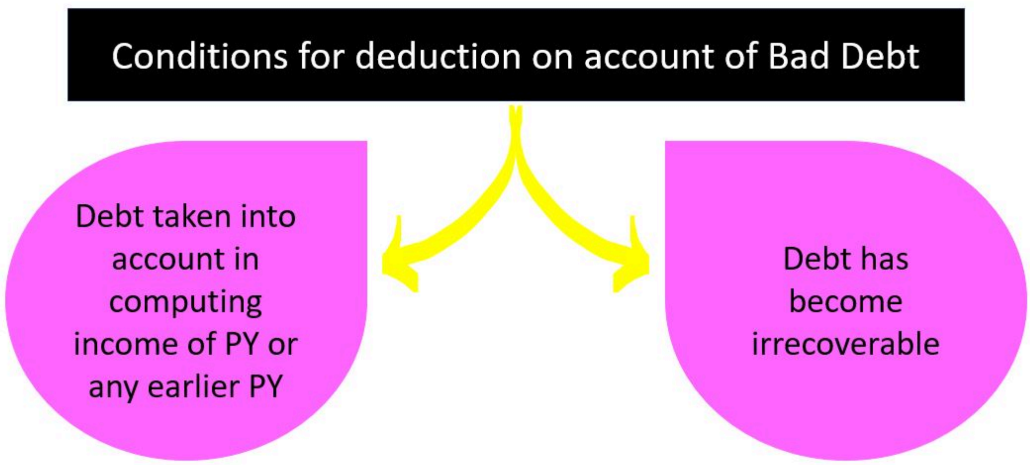
14. Deductions under Section 36

Employer's contribution towards the approved gratuity fund created by him exclusively for the benefit of his employees under an irrevocable trust is allowable as deduction.

14. Deductions under Section 36

Any such contribution received by the employer from his employees towards provident fund (or any welfare fund) shall be allowed as deduction, only if such sum is credited by the employer to employee's account in the relevant fund on or before due date.

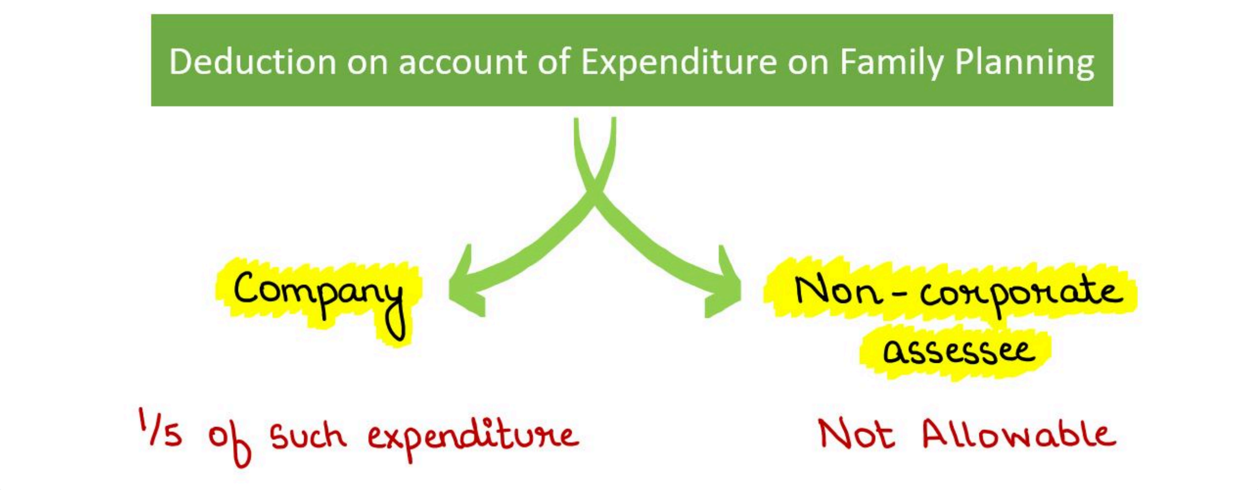
14. Deductions under Section 36



Amount of any debt or part is allowable as deduction subject to the following conditions:
(a) the debt has been taken into account in computing the income of the assessee of that previous year or of an earlier previous year, or represents money lent in the ordinary course of business of banking or money-lending which is carried on by the assessee; and
(b) it has been written off as irrecoverable in the accounts of the assessee for that previous year.

Further, no allowance can be claimed in respect of bad debts of a business which has been discontinued before the commencement of the previous year. Such bad debts cannot be deducted even from profits of a separate existing business. The debt must be incidental to the business or profession of the assessee.

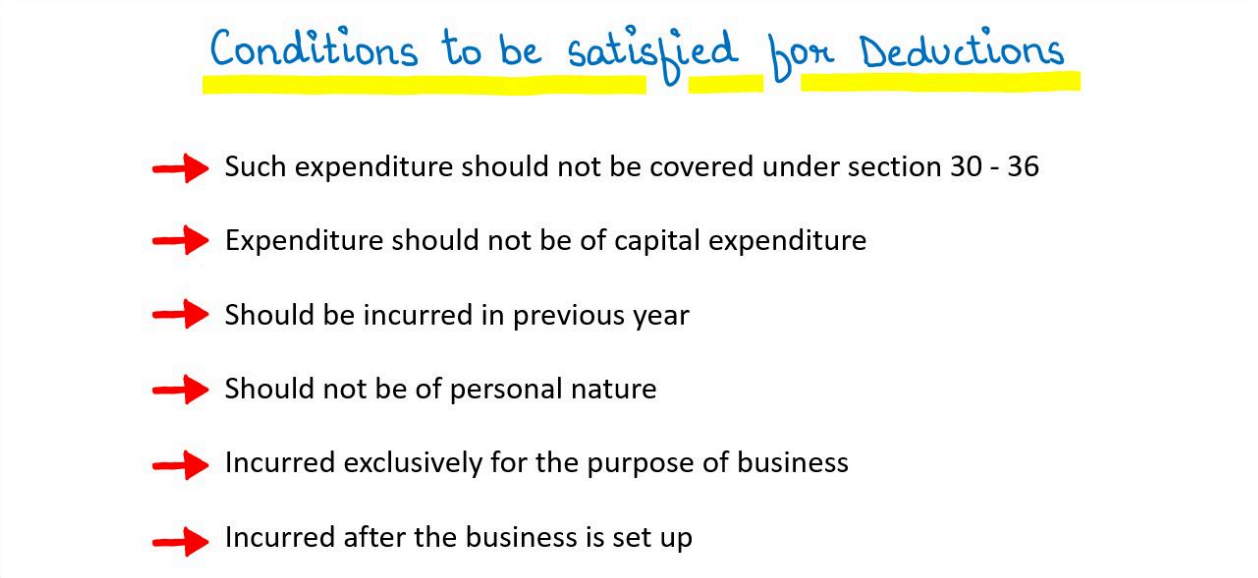
14. Deductions under Section 36



Any bonafide expenditure of revenue nature incurred by a company for the purpose of promoting family planning amongst its employees will be allowed as a deduction in computing the company's business income. Where, the expenditure is of capital nature, 1/5th of such expenditure will be deducted in the previous year, in which it was incurred and in each of the four immediately succeeding previous years. This deduction is allowable only to companies and not to other assessees. The assessee would be entitled to carry forward and set off the unabsorbed part of the allowance in the same way as unabsorbed depreciation.

15. General Deduction (Sec. 37(1))

This is a residuary section under which only business expenditure is allowable but not the business losses, *for example*, those arising out of embezzlement, theft, destruction of assets, misappropriation by employees, etc.



The following conditions should be fulfilled, in order to claim deduction:
(a) The expenditure should not be of the nature described in Sections 30 to 36.
(b) It should have been incurred by the assesse in the previous year.
(c) It should be in respect of a business carried on by the assessee, the profits of which are being computed and assessed.
(d) It must have been incurred after the business was set up.
(e) It should not be in the nature of any personal expenses of the assessee.
(f) It should have been laid out or expended wholly and exclusively for the purposes of such business.
(g) It should not be in the nature of capital expenditure.
(h) The expenditure should not have been incurred by the assessee for any purpose which is an offence or is prohibited by law.

Disallowance of CSR (Corporate Social Responsibility) expenditure

Any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in Section 135 of the Companies Act, 2013 shall not be deemed to have been incurred for the purpose of business and, hence, **shall not be allowed as deduction** under Section 37. However, CSR expenditure, which is of the nature described in Sections 30 to 36 or Sec. 80G, shall be allowed as deduction under those sections, subject to fulfilment of conditions, if any, specified therein.

Advertisement Expenses (Sec. 37(2B))

Deduction is not available in respect of expenditure incurred by an assessee on advertisement in any souvenir, brochure, pamphlet or the like published by a political party. Advertisement expenditure in a magazine owned by a political party is deductible under Sec. 80GGB, if the taxpayer is an Indian Company, but the same is not deductible under Sec. 80GGC, if the taxpayer is a person other than an Indian Company.

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16. Specific Disallowances

The expenses given by Sections 40, 40A and 43B which are expressly disallowed by the Act while computing income chargeable under the head “Profits and gains of business or profession” are given next.

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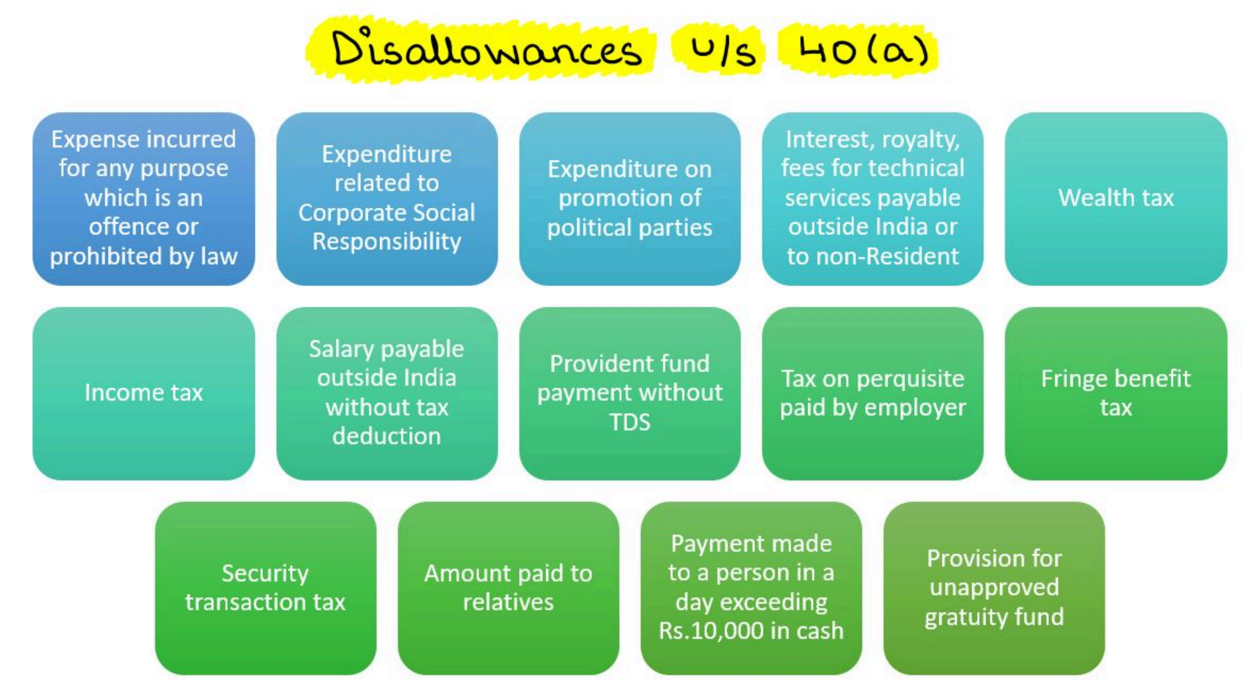
16. Specific Disallowances



Following amounts are not deductible under Section 40(a) of the Act.

a) Interest, royalty, fees for technical services payable to a non-resident

b) Securities transaction tax

c) Fringe benefit tax

d) Income-tax

e) Wealth-tax

f) Salary payable outside India without tax deduction

g) Provident fund payment without tax deduction at source

h) Tax on perquisite paid by the employer.

Disallowance on non-deduction and non-deposit of TDS

Section 40(a)(ia) provides that 30% of any sum payable to a resident, on which tax is deductible at source shall be disallowed if: (i) such tax has not been deducted; or (ii) such tax, after deduction, has not been paid on or before the due date.

With effect from AY 2020-21, a relief is given in case (i) and not in case (ii), if following 2 conditions are satisfied:
(a) tax is deductible on the aforesaid payments but it is not deducted (wholly or partly) by the payer, and
(b) the payer is not deemed to be an assessee-in-default under the first proviso to Section 201(1).

If the above conditions are satisfied, then, for the purpose of this section, it shall be deemed, that the payer has deducted and paid the tax on such amount on the date of the furnishing of return of income by the recipient.

16. Specific Disallowances

As per Section 40(2)(a), where the assessee incurs any expenditure in respect of which payment has been or is to be made to any person referred to as **specified person**, and the Assessing Officer is of opinion that such expenditure is excessive or unreasonable having regard to the fair market value of the goods, services or facilities for which the payment is made or the legitimate needs of the business or profession of the assessee or the benefit derived by or accruing to him therefrom, so much of the expenditure as is so considered by him to be excessive or unreasonable shall not be allowed as a deduction.

The specified person, for example, with respect to an 'individual' includes:

- any relative of the individual assessee;
- any person who carries on a business or profession, if:
    - the individual assessee has a substantial interest in the business of that person or
    - any relative of the individual assessee has a substantial interest in the business of that person.

The term ‘relative’, in relation to an individual, means husband, wife, brother or sister or any lineal ascendant or descendant of that individual.

Likewise, specified person with respect to company, firm, HUF or AOP etc. are also specified under the Section.

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16. Specific Disallowances

Cash payments in excess of Rs. 10,000 are 100% disallowed [Sec.40A(3)].

This rule is **not applicable in few cases** as given below:
a) Payment made to a bank or to Government
b) Payment through banking system
c) Payment made by book adjustment by an assessee
d) Payment made to a cultivator, grower or producer in respect of the purchase of agricultural or forest produce, etc.
e) Payment made to a producer in respect of purchase of the products manufactured or processed without the aid of power in a cottage industry
f) Payment made to a person who ordinarily resides or carries on business in a village not served by any bank
g) Payment of terminal benefits, such as gratuity, retrenchment compensation, etc., not exceeding Rs. 50,000
h) Payment made by an assessee by way of salary to his employee after deducting tax and when such employee is temporarily posted for a continuous period of 15 days or more in a place other than normal place of duty or on a ship and does not maintain any bank account at such place or ship
i) Payment required to be made on a day on which the banks were closed either on account of holiday or strike
j) Payment made by any person to his agent who is required to make payment in cash for goods or services on behalf of such person
k) Payment made by an authorized dealer or a money changer against purchase of foreign currency or travellers cheques in the normal course of his business.

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16. Specific Disallowances

Provision for gratuity fund (for meeting future liability) is deductible only if such gratuity fund is an approved gratuity fund. In other words, any provision for unapproved gratuity fund is not deductible.

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16. Specific Disallowances

The following sums are allowed as deduction only based on actual payment within the time limits specified in Section 43B:
(a) Any sum payable by way of tax, duty, cess or fee, by whatever name called.
(b) Any sum payable by the assessee as an employer by way of contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees.
(c) Bonus or Commission for services rendered payable to employees.
(d) Any sum payable by the assessee as interest on any loan or borrowing from any public financial institution or a SFC (State Finance Corporation) or a State Industrial Investment Corporation.
(da) Any sum payable by the assessee as interest on any loan or borrowing from a deposit taking non-banking financial company or systematically important non-deposit taking non-banking financial company [As such classification for non-banking financial companies is no longer followed by the Reserve Bank of India for the purposes of asset classification, therefore, **Finance Act, 2023** substitutes the words "such class of non-banking financial companies as may be notified by the Central Government in this behalf", w.e.f. 01.04.2024].
(e) Interest on any loan or advance from a scheduled bank or co-operative bank other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank on actual payment basis.
(f) Any sum paid by the assessee as an employer in lieu of earned leave of his employee.
(g) Any sum payable by the assessee to the Indian Railways for use of Railway assets.
(h) any sum payable by the assessee to a micro or small enterprise beyond the time limit specified in section 15 of the Micro, Small and Medium Enterprises Development (MSMED) Act 2006 **(inserted vide Finance Act, 2023).**

Note that Section 43B is applicable if an assessee maintains books of account on mercantile basis. This section provides for certain deductions to be allowed only in the year in which payment is actually made (in other words, deductions covered by section 43B are allowed on payment basis, even if the assessee maintains books of account on mercantile basis). However, there is an exception. If payment is made on or before the due date of submission of return of income [as given by section 139(1)], deduction is allowed on accrual basis.

In order to promote timely payments to micro and small enterprises, the above provisions have been amended (with effect from the assessment year 2024-25) to include payments made to such enterprises within the ambit of section 43B. Clause (h) has been inserted in section 43B and proviso to section 43B has been amended.

According to MSMED Act, 2006, where any person purchases goods/services from a micro/small enterprise, the payment shall be made before the date agreed upon between him and supplier in writing. In no case the period agreed upon between the supplier and the buyer in writing shall exceed 45 days. If, however, there is no such agreement, the payment shall be made within 15 days of acceptance/deemed acceptance of goods/services.

Now the amendment vide Finance Act, 2023 provides as follows.
If payment is made beyond time-limit
If payment is made by an assessee to a micro or small enterprise beyond the time-limit specified under MSMED Act, such payment will be deductible in the year making payment.

If payment is made within the time-limit
If payment is made by an assessee to a micro or small enterprise within the time-limit specified under MSMED Act, such payment will be deductible on accrual basis (if assessee maintains books of account on mercantile basis).

17. Computation of Taxable Income from Business

Computation of Taxable Income from Business is done as table below.

Particulars	Amount	Amount
Net Profit as per Profit and Loss Account		XX
Add: Inadmissible expenses debited to P & L A/c	XX	
Business Income not credited to P & L A/c	XX	
Overvaluation of opening stock	XX	
Undervaluation of closing stock	XX	
Notional Loss	XX	XX
		XX
Less: Admissible expenses not debited to P & L A/c	XX	
Tax-free incomes credited to P & L A/c	XX	
Non-business incomes credited to P & L A/c	XX	
Undervaluation of opening stock	XX	
Overvaluation of closing stock	XX	
Notional Profit	XX	(XX)
Taxable Income from Business		XX

18. Maintenance and Audit of Books of Accounts

Following persons or entities are required to maintain the books of account and other documents, if income/turnover/ gross receipts, exceed the prescribed limits [Section 44AA (2)]:

Person(s) or entities	**Limit**	
	Income exceeding	**Total Sales turnover/ Gross Receipts exceeding**
In case of Individual or HUF carrying on any business or profession (other than notified professions): (a) Existing business or profession: (b) Newly set up business or profession	 Rs. 2,50,000 Rs. 2,50,000	 Rs. 25,00,000 in any one of 3 years immediately preceding the accounting year. Rs. 25,00,000 during the previous year.
Persons (other than individual or HUF) carrying on any business or profession (other than notified professions) (a) Existing business or profession: (b) Newly set up business or profession:	 Rs. 1,20,000 Rs. 1,20,000	 Rs. 10,00,000 in any one of 3 years immediately preceding the accounting year. Rs. 10,00,000 during the previous year.
Prescribed class of persons such as persons carrying on legal, medical, engineering, or architectural profession or the profession of accountancy or technical consultancy or interior decoration or authorised representative or film artist (a) Existing profession: (b) Newly set up profession:	- -	Rs. 1,50,000 in all the 3 years immediately preceding the previous year. Rs. 1,50,000 in that year.

18. Maintenance and Audit of Books of Accounts

Every person carrying on business/profession is required to get his accounts audited, if his total sales, turnover or gross receipts exceeds Rs. 1 crore (in the case of business) or Rs. 50 lakh (in the case of profession) in any previous year. By an amendment made by the Finance Act, 2021, the limit of Rs. 1 crore was raised to Rs. 10 crore where at least 95% of receipts/payments are in non-cash mode.

Note: This section is not applicable to the person, who opts for presumptive taxation Scheme under Section 44AD and his total sales or turnover does not exceed Rs 2 crores. However, section 44AB has been amended (with effect from the **assessment year 2024-25**). After the amendment, the provisions of section 44AB shall not apply to the person, who declares profits and gains for the previous year in accordance with the provisions of section 44AD(1) or 44ADA(1).

18. Maintenance and Audit of Books of Accounts

Under 'Presumptive taxation', a person does not have to maintain accounting records or draw up a profit & loss account. He is also exempt from getting his accounts audited. He can simply pay tax @ 8% of his gross receipts. However, to be able to take benefit of this scheme, the gross receipts in a financial year should be Rs 1 crore or less. In Budget 2016, this limit has been increased to Rs 2 crores, which means small businesses, kirana shops, who have gross receipts under Rs 2 crores, can choose assumed income to be 8% of their receipts.

The following businesses/ persons are not covered under Section 44AD:
a) Business of plying, hiring or leasing goods carriages referred to in Section 44AE.
b) A person who is carrying on any agency business.
c) A person who is earning income in the nature of commission or brokerage.
d) Any business whose total turnover or gross receipts exceeds Rs. 2 Crore.

This is great advantage to small businesses which have meagre resources and do not have the time, money or energy to dedicate to a full-time in-house accounting person. Those who opt for this scheme, do not have to pay advance tax. They used to file their tax returns in ITR-4S (discontinued from AY 17-18). Now, they are required to file ITR 4.

In case of a person, who is opting for the presumptive taxation scheme of Section 44AD, the provisions of allowances/disallowances as provided under the Income-tax Law, will not apply and income computed at the presumptive rate of 8% (or 6%*), will be the final taxable income of the business covered under the presumptive taxation scheme and no further expenses will be allowed or disallowed. However, the assessee can claim deduction under Chapter VI-A (i.e., all deductions under Sections 80C to 80U).

**Note: Presumptive income shall be calculated at rate of 6% in respect of total turnover or gross receipts which is received by an account payee cheque or draft or use of electronic clearing system or through prescribed electronic mode.*

Presumptive taxation scheme for assessees engaged in eligible profession (Section 44ADA)
Under Section 44ADA, presumptive taxation scheme is available for a resident assessee who is engaged in the following professions: legal / medical / engineering / architectural / accountancy / technical consultancy / interior decoration, or any other profession as notified by the Central Board of Direct Taxes (CBDT), in the Official Gazette and whose turnover / gross receipts does not exceed Rs. 50 Lakhs in the PY.

Presumptive Income: 50% of the total gross receipts or such higher sum as may be declared by the assessee shall be deemed as income under the head Profit and Gains of Business and Profession (PGBP).

Amendment

Note that in order to ease compliance and to promote non-cash transactions, the threshold limits under sections 44AD and 44ADA has been enhanced (with effect from AY 2024-25) as follows:

Section 44AD: Where in the case of an eligible business, the amount (or aggregate of the amounts) received during the previous year, in cash, does not exceed 5% of the total turnover or gross receipts, the threshold limit of Rs. 3 crore will apply.

Section 44ADA: Where in the case of an eligible profession, the amount (or aggregate of the amounts) received during the previous year, in cash, does not exceed 5% of the total gross receipts, the threshold limit of Rs. 75 lakhs will apply.

In the aforesaid cases, the receipt by a cheque/draft, which is not account payee, shall be deemed to be the receipt in cash.

1. Introduction

Profits or gains arising from the transfer of a capital asset, in a previous year, are taxable as capital gains under the head **Capital Gains**. This gain is not a regular income like salary, or house rent. It is a one-time gain, in other words, the capital gain is not recurring, i.e., does not occur again and again periodically. Opposite of gain is called loss; therefore, there can be a loss under the head capital gain. However, the term 'capital loss' should not be used for such loss, as it is incorrect. Capital Loss means the loss on account of destruction or damage of capital asset. Thus, whenever there is a loss on sale of any capital asset, it will be termed as **loss under the head capital gain** (However, for the sake of convenience the term **capital loss** may be used).

The capital gain is chargeable to income tax, if the following conditions are satisfied:
a) There is a capital asset.
b) Transfer of capital assets should take place during the previous year.
c) There should be gain or loss on account of such transfer of capital asset.
d) Such capital gain should not be exempted under Sections 54, 54B, 54D, 54EC, 54EE, 54F, 54G, 54GA and 54GB.

2. Tax Rates on Capital Gains

The following incomes are taxable at the rates specified by the Income Tax Act as specified below.

Type of Tax	Condition	Rate of Tax
Long-term capital gains tax (Section 112)	Except on sale of equity shares/ units of equity-oriented fund	20%
Long-term capital gains tax (Section 112A)	On sale of Equity shares/ units of equity-oriented fund	10% over and above Rs 1 lakh
Short-term capital gains tax	When securities transaction tax is not applicable	It is taxable like revenue income and the taxpayer is taxed according to his income tax slab.
Short-term capital gains tax (Section 111A)	When securities transaction tax is applicable	15%

Simplification of Taxation of Capital Gains (Budget 2024)

Note that the Budget 2024 has brought the following changes with respect taxation of Capital Gains.

- For classifying assets into long-term and short-term, there will only be 2 holding periods: 12 months and 24 months. The 36-month holding period has been removed.
- The holding period for all listed securities is 12 months. All listed securities with a holding period exceeding 12 months are considered Long-Term. The holding period for all other assets is 24 months.
- Unlisted bonds and debentures are brought in line with the taxation on debt mutual funds and market-linked debentures. They will attract tax on capital gains at applicable slab rates. (i.e., they will be treated as short-term irrespective of the period of holding.)
- The taxation of Short-Term Capital Gain for listed equity shares, a unit of an equity-oriented fund, and a unit of a business trust has been increased to 20% from 15%. Other financial and non-financial assets which are held for short term shall continue to attract the tax at slab rates.
- For the benefit of the lower and middle-income classes, the limit on the exemption of Long-Term Capital Gains on the transfer of equity shares or equity-oriented units or units of Business Trust has increased from Rs.1 Lakh to Rs.1.25 lakh per year. However, the rate at which it is taxed has increased from 10% to 12.5%.
- The exemption limit to Rs. 1.25 lakhs has been increased for the whole of the year, whereas the tax rate changed on 23rd July 2024.
- The tax on long-term capital gains on other financial and non-financial assets is reduced from 20% to 12.5%. While on the other hand, the indexation benefit that previously was available on sale of long-term assets, has now been done away with. So, any sale of long term asset made from 23rd July, 2024, will attract tax rate of 12.5% only without indexation benefit.
- However, it is to be noted that the provision regarding availing the benefit of FMV of asset as on 01.04.2001 as cost while selling the asset, is still available even after the recent changes.

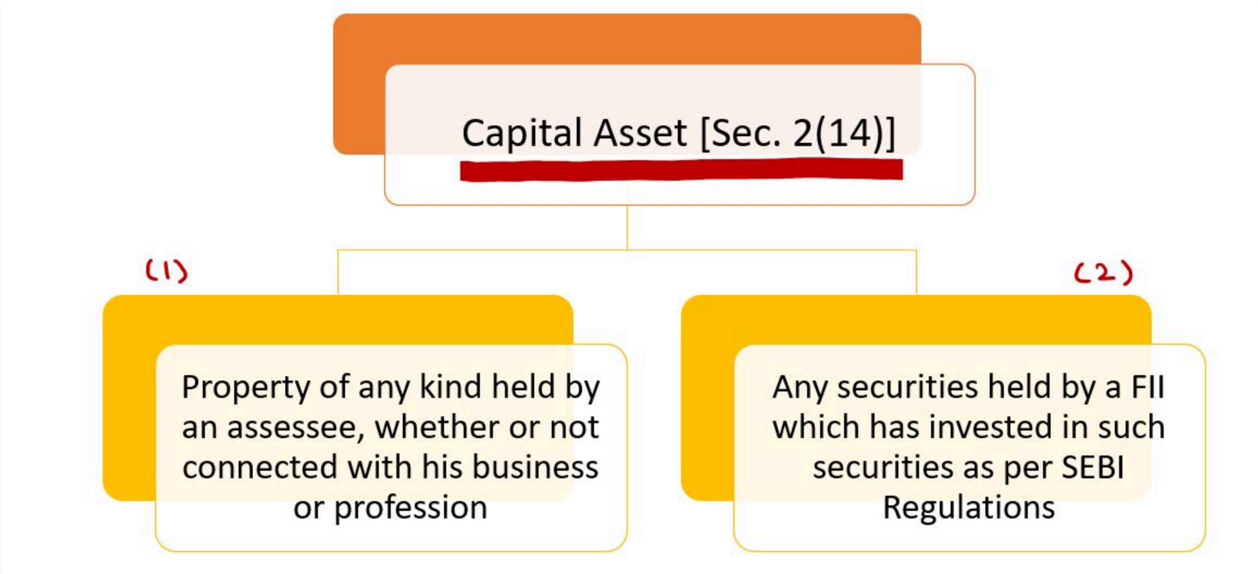
3. Key Terms

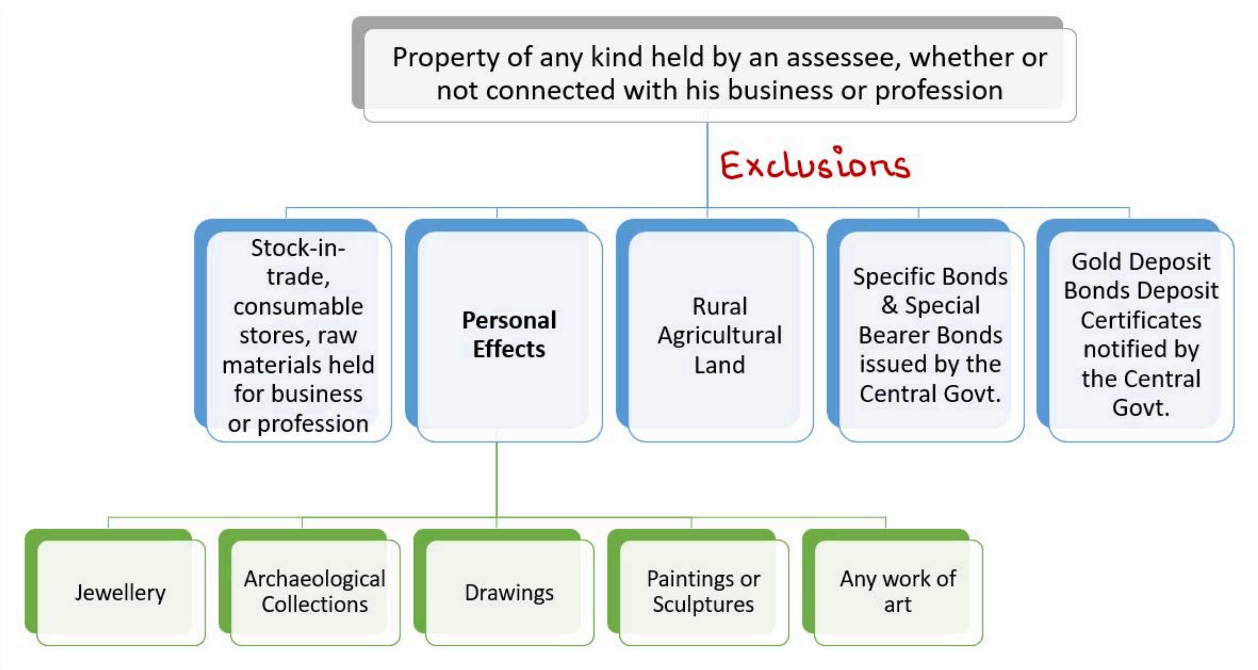
Let us discuss a few key terms connected with capital gains one by one.

3. Key Terms

Capital gain arises only when a capital asset is transferred. If the asset transferred is not a capital asset, it will not be covered under the head 'capital gain'.

What is Capital Asset





According to Section 2 (14) of the Income Tax Act, 1961, a capital asset means:
(a) property of any held by an assessee, whether or not connected with his business or profession;
(b) any securities held by a Foreign Institutional Investor which has invested in such securities in accordance with regulations made under SEBI Act.
(c) any unit linked insurance policy (ULIP) issued on or after 01.02.2021, to which exemption under section 10 (10D) does not apply on account of:
(1) premium payable exceeding Rs. 2,50,000 for any of the previous years during the term of such policy; or
(2) the aggregate amount of premium exceeding Rs. 2,50,000 in any of the previous years during the term of any such ULIP(s), in a case where premium is payable by a person for more than one ULIP issued on or after 01.02.2021.

However, the following assets are **EXCLUDED** from the definition of 'Capital Assets'.
a) Stock in trade (other than securities referred to in point (b) above), consumable stores or raw material held for the purpose of business or profession.
b) Agricultural land in rural area in India.

c) Items of personal effects, i.e., moveable property (including wearing apparel and furniture) held for personal use (including the use by any dependant family member).

However, the following are not ‘personal effects’. In other words, the following are ‘capital assets’, even if these are for personal use:

1) Jewellery,

2) Archaeological collections,

3) Drawings, paintings, sculpture or any work of art.

d) A few gold bonds and special bearer bonds (this point does not have any practical utility).

e) Gold Deposit bonds issued under Gold Deposit Scheme, 1999 or deposit certificates issued under the Gold Monetisation Scheme, 2015 and Gold Monetisation Scheme, 2018 notified by the Central Government.

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3. Key Terms

There are two types of capital assets – short term and long term.

The new provisions for taxation of capital gains come into force from 23.7.2024 and shall apply to any transfer made on or after 23.7.2024. These provisions are given below.

Prior to July 2024

Prior to amendment introduced by Budget 2024, if 'Period of Holding' is more than 36 months, the capital asset is long term, otherwise it is short term. However, in the following cases, the capital asset held for more than 12 months was treated as long-term capital assets:

- Listed Equity or Preference shares,
- Securities like debentures, government securities, which are listed in recognised stock exchange,
- Units of UTI
- Units of Equity Oriented Mutual Funds
- Zero Coupon Bonds

Moreover, unlisted equity / preference shares (from AY 2017-18) and immovable property (being land/ building) (from AY 2018-19) held for more than 24 months were treated as Long Term Capital Assets.

This means that earlier there were 3 holding period for considering an asset to be a long- term capital asset.

After July 2024

Now the holding period has been simplified. There are only two holding periods - for listed securities, it is one year, for all other assets, it is two years.

The holding period of all listed assets will be now one year. Therefore, for listed units of business trusts (ReITs, InVITs) holding period is reduced from 36 months to 12 months. The holding period of gold, unlisted securities (other than unlisted shares) is also reduced from 36 months to 24 months. The holding period of immovable property and unlisted shares remains the same as earlier i.e. 24 months.

Accordingly, the new definition of 'Short Term Capital Asset' and 'Long-term Capital Asset' is as follows:

A. *Short Term Capital Asset*

Capital asset held for not more than 24 months (36 months if the transfer takes place before 23-07-2024) immediately prior to the date of transfer shall be deemed as short-term capital asset. However, the following assets held for not more than 12 months shall be treated as short-term capital assets:

(a) Equity or preference shares in a company which are listed in any recognized stock exchange in India;
(b) Other listed securities;
(c) Units of UTI;
(d) Units of equity oriented funds; or
(e) Zero Coupon Bonds.

B. *Long Term Capital Asset*

Capital Asset that held for more than 24 months (36 months if the transfer takes place before 23-07-2024) or 12 months, as the case may be, immediately preceding the date of transfer is treated as long-term capital asset.

3. Key Terms

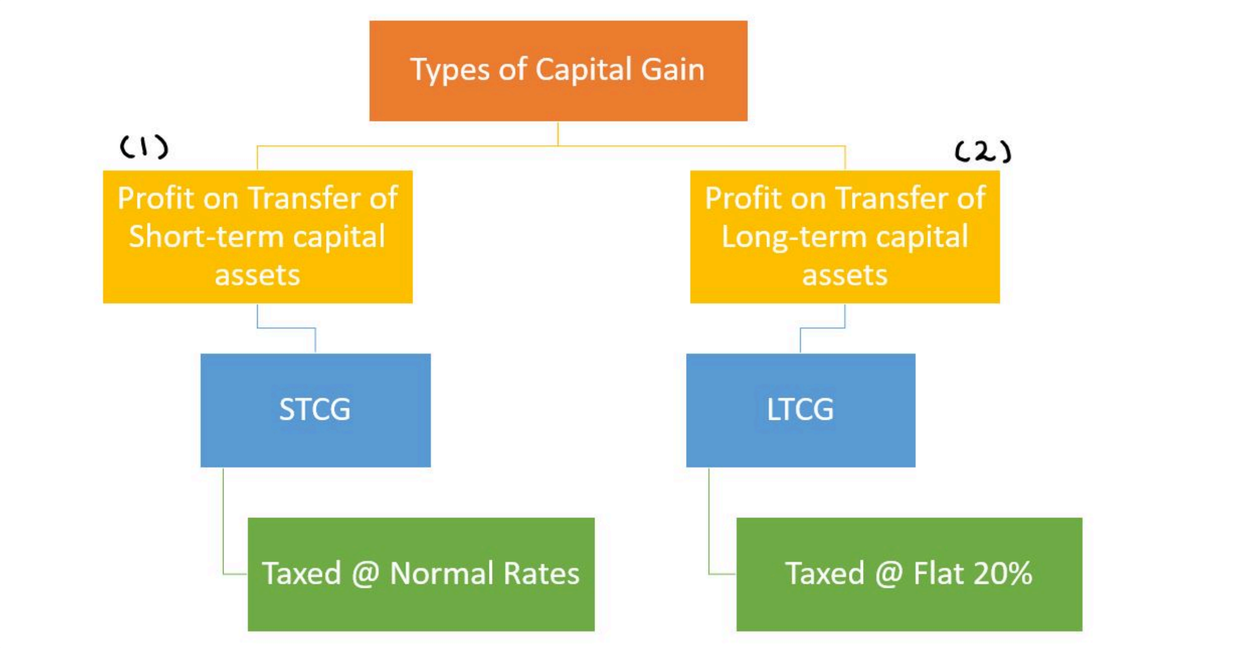
State giving reason, whether the asset is short term or long term in the cases given below:
1) X purchases a house property on March 10, 2023 and transfers it on June 6, 2024.
2) Y purchases listed shares in an Indian company March 10, 2023 and transfers it on June 6, 2024.
3) Z acquires units of an equity oriented mutual fund on July 7, 2023 and he transfers these units on July 10, 2024.
4) A purchases diamonds on September 12, 2021 and gifts the same to his friend B on December 31, 2022. B transfers the asset on October 20, 2024.
5) C purchases unlisted shares in a company on November 21, 2022; the company transfers shares in the name of C: January 5, 2023. These shares are transferred by C on December 20, 2024.

Solution:

Taxpayer	**Asset**	**Minimum Period to become Long-term capital asset**	**Period of holding**	**Short-term/long term**
X	House Property	24 months +	March 10, 2023 to June 6, 2024 (i.e. 14 months & 28 days)	Short-term
Y	Listed Shares	12 months +	14 months & 28 days	Long-term
Z	Units of Equity oriented MF	12 months +	12 months & 4 days	Long-term
B	Diamonds	36 months +	September 12, 2021 to October 20, 2024	Long-term
C	Unlisted Shares	24 months +	November 21, 2022 to December 20, 2024	Long-term

Notes:
1. If an asset is acquired by gift, will etc., then the period of holding of the previous owner is also taken into consideration.
2. In the case of shares, the purchase date by the broker is taken as the date of acquisition.

3. Key Terms

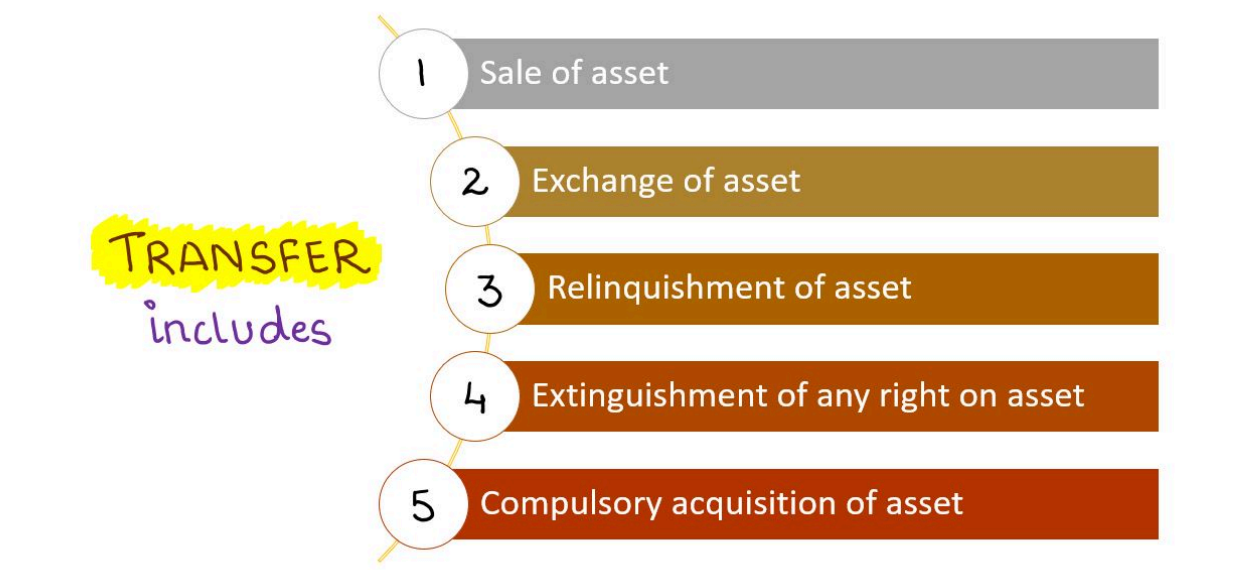


The tax incidence under the head 'Capital Gains' depends upon whether the capital gain is short-term or long term. The profit on transfer of STCA (Short Term Capital Asset) is treated as **Short Term Capital Gains** (STCG) while that on LTCA (Long Term Capital Asset) is known as **Long Term Capital Gains** (LTCG).

While calculating tax, the STCG is included in Total Income and taxed as per normal rates while LTCG is taxable at a flat rate of 20%. Further, in case of transfer of depreciable asset (other than power generating units eligible for depreciation on SLM basis), capital gain (if any) is taken as short-term capital gain, irrespective of period of holding.

3. Key Terms

Transfer, in relation to a capital asset, includes sale, exchange or relinquishment of the asset or extinguishments of any right therein or the compulsory acquisition, thereof, under any law.



In simple words, 'Transfer' includes:
(a) Sale of asset,
(b) exchange of asset,
(c) relinquishment of asset (means surrender of asset),
(d) extinguishments of any right on asset (means reducing any right on asset), and
(e) compulsory acquisition of asset.

3. Key Terms

Assets of a company distributed to its shareholders on liquidation

Distribution of capital assets on partition of HUF

Transfer under a gift or will

Transfer of CA from a company to its wholly owned Indian subsidiary company

Transfer of CA by a subsidiary Company to its 100% holding company, being an Indian Company

Transfer of CA from amalgamating to amalgamated Indian company

Transfer from demerged company to the resulting Indian company

Transfer or issued of shares by a resulting company, in a scheme of demerger

Transfer of shares by a shareholder in a scheme of amalgamation

Transfer on conversion of bonds or debentures etc. into shares or debentures

Conversion of preference shares into equity shares

Transfer of capital assets under reverse mortgage

Redemption of sovereign gold bonds issued by RBI, by an individual

Transfer to government any capital asset, for example-painting, drawing, any work of Art etc.

Section 47 specifies certain transactions which **will not be regarded as a transfer**, as given below:
1) Distribution of assets in kind by a company to its shareholders on its liquidation.
2) Any distribution of capital assets on total / partial partition of HUF.
3) Any transfer of a capital asset under a gift / will / irrevocable trust (doesn't include ESOPs).
4) Transfer of asset between Holding Company to its wholly owned Indian Subsidiary Company.
5) Transfer of capital asset in the scheme of amalgamation/ demerger, if the transferee company is an Indian Company.
6) Transfer of shares in amalgamating company/ demerged company in lieu of allotment of shares in amalgamated company/ resulting company, in the above case.
7) Transfer of capital asset in a scheme of amalgamation of a banking company with a banking institution.
8) Transfer of shares in an Indian Company held by a foreign company to another foreign company in a scheme of amalgamation/ demerger of two foreign companies, if a few conditions are satisfied.
9) Transfer of capital asset by a non-resident of foreign currency convertible bonds or Global Depository Receipts to another non-resident, if the transfer is made outside India and if a few conditions are satisfied.
10) Transfer by way of redemption of sovereign gold bonds, issued by RBI, by an individual.
11) Transfer of any capital asset (work of art, book, manuscript, drawing, painting, photograph or print) to the Government / University / National Museum / National Art Gallery.
12) Transfer by way of conversion of bonds / debentures / debenture stock into shares or debentures of that Company.
13) Transfer by way of conversion of preference shares of a company into equity shares of that company.
14) Land transferred by a sick industrial company, if a few conditions are satisfied.
15) Transfer of capital asset by a private company / unlisted public company to a limited liability partnership, in the case of conversion of company into LLP, if a few conditions are satisfied.
16) Transfer of capital assets at the time of conversion of a firm/ sole proprietary concern in a company, if a few conditions are satisfied.
17) Any transfer involved in a scheme for lending of any securities, if a few conditions are satisfied.
18) Any transfer of capital asset in a reverse mortgage.
19) Transfer of capital asset, being government security carrying periodic payment of interest, outside India, by a non-resident to another non-resident.
20) Transfer of a capital asset, being share of a special purpose vehicle, to a business trust, in exchange of units allowed by that trust to the transferor.
21) Transfer by a unit holder under consolidation plans / schemes of Mutual Fund.
22) Transfer by a unitholder of units held by him in the consolidating plan of a mutual fund scheme, made in consideration of the allotment to him of units, in the consolidated plan of that scheme of the mutual fund.
23) Transfer, made outside India, of a capital asset, being rupee denominated bond of an Indian company issued outside India, by a non-resident to another non-resident.

24) Transfer of capital asset (being bonds/ GDR referred to in Sec. 115AC(1) or rupee denominated bond of an Indian company or derivative) made by a non-resident on a recognized stock exchange located in international financial services centre and where the consideration is paid/payable in foreign currency.

Amendment

Section 47 has been amended **vide Finance Act 2023** to provide that conversion into EGR (Electronic Gold Receipt) or EGR into gold shall not be regarded as transfer for the purpose of computing capital gains.

Also, the said section has been amended to provide that any transfer of a capital asset (being an interest in a joint venture held by a public sector company) in exchange of shares in a company incorporated outside India by a foreign Government, will not be treated as "transfer" for the purpose of computation of capital gain.

"Joint venture" shall mean a business entity, as may be notified by the Central Government.

3. Key Terms

State giving reasons whether the capital gain is taxable in the following cases:
1. A house property is purchased by a Hindu undivided family in 1950 for Rs. 40,000. It is given to one of the family members in 2023-24 at the time of partition of the family.
2. Y purchases gold in 1974 for Rs. 10,000. In 2023-24, it is gifted to his son at the time of his marriage.
3. Z purchases 10 convertible debentures in 1987 which are converted into 100 shares in 2023 by the company.
4. A Ltd. is 100% holding company of B Ltd. A Ltd. transfers a capital asset (acquired in 1987 for Rs. 50,000) to B Ltd. on June 16, 2023 for Rs. 2,70,000. B Ltd. is an Indian company, while A Ltd. is a foreign company. The capital asset is transferred as capital asset.
5. Suppose in 4 above, the capital asset is transferred as stock in trade.

Solution:

Case	Treatment
1	Distribution of a capital asset by a Hindu undivided family to its members at the time of partition is not treated as transfer. As the element of transfer is missing, capital gain is not chargeable to tax.
2	Transfer by way of gift is not treated as transfer, therefore, no capital gain tax liability arises in the case of gift.
3	No capital gains tax liability will arise in the case of conversion of bonds into shares, as such conversion is not treated as transfer.
4	Any transfer between a holding company and 100% subsidiary company is not treated as transfer, if the transferee company is an Indian company. In this case, therefore, the element of transfer is missing and hence capital gains tax liability does not arise.
5	The rule stated in 4 above is not applicable, if a capital asset is transferred as a stock in trade, therefore in this case, capital gain is chargeable to tax.

3. Key Terms

Cost Inflation Index is calculated to match the prices to the inflation rate. In simple words, an increase in the inflation rate, over a period of time, will lead to an increase in the prices. Prices of goods increase over the time, resulting in a fall in the purchasing power (quantity of goods that one unit of money can buy) of money.

For example, if 2 units of goods could be bought for Rs. 100 today, tomorrow only 1 unit might be available for Rs. 100 due to increasing inflation. Cost Inflation Index (CII) is used for calculating the estimated increase in the prices of goods and assets year-by-year due to inflation.

The Central Government specifies the cost inflation index, by notifying in the official gazette. Initially, 1981-82 was considered as the base year. But, taxpayers were facing hardships in getting the properties valued, which were purchased before 1st April, 1981. Tax authorities were also finding it difficult to rely on the valuation reports. Hence, the government decided to shift the base year to 2001 so that valuations can be done quickly and accurately.

The current cost inflation index is as follows:

S. No	Financial Year	Cost Inflation Index
1	2001-02 (base year)	100
2	2002-03	105
3	2003-04	109
4	2004-05	113
5	2005-06	117
6	2006-07	122
7	2007-08	129
8	2008-09	137
9	2009-10	148
10	2010-11	167
11	2011-12	184
12	2012-13	200
13	2013-14	220
14	2014-15	240
15	2015-16	254
16	2016-17	264
17	2017-18	272
18	2018-19	280
19	2019-20	289
20	2020-21	301
21	2021-22	317
22	2022-23	331
23	2023-24	348
24	2024-25	363

The Capital gain arises when the net sale consideration of a capital asset is more than the cost. Since ‘cost of acquisition’ is historical, the concept of indexed cost allows the taxpayer to factor in the impact of inflation on cost. Consequently, a lower amount of capital gains is taxed, as compared to the computation using historical cost.

Formula for computing indexed cost is:

$$\frac{\text{Index for the year of sale}}{\text{Index in the year of acquisition}} \times \text{Cost}$$

Let us understand this with the help of an example. If a property purchased in 2007-08 for Rs 20 lakh were to be sold in 2022-23 for Rs 80 lakh, indexed cost = (331/129) × 20 = Rs 51.31 lakh. And the long-term capital gains would be Rs. 28.69 Lakhs, that is, Rs 80 lakh minus Rs 51.31 lakh.

3. Key Terms

Difference between Short-Term and Long-Term Capital Gain is tabled below.

Short-term capital gain	Long term capital gain
Short-term capital gain is the profit or gain arising on transfer of Short-term capital assets, i.e., those capital assets which are held by an assessee for not more than 36 months (or 12 months for shares etc.) immediately preceding the date of their transfer.	Long-term capital gain is the gain arising on transfer of Long-term capital assets, i.e., those capital assets which are held by an assessee for more than 36 months immediately preceding the date of their transfer.
Cost of Acquisition has to be deducted from Full value of consideration.	Indexed Cost of Acquisition has to be deducted from Full value of consideration.
Cost of Improvement has to be deducted from Full value of consideration.	Indexed Cost of Improvement has to be deducted from Full value of consideration.
Exemptions are available u/s 54B/54D/54G/54GA.	Exemptions are available u/s 54/54B/54D/54EC/54EE/54F/54G/54GA/54GB.

4. Computation of Capital Gains

Mode of Computation of Capital Gains is provided under Section 48 of the Income Tax Act 1961. The capital gain can be computed by subtracting the cost of capital asset from its transfer price, i.e., the sale price.

The computation can be made by making a following simple statement.

Statement of Short-term Capital Gains

Particulars	Amount
Full Value of Consideration	XXX
Less: Expenditure on transfer (wholly & exclusively)	XX
Cost of Acquisition (COA)	XX
Cost of Improvement (COI)	XX
Gross ST Capital Gains	XXX
Less: Exemption u/s 54B/ 54D/54G/54GA	XX
Taxable ST Capital Gains	XXX

Statement of Long-term Capital Gains

Particulars	Amount
Full Value of Consideration	XXX
Less: Expenditure on transfer (wholly & exclusively)	XX
Indexed Cost of Acquisition (COA)	XX
Indexed Cost of Improvement (COI)	XX
Gross LT Capital Gains	XXX
Less: Exemption u/s 54/54B/ 54D/54EC/55EE/54F/54G/54GA/54GB	XX
Taxable LT Capital Gains	XXX

* Short-term capital gain or loss from sale of depreciable asset will arise only in the following two situations:
(a) When on last day of the previous year, WDV of the block of asset is nil; or
(b) When on last day of the previous year, block ceases to exist.

Note 1: Indexed Cost of Acquisition and Improvement: In case of transfer of long-term capital assets, before 23-07-2024* indexed cost of acquisition and indexed cost of improvement shall be deducted from the full value of consideration.

Note 2: The Finance Act, 2024 removed the indexation benefit and introduced a uniform tax rate of 12.5% on long-term capital gains. As per the amendment, no indexation benefit is allowed while computing capital gain from long-term capital assets transferred on or after 23-07-2024. However, the Government has introduced a grandfathering provision. This provision allows resident individuals and resident HUFs to still apply indexation on land or building acquired before 23-07-2024 and pay tax at the old rate of 20% if the tax under the new law (i.e., tax calculated at 12.5% without indexation benefit) results in a higher amount.

4. Computation of Capital Gains

Full value of consideration means & includes the whole/complete sale price or exchange value or compensation including enhanced compensation received in respect of capital asset in transfer.

The following points are important to note in relation to full value of consideration.
a) The consideration may be in cash or kind.
b) The consideration received in kind is valued at its fair market value.
c) It may be received or receivable.
d) The consideration must be actual, irrespective of its adequacy.

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4. Computation of Capital Gains

Expenditure incurred wholly and exclusively for transfer of capital asset is called expenditure on transfer. It is fully deductible from the full value of consideration while calculating the capital gain.

Examples of expenditure on transfer are the commission or brokerage paid by seller, any fees like registration fees, cost of stamp papers, travelling expenses, litigation expenses incurred for transferring the capital assets etc. Expenditure incurred by buyer at the time of buying the capital assets like brokerage, commission, registration fees, cost of stamp paper etc. are to be added in the cost of acquisition before indexation.

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4. Computation of Capital Gains

Cost of Acquisition (COA) means any capital expense at the time of acquiring capital asset under transfer, Expenses of capital nature, for completing or acquiring the title, are included in the cost of acquisition. Interest on money borrowed to purchase asset is part of actual cost of asset. The amount paid for discharge of mortgage is part of 'cost of acquisition', if the mortgage was not created by the transferor.

Note: Section 48 provides that the income chargeable under the head "Capital gains" shall be computed, by deducting the cost of acquisition/cost of improvement from the full value of the consideration received or accruing as a result of the transfer of the capital asset. Interest on capital borrowed for the purpose of financing acquisition, construction/reconstruction/renewal of house property is deductible under section 24(b).

One can have double deduction of interest paid on borrowed capital for acquiring (or renewing or reconstructing, etc.) a property. Firstly, it is claimed in the form of deduction under section 24(b) from the income from house property. Secondly, while computing capital gains on transfer of such property the same interest also forms a part of cost of acquisition/cost of improvement under section 48.

In order to prevent this double deduction, section 48 has been amended **with effect from the assessment year 2024-25** to provide that the cost of acquisition or the cost of improvement shall not include the amount of interest claimed as deduction under section 24 or Chapter VIA.

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4. Computation of Capital Gains

For computing long-term capital gains, knowledge of '**cost inflation index**' is necessary. The capital gains will be computed after deducting the indexed cost of acquisition (purchase) from the full value of consideration. The cost of purchase of the asset will be increased by applying the Cost Inflation Index (CII). Once the cost inflation index is applied to the cost of acquisition, it becomes indexed cost of acquisition. In computing capital gains arising from the transfer of a long-term capital asset, deduction can be claimed for the cost of acquisition and the cost of improvement, after indexing them.

Indexed Cost of Acquisition means an amount which bears to the cost of acquisition, the same proportion as CII for the year in which the asset is transferred bears to the CII for the first year in which the asset was held by the assessee, or for the year beginning on 1st April, 2001, whichever is later.

If the asset has been acquired prior to 1.4.2001

Indexed Cost of acquisition

$$\underbrace{\text{Fair market value of asset on April 1, 2001 or COA}}_{\text{Whichever is more}} \times \frac{\text{CII of Year of transfer}}{\text{CII of year 2001-02}}$$

If the asset has been acquired on or after 1.4.2001

Indexed Cost of acquisition

$$\text{COA} \times \frac{\text{CII of Year of transfer}}{\text{CII of year 2001-02}}$$

If capital assets were acquired before 1.4.2001, the assessee has the option to have either actual cost of acquisition or fair market value as on 1.4.2001, as the cost of acquisition. If assessee chooses the value as on 1.4.2001, then the indexation will also be done as per the CII of 2001 and not as per the year of acquisition.

When Benefits of Indexation not available

Benefit of Indexation is not available in the cases given below, even if long-term capital asset is transferred:

Sl. No.	Capital Assets	Transferor
1	Bonds or debentures (other than capital indexed bonds issued by the Government or Sovereign Gold Bond issued by RBI)	Any person
2	Shares and Debentures in Indian Company acquired by utilizing convertible foreign exchange	Non-Resident
3	Equity share in a company or a unit of equity oriented Mutual Fund or a unit of a business trust	Any person
4	Depreciable asset (other than an asset used by a power generating unit eligible for depreciation on straight line basis)	Any person

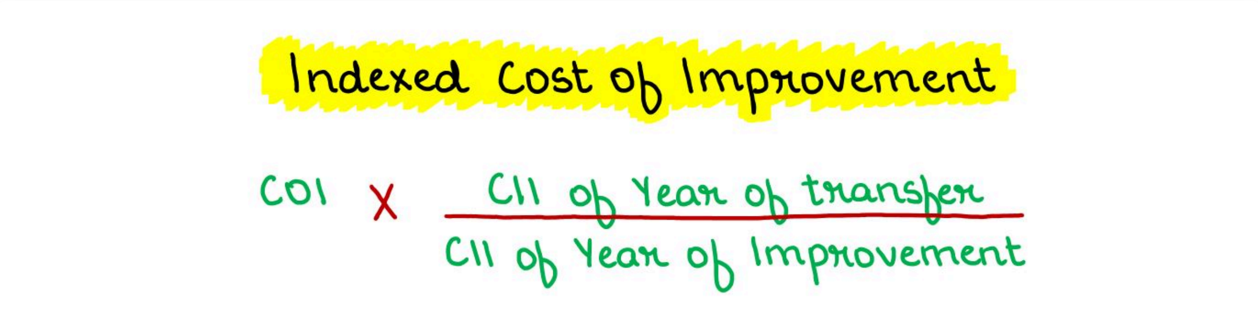
5	Undertaking/division transferred by way of slump sale	Any person
6	Units purchased in foreign currency as given in Section 115AB	Offshore Fund
7	Global Depository Receipts (GDR) purchased in foreign currency as given in Section 115AC	Non- resident
8	Global depository receipts (GDR) purchased in foreign currency as given in Section 115ACA	Resident Individual
9	Securities as given in Section 115AD	FIIs (Foreign Institutional Investors)

4. Computation of Capital Gains

Cost of Improvement (COI) is the capital expenditure incurred by an assessee for making any addition or improvement in the capital asset. It also includes any expenditure incurred in protecting or curing the title. In other words, cost of improvement includes all those expenditures, which are incurred to increase the value of the capital asset.

4. Computation of Capital Gains

Indexed Cost of Improvement (COI) means an amount which bears to the cost of improvement, the same portion as cost inflation index, for the year in which the asset is transferred, bears to the cost inflation index, for the year in which the improvement to asset took place.



Any cost of improvement incurred before 1st April, 2001 is not considered or it is ignored. The reason behind it is that, for carrying any improvement in asset before 1st April, 2001, asset should have been purchased before 1st April, 2001.

If asset is purchased before 1st April, 2001, we consider the fair market value. The fair market value of asset on 1st April, 2001, will certainly include the improvement made in the asset.

5. Capital gain in Special Cases

There are certain cases in which the method of computation is different. Let us discuss few significant cases (and not all) one by one.

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5. Capital gain in Special Cases

If a person has acquired a capital asset in the following circumstances, then, to calculate capital gain at the time of transfer of such asset, cost to the previous owner is taken as COA.
a) Acquisition of property **on any distribution of assets** on the total/ partial partition of an HUF;
b) Acquisition of property **under a gift or will**;
c) Acquisition of property:

1. By **succession**, inheritance or devolution; or
2. On any **distribution of assets** on the dissolution of firm, BOI or AOPs, where such dissolution had taken place before 01.04.1987; or
3. On **distribution of assets** on liquidation of a company; or
4. Under a transfer to a **revocable / irrevocable trust**; or
5. By a wholly-owned Indian **subsidiary company from its holding company**; or
6. By an **Indian holding company from its wholly-owned subsidiary** company; or
7. Under a scheme of **amalgamation/demerger**
8. Under a scheme of **conversion of private company**/unlisted company into LLP; or
9. On transfer in the case of **conversion of firm**/sole-proprietary concern into company.

d) Acquisition of property, **by an HUF**, where one of its members has converted his self-acquired property into joint family, after 31.12.1969.

For example, X purchases a capital asset in November 2024 for Rs. 40,000. He transfers this asset to his friend, Y, by gift during December 2024. Y dies during March 2025 and the asset is transferred by his will to Mrs. Y. Mrs. Y transfers this property during June 2025 for a consideration of Rs. 90,000. To calculate capital gain in the hands of Mrs. Y, COA of the capital asset to X (i.e. Rs. 40,000) will be considered and capital gain will be Rs. 50,000.

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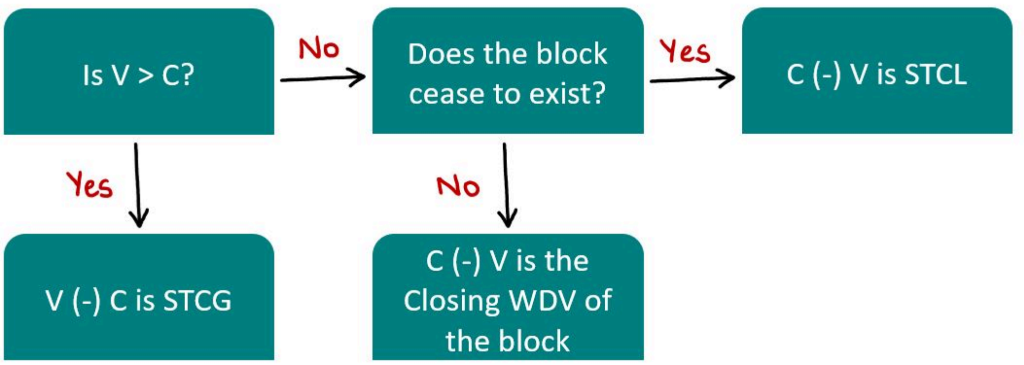
5. Capital gain in Special Cases

Mr. E purchased a house on 28.06.2008 for Rs. 4,10,000 and paid Rs. 10,000 for getting the property registered in his name. On 15.06.2009, he spent Rs. 1,80,000 on improvement of the house. The house was sold on 21.10.2024 for Rs. 25,00,000. Commission of Rs. 45,000 was paid on the sale of the house. Compute the capital gain. CII for financial year 2008-09, 2009-10 and 2024-25 is 137, 148 and 363, respectively.

Solution:

Computation of Capital Gain	**(Amt. in Rs.)**	
Sale consideration		25,00,000
Less: 1. Expenses on transfer	45,000	
2. Indexed cost of acquisition (420000 × $\frac{363}{137}$)	11,12,847	
3. Indexed cost of improvement (180000 × $\frac{363}{148}$)	4,41,486	15,99,333
Long Term Capital Gain		**9,00,667**

5. Capital gain in Special Cases



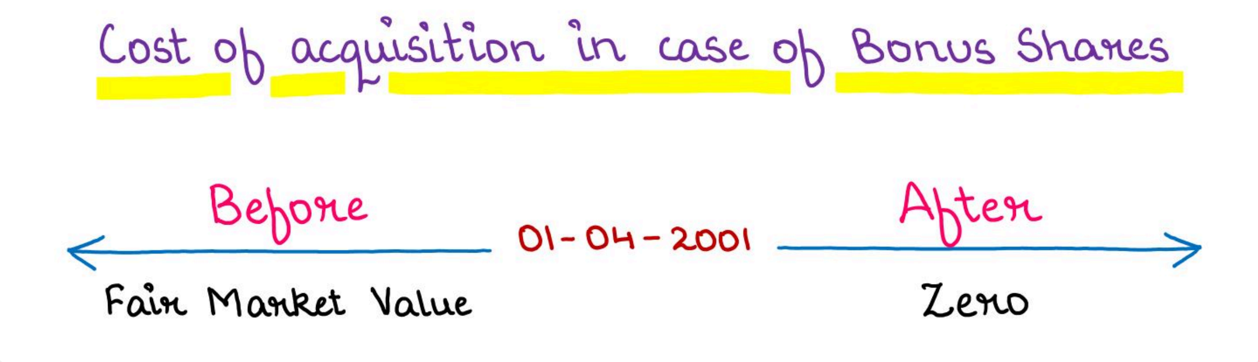
V	Full value of consideration
C	Opening WDV of Block (+) Actual Cost of Asset acquired in the Block during the P.Y. (+) Expenses in connection with transfer of asset
STCG	Short-term Capital Gain
STCL	Short-term Capital Loss
WDV	Written Down Value

If a depreciable asset is transferred, capital gain or loss under the head capital gains shall be calculated only in two cases:
(a) When the WDV of the block of assets on the last day of the previous year becomes *zero*.
(b) When the block of assets becomes empty on the last day of the previous year.

Only in these two cases, capital gain (loss) arises on the transfer of a depreciable asset. COA, in such case, will be the depreciated value of the block of assets on the first day of the previous year plus actual cost of assets (falling in the same block of assets) acquired at any time during the previous year. Further, capital gain or loss, which arises on transfer of depreciable assets, is always taken as short-term capital gain/loss.

5. Capital gain in Special Cases

If bonus shares were allotted before April 1, 2001, COA is the fair market value on April 1, 2001. If bonus shares are allotted after April 1, 2001, COA is taken as **zero**.



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5. Capital gain in Special Cases

In the case of transfer of self-generated goodwill of a business, right to manufacture/ produce an article/thing or right to carry on business, the COA and COI are taken as *nil*. On transfer of any other self-generated asset, capital gain is always **zero**. If capital asset, being goodwill of a business, right to manufacture/ produce an article/ thing or right to carry on business, is purchased, then at the time of transfer, cost of improvement is taken as **nil** (means where these assets have been purchased, then COA will be taken as actual cost of acquisition).

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5. Capital gain in Special Cases

Amount realized by an existing shareholder by selling rights entitlement (i.e., right to acquire additional shares in the company at a pre-determined price) is taxable in the year of transfer of the right entitlement. COA of right entitlement is always taken as *zero* and the capital gain is deemed as STCG.

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6. Exemptions from Capital gains

Exemption means a reduction from the taxable amount of capital gain, on which tax will not be levied and paid. The exemptions are given under Section 54. It is to be noted that the aggregate amount of exemption cannot exceed the quantum of capital gain.

Exemption under section 10

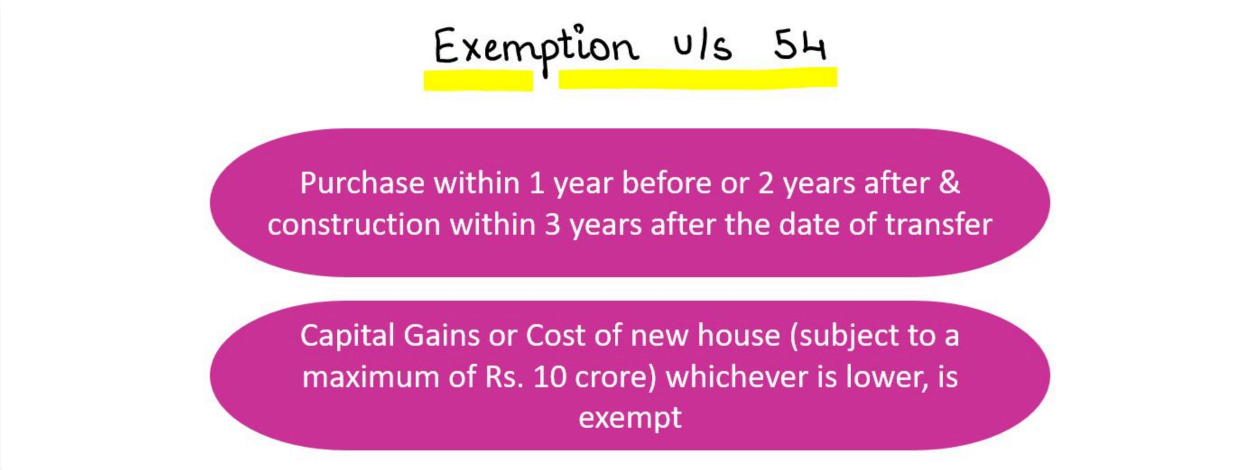
With a view to mitigate the hardship faced by the farmers whose agricultural land situated in specified urban limits has been compulsorily acquired, section 10(37) exempts the capital gains arising to an individual or a HUF from transfer of agricultural land by way of compulsory acquisition.

Such exemption is available, where the compensation or the enhanced compensation or consideration, as the case may be, is received on or after 01.04.2004.

The exemption is available only when such land has been used for agricultural purposes during the preceding 2 years immediately preceding the date of transfer by such individual or a parent of his or by such HUF.

6. Exemptions from Capital gains

The exemption u/s 54 relates to the capital gain arising out of transfer of residential house. The exemption is available to only Individual assessee or HUF. The exemption relates to the capital gains arising on the transfer of a residential house.



Conditions for exemption

Exemption is available if:

a) House Property transferred was used for residential purpose.

b) House Property was a long-term capital asset.

c) The assessee has purchased another house property within a period of 1 year before or 2 years after the date of transfer or has constructed another house property within 3 years of date of transfer, i.e., the construction of the new house property should be completed within 3 years. The date of starting of construction is irrelevant.

d) The new residential house should be in India.

e) The amount of exemption for the long-term capital gain shall be *lower of the following*:

1. Capital gains arising on transfer of residential house, or

2. Investment made in purchase or construction of a new residential house property. Hence, the balance capital gains (if any) will be taxable.

However, where the amount of the capital gain does not exceed Rs. 2 crore, the assessee, may at his option, purchase or construct 2 residential houses in India.

Further, where during any AY, the assessee has exercised the option of 2 houses referred above, he shall not be subsequently entitled to exercise the option for the same or any other assessment year. Therefore, now the exemption can be claimed for purchase/construction of 2 residential houses instead of one (from the AY 2020-21). The benefit is available only when the capital gain does not exceed Rs. 2 crore. Further, this benefit is available only once in a lifetime. The new house property should not be transferred within 3 years from the date of its acquisition.

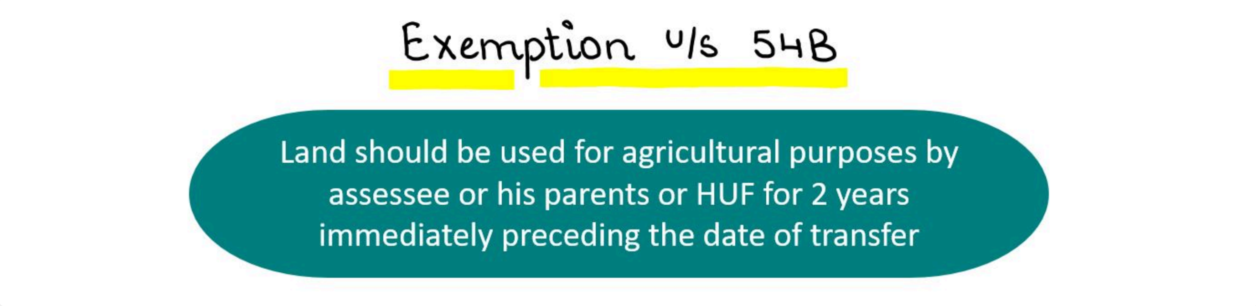
Quantum of Exemption is the actual amount invested in new asset or capital gain, whichever is less.

Amendment

With effect from 1st April 2023 **(i.e., A.Y. 2024-25)**, maximum deduction allowed under Section 54 has been capped to Rs. 10 crore and consequently the cost of the new asset will be limited to Rs. 10 Crore.

6. Exemptions from Capital gains

Section 54B gives relief to a taxpayer who sells his agricultural land and from the sale proceeds, he acquires another agricultural land. The benefit of Section 54B is available only to an individual or a HUF.



Conditions for Exemption
Following conditions should be satisfied to claim the benefit of Section 54B.
1) The asset transferred should be agricultural land.
2) The land may be a long-term capital asset or short-term capital asset.
3) The agricultural land should be used by the individual or his parents for agricultural purpose, at least for a period of 2 years, immediately preceding the date of transfer. In case of HUF, the land should be used by any member of HUF.
4) Within a period of 2 years, from the date of transfer of old land, the taxpayer should acquire another agricultural land (may be in rural area or urban area).

The **quantum of exemption** is the actual amount invested in new asset or capital gain, whichever is less.

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6. Exemptions from Capital gains

Exemption under Section 54D is allowed, provided the assessee has Capital Gains on Compulsory Acquisition of Industrial Undertaking. It is available to all assessees.

Conditions for Exemption
Following conditions must be satisfied to avail this exemption:
a) The assessee should have invested the amount in Land and Building for the purpose of Industrial Undertaking within a period of 3 years after the date of Payment by Government.
b) The assessee should have been using such Land and Building for the purpose of Industrial Undertaking for a period of at least 2 years, at the time of Acquisition.
c) The Land and Building, so purchased, should not be transferred for a period of at least 3 years.

The **quantum of exemption** is the actual amount invested in new asset or capital gain, whichever is less.

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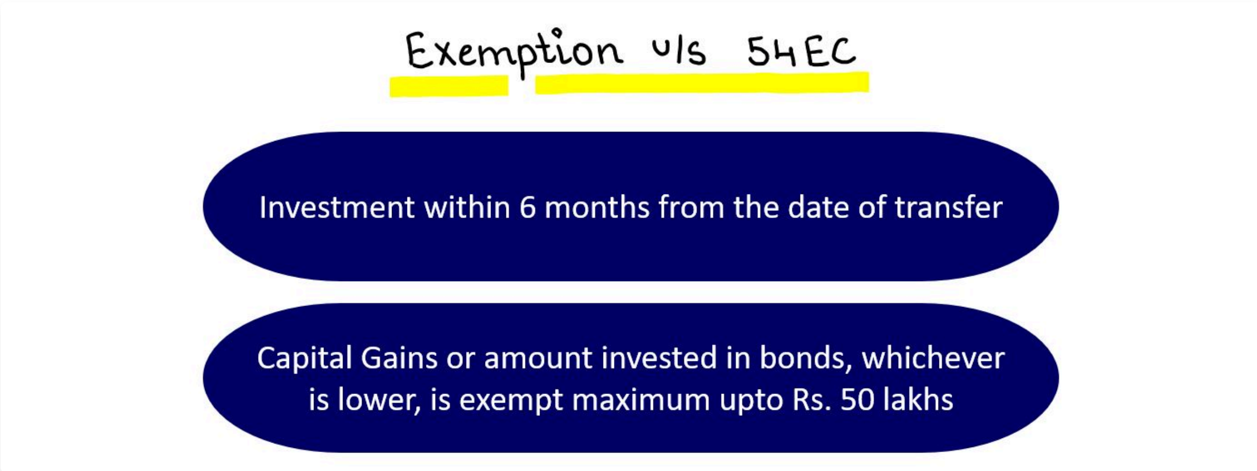
6. Exemptions from Capital gains

These exemptions are available, in case, the capital gain is invested in specified securities including government securities, saving certificates, units of UTI, specified debentures, etc. It is available to any assessee. The investment should be made within 6 months from the date of transfer.

6. Exemptions from Capital gains

Exemption under Section 54EC of the Income Tax Act, 1961 is available to any assessee, in case the long-term capital gain is invested into the long term specified assets. Long term specified assets means any bond redeemable after a period of 5 years from financial year 2018-19. The said bonds should have been issued on or after 1st April, 2000.

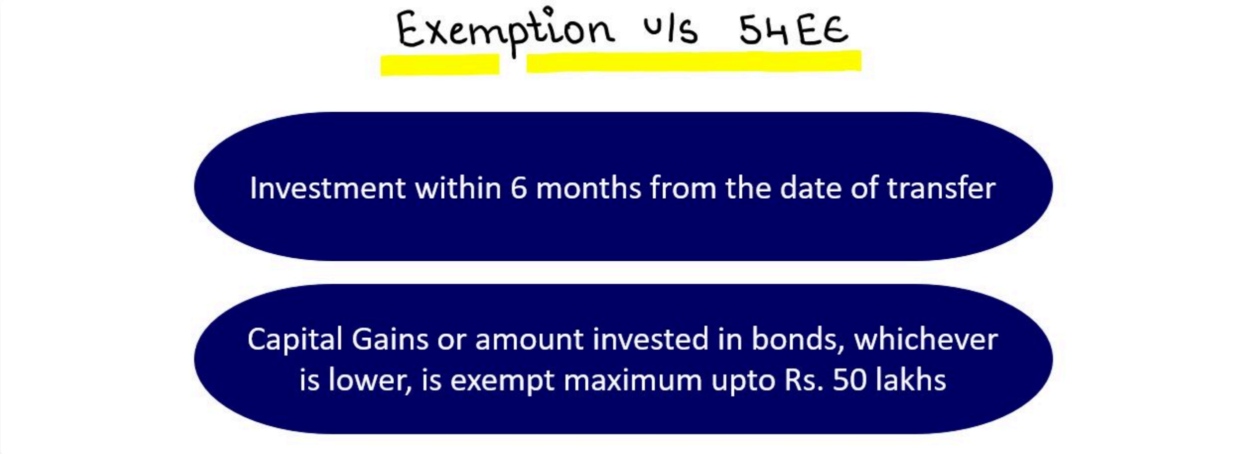


Qualifying bonds are listed hereunder:
a) Bonds issued by the National Bank for Agriculture and Rural Development, established under Section 3 of the National Bank for Agriculture and Rural Development Act, 1981
b) Bonds issued by the National Highways Authority of India, constituted under Section 3 of the National Highways Authority of India Act, 1988
c) Bonds issued by Rural Electrification Corporation
d) Bonds issued by Power Finance Corporation Limited (Government has notified that said bonds should be issued on or after 15th June, 2017)
e) Bonds issued by Indian Railway Finance Corporation (Government has notified that said bonds should be issued on or after 8th August, 2017)

Exemption is available under Section 54EC of the Income Tax Act to the extent of capital gain as invested in long term specified assets. However, the maximum limit is Rs. 50 Lakhs. The new asset should not be transferred within 5 years. Moreover, the new asset should not be converted into money or any loan or advance should not be taken on the security of the new asset, within 5 years from the date of acquisition of the new asset. The time-limit for acquiring new asset is 6 months from the date of transfer.

The **quantum of exemption** is the actual amount invested, subject to maximum of Rs. 50 Lakhs per financial year, in new asset or capital gain, whichever is less.

6. Exemptions from Capital gains

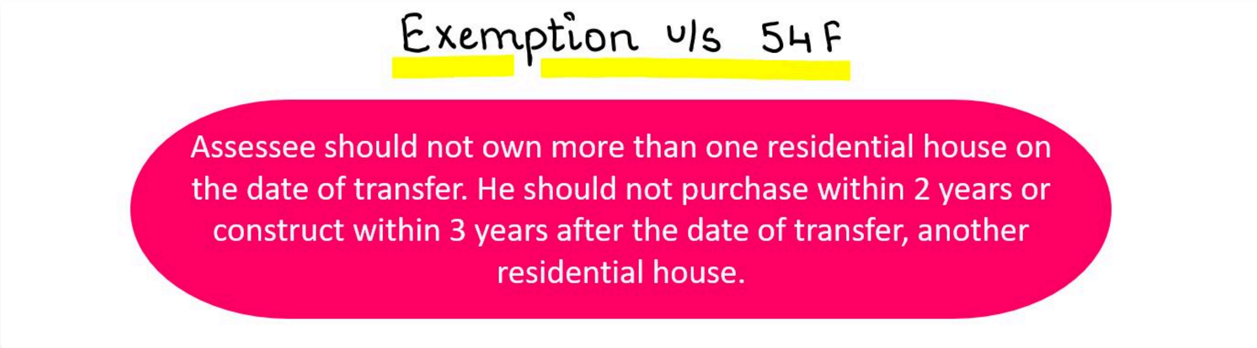


This exemption is available to any assessee, on satisfaction of following conditions:
a) The assessee has transferred a long-term capital asset
b) Investment of Long-term Capital Gain (whole or any part) in long-term specified assets (to be notified by Government to finance start-ups in India)
c) Within 6 months from date of transfer of original asset
d) The amount of such investment (made on or after April 1, 2016) during any financial year cannot exceed Rs. 50 Lakhs.

The quantum of exemption, in such case, is the entire LTCG or amount invested in the bonds, whichever is lower. Units so acquired should not be transferred for a period of 3 years, and if that happens before 3 years, the capital gain exempted earlier, shall be taxed as long-term capital gain in that year. Moreover, the new asset should not be converted into money, or any loan or advance should not be taken on the security of the new asset within 3 years from the date of acquisition of the new asset. The time-limit for acquiring new asset is 6 months from the date of transfer.

6. Exemptions from Capital gains

Under Section 54F of the Income Tax Act, 1961, exemption of capital gain is available in case of transfer of long-term capital assets, not being a residential house. The exemption under Section 54F is available only to individual and HUF. Exemption is available if capital gain has arisen on account of transfer of any long-term capital assets other than residential house.



Net consideration arisen on account of transfer of long-term capital assets has been invested as follows:
a) Net consideration has been re-invested in purchase of one residential house within a period of 1 year before the date of transfer or within a period of 2 years after the date of transfer; or
b) Net consideration has been re-invested in construction of one residential house in India within a period of 3 years from the date of transfer.

In case, where only part of the net consideration is invested in purchase / construction of residential house, then, only proportionate amount of long-term capital gain, would be exempted under Section 54F. The new asset should not be transferred within 3 years, from the date of its acquisition. Moreover, within 3 years from the date of transfer of original assets, the taxpayer should not complete construction of another residential house property and within 2 years from the date of transfer of the original assets, the taxpayer should not purchase another residential house property.

Further, exemption u/s 54F has been granted to the assessee with a view to encourage construction of one residential house. The construction/purchase of a house, other than one residential house, is not covered by Section 54F of the Act. The concession provided u/s 54F w.e.f. 1.4.2001, would not be available in a case where the assessee already owns, on the date of transfer of the original asset, more than one residential house.

The quantum of exemption is the whole of capital gain, if the cost of the new residential house is not less than net consideration.

Otherwise,

$$\text{LTCG} \times \frac{\text{Amount Invested}}{\text{Net Consideration Price}}$$

Note: With effect from 1st April 2023 **(i.e., A.Y. 2024-25)**, maximum deduction allowed under Sec 54F will be capped to Rs. 10 crore and consequently the cost of the new asset will be limited to Rs. 10 Crore.

6. Exemptions from Capital gains

Exemption is allowed, provided, the assessee has Capital Gains in connection with transfer of machinery, plant, building or land used for the business of an industrial undertaking, situated in an urban area, due to shifting from Urban area to Rural area. It is allowed to any assessee, being an industrial undertaking.

Conditions for Exemption
The conditions to be satisfied are as follows:
1) The assessee should have invested the amount in Land and Building or Plant and Machinery (Not Furniture & Fixture) in order to shift undertaking to rural area either 1 year before or 3 years after the date of transfer.
2) The asset, so purchased, should not be transferred for a period of at least 3 years.

The **quantum of exemption** is, investment in the new asset or capital gain, whichever is lower.

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6. Exemptions from Capital gains

Exemption is allowed, provided the assessee, has Capital Gains in connection with transfer of machinery, plant, building or land, used for the business of an industrial undertaking, situated in an urban area due to shifting to any Special Economic Zone (SEZ), whether developed in any urban area or any other area. It is allowed to any assessee, being an industrial undertaking.

Conditions for Exemption
The conditions to be satisfied are as follows:
a) The assessee should have invested the amount in Land and Building or Plant and Machinery (Not Furniture & Fixture) for the purpose of Industrial Undertaking either 1 year before or 3 years after the date of transfer.
b) The asset, so purchased, should not be transferred for a period of at least 3 years.

The **quantum of exemption** is, investment in the new asset or capital gain, whichever is lower.

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6. Exemptions from Capital gains

This exemption is available to individual and HUF, in connection with long-term capital gain, from the transfer of residential property (i.e. house or plot of land) which takes place during April 1, 2012 to March 31, 2017, and where investment is in eligible start-up, the residential property can be transferred up to March 31, 2021.

Conditions for Exemption

The conditions to be satisfied are as follows:

a) The amount of consideration should be utilized by the assessee before the due date of furnishing of return of income under Section 139(1).

b) The amount should be invested for subscription in equity shares of an eligible company (if the full amount is not utilized, the exemption shall be allowed proportionate to the amount so invested).

c) The amount of subscription, as share capital, is to be utilized by such eligible company, for the purchase of new asset (eligible plant & machinery), within a period of 1 year from the date of subscription in the equity shares.

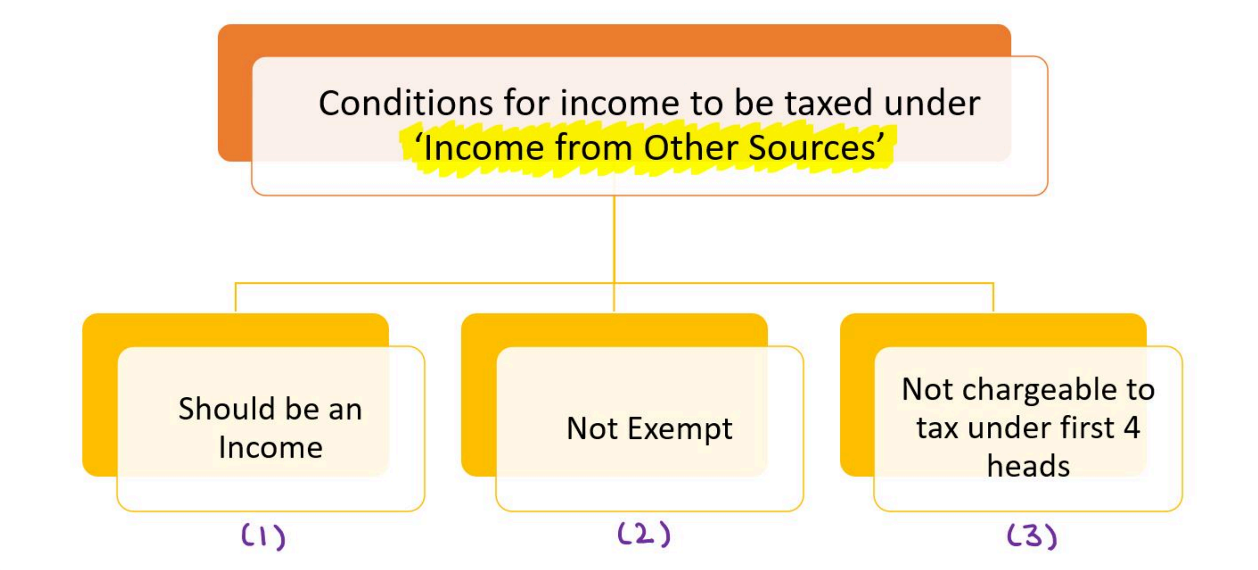
d) The equity shares of the company or the new asset acquired by the company should not be sold or otherwise transferred by the assessee or the company, as the case may be, within a period of 5 years (in case of eligible start-ups, 3 years for computer or computer software) from the date of acquisition.

If the cost of new equity shares of eligible company is not less than the net consideration, the quantum of exemption is the whole of the capital gain.

Otherwise,

$$\text{LTCG} \times \frac{\text{Amount Invested}}{\text{Net Consideration Price}}$$

1. Introduction



Income from other sources is the last and residual head of income. Hence, as per Sec. 56(1) of Income Tax Act, 1961, any income which is not specifically taxed under any other head of income, will be taxed under this head. Further, there are certain incomes which are always taxed under this head.

Following conditions must be satisfied, before it can be taxed under the head Income from Other Sources:
(a) There must be an income;
(b) Such income is not exempt under the provisions of the Income Tax Act, 1961;
(c) Such income is not chargeable to tax under any first four heads, viz., *Income from Salary*, *Income from House Property*, *Profits and Gains of Business or Profession* and *Income from Capital Gains*.