

# Basic Concept of Income Tax

## Lesson 2

### KEY CONCEPTS

■ Person ■ Assessee ■ Assessment Year ■ Previous Year ■ Average Rate of Tax ■ Maximum Marginal Rate ■ Income ■ Total Income ■ Capital Receipt ■ Revenue Receipt ■ Control and Management of Affairs ■ Place of Effective Management 'POEM'

### Learning Objectives

#### To understand:

- An overview of Finance Bill
- Some basic concepts like Assessment Year, Previous Year, Income, Person, Assessee etc.
- Distinguish between Capital and Revenue Receipts
- Basic steps in calculation of tax liability
- Concept of Residential Status
- Importance of Residential status for tax purposes
- Basis of Charge of Income Tax
- Scope of total income

### Lesson Outline

- An Overview of Finance Bill
- Important Definitions
- Person [Section 2(31)]
- Assessee [Section 2(7)]
- Assessment year [Section 2(9)]
- Previous year [Section 3]
- India [Section 2(25A)]
- Maximum Marginal Rate and Average Rate of Tax
- Income [Section 2(24)]
- Concept of Income
- Total Income [Section 2(45A)]
- Capital and Revenue Receipts
- Case Law
- Charge of Income Tax [Section 4]
- Residential Status [Section 6]
- Test of residence for Individuals
- Test of residence for HUF
- Test for residence for Firm, AOP/BOI
- Test for residence of Companies
- Place of Effective Management 'POEM'
- Scope of total Income [Section 5]
- Income received or deemed to be received in India
- Income accrue or arise in India
- Income deemed to accrue or arise in India [Section 9]
- Computation of Taxable Income and Tax Liability of an Assessee
- Lesson Round-Up
- Test Yourself
- List of Further Readings
- Other References

**REGULATORY FRAMEWORK**

<i>Sections</i>	<i>Income Tax Act, 1961</i>
Section 2(31)	Person
Section 2(7)	Assessee
Section 2(9)	Assessment Year
Section 3	Previous Year
Section 2(25A)	India
Section 2(10)	Average Rate of Income-tax
Section 2(29C)	Maximum Marginal Rate
Section 2(24)	Income
Section 2(45)	Total Income
Section 4	Charge of Income Tax
Section 6	Residential Status
Section 5	Scope of Total Income
Section 9	Income deemed to accrue or arise in India

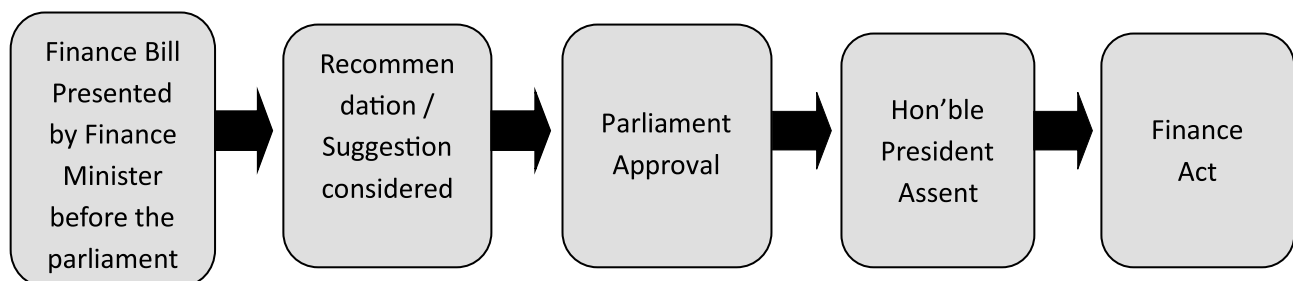
**AN OVERVIEW OF FINANCE BILL**

The Income tax Act contains the provisions for determination of taxable income, determination of tax liability, procedure for assessment, appeal, penalties and prosecutions. It also lays down the powers and duties of various income tax authorities. The income tax law in India consists of the following components:

<b>Components of Income Tax Law</b>	
<b>Income Tax Act, 1961</b>	This Act came into force on 1st April, 1962 and contains sections 1 to 298, wherein each section may have sub-sections, clauses or sub-clauses and may also have Provisos and Explanations.
<b>Annual Finance Act</b>	Every year Budget is presented before the parliament by the Finance Minister. One of the important components of the Budget is the Finance Bill. This Bill contains various amendments in the Income-Tax Act and other tax laws to prescribe the additions and deletions therein. When the Finance Bill is approved by both the houses of parliament and receives the assent of President, it becomes the Finance Act.
<b>Income Tax Rules, 1962</b>	For implementation of the Act and for administration of the direct taxes, Central Board of Direct Taxes (CBDT) is empowered to frame these rules from time to time. These rules are collectively called as the Income-tax Rules, 1962.

<b>Notifications</b>	Notifications are issued either by Central Government or by CBDT to take care the procedural aspects of the Act from time to time. These notifications are binding on everyone, i.e., on Income Tax Authorities as well as on the assessees.
<b>Circulars/ Clarifications</b>	Circulars and clarifications are issued by the CBDT to clarify the doubts regarding the scope and meaning of certain provisions of the law and primarily to provide guidance to the Income Tax officers. These circulars are binding on the Income Tax Authorities but not on the assessee however an assessee can take benefit of these circulars.
<b>Judicial Decisions (Case Laws)</b>	Decisions pronounced by Supreme Court become Judicial Precedent and are binding on all the courts, Appellate Tribunal, Income Tax Authorities and on assesses. Further, High Court decisions are binding on assesses and Income Tax Authorities which come under its jurisdiction unless it is overruled by a higher authority. The decision of a High Court can not bind other High Court.

Finance Bill as part of the Union Budget is presented usually in the month of February every year and this bill contains amendments in direct as well as indirect taxes. It is presented in the Parliament by the Union Finance Minister. The finance bill is passed by both the houses of Parliament after it is being tabled and necessary recommendation / amendments have been made in it. Once the bill has been passed by the Parliament, it goes to the Hon'ble President of India for presidency assent. After President's assent, the finance bill becomes the Finance Act.



The Finance Bill is presented contains detailing the imposition, abolition, remission, alteration or regulation of taxes proposed in the Budget. It is through the Finance Act that amendments are made to the various Acts like Income Tax Act 1961, Customs Act, 1962 etc. In short, Finance Bill can be considered as an umbrella Act. When the proposals are introduced to the Parliament it is called as a Finance Bill. Once it is passed by the Parliament and assented to by the President, Finance Bill becomes the Finance Act for that year. Finance Bills for various years are available at the website <http://indiabudget.nic.in/>

The effective date of applicability of provisions of the Finance Act is usually mentioned in the notification in the official gazette or in the Act itself. Generally, the amendments by the Finance Act are made applicable from the first day of the next financial year. Likewise, amendments by Finance Act, 2021 are effective from 1st April, 2021. Regarding indirect taxes, the ad valorem tax rates (tax rates based on value) are effective from the midnight of the date of presentation of the Union Budget.

### IMPORTANT DEFINITIONS

All incomes are categorized under five Heads of Income under the Income tax Law. There is a charging section under each head of income which defines the scope of income chargeable under that particular head. Accordingly income earned is classified under the following heads:

- a. Income under the head Salary
- b. Income under the head House Property

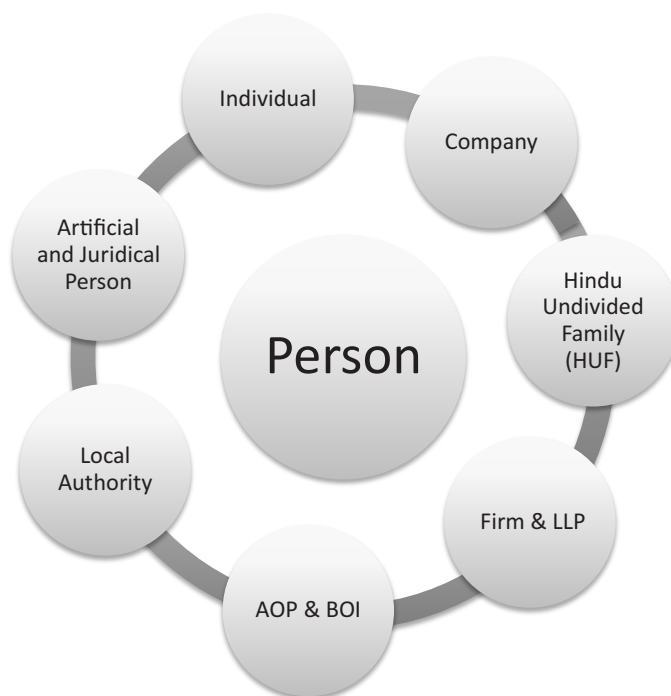
- c. Income under the head Profits and Gains from Business and Profession (PGBP)
- d. Income under the head Capital Gains
- e. Income under the head Other Sources.

Every person, whose total Income of the previous year exceeds the maximum amount which is not chargeable to tax, is an assessee and such total income shall be chargeable to Income Tax at the rates prescribed in the Act for that relevant assessment year. However this Total income shall be determined on the basis of the residential status of an assessee.

Therefore, for the purposes of levy income tax, one must have an understanding of the various concepts or definitions such as previous year, assessment year, Income, total income, person, assessee, residential status etc. These as explained as under:

#### Person [Section 2(31)]

Income-tax is charged in respect of the total income of the previous year of every person. Hence, it is important to know the definition of the word person. As per section 2(31), Person includes:



- ❖ **Individual:** An individual is a natural human being; i.e.; male, female, minor or a person of sound or unsound mind.
- ❖ **HUF:** Hindu Undivided Family ('HUF') is treated as a 'person' under section 2(31) of the Income-tax Act, 1961 and is considered as separate entity for the purpose of assessment under the Act. Under Hindu Law, an HUF is a family which consists of all persons lineally descended from a common ancestor and includes their wives and unmarried daughters. An HUF cannot be created under a contract, it is created automatically in a Hindu Family. Jain and Sikh families even though are not governed by the Hindu Law, but they are treated as HUF under the Act. For Details about HUF: please refer weblink:

[https://www.incometaxindia.gov.in/pages/i-am/huf.aspx#:~:text=Hindu%20Undivided%20Family%20\('HUF',of%20assessment%20under%20the%20Act.](https://www.incometaxindia.gov.in/pages/i-am/huf.aspx#:~:text=Hindu%20Undivided%20Family%20('HUF',of%20assessment%20under%20the%20Act.)

- ❖ **Company:** Section 2(17) of the Income tax Act, 1961 defines the term company to mean :
  - i. any Indian company, or
  - ii. any body corporate incorporated by or under the laws of a country outside India, i.e., a foreign company, or
  - iii. any institution, association or body which is or was assessable or was assessed as a company for any assessment year under the Indian Income Tax Act, 1922 or which is or was assessable or was assessed under this Act as a company for any assessment year commencing on or before the 1st day of April, 1970, or
  - iv. any institution, association or body, whether incorporated or not and whether Indian or non-Indian, which is declared by general or special order of the CBDT to be a company only for such assessment year or assessment years as may be specified by the order of CBDT.
- ❖ **Firm:** It includes a partnership firm whether registered or not and shall include a Limited Liability Partnership as defined in the Limited Liability Partnership Act, 2008.
- ❖ **Association of Person 'AOP' :** Two or more persons join in for a common purpose or common action to produce income, profits or gains. It may consist of individuals, HUF, companies, firms, etc. as members of AOP. The object of the formation of AOP must be to produce income. It is not enough that the persons receive the income jointly.
- ❖ **Body of Individuals 'BOI':** BOI denote the status of persons who are assessable in like manner and to the same extent as the beneficiaries individually.

Only individuals can be the members

Individuals join together for common purposes

Is there any difference between AOP and BOI

<b>Association of Person 'AOP'</b>	<b>Body of Individual 'BOI'</b>
An association implies a voluntary getting together for a definite purpose	Body of individuals would be just a body without an intention to get-together
Members of an association of persons can be individual or non-individuals (i.e. artificial persons)	Members of body of individuals can be individuals only
The object of the formation of AOP must be to produce income.	The object of the formation of BOI is not to produce income. It is formed for the social welfare.

- ❖ **A Local Authority:** It means a municipal committee, district board, body of port commissioners, or other authority legally entitled to or entrusted by the Government with the control and management of a Municipal or local fund.
- ❖ **Every artificial / juridical person not falling within any of the above categories:** This is a residuary

clause. If the assessee does not fall in any of the first six categories, he is assessed under this clause. Generally, a statutory corporation, deity or charitable institution or an endowment for charitable or religious purposes falls under artificial juridical person.

### Assessee [Section 2(7)]

“Assessee” means a person by whom any tax or any other sum of money is payable under this Act, and includes:

- (a) every person in respect of whom any proceeding under this Act has been taken for the assessment of his income or assessment of fringe benefits or of the income of any other person in respect of which he is assessable, or of the loss sustained by him or by such other person, or of the amount of refund due to him or to such other person ;
- (b) every person who is deemed to be an assessee under any provision of this Act ;
- (c) every person who is deemed to be an assessee in default under any provision of this Act.

Accordingly, assessee can be categorized as under:

<b>Assessee</b>	<b>Example</b>
<b>Assessee:</b> An individual who is liable to pay taxes for the income earned during a financial year is known as a normal assessee.	Mr. A is a salaried individual who has been paying taxes on time on his income.
<b>Representative Assessee:</b> There may be a case in which a person is liable to pay taxes for the income or losses incurred by a third party. Such a person is known as a representative assessee.	Mr. X. He has been residing abroad for the past 7 years. However, he receives rent for two house properties he owns in India. He takes the help of a relative, Mr. Y, to file taxes in India. In this case, Mr. Y acts as a representative assessee. If the assessing officer plans to investigate the tax filing, Mr. Y will be asked to provide the necessary documents as he is the guardian of the property and represents Mr. X.
<b>Deemed Assessee:</b> An individual might be assigned the responsibility of paying taxes by the legal authorities and such individuals are called deemed assesseees.	Deemed assesseees can be: <ul style="list-style-type: none"> <li>● The eldest son or a legal heir of a deceased person who has expired without writing a will.</li> <li>● The executor or a legal heir of the property of a deceased person who has passed on his property to the executor in writing.</li> <li>● The guardian of a lunatic, an idiot, or a minor.</li> <li>● The agent of a non-resident Indian receiving income from India.</li> </ul>
<b>Assessee in Default:</b> Assessee-in-default is a person who has failed to fulfill his statutory obligations as per the income tax act such as not paying taxes to the government or not file his income tax return.	An employer is supposed to deduct taxes from the salary of his employees before disbursing the salary. He is, then, required to pay the deducted taxes to the government by the specified due date. If the employer fails to deposit the tax deducted, he will be considered as an assessee-in-default.

**Assessment Year [Section 2(9)]**

“Assessment year” means the period of twelve months commencing on 1st April every year. Therefore, the period beginning on 1st April of one year and ending on 31st March of the next year. Income of previous year of an assessee is taxed during the following assessment year at the rates prescribed by the relevant Finance Act.

**Exception to the General Rule:** In the following situation, the Income of previous year of an assessee is assessed in the previous year itself:

1. **Income of Non-Resident from Shipping:** [Section 172]- A non resident who is carrying on a shipping business and earns income at any port in India, shall be charged to tax before the ship is allowed to leave Indian Port. Hence income is deemed and computed at a presumptive rate of 7.5% of the amount of the fare/ freight charged by the non-resident ship from the Indian port.
2. **Income of persons leaving India either permanently or for long duration:** [Section 174]- When it appears to the Assessing Officer (A.O.) that an individual may leave India and has no intentions of returning back during an assessment year, then the income is charged to tax during the same Assessment year.
3. **Income of bodies formed for short duration:** [Section 174A]- When it appears to the Assessing Officer (A.O.) that any organization is formed for a particular event and is likely to be dissolved during the current assessment year.
4. **Income of person trying to transfer his assets with a view to avoid tax:** [Section 175]- When it appears to the Assessing Officer (A.O.) that during the current assessment year any person is likely to charge, sell, transfer, dispose of or otherwise part with any of his assets to avoid payment of any liability under this Act, the total income of such person for the period from the expiry of the previous year to the date, when the Assessing Officer commences proceedings under this section is chargeable to tax in that assessment year.
5. **Income of discontinued business:** [Section 176]- Where any business or profession is discontinued in any assessment year, the income of the period from the expiry of the previous year up to the date of such discontinuance may, at the discretion of the Assessing Officer, be charged to tax in that assessment year.

**Previous Year [Section 3]**

Income tax is payable on the income which is earned during the Previous Year and it is assessed in the immediately succeeding financial year which is called an Assessment Year.

All assesses are required to follow a uniform previous year, i.e., The Financial Year (1st April to 31st March) as their Previous year. Although assessee may maintain books of accounts on calendar year basis (1st January to 31st December) but his previous year for income tax purposes shall be the Financial year.

Each financial year is both, a previous year as well as an assessment year. It is the previous year for the income earned during the financial year and assessment year for the income earned during the preceding previous year. For example financial year 2025-26 is the previous year for the income earned during the financial year 2025-26 and assessment year for the income earned during the previous year 2024-25.

In case of newly set up business or profession or a source of income newly coming into existence, the first previous year will be the period commencing from the date of setting up of business/profession or as the case may be, the date on which the source of income newly comes into existence and ending on the immediately following March, 31.

**Example 1:** Y & b, a firm, sets up a new business on May 15, 2025. What is the previous year for the assessment year 2026-27.

**Answer :** Previous year for the assessment year 2026-27 is the period commencing on May 15, 2025 and ending on March 31, 2026.

**Example 2 :** A joins an Indian company on February 17, 2025. Prior to joining this Indian company, he was not in employment nor does he have any major source of income. Determine the previous year of A for the assessment years 2025-26 and 2026-27.

**Answer :** Previous years for the assessment years 2025-26 and 2026-27 will be as follows:

Previous year	Assessment year
February 17, 2025 to March 31, 2025	2025-26
April 1, 2025 to March 31, 2026	2026-27

### India [Section 2(25A)]

The term 'India' means –

- (i) the territory of India as per Article 1 of the Constitution,
- (ii) its territorial waters, seabed and subsoil underlying such waters,
- (iii) continental shelf,
- (iv) exclusive economic zone, or
- (v) any other specified maritime zone and the air space above its territory and territorial waters.

Specified maritime zone means the maritime zone as referred to in the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976.

### Maximum Marginal Rate and Average Rate of Tax

**“Average Rate of income-tax”** means the rate arrived at by dividing the amount of income-tax calculated on the total income, by such total income. [Section 2(10)]

**“Maximum Marginal Rate”** to mean the rate of income-tax (including surcharge on the income-tax, if any) applicable in relation to the highest slab of income in the case of an individual, AOP or BOI, as the case may be, as specified in Finance Act of the relevant year. [Section 2(29C)]

### Income [Section 2(24)]

“Income is the consumption and savings opportunity gained by an entity within a specific timeframe, which is generally expressed in monetary terms. However, for households and individuals, “income is the sum of all the wages, salaries, profit, interests payments, rents, and other forms of earnings received in a given period of time.”

In general terms, Income is a periodical monetary return with some sort of regularity. However, the Income Tax Act, even certain income which does not arise regularly are treated as income for tax purposes e.g. Winnings from lotteries, crossword puzzles.

The definition of Income as given in Section 2(24) of the Act starts with the word includes therefore the list is inclusive not exhaustive. The definition enumerates certain items, including those which cannot ordinarily be considered as income but are treated statutorily as such.

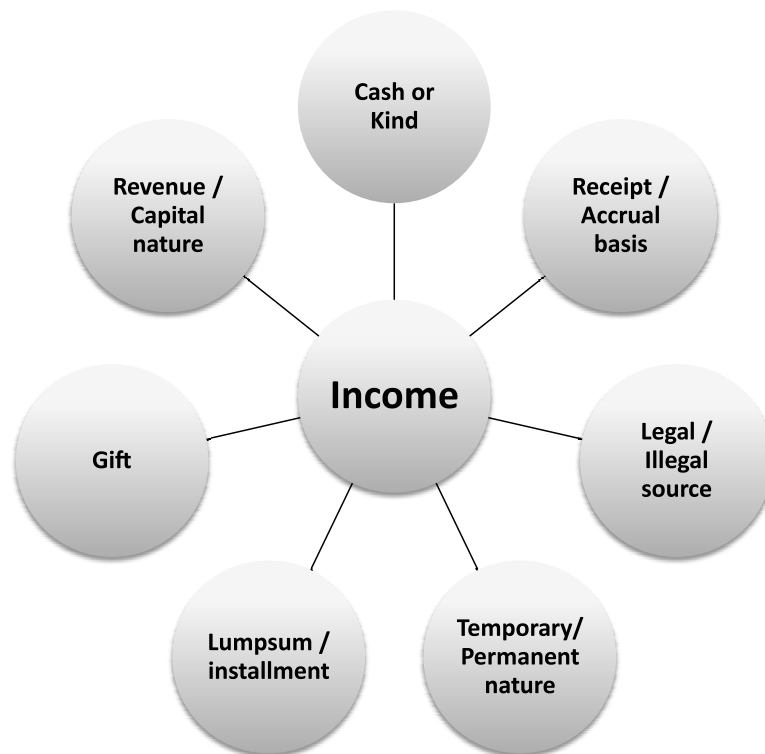
As per section 2(24), the term income includes:

<b>S. No.</b>	<b>Income</b>	<b>Taxable Head</b>
1.	Profits and gains	PGBP
2.	Dividend	Other Sources
3.	Voluntary contributions	Generally exempt under Section 11 and 12
4.	The value of any perquisite or profit in lieu of salary	Salary
5.	Any special allowance or benefit specifically granted to the employee to meet expenses wholly, necessarily and exclusively for the performance of the duties of an office or employment of profit	Salary (Generally exempt)
6.	City Compensatory Allowance/ Dearness allowance	Salary
7.	Benefit or Perquisite to a Director / a person having substantial interest/ relative of director	Salary (If as per employment agreement) Else under Other Sources (If not in the terms of employment agreement)
8.	Any Benefit or perquisite to a Representative Assessee	Other Sources
9.	Deemed profits chargeable to tax under section 28 or section 41 or section 59.	PGBP
10.	Capital Gain	Capital Gains
11.	Insurance Profit	PGBP
12.	Banking income of a Co-operative Society	PGBP
13.	Winnings from Lottery	Other Sources
14.	Employees Contribution Towards Provident Fund	PGBP if not deposited by the assessee to the specified fund
15.	Amount Received under Keyman Insurance Policy	PGBP

<i>S. No.</i>	<i>Income</i>	<i>Taxable Head</i>
16.	<p><b>Amount received for not carrying out any activity</b> : Any sum referred to in Section 28(va), i.e. any sum, whether received or receivable in cash or kind, under an agreement for -</p> <p>(i) not carrying out any activity in relation to any business or profession</p> <p>(ii) not sharing any know-how, patent, copyright, trademark, license, franchise or any other business or commercial right of similar nature or information or technique likely to assist in the manufacture or processing of goods or provision for services</p>	PGBP
17.	Any sum referred to in clause (v) or (vi) of sub-section (2) of section 56	Other Sources
18.	Gift received for an amount exceeding Rs. 50,000	Other Sources
19.	Any consideration received for issue of shares as exceeds the fair market value of the shares referred in section 56(2) (viib)	Other Sources
20.	Amount received as an advance or otherwise in the course of negotiation for transfer of a capital asset referred to in clause (ix) of section 56(2)	Other Sources
21.	Any sum of money or value of property received without consideration or for inadequate consideration as referred to in clause (x) of Section 56(2)	Other Sources
22.	Any compensation or payment in connection with termination of employment as referred under clause (xi) of Section 56(2)	Other Sources
23.	Any specified sum received by a unit holder from a business trust with respect to a unit held by him [clause (xii) of sub-section (2) of section 56]	Other Sources
24.	Any sum received, including the amount allocated by way of bonus under a life insurance policy, other than the sum received under a unit linked insurance policy and keyman insurance policy which is not to be excluded from the total income of the previous year in accordance with the provisions of clause (10D) of section 10, the sum so received as exceeds the aggregate of the premium paid, during the term of such life insurance policy, and not claimed as deduction under any other provision of this Act, [clause (xiii) of sub-section (2) of section 56]	Other Sources

<i>S. No.</i>	<i>Income</i>	<i>Taxable Head</i>
25.	Assistance in the form of a subsidy or grant or cash incentive or duty drawback or waiver or concession or reimbursement (by whatever name called) by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee other than the subsidy or grant or reimbursement which is taken into account for determination of the actual cost of the asset in accordance with the provisions of Explanation 10 to clause (1) of section 43.	PGBP

### CONCEPT OF INCOME



- **Cash or kind**

Income may be received in cash or kind. When the income is received in kind, its valuation will be made in accordance with the rules prescribed in the Income-tax Rules, 1962.

- **Receipt basis/ Accrual basis**

Income arises either on receipt basis or on accrual basis. It may accrue to a taxpayer without its actual receipt. The income in some cases is deemed to accrue or arise to a person without its actual accrual or receipt. Income accrues where the right to receive arises.

- **Legal or illegal source**

The income-tax law does not make any distinction between income accrued or arisen from a legal source and income tainted with illegality. In *CIT v. Piara Singh* (1980) 3 Taxman 67, the Supreme Court

has held that if smuggling activity can be regarded as a business, the confiscation of currency notes by customs authorities is a loss which springs directly from the carrying on of the business and is, therefore, permissible as a deduction.

- **Temporary/Permanent**

There is no difference between temporary and permanent income under the Act. Even temporary income is taxable under the Income Tax Act.

- **Lumpsum / Instalments**

Income whether received in lump sum or in installment is liable to tax. For example: Arrears of salary or bonus received in lump sum is income and charged to tax as salary.

- **Gifts**

Normally, gifts constitute a capital receipt in the hands of the recipient. However, certain gifts are brought within the purview of income-tax, for example, receipt of property without consideration is brought to tax under section 56(2)(x). Gifts of personal nature do not constitute income subject to maximum of Rs. 50,000 received in cash. The recipient of gifts like birthday, marriage gifts, etc. is not liable to income-tax as received in kind however as per the Finance Act, 2009 gifts in kind having fair value upto Rs. 50,000 are not liable to tax but having fair value of more than Rs. 50,000 is wholly taxable.

- **Revenue or Capital receipt**

Income-tax, as the name implies, is a tax on income and not a tax on every item of money received. Therefore, unless the receipt in question constitutes income as distinguished from capital, it cannot be charged to tax. For this purpose, income should be distinguished from capital which gives rise to income. However, some capital receipts have been specifically included in the definition of income.

#### **Total Income [Section 2(45)]**

The term "total income" means the total amount of income referred to in section 5, computed in the manner laid down in this Act.

### **CAPITAL AND REVENUE RECEIPTS**

The Act contemplates a levy of tax on income and not on capital and hence it is very essential to distinguish between capital and revenue receipts. Capital receipts cannot be taxed, unless they fall within the scope of the definition of "income" and so the distinction between capital and revenue receipts is material for tax purposes.

Certain capital receipts which have been specifically included in the definition of income are compensation for modification or termination of services, income by way of capital gains etc.

It is not possible to lay down any single test or any single criterion as decisive, final and universal in application to determine whether a particular receipt is capital or revenue in nature. Hence, the capital or revenue nature of the receipt must be determined with reference to the facts and circumstances of each case.

#### **Criteria for determining whether a receipt is capital or revenue in nature**

An amount referable to fixed capital is a capital receipt whereas a receipt referable to circulating capital would be a revenue receipt. While the latter is chargeable to tax, the former is not subject to income-tax unless otherwise expressly provided.

The Income-tax Act does not define the term “Capital receipt” & “Revenue receipt”. Also, it has not laid down the criterion for differentiating the capital and revenue receipt. Yet, it has exempted certain capital receipts from taxation while certain capital receipts have been taken into ambit of capital receipts chargeable as capital gains.

Whether a particular receipt is of the nature of income or capital is explained below by the following examples. The following test can be applied to determine the nature of particular receipt.

<b>Base</b>	<b>Explanation</b>	<b>Example</b>
<b>Type of capital will depend upon the nature of business</b>	The very same thing may be fixed capital in the hands of one business but circulating capital in the hands of another.	An amount received on account of sale of trading goods or receipts in respect of circulating capital or of flowing capital is revenue receipt, for example sale of a motor car by a dealer. On the other hand a receipt on account of sale of fixed assets is a capital receipt, for example, amount received on sale of a motor car by a person who is not a car dealer.
<b>Nature of receipt also depends upon the reference to the recipient</b>	Whether a particular receipt is capital or revenue in nature must be determined with reference to the recipient who is sought to be taxed as the assessee. For tax purposes the capital or revenue character of the receipt must be determined on the basis of the nature of the trade in the course of which or in connection with which it arises.	<ul style="list-style-type: none"> <li>● The reimbursement of capital outlay is a capital receipt even if the total amount received exceeds the cost of the outlay itself.</li> <li>● Compensation received for the loss of a capital asset is a receipt of a capital nature whereas the compensation received for damage to or loss of a trading asset is a revenue receipt.</li> <li>● A capital asset is converted into income and the price realized on its sale takes form of the periodic payments of a revenue nature.</li> <li>● Where a person sells his properties and the sale price is payable to him by the purchaser in the form of annuities of a fixed sum so long as the seller is alive or until he attains a particular age.</li> </ul>
<b>Capital and Revenue Receipts in Relation To Business Activities</b>	Profits and gains arising from various transactions which are entered into in the ordinary course of the business of the tax payers or those which are incidental to or closely associated with his business would be revenue receipts chargeable to tax. But even in these cases the receipts may be of a capital nature in certain circumstances.	<ul style="list-style-type: none"> <li>● Profits on purchase and sale of shares by a share broker on his own account</li> <li>● Profits arising from dealings in foreign exchange by a banker or other financial institutions</li> <li>● Income from letting out buildings owned by a company to its employees etc.</li> </ul> <p>For instance, profit on sale of shares and securities held by a bank as investments would be of a capital nature. Where profits arise from transactions which are outside the normal dealing of the assessee, although connected with his business, the taxable nature or otherwise of the profits would depend upon the fact whether or not the transaction(s) in question constitute(s) trading activity.</p>

**CAPITAL AND REVENUE EXPENDITURE**

The expenditures that are incurred by an organisation for long-term benefits are known as capital expenditures. These expenditures serve the purpose of increasing the capacity or capabilities of the long-term asset by either enhancing or adding new assets to the organisation.

Revenue expenditure is referred to as the expenditure incurred by an organisation to manage the day-to-day functions of a business, which include employee wages, inventory, rent, electricity, insurance, stationery, postage, and taxes.

**Illustration 1:**

State whether the following are capital or revenue receipts/expenses and give your reasons:

1. ABC & Co. received Rs. 5,00,000 as compensation from XYZ & Co. for premature termination of contract of agency.
2. Sales-tax collected from the buyer of goods.
3. PQR Company Ltd. instead of receiving royalty year by year, received it in advance in lump sum.
4. An amount of Rs. 1,50,000 was spent by a company for sending its production manager abroad to study new methods of production.
5. Payment of Rs. 50,000 as compensation for cancellation of a contract for the purchase of machinery with a view to avoid an unnecessary expenditure.
6. An employee director of a company was paid Rs. 3,50,000 as a lump sum consideration for not resigning from the directorship.

**Solution:**

1. Receipt in substitution of a source of income is a capital receipt. Therefore, the amount received by ABC & Co. from XYZ & Co. for premature termination of an agency contract is a capital receipt though the same is taxable under Section 28(ii)(c).
2. Sales-tax is the liability of a seller to pay to the Government on the sale of goods made by him, which is allowed as deduction as revenue expenditure. If any part of Sales-tax is collected from the buyer of goods that may be treated as a revenue receipt. Thus the sales-tax collected from the buyer of goods is a revenue receipt.
3. Receipt of lump sum royalty in lieu of future royalties is a revenue receipt, as it is an income from royalty.
4. Amount spent by a company for sending its production manager abroad to study new methods of production is revenue expenditure to be allowed as a deduction. Because the new knowledge and exposure of that manager will assist the company in improving its existing methods of production etc.
5. This is a capital expenditure, as any expenditure incurred by a person to free himself from a capital liability is a capital expenditure. In the given case, the payment of Rs. 50,000 for cancelling the order for purchase of the machinery has helped the assessee to become free from an unnecessary capital liability.
6. The amount of Rs. 3,50,000 received for not resigning from the directorship is a reward received from the employer. Therefore it is a revenue receipt.

**Illustration 2:**

Which of the following is not a revenue receipt?

- (i) Compensation received for the loss of a capital asset
- (ii) Compensation received for damage to or loss of a trading asset.
- (iii) Profits on purchase and sale of shares by a share broker on his own account.
- (iv) Income from letting out buildings owned by a company to its employees etc

**Options:**

- a) i only
- b) i and ii both
- c) i, ii, and iii
- d) All of the above

**Answer: (a)**

**CASE LAW**

<b>09.07.2010</b>	<b><i>CIT (Appellant) v. Saurashtra Cement Ltd. (Respondent)</i></b>	<b><i>Supreme Court</i></b>
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**Liquidated Damages – Capital Receipt or Revenue Receipt?**

**Facts of the Case:** The assessee, engaged in the manufacture of cement etc; entered into an agreement with M/s Walchandnagar Industries Limited, Bombay, (hereinafter referred to as “the supplier”) on 1st September, 1967 for purchase of additional cement plant from them for a total consideration of Rs.1,70,00,000/-. As per the terms of contract, the amount of consideration was to be paid by the assessee in four instalments. The agreement contained a condition with regard to the manner in which the machinery was to be delivered and the consequences of delay in delivery.

In the event of delays in deliveries except the reason of Force Majeure, the Suppliers shall pay the Purchasers an agreed amount by way of liquidated damages without proof of damages actually suffered at the rate of 0.5% of the price of the respective machinery and equipment to which the items were delivered late, for each month of delay in delivery completion. It is further agreed that the total amount of such agreed liquidated damages shall not exceed 5% of the total price of the plant and machinery.” The supplier defaulted and failed to supply the plant and machinery on the scheduled time and, therefore, as per the terms of contract, the assessee received an amount of Rs.8,50,000 from the supplier by way of liquidated damages.

During the course of assessment proceedings for the relevant assessment Year, a question arose whether the said amount received by the assessee as damages was a capital or a revenue receipt.

**Judgement:** Supreme Court held that it was clear from the agreement that the liquidated damages were to be calculated at 0.5 per cent of the price of the respective machinery and equipment which were delivered late, for each month of delay, without proof of the actual damages suffered by the assessee on account of the delay. The delay in supply could be of the whole plant or a part thereof but the determination of damages was not based upon the calculation made in respect of loss of profit on account of supply of a particular part of the plant. It was evident that the damages to the assessee were directly and intimately linked with

the procurement of a capital asset, i.e., the cement plant, which would obviously lead to delay in coming into existence of the profit-making apparatus, rather than a receipt in the course of profit-earning process. Compensation paid for the delay in procurement of capital asset amounted to sterilization of the capital asset of the assessee as supplier had failed to supply the plant within time as stipulated in the agreement. The amount received by the assessee towards compensation for sterilization of the profit-earning source and not in the ordinary course of its business, was a capital receipt in the hands of the assessee.

### CHARGE OF INCOME TAX [SECTION 4]

Section 4 of the Act is the charging section. It lays down the basis on which tax is imposed. Section 4 of Income Tax Act is the most effective and operative of the various provisions in the Act since, it is because of this section alone that all other sections become enforceable. The charging section is the backbone of the Act, it lays down the provisions as to what are taxable and at what rates; income of which period is taxable and in whose hands. Accordingly, the section provides that:

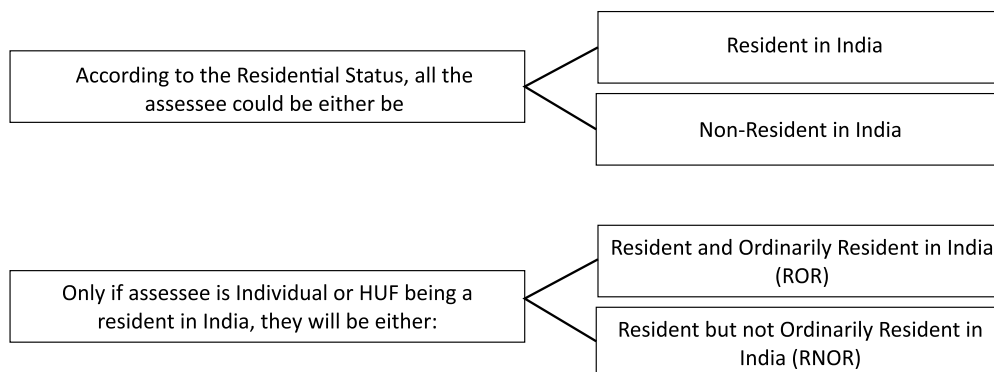
- (a) Income tax shall be charged at the rate or rates prescribed in the Finance Act for the relevant previous year, tax computation is in Assessment Year.
- (b) the charge of tax is on various persons specified u/s 2(31),
- (c) the income sought to be taxed is that of the previous year and not of the of assessment year,
- (d) the levy of tax on the assessee is on his total or taxable income computed in accordance with and subject to the appropriate provisions of the Income Tax Act, including provisions for the levy of additional Income-tax.

Provided that where by virtue of any provision of this Act income-tax is to be charged in respect of the income of a period other than the previous year, income-tax shall be charged accordingly.

### RESIDENTIAL STATUS [SECTION 6]

Total Income of an assessee cannot be computed unless the person's residential status in India during the previous year is known because the taxability of an assessee is dependent on the Residential status during any Previous Year. Thus, determining residential status of a person is important steps for calculating tax liability of a person.

Section 6 of the Income Tax Act prescribes the criteria to determine the residential status of all tax payers for purposes of income-tax. An assessee's residential status must be determined with reference to the previous year in respect of which the income is sought to be taxed. i.e. the residential status of a person must be determined every year because the residential status of a person may change from one year to next year and so on depending upon the situation.



There are different tests to be applied for different types of person, let us understand test for each category of person:

## TEST OF RESIDENCE FOR INDIVIDUAL

### Resident

#### Basic Conditions

Under Section 6(1) of the Income-tax Act, an individual is said to be resident in India in any previous year if period of physical stay in India is

- a. 182 days or more in that previous year, OR
- b. 60 days or more in that Previous Year AND 365 days or more in Preceding 4 years

If an assessee fails to meet both the above criteria in any Previous Year, then he is considered as Non-Resident for tax purpose in that Previous Year.

#### Exception to the Basic Condition

In case of the following individuals:

- (a) being a citizen of India, who leaves India in any previous year as a member of the crew of an Indian ship as defined in clause (18) of section 3 of the Merchant Shipping Act, 1958, or for the purposes of employment outside India, the provisions of the second condition shall apply in relation to that year as if for the words “sixty days (60 days)”, occurring therein, the words “one hundred and eighty-two days (182 days)” had been substituted.
- (b) being a citizen of India, or a person of Indian origin within the meaning of Explanation to clause (e) of section 115C, who, being outside India, comes on a visit to India in any previous year, the provisions of the second condition shall apply in relation to that year as if for the words “sixty days (60 days)”, occurring therein, the words “one hundred and eighty-two days (182 days)” had been substituted. ***However, in case of the citizen or person of Indian origin in the above cases having total income, other than the income from foreign sources, exceeding fifteen lakh rupees during the previous year, for the words “sixty days” occurring therein, the words “one hundred and twenty days” had been substituted. [Amended vide Finance Act, 2020]***

**Deemed Resident:** An Individual will be considered as Deemed Resident in the below case:

- Individual being a Citizen of India, AND
- having Total Income in excess 15 lakhs in the Previous Year (Other than foreign Source) AND
- not liable to tax in any other country/territory, by reason of domicile, residence or any similar criteria.

**[Section 6(1A) i.e. concept of Deemed Resident introduced vide Finance Act, 2020]**

### Non-Resident (NR)

If an individual does not satisfy any of the above basic conditions then, he will be treated as Non-Resident. It must be noted that the fulfillment of any one of the above conditions (a) or (b) as applicable will make an individual resident in India for tax purposes. Further it is to be noted that these conditions are alternative and not cumulative in their application.

### Resident and Ordinarily Resident (ROR)

An individual may become a resident and ordinarily resident in India if he satisfies both the following conditions given u/s 6(1) besides satisfying any one of the above mentioned conditions:

- (i) he is a resident in atleast any two out of the ten previous years immediately preceding the relevant previous year, and
- (ii) he has been in India for 730 days or more during the seven previous years immediately preceding the relevant previous year.

### Resident but Not Ordinarily Resident (RNOR)

An individual is not ordinarily resident in any previous year if –

- (a) he has been a non-resident in India in nine out of the ten previous years preceding that year; or
- (b) he has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, seven hundred and twenty-nine days (729 days) or less;
- (c) a citizen of India, or a person of Indian origin, having total income, other than the income from foreign sources, exceeding fifteen lakh rupees during the previous year, who has been in India for a period or periods amounting in all to one hundred and twenty days or more but less than one hundred and eighty- two days; or
- (d) a citizen of India who is deemed to be resident in India under clause (1A).

*Explanation:* “income from foreign sources” means income which accrues or arises outside India (except income derived from a business controlled in or a profession set up in India).

### Important Points

- The fact that an assessee is resident in India in respect of one year does not automatically mean that he would be resident in the preceding or succeeding years as well. Consequently, the residential status of the assessee should be determined for each year separately. This is in view of the fact that a person resident in one year may become non-resident or not ordinarily resident in another year and vice versa.
- It must also be noted that the residential status of an individual for tax purposes is neither based upon nor determined by his citizenship, nationality and place of birth or domicile. This is because of the fact that, for tax purposes, an individual may be resident in more than one country in respect of the same year.
- The common feature in both the above conditions is the stay of the individual in India for a specified period. The period of stay required in each of the conditions need not necessarily be continuous or consecutive nor it is stipulated that the stay should be at the usual place of residence, business or employment of the individual. Purpose of stay is immaterial in determining the residential status.
- The stay may be anywhere in India and for any length of time at each place in cases where the stay in India is at more places than one, what is required is the total period of stay should not be less than the number of days specified in each condition.
- While determining residential status, the day of leaving and returning to India should be considered as a stay in India.
- Person of Indian Origin is one who is, or either of his parents or grandparents were born in Undivided India.

- India means territory of India, its territorial waters, continental shelf, Exclusive Economic Zone (upto 200 nautical miles) and airspace above its territory and territorial waters.
- Where the exact arrival and departure time is not available then the day he comes to India and the day he leaves India is counted as stay in India.

**Illustration 3:**

Mr. A, an Indian Citizen, is living in Mumbai since 1950, he left for China on July 1, 2020 and comes back on August 7, 2025. Determine his residential status for the assessment year 2026-27.

**Solution:**

Stay in India for a minimum period of 182 days in the previous year : Mr. A has stayed in India for 237 (viz. 25 + 30 + 31 + 30 + 31 + 31 + 28 + 31) days in the previous year 2025-26.

So, this test is satisfied.

So, Mr. A shall be a resident in India during the previous year 2025-26. (Assessment Year 2026-27). Keeping in view the facts of the given case, Mr. A satisfies the two additional conditions also namely: He is resident in two out of ten previous years preceding the relevant previous year.

<i>PY</i>	<i>Stay in PY (days)</i>	<i>Stay during PY (days)</i>	<i>Basic Condition Satisfied</i>	<i>Resident/Non-Resident</i>
2024-25	Nil	-	None	Non-Resident
2023-24	Nil	-	None	Non-Resident
2022-23	Nil	-	None	Non-Resident
2021-22	Nil	-	None	Non-Resident
2020-21	30+31+30+1= 92	365 days	Second	Resident
2019-20	366	366	First	Resident

His stay in India is also more than 730 days in 7 previous years preceding the relevant previous year. As he left for China on 1st July 2020.

<b>PY</b>	<b>Stay (days)</b>
2024-25	Nil
2023-24	Nil
2022-23	Nil
2021-22	Nil
2020-21	92
2019-20	366

2018-19	365
Total Stay in 7 Previous Years	823

Hence, Mr. A is resident and ordinary resident in India for the assessment year 2026-27

**Illustration 4:**

Mr. Steve Waugh, the Australian cricketer comes to India for 100 days every year. Find out his residential status for AY 2026-27.

**Solution:**

**Step 1 :** The total stay of Mr. Steve Waugh in the last 4 preceding years is 400 days and his stay in India during the previous year is 100 days. Since, he satisfied the second condition in section 6(1), he is resident.

**Step 2 :** Since his total stay in India in the last 7 years preceding the previous years is 700 days, he does not satisfy the minimum requirement of 730 days in 7 years.

Therefore the residential status of Mr. Steve Waugh for the assessment year 2026-27 is Resident but not ordinarily resident in India.

**Illustration 5:**

Dr. A, an Indian Citizen and a Professor in IIM, Lucknow, left India on September 15, 2025 for USA to take up a Professor's job in MIT, USA. Determine his residential status for the assessment year 2026-27.

**Solution:**

Dr. A being a citizen of India and who has gone out of the country for employment, will be governed by 182 days test only and therefore the second condition under section 6(1), i.e. 60 days during relevant previous year shall not be applicable.

Dr. A stayed in India for 168 (viz. 30 + 31 + 30 + 31 + 31 + 15) days only in the relevant previous year.

Hence, Dr. A shall be a non-resident in India for the assessment year 2026-27 as condition by stay of 182 days in relevant previous year is not satisfied.

**Illustration 6:**

Mr. Anil, an Indian citizen, leaves India on 22nd September, 2025 for the first time to work as an Engineer in France. Determine his residential status for AY 2026-27.

**Solution:**

During the previous year 2025-26, Mr. Anil, an Indian citizen, was in India for 175 days (i.e. 30 + 31 + 30 + 31 + 31 + 22). He does not satisfy the minimum criteria of 182 days. Also since he is an Indian citizen leaving India for the purpose of employment outside India, the second condition u/s 6(1) is not applicable to him.

Therefore Mr. Anil is non-resident for the AY 2026-27.

**CASE LAW****April 3, 2009****Manoj Kumar Reddy V. Income Tax Officer (International Taxation)****ITAT**

**Facts of the Case:** The case relates to AY 2005-06. The assessee was an employee of an Indian company. On 23.01.2004, the employer Indian company issued a deputation letter to the assessee and directed him to work on some specified project in USA. As per the deputation order, it was mentioned that he will remain continued to be employed under the Indian company only.

During the deputation period, he came to India and stayed in India from 18.08.2004 to 06.09.2004. After completing his work he returned back to India on 31.01.2005 at 4 A.M. Summary of his stay in India is given below:-

Previous Year	No. of days in India
2000-01	365
2001-02	365
2002-03	365
2003-04	306
2004-05	78

Following contentions were observed by ITAT in this case:-

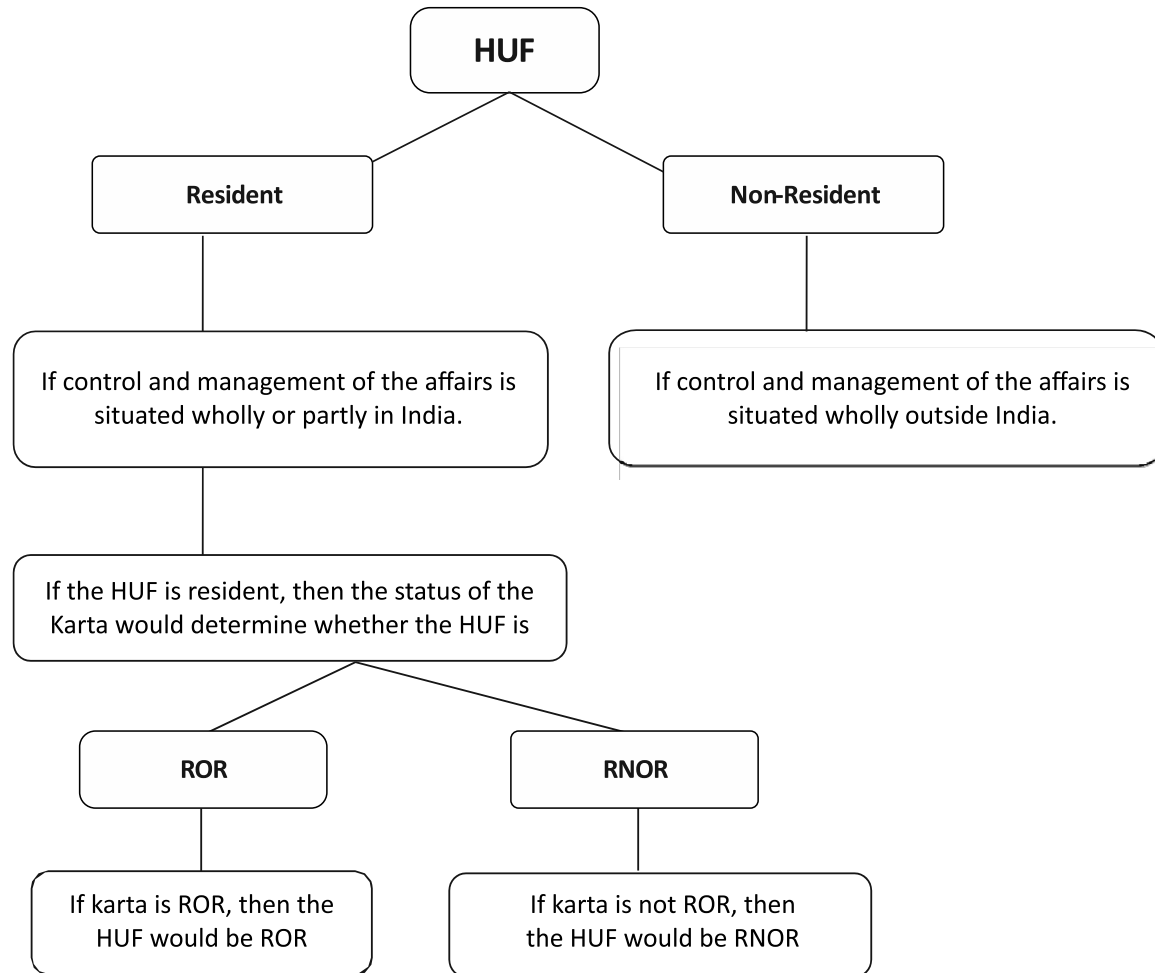
- During PY 2004-05, total stay of assessee in India was for a period less than 182 days. Hence, first limb of Section 6(1) shall not apply.
- As far as second limb of Section 6(1) is concerned. It is getting applicable as stay in India during the PY is for 78 days i.e. more than 60 days and total stay in all 4 PY preceding PY 2004-05 is exceeding 365 days. However, benefit given in explanation 1 to the second limb also needs to be examined.

Explanation 1 clause (a) applies where assessee leaves India for employment purpose. ITAT relied on decision of Authority of Advance Ruling in case of British Gas India (P) Ltd. [2006] 285 ITR 218 (New Delhi) where it was held that for purpose of “employment outside India”, even assessee on deputation sent outside India by an Indian employer is also covered. However, clause (a) of Explanation 1 shall apply for that year only in which the assessee is leaving India for employment, i.e. PY 2003-04 in this case. Hence, Clause (a) of Explanation 1 is applicable for PY 2003-04 only not for PY 2004-05.

Clause (b) to Explanation 1: The assessee was for a “visit” in India from outside India during 18.08.2004 to 06.09.2004. However, he returned back to India on 31.01.2005. The period after 31.01.2005 cannot be treated as “visit”. Hence, clause (b) to Explanation 1 cannot apply. However, to determine period of stay under second limb of Section 6(1) period of visit shall be excluded. Hence, total stay during PY 2004-05 will be reckoned from 31.01.2005 to 31.03.2005.

**Judgement:** ITAT held that assessee’s total stay was for a period of 59 days only. 31.01.2005 was not included because he arrived in India at 4 A.M. The residential status of assessee - Non-Resident.

### TESTS OF RESIDENCE FOR HINDU UNDIVIDED FAMILIES 'HUF'



#### Place of Control and Management

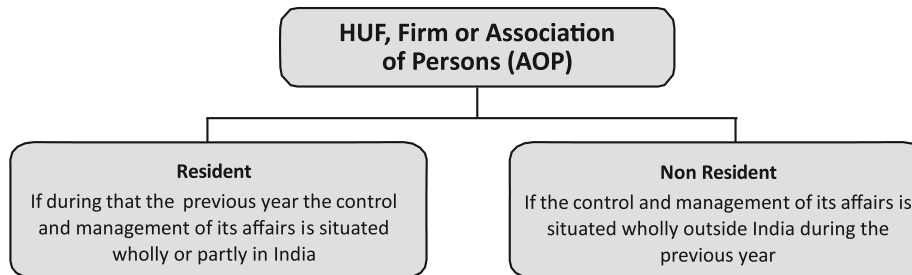
The expression control and management refers to the functions of decision-making and issuing directions but not the places where from the business is carried on. In other words, the Control and Management means taking policy decisions relating to business. Policy decisions are concerning finance, marketing, production, advertising, personnel etc. It does not mean day to day operations of the concern / assessee. The control and management is situated at that place where policy decisions are taken.

The business may be done from outside India and yet its control and management may be wholly within India. Therefore, control and management of a business is said to be situated at a place where the head and brain of the business is situated. The place of control may be different from the usual place of running the businesses and sometimes even the registered office of the assessee. But control and management do imply the functioning of the controlling and directing power at a particular place with some degree of permanence.

- Control and Management of HUF : It is with Karta or its Manager (who are co-parcener).
- Control and Management of Firm/AOP : It is with Partners/Members.

“Control and Management” means de facto control and management and not merely the right to control or

manage. Control and management is situated at a place where the head, the seat and the directing powers are situated. The mere fact that the family has a house in India, where some of its members reside or the karta is in India in the previous year, does not constitute that place as the seat of control and management of the affairs of the family unless the decisions concerning the affairs of the family are taken at that place. Although, it is the karta who normally has control and management of the affairs of a Hindu Undivided Family yet any other coparcener can control and manage the affairs. Therefore, the mere fact of absence of the karta does not make the family non-resident.



### An HUF can be “not ordinarily resident”

If manager/karta has been a not ordinarily resident in India in the previous year in accordance with the tests applicable to individuals. Where, during the last ten years the kartas of the H.U.F. had been different from one another, the total period of stay of successive kartas of the same family should be aggregated to determine the residential status of the karta and consequently the H.U.F.

In other words, if Karta of Resident HUF satisfies both the following additional conditions (as applicable in case of Individual) then Resident HUF will be ROR, otherwise it will be RNOR :

#### **Additional Conditions:**

- (1) Karta of Resident HUF should be resident in atleast 2 previous years out of 10 previous years immediately preceding relevant previous year.
- (2) Stay of Karta during 7 previous years immediately preceding relevant previous year should be 730 days or more.

#### **Important Note:**

- It is immaterial whether Karta is Resident or Non-Resident during relevant previous year, for the purpose of determining whether HUF is ROR or RNOR. If Karta satisfies both the additional conditions, then HUF will be ROR, otherwise RNOR.
- Firms, association of persons, local authorities and other artificial juridical persons can be either resident (ordinarily resident) or non-resident in India but they cannot be not ordinarily resident in India.
- Even if negligible portion of the control and management of the affairs is exercised from India, it will be sufficient to make the family, firm or the association resident in India for tax purposes. For instance, if the affairs of a firm are controlled partly from India and partly from Bangladesh, the firm would be resident in India.
- While the control and management of the affairs of the firm or family would necessarily be exercised by the partners of the firm or members of the family, the residential status of the members or partners is generally irrelevant for determining the residential status of the firm or family. But in cases where the residential status of the partners materially affects or determines the place of control and management of the affairs of the firm, the residential status of the member or partners should also be taken into account in determining the residential status of the firm or the family.
- The mere fact that all the partners are resident in India does not necessarily lead to the conclusion that

the firm is resident in India because there may be cases where even though the partners are resident in India, control and management of the affairs of the firm is exercised from outside India.

- A Hindu Undivided Family would generally be presumed to be resident in India unless the assessee proves to the tax authorities that the control and management of its affairs is situated wholly outside India during the relevant accounting year.

### CASE LAW

1.	<i>CIT v. PL. M. TT.</i>	<i>Madras High Court</i>
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***Proof of power or capacity to control and manage is not relevant for determining the control and management. What is necessary is to test the actual power or control.***

Where all partners of a firm were residing in India and they appointed a power of attorney in Ceylon (now Sri Lanka) who was entirely in charge of the business and the partners did not play any role in control and management, it was held that the firm was not tax resident in India. The High Court of Madras in *CIT v. PL. M. TT.* Firm held that as per the terms of the deed de jure control remained with the principal but de facto control or actual control was with the agent. Thus, rather than mere proof of power or capacity to control and manage, the actual power or control was relevant.

2.	<i>Saraswati Holding Corpn. Inc v. Dy. DIT (IT)</i>	<i>ITAT</i>
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***Day to Day affairs of the business is not sufficient for determining the Control and Management of affairs.***

Interpreting the phrase 'control and management of affairs' in *Saraswati Holding Corpn. Inc v. Dy. DIT(IT)*<sup>4</sup>, the ITAT held that control and management of affairs do not mean the control and management of the day-to-day affairs of the business. The fact that discretion to conduct operations of business is given to some person in India would not be sufficient. The words 'control and management of affairs' refer to head and brain, which directs the affairs of policy, finance, disposal of profits and such other vital things consisting the general and corporate affairs of the company. Thus, where decisions on investments were taken by directors outside India, the income from investments made in India could not be taxed in the hands of the company only because a few persons had been given authority to conduct the affairs.

### ***Illustration 7:***

An HUF, whose affairs of business are completely controlled from India. Determine its Residential status for AY 2026-27 (a) if Karta is ROR in India for that year (b) If Karta is NR in India but he satisfies both the additional conditions (c) If Karta is RNOR in India.

#### **Solution:**

HUF would be Resident in India as Control and Management is wholly situated in India. Determination of whether HUF is ROR or RNOR:

- HUF is ROR in India as Karta would be satisfying both the additional conditions (because he is ROR).
- HUF is ROR in India as Karta is satisfying both the additional conditions. Karta's Residential status during relevant previous year (i.e. resident/non-resident) is irrelevant.
- HUF is RNOR as Karta does not satisfy both the additional conditions.

**Illustration 8:**

Karta of an Hindu Undivided Family comes to India every year for a minimum period of 60 days and maximum 91 days. Determine residential status of the HUF for the assessment year 2026-27.

**Solution:**

Hindu Undivided Family is resident since the karta has come to India for at least 60 days but the stay of karta during seven years can be maximum 637 (91 x 7) days. Hence HUF can be considered as resident but not ordinarily resident.

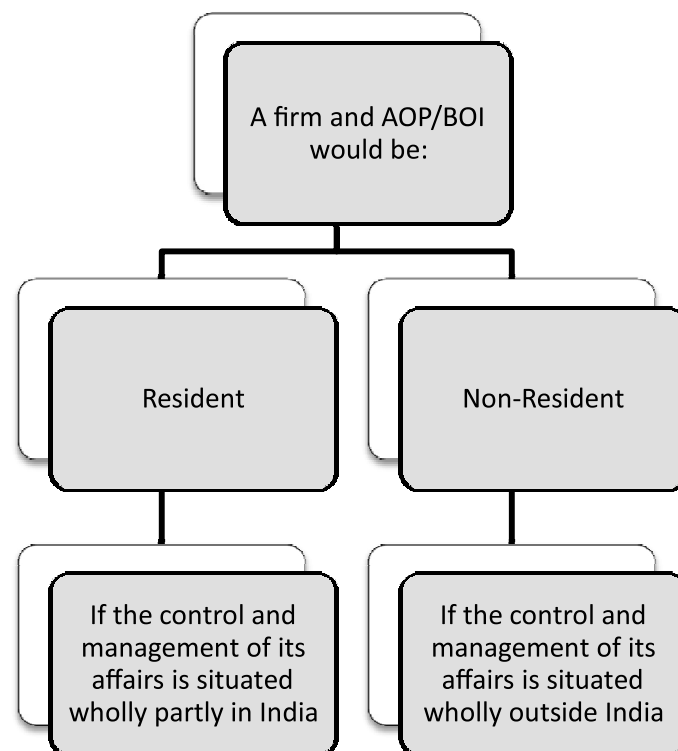
**Illustration 9:**

Hindu Undivided Family is being managed partly from Mumbai and partly from Japan. The Karta of HUF is a foreign citizen and comes to visit in India every year since 1980 in the month of April for 105 days.

Determine residential status of HUF for AY 2026-27.

**Solution:**

Since the control and management of the affairs of HUF is partly managed from Mumbai and therefore HUF is resident in India. Further, the Karta of HUF is also satisfying both of additional conditions of section 6 (6)(b) and therefore HUF is resident and ordinarily resident in India during the AY 2026-27.

**TEST OF RESIDENCE FOR FIRM AND AOP/BOI**

- Business and the whole of it may be done outside India and yet the control and management of that business may be wholly within India.
- It is entirely irrelevant where the business is done and where the income has been earned. What is relevant and material is from which place has that business been controlled and managed.

**Illustration 10:**

AB & Co. is a partnership firm whose operations are carried out in India. However, all meetings of partners take place outside India as all the partners are settled abroad. Determine Residential status of firm for AY 2026-27.

**Solution:**

AB & Co. is Non-Resident in India during relevant previous year as Control and Management (place where policy decisions are taken, here it is the place where meetings are held) is wholly situated outside India.

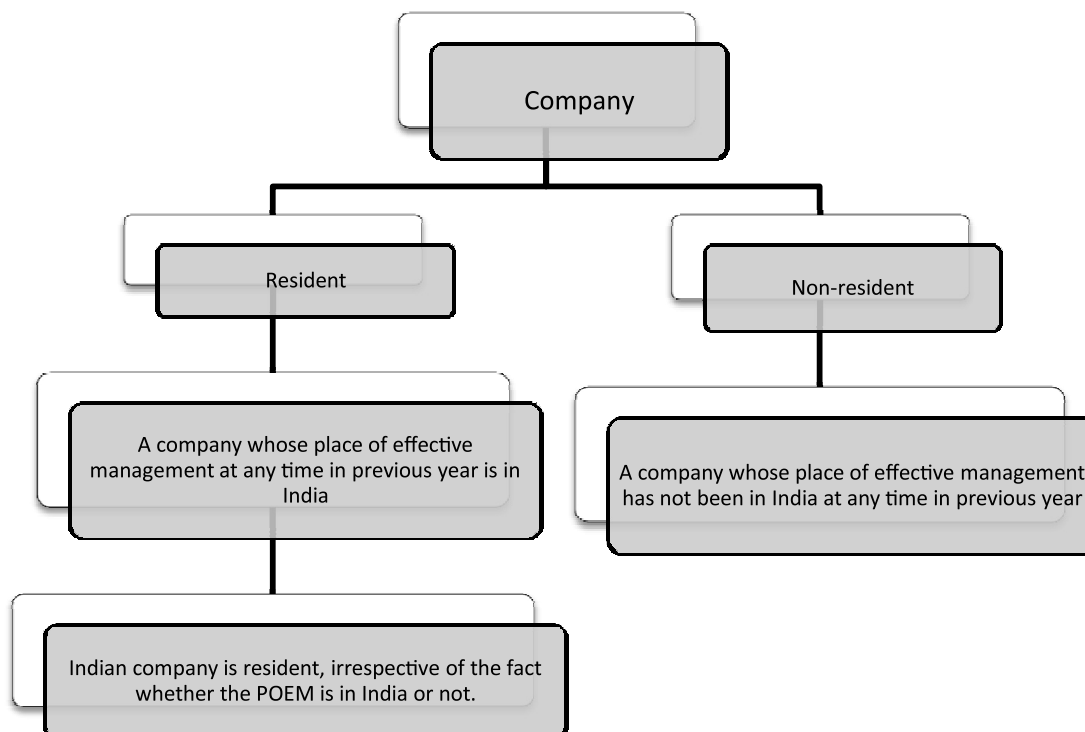
Once the residential status of an individual is identified, the rule of taxation could be applied to determine whether an income is to be taxed or not.

**TEST OF RESIDENCE FOR COMPANIES**

A company shall be said to be resident in India in any previous year, if –

- (i) it is an Indian company; or
- (ii) its place of effective management, in that year, is in India.

Accordingly, all Indian companies are always resident in India regardless of the place of its place of effective management. However, in the case of a foreign company the place of effective management is the basis on which the company's residential status is determinable.



For this purpose, Place of Effective Management means a place where Key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance made.

**Note:** Vide Circular No 08 of 2017 dated 23rd February, 2017, it has been clarified that the POEM provisions shall

not apply to a company having turnover or gross receipts of Rs. 50 crore or less in a financial year. So, in that cases, the criteria for determining the residential status would be Control and Management of the affairs.

Please refer details: [https://www.incometaxindia.gov.in/communications/circular/circular25\\_2017.pdf](https://www.incometaxindia.gov.in/communications/circular/circular25_2017.pdf)

### Guiding Principles for Determination of Place of Effective Management (POEM)

The process of determination of POEM would be primarily based on the fact as to whether or not the company is engaged in active business outside India. The PoEM concept is one of substance over form and since “residence” is to be determined for each year, POEM will also be required to be determined on year to year basis. An entity may have more than one place of management, but it can have only one place of effective management at any point of time.

The test of PoEM is based on whether the entity is earning only passive income and its operations are so structured that it is present or active in a country without paying applicable taxes. Thus, a company having key managerial people stationed in India with substantial asset base in India and selling goods through a subsidiary may yet claim that it has no PE in India and being incorporated outside India, it could end up paying very little tax. The concept of PoEM thus examines whether the company is in fact a tax resident of a foreign state with substantial operations outside India or whether the incorporation or having different places of business is only a device to evade tax by being a non-resident.

As per the PoEM guidelines, a company shall be said to be engaged in “active business outside India” if the passive income is not more than 50% of its total income and

- (i) less than 50% of its total assets are situated in India; and
- (ii) less than 50% of total number of employees are situated in India or are resident in India; and
- (iii) the payroll expenses incurred on such employees is less than 50% of its total payroll expenditure.

**Explanation :** For the aforesaid purpose :

The income shall be	As computed for tax purpose in accordance with the laws of the country of incorporation; or as per books of account, where the laws of the country of incorporation do not require such a computation.
The value of assets	<ul style="list-style-type: none"> <li>● In case of an individually depreciable asset, shall be the average of its value for tax purposes in the country of incorporation of the company at the beginning and at end of the previous year; and</li> <li>● In case of a pool of fixed assets being treated as a block for depreciation, shall be the average of its value for tax purposes in the country of incorporation of the company at the beginning and at end of the year;</li> <li>● In case of any other asset, shall be its value as per books of account.</li> </ul>
The number of employees	the number of employees shall be the average of the number of employees as at the beginning and at the end of the year and shall include persons, who though not employed directly by the company, perform tasks similar to those performed by the employees.
Pay roll	the term “pay roll” shall include the cost of salaries, wages, bonus and all other employee compensation including related pension and social costs borne by the employer.

Head Office	<p>“Head Office” of a company would be the place where the company senior management and their direct support staff are located or, if they are located at more than one location, the place where they are primarily or predominantly located.</p> <p>A company head office is not necessarily the same as the place where the majority of its employees work or where its board typically meets.</p>
Passive income	<p>“Passive income” of a company shall be aggregate of, income from the transactions where both the purchase and sale of goods is from / to its associated enterprises; and income by way of royalty, dividend, capital gains, interest or rental income.</p> <p><i>Note</i> : any income by way of interest shall not be considered to be passive income in case of a company which is engaged in the business of banking or is a public financial institution, and its activities are regulated as such under the applicable laws of the country of incorporation.</p>
Senior Management	<p>“Senior Management” in respect of a company means the person or persons who are generally responsible for developing and formulating key strategies and policies for the company and for ensuring or overseeing the execution and implementation of those strategies on a regular and on- going basis. While designation may vary, these persons may include : (i) Managing Director or Chief Executive Officer; (ii) Financial Director or Chief Financial Officer; (iii) Chief Operating Officer; and (iv) The heads of various divisions or departments.</p>

The conditions of having earned passive income of less than 50% and having less than 50% of assets, employees and payroll expenses have to be satisfied cumulatively. Thus, merely because say 95% of the income of a company is from royalty but 90% of its assets are outside India, it need not be scrutinized for PoEM since other conditions are not met. The company would be engaged in active business outside India. The idea is to identify such companies who may be trying to evade taxes by merely having incorporation or a set of directors operating from outside India while in substance it is carrying out activity in India and earning incomes which should be subject to tax in India.

The place of effective management in case of a company engaged in active business outside India shall be presumed to be outside India if the majority meetings of the board of directors of the company are held outside India. However, it is established that the Board of directors of the company are standing aside and not exercising their powers of management and such powers are being exercised by either the holding company or any other person (s) resident in India, then the place of effective management shall be considered to be in India. For the purpose of determining whether the company is engaged in active business outside India, the average of the data of the previous year and two years prior to that shall be taken into account. In case the company has been in existence for a shorter period, then data of such period shall be considered.

The determination of POEM would be a two stage process as follows:

**First Stage:** Identification or ascertaining the person or persons who actually make the key management and commercial decision for conduct of the company business as a whole.

**Second Stage :** Determination of place where these decisions are in fact being made.

**Note :** The place where these management decisions are taken would be more important than the place where such decisions are implemented. For the purpose of determination of POEM it is the substance which would be conclusive rather than the form.

**Some of the guiding principles for determining the POEM**

- (a) The location where a company's Board regularly meets and makes decisions may be the company place of effective management provided, the Board retains and exercises its authority to govern the company; and in substance, make the key management and commercial decisions necessary for the conduct of the company business as a whole. Mere formal holding of board meetings at a place would by itself not be conclusive for determination of POEM being located at that place.

**Note :** A company's board may delegate some or all of its authority to one or more committees such as an executive committee consisting of key members of senior management. In these situations, the location where the members of the executive committee are based and where that committee develops and formulates the key strategies and policies for mere formal approval by the full board will often be considered to be the company's place of effective management.

- (b) The location of a company's head office will be a very important factor in the determination of the company's place of effective management because it often represents the place where key company decisions are made. The following points need to be considered for determining the location of the head office of the company :

If the company's senior management and their support staff are based in a single location and that location is held out to the public as the company's principal place of business or headquarters then that location is the place where head office is located. If the company is more decentralized (for example where various members of senior management may operate, from time to time, at office located in the various countries) then the company's head office would be the location where these senior managers :

- i. are primarily or predominantly based; or
- ii. normally return to following travel to other locations; or
- iii. meet when formulating or deciding key strategies and policies for the company as a whole.

In situations where the senior management is so decentralised that it is not possible to determine the company's head office with a reasonable degree of certainty, the location of a company's head office would not be of much relevance in determining that company's place of effective management.

- (c) The use of modern technology impacts the place of effective management in many ways. It is no longer necessary for the persons taking decision to be physically present at a particular location. Therefore physical location of board meeting or executive committee meeting or meeting of senior management may not be where the key decisions are in substance being made. In such cases the place where the directors or the persons taking the decisions or majority of them usually reside may also be a relevant factor. It may be clarified that day to day routine operational decisions undertaken by junior and middle management shall not be relevant for the purpose of determination of POEM.

If the above factors do not lead to clear identification of POEM then the following secondary factors can be considered :

- i. Place where main and substantial activity of the company is carried out; or
- ii. Place where the accounting records of the company are kept.

The determination of POEM is to be based on all relevant facts related to the management and control of the company, and is not to be determined on the basis of isolated facts that by itself do not establish effective management, as illustrated by the following examples:

- i. The fact that a foreign company is completely owned by an Indian company will not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.
- ii. The fact that there exists a Permanent Establishment of a foreign entity in India would itself not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.
- iii. The fact that one or some of the Directors of a foreign company reside in India will not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.
- iv. The fact of, local management being situated in India in respect of activities carried out by a foreign company in India will not, by itself, be conclusive evidence that the conditions for establishing POEM have been satisfied.
- v. The existence in India of support functions that are preparatory and auxiliary in character will not be conclusive evidence that the conditions for establishing POEM in India have been satisfied.
- vi. The place where day to day, operational decisions are taken would not be PoEM.

Further, based on the facts and circumstances if it is determined that during the previous year the POEM is in India and also outside India then POEM shall be presumed to be in India if it has been mainly /predominantly in India.

**Example 1:** Company A Co. is a sourcing entity, for an Indian multinational group, incorporated in country X and is 100% subsidiary of Indian company (B Co.). The warehouses and stock in them are the only assets of the company and are located in country X. All the employees of the company are also in country X. The average income wise breakup of the company's total income for three years is:

- i. 30% of income is from transaction where purchases are made from parties which are non-associated enterprises and sold to associated enterprises;
- ii. 30% of income is from transaction where purchases are made from associated enterprises and sold to associated enterprises;
- iii. 30% of income is from transaction where purchases are made from associated enterprises and sold to non-associated enterprises; and
- iv. 10% of the income is by way of interest.

**Interpretation:** In this case passive income is 40% of the total income of the company. The passive income consists of :

- i. 30% income from the transaction where both purchase and sale is from/to associated enterprises; and
- ii. 10% income from interest.

The A Co. satisfies the first requirement of the test of active business outside India. Since no assets or employees of A Co. are in India the other requirements of the test is also satisfied. Therefore company is engaged in active business outside India.

**Example 2:** The other facts remain same as that in Example 1 with the variation that A Co. has a total of 50 employees. 47 employees, managing the warehouse, storekeeping and accounts of the company, are located in country X. The Managing Director (MD), Chief Executive Officer (CEO) and sales head are resident in India. The total annual payroll expenditure on these 50 employees is of Rs. 5 crore. The annual payroll expenditure in respect of MD, CEO and sales head is of Rs. 3 crore.

**Interpretation:** Although the first limb of active business test is satisfied by A Co. as only 40% of its total income is passive in nature. Further, more than 50% of the employees are also situated outside India. All the assets are

situated outside India. However, the payroll expenditure in respect of the MD, the CEO and the sales head being employees resident in India exceeds 50% of the total payroll expenditure. Therefore, A Co. is not engaged in active business outside India.

**Example 3:** The basic facts are same as in Example 1. Further facts are that all the directors of the A Co. are Indian residents. During the relevant previous year 5 meetings of the Board of Directors are held of which two were held in India and 3 outside India with two in country X and one in country Y.

**Interpretation:** A Co. is engaged in active business outside India as the facts indicated in Example 1 establish. The majority of board meetings have been held outside India. Therefore, the POEM of A Co. shall be presumed to be outside India.

**Example 4:** The facts are same as in Example 1 but it is established by the Assessing Officer that although A Co.'s senior management team signs all the contracts, for all the contracts above Rs. 10 lakh the A Co. must submit its recommendation to B Co. and B Co. makes the decision whether or not the contract may be accepted. It is also seen that during the previous year more than 99% of the contracts are above Rs. 10 lakh and over past years also the same trend in respect of value contribution of contracts above Rs. 10 lakh is seen.

**Interpretation:** These facts suggest that the effective management of the A Co. may have been usurped by the parent company B Co. Therefore, PoEM of A Co. may in such cases be not presumed to be outside India even though A Co. is engaged in active business outside India and majority of board meeting are held outside India.

**For Detailed POEM Guidelines:**

<http://www.incometaxindia.gov.in/news/circular06/2017.pdf>

## SCOPE OF TOTAL INCOME [SECTION 5]

Section 5 of Income Tax Act, 1961 provides Scope of total Income in case of person who is a resident, in the case of a person not ordinarily resident in India and person who is a non-resident. Income can be from any source which (a) is received or is deemed to be received in India in such year by or on behalf of such person ; or (b) accrues or arises or is deemed to accrue or arise to him in India during such year ; or (c) accrues or arises to him outside India during such year .

Scope of total income has been defined on the basis of Residential status

### (A) Resident and Ordinarily Resident Assessee

According to Sub-section (1) of Section 5 of the Act the total income of a resident and ordinarily resident assessee would consist of :

- (i) income received or deemed to be received in India during the accounting year by or on behalf of such person;
- (ii) income which accrues or arises or is deemed to accrue or arise to him in India during the accounting year;
- (iii) income which accrues or arises to him outside India during the accounting year.

*It is important to note that under clause (iii) only income accruing or arising outside India is included. Income deemed to accrue or arise outside India is not includible.*

### (B) Resident but Not Ordinarily Resident In India

Proviso to section (1) of section 5 the total income in case of resident but not ordinarily resident in India

- (i) income received or deemed to be received in India during the accounting year by or on behalf of such person;
- (ii) income which accrues or arises or is deemed to accrue or arise to him in India during the accounting year;
- (iii) income which accrues or arises to him outside India during the previous year if it is derived from a business controlled in or a profession set up in India.

**(C) Non-Resident**

Sub-section (2) of Section 5 provides that the total income of a non-resident would comprise of :

- (i) income received or deemed to be received in India in the accounting year by or on behalf of such person;
- (ii) income which accrues or arises or is deemed to accrue or arise to him in India during the previous year.

**Rule of Taxation on the basis of Residential Status**

Nature of Income	ROR	RNOR	NR
Income received in India (Whether accrued in or outside India)	Taxed	Taxed	Taxed
Income deemed to be received in India (Whether accrued in or outside India)	Taxed	Taxed	Taxed
Income accruing or arising in India (Whether received in India or outside India)	Taxed	Taxed	Taxed
Income deemed to accrue or arise in India (Whether received in India or outside India)	Taxed	Taxed	Taxed
Income received and accrued outside India from a business controlled or a profession set up in India	Taxed	Taxed	Not Taxed
Income received and accrued outside India from a business controlled from outside India or a profession set up outside India	Taxed	Not Taxed	Not Taxed
Income earned and received outside India but later on remitted to India (Whether tax incidence arises at the time of remittance)	Not Taxed	Not Taxed	Not Taxed

**Explanation 1** - Income accruing or arising outside India shall not be deemed to be received in India within the meaning of this section by reason only of the fact that it is taken into account in a balance sheet prepared in India.

**Explanation 2** - For the removal of doubts, it is hereby declared that income which has been included in the total income of a person on the basis that it has accrued or arisen or is deemed to have accrued or arisen to him shall not again be so included on the basis that it is received or deemed to be received by him in India.

**INCOME RECEIVED OR DEEMED TO BE RECEIVED IN INDIA**

**Income received in India:** Income received in India is taxable regardless of the assessee's residential status therefore it has great significance.

- (i) The receipt contemplated for this purpose refers to the first receipt of the amount in question as the income of the assessee.

For instance, if A receives his salary at Delhi and sends the same to his father, the salary income of A is a receipt for tax purposes only in the hands of A; his father cannot also be said to have received income when he receives a part of the income of A. In the hands of A's father it is only a receipt of a sum of money but not a receipt of income.

- (ii) **Method of Accounting:** Although receipt of income is not the sole test of its taxability, the receipt of income would be the primary basis for determining the taxability of the amount in cases where the assessee follows the cash system of accounting; however, where the assessee follows the mercantile system of accounting, the income would become taxable as the income of the accounting year in which it falls due to the assessee regardless of the date or place of its actual receipt.
- (iii) While considering the receipt of income for tax purposes both the place and the date of its receipt must be taken into account. The income in question should be not only received during the accounting year relevant to the assessment year but must also be received in India in order to constitute the basis of taxation. Thus, if an item of income is received outside India and after a few years is brought into India the subsequent receipt of the same amount in India should not be taken as the basis of taxing the same since the same income cannot be received twice and it will be known as Remittances.
- (iv) For the purpose of taxation both actual and constructive receipt must be taken into account. Receipt by some other person on behalf of the assessee should be treated as receipt by the assessee for being taxed in his hands.
- (v) The question of taxability of a particular income received by the assessee depends upon the nature of income. For instance, income from salaries and interest on securities would attract liability to tax immediately when it falls due to the assessee regardless of its actual receipt by or on behalf of the assessee.

**Income deemed to be received in India:** In addition to the income actually received by the assessee or on his behalf, certain other incomes not actually received by the assessee and/or not received during the relevant previous year, are also included in his total income for income tax purposes. Such incomes are known as income deemed to be received. Some of the examples of such income are:

- (i) All sums deducted by way of taxes at source.
- (ii) Incomes of other persons which are included in the income of the assessee i.e. clubbing provision.
- (iii) The amount of unexplained or unrecorded investments.
- (iv) The amount of unexplained or unrecorded moneys, etc.
- (v) The annual accretion in the previous year to the balance standing at the credit of an employee participating in a Recognised Provident fund to the extent provided in Rule 6 of Part A of the Fourth Schedule [Section 7(i)]. The contributions made by the employer to Recognised Provident Fund in excess of 12% of the employees salary and the interest credited to the Provident Fund account of the employee

in excess of the prescribed rate shall be included in the salary income of the employee. This amount is known as annual accretion.

- (vi) The transferred balance in a Recognised Provident Fund to the extent provided in Rule 11(4) of Part A - Fourth Schedule [Section 7(ii)].
- (vii) Any dividend declared by a Company or distributed or paid by it within the meaning of Section 2(22) [Section 8(a)].
- (viii) Any interim dividend unconditionally made available by the Company to the member who is entitled to it [Section 8(b)].

### INCOME ACCRUE OR ARISE IN INDIA

The accrual of income is different and distinct from the receipt of income discussed above. Sometimes in the context of accrual or arise the word earned is used. A person may be said to have earned his income in the sense that he has contributed to the production by rendering of goods or services. But in order that the income may be said to have accrued to him, an additional element is necessary, that is, he must have created a debt in his favour. Income is said to accrue when it comes into existence for the first time or at the point of time when the right to receive the income arises although the right may be exercised or exercisable at a future date. Income is said to be received when it reaches the assessee. When the right to receive the income becomes vested in the assessee, it is said to accrue or arise.

Income is said to accrue only to that person who is lawfully entitled to that income. Income accrues at the place where the source of the income is situated, which may or may not be the same as the place from which the business activities are carried on. Normally, income accrues at the place where the contract yielding the income is entered into and for this purpose the contract should be taken to have been entered into at the place where the offer is accepted.

#### CASE LAW

2018

*CIT v. Millennium Estate (P.) Ltd.*

***Income in respect of sale of flats accrued when possession of flat was given and not when allotment letter was issued [in favour of assessee]***

The assessee carried on business as a contractor and developer. During scrutiny, the Assessing Officer found that an amount was shown as advances received from its buyers. The assessee submitted that aforesaid amounts were received as advance at time of allotment on 14-3-2007 and that further consideration was received on 1-4-2007, when possession of flat was given, and, thus, said sum was chargeable to tax in next assessment year. However, the Assessing Officer treated said sum as accrued income in subject assessment year holding that sale of flats had taken place when they were allotted under an allotment letter.

Held that from the allotment letter and possession letter, it was very evident that possession of flats was given on receipt of total consideration, i.e., only on 1-4-2007. The said amount was an advance during subject assessment year and said income accrued as income in assessment year 2007-08.

2018

*Principal CIT v. Davangere Urban Co-operative Bank Ltd.*

***Income from Non Performing Assets (NPA) should be assessed on cash basis and not on mercantile basis, despite assessee following mercantile system of accounting [Assessment year 2010-11] [in Favour of assessee]***

Held that Income from NPA should be assessed on cash basis and not on mercantile basis, despite the assessee following mercantile system of accounting. In view of aforesaid legal position, the Assessing Officer was not justified in bringing to tax on interest on non-performing assets on accrual basis just because the assessee followed hybrid system of accounting.

### **INCOME DEEMED TO ACCRUE OR ARISE IN INDIA [SECTION 9]**

Certain types of income are deemed to accrue or arise in India even though they may actually accrue or arise outside India. The categories of income which are deemed to accrue or arise in India are :

- (1) Any income accruing or arising to an assessee in any place outside India whether directly or indirectly
  - (a) through or from any business connection in India,
  - (b) through or from any property in India,
  - (c) through or from any asset or source of income in India, or
  - (d) through the transfer of a capital asset situated in India [Section 9(1)(i)].
- (2) Income, which falls under the head “Salaries”, if it is earned in India. Salary payable for service rendered in India would be treated as earned in India. Further, any income under the head “Salaries” payable for rest period or leave period which is preceded and succeeded by services rendered in India, and forms part of the service contract of employment, shall be regarded as income earned in India [Section 9(1)(ii)].
- (3) Income from Salaries which is payable by the Government to a citizen of India for services rendered outside India (However, allowances and perquisites paid outside India by the Government is exempt) [Section 9(1)(iii)].
- (4) Dividend paid by a Indian company outside India [Section 9(1)(iv)].
- (5) Interest [Section 9(1)(v)]
- (6) Royalty [Section 9(1)(vi)]
- (7) Fees for technical services [Section 9(1)(vii)]
- (8) income arising outside India, being any sum of money referred to in sub-clause (xvii) of clause (24) of section 2, paid by a person resident in India.

#### **(1) (a) Income by virtue of Business Connection**

In cases where all the operations or activities of a business are not carried on in India but a part of them arise by virtue of the business connection in India, the income which is deemed to accrue or arise in India, should be taken to be only that part which could reasonably be attributed to the operations carried on in India. Rule 10 of the Income-tax Rules contains the basis on which the income attributable to the operations carried out in India could be deemed to accrue or arise in India.

However, where a substantial part of a non-residents output is sold in the Indian market through brokers to various customers in India, or mere rendering of services outside India to a person carrying on business in India does not amount to a business connection in India.

Similarly, where an Indian exporter selling goods through non-resident selling agents, receives sale price in India, credits commission on sales to non-resident agents in his books of account and remits the amount to them later, such commission to non-residents is neither received or deemed to be received in India nor deemed to accrue or arise in India [*C.I.T. v. Toshoku Ltd. (1980) 125 ITR p. 525 (S.C.)*].

The expression business connection includes:

- (i) the maintenance of a branch office, factory, agency, receivership, management or other establishment for the purchase or sale of goods or for transacting any other business;
- (ii) the erection of a factory where the raw products purchased locally are processed or converted into some form suitable for export outside India;
- (iii) appointing an agent or agents in India for the systematic and regular purchase of raw materials or other commodities or for the sale of the non-resident's goods, or for any other purpose;
- (iv) the formation of a close financial association between a resident and a non-resident company which may or may not be related to one another as a holding and subsidiary company;
- (v) the formation of a subsidiary company to sell or otherwise deal with the products of the non-resident parent company;
- (vi) the grant of a continuing license to a non-resident for the purpose of exploitation for profit of an asset belonging to the non-resident;
- (vii) any business activity carried out through a person acting on behalf of the non-resident if.
  - He must have an authority which is habitually exercised to conclude contracts on behalf of the non-resident. However, if his activities are limited to the purchase of goods or merchandise for the non-resident, this provision will not apply.
  - Where he has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident, a business connection is established.
  - Business connection is also established where he habitually secures orders in India, mainly or wholly for the non-resident. Further, there may be situations when other non-residents control the above-mentioned non-resident. Secondly, this non-resident may also control other non-residents. Thirdly, all other non-residents may be subject to the same common control, as that of the non-resident. In all the three situations, business connection is established, where a person habitually secures orders in India, mainly or wholly for such non-residents. Exception: "Business connection", however, shall not be held to be established in cases where the non-resident carries on business through a broker, general commission agent or any other agent of an independent status, if such a person is acting in the ordinary course of his business. A broker, general commission agent or any other agent shall be deemed to have an independent status where he does not work mainly or wholly for the non-resident.
- (viii) Significant economic presence of a non-resident in India shall constitute "business connection" in India and "significant economic presence" for this purpose, shall mean:
  - (a) transaction in respect of any goods, services or property carried out by a non-resident with any person in India including provision of download of data or software in India, if the aggregate of

payments arising from such transaction or transactions during the previous year exceeds such amount as may be prescribed; or

- (b) systematic and continuous soliciting of business activities or engaging in interaction with such number of users in India, as may be prescribed:

Provided that the transactions or activities shall constitute significant economic presence in India, whether or not –

- (i) the agreement for such transactions or activities is entered in India; or
- (ii) the non-resident has a residence or place of business in India; or
- (iii) the non-resident renders services in India

Provided further that the transactions or activities which are confined to the purchase of goods in India for the purpose of export shall not constitute significant economic presence in India.

Provided further that only so much of income as is attributable to the transactions or activities referred to in clause (a) or clause (b) shall be deemed to accrue or arise in India.

### **No Business connection in India in following cases of Non-Resident**

1. Tax Exemption for encouraging Export: For the purpose of encouraging exports, a specific tax concession has been given by providing that no income shall be deemed to accrue or arise in India to a non-resident through or from his operations which are confined to the purchase of goods in India for the purpose of export. Consequently, the exemption would not be available if the goods purchased in India are sold in India or are not exported outside India. Further, if the non-resident works up the raw-materials into finished or semi-finished products, the exemption would be withdrawn and he would become chargeable on such portion of the profits as is attributable to his manufacturing it in India.
2. Operations confined to collection of news and views for transmission outside India by or on behalf of Non Resident who is engaged in the business of running news agency or of publishing newspapers, magazines or out and out sale by the parties concerned journals;
3. Operations confined to shooting of cinematograph films in India if such Non-Resident is :
  - (a) an Individual - he should not be a citizen of India; or
  - (b) a firm - the firm should not have any partner who is a citizen of India or who is resident in India; or
  - (c) a company - the company does not have any shareholder who is a citizen of India or who is resident in India.

### **(1) (b) Income arising from any property in India**

Income arising in a foreign country from any property situated in India would be deemed to accrue or arise in India. In this context, the term property does not refer to house property alone but it refers to all tangible properties whether movable or immovable. For instance, the rent or hire charges for the use of buildings or machinery of the assessee which, under an agreement are payable only outside India, would be deemed to accrue or arise in India.

### **(1) (c) Income arising from any assets or source of Income in India**

Income arising through or from any asset or source of income in India would also be deemed to accrue or arise in India. In this context, the term source means not a legal concept but something which a practical man would regard as a real source of income.

**(1) (d) Income arising from transfer of any capital assets situated in India**

- Capital gains arising to an assessee from the transfer of a capital asset situated in India would be deemed to accrue or arise in India irrespective of the fact whether the capital asset in question represents a movable or immovable property or a tangible or intangible asset.
- It is also immaterial whether the consideration for the transfer of the capital asset is actually paid or payable in India or outside.
- The place of registration of the document of transfer of property is equally immaterial.
- However, if the capital asset, prior to the transfer, is situated outside India, the provisions of Section 9(1) would not apply to deem the capital gains arising on the transfer as accruing or arising in India for purposes of its taxation in India.

**(2) Income from Salaries**

- Income which is chargeable under the head Salaries / Pension is deemed to accrue or arise in India in all cases when earned in India. For this purpose income is said to be earned in India if the services are rendered in India.
- The actual place of accrual of the salaries, the residential status of the employer, the citizenship or nationality of the employee and whether the employee is a Government servant or an employee of private enterprise are immaterial. However, under Sub-section (2) of Section 9, any pension payable outside India to a person residing permanently outside India should not be deemed to accrue or arise in India if the pension is payable to civil servants and retired judges provided they were appointed before the 15th August, 1947 and continued to serve after the constitution came into operation.

Barring this exception, non-residents and not ordinarily residents entitled to receive salary or pension earned by them in India would be deemed to receive income which has accrued in India even though the income may be actually accruing and received outside India.

**(3) Income from Salaries which is payable by the Government to a citizen of India for services rendered outside India**

- Income from salaries payable by the Government to a citizen of India outside India for his services rendered outside India, is deemed to accrue or arise in India even though the income is actually accruing outside India and is also received outside India. Thus, under this provision, salary income of all Government servants, working outside India is deemed to accrue in India. In the absence of this provision they would not be chargeable to tax in respect of such income as they would, after some time, become non-residents.

This provision to deem income as accruing in India applies only in respect of their income from salary but not in respect of the allowances and perquisites to which they are entitled to while serving in a foreign country. Section 10(7) of the Income-tax Act, 1961 contains a specific provision to exempt Government servants from tax on their services in a foreign country partly to meet the higher cost of living in that country.

- Salaries paid by the Indian Government in a foreign country to citizens of the foreign country should not, however, be deemed to accrue in India since this provision applies only to Indian citizens employed by the Government who are rendering service outside India.

**(4) Dividend paid by a Indian company outside India**

- Dividend paid by any Indian company outside India is deemed to accrue or arise in India and the income is consequently chargeable to income-tax irrespective of the fact whether the dividend is interim dividend or a final dividend and whether it is an actual dividend or a notional dividend.
- The place of declaration of the dividend is immaterial and the date of payment is equally immaterial for deeming the income to accrue in India.
- Normally, dividend income arises at the place where the source of income is situated, i.e., where the shares yielding the income are kept. Shares are said to be situated at the place where the share register of the company is kept. While the share register of a company should ordinarily be kept at the place where its registered office is located, even if the share register is kept outside India and the dividends are declared outside India, the dividend would still be deemed to accrue in India because the company is an Indian company.
- Dividends declared by foreign companies outside India would not, however, be deemed to accrue or arise in India even in cases where the foreign company is resident in India because of the control and management of its affairs being situated wholly in India.
- In order to deem the dividend income as arising in India, the residential status of the shareholder as also the status of the assessee, whether he is an individual, company or local authority, are irrelevant.

**(5) Interest**

Interest payable in following cases will be deemed to accrue or arise in India and will be taxable in the hands of recipient irrespective of his residential status (i.e., ROR, RNOR or NR).

Interest payable by :

- Government; or
- A Resident in India, except where interest is payable in respect of moneys borrowed and used for the purpose of business or profession carried outside India or earning any income from any source outside India (i.e., Interest payable by a Resident for loan used in India for any purpose, whether for business or profession or otherwise);
- A Non-Resident in India provided interest is payable in respect of moneys borrowed and used for a business or profession carried on in India (i.e., Interest payable by a Non-Resident for loan used for only business or profession in India).

**(6) Royalty**

Royalty payable in following cases will be deemed to accrue or arise in India and will be taxable in the hands of recipient irrespective of his residential status (i.e., ROR, RNOR or NR).

Royalty payable by:

- Government; or
- A Resident in India except where it is payable in respect of any right/information/property used for the purpose of a business or profession carried on outside India or earning any income from any source outside India (i.e., Royalty payable by a Resident for right/information/property used for any purpose in India whether business or profession or for earning other incomes);
- A Non-Resident in India provided royalty is payable in respect of any right/information/property used

for the purpose of the business or profession carried on in India or earning any income from any source in India (i.e., Royalty payable by a Non-Resident for right/information/property used for any purpose in India whether business or profession or for earning other incomes).

### (7) Fees for Technical Services

Fees for technical services payable in following cases will be deemed to accrue or arise in India and will be taxable in the hands of recipient irrespective of his residential status (i.e., ROR, RNOR or NR).

Fees for technical services payable by:

- Government; or
- A Resident in India except where services are utilized for the purpose of a business or profession carried on outside India or earning any income from any source outside India (i.e., Fees for technical services payable by a Resident for services utilised for any purpose in India whether business or profession or for earning other incomes);
- A Non-Resident in India provided fee is payable in respect of services for the purpose of a business or profession carried on in India or earning any income from any source in India (i.e., Fees for technical services payable by a Resident for services utilised for any purpose in India whether business or profession or for earning other incomes);

### (8) Income arising outside India, being any sum of money referred to in sub-clause (xviiia) of clause (24) of section 2, paid by a person resident in India –

- (a) on or after the 5th day of July, 2019 to a non-resident, not being a company, or to a foreign company; or
- (b) on or after the 1st day of April, 2023 to a person not ordinarily resident in India within the meaning of clause (6) of section 6.

#### **Illustration 11:**

Mr. X earns the following income during the previous year ended 31st March, 2026. Determine the income liable to tax for the assessment year 2026-27 if Mr. X is (a) resident and ordinarily resident in India, (b) resident and not ordinarily resident in India, and (c) non-resident in India during the previous year ended 31st March, 2026.

- Profits on sale of a building in India but received in Holland – Rs. 20,000
- Pension from former employer in India received in Holland – Rs. 14,000
- Interest on U.K. Development Bonds (1/4 being received in India) – Rs. 20,000
- Income from property in Australia and received in U.S.A. – Rs. 15,000
- Income earned from a business in Abyssinia which is controlled from Zambia (Rs. 30,000 received in India) – Rs. 70,000
- Dividend on shares of an Indian company but received in Holland – Rs. 10,000
- Profits not taxed previously brought into India – Rs. 40,000
- Profits from a business in Nagpur which is controlled from Holland – Rs. 27,000

**Solution :** Computation of income liable to tax :

<i>Particular</i>	<i>Resident &amp; Ordinarily Resident (Rs.)</i>	<i>Resident but not Ordinarily Resident (Rs.)</i>	<i>Non-Resident (Rs.)</i>
Profits on sale of a building in India but received in Holland (accrued in India received outside India)	20,000	20,000	20,000
Pension from former employer in India received in Holland (accrued in India, received out of India)	14,000	14,000	14,000
Interest on U.K. Development Bonds (Accrued out of India, 1/4th received in India)	5,000	5,000	5,000
Interest on U.K. Development Bonds (Accrued out of India, 3/4th received out of India)	15,000	Nil	Nil
Income from property in Australia and received in U.S.A. (Accrued and received out of India)	15,000	Nil	Nil
Income earned from a business in Abyssinia which is controlled from Zambia (Business controlled outside India)	70,000	30,000	30,000
Dividend on shares of an Indian company but received in Holland (Accrued in India)	10,000	10,000	10,000
Profits not taxed previously brought into India (Not an income so not taxable)	Nil	Nil	Nil
Profits from a business in Nagpur which is controlled from Holland (Accrued in India)	27,000	27,000	27,000
<b>Total</b>	<b>1,76,000</b>	<b>1,06,000</b>	<b>1,06,000</b>

**Illustration 12:**

A had the following income during the previous year ended 31st March, 2026:

- Salary Received in India for three Months - Rs. 9,000
- Income from house property in India - Rs. 13,470
- Interest on Saving Bank Deposit in State Bank of India - Rs. 1,000
- Amount brought into India out of the past untaxed profits earned in Germany - Rs. 20,000
- Income from agriculture in Indonesia being invested there - Rs. 12,350
- Income from business in Bangladesh, being controlled from India - Rs. 10,150
- Dividends received in Belgium from French companies, out of which Rs. 2,500 were remitted to India - Rs. 23,000

You are required to compute his total income for the assessment year 2026-27 if he is : (i) a resident; (ii) a not ordinarily resident, and (iii) a Non-resident.

**Solution :**

Computation of total income of A is given below:

<i>Particular</i>	<i>Resident &amp; Ordinarily Resident (Rs.)</i>	<i>Resident but not Ordinarily Resident (Rs.)</i>	<i>Non-Resident (Rs.)</i>
Salary Received in India for three Months (Indian received in India)	9,000	9,000	9,000
Income from house property in India (Income accrue or arise in India)	13,470	13,470	13,470
Interest on Saving Bank Deposit in State Bank of India (Income accrue or arise in India)	1,000	1,000	1,000
Amount brought into India out of the past untaxed profits earned in Germany ( not an income, hence not taxable)	Nil	Nil	Nil
Income from agriculture in Indonesia being invested there (Income accrue or arise outside India)	12,350	Nil	Nil
Income from business in Bangladesh, being controlled from India (it is supposed that the money is not received in India) (Income accrued outside India from a business controlled from India)	10,150	10,150	Nil
Dividends received in Belgium from French companies (Income accrue outside India. Remittance to India is irrelevant)	23,000	Nil	Nil
<b>Total</b>	<b>68,970</b>	<b>33,620</b>	<b>23,470</b>

**Illustration 13 :**

Mr. Y earns the following income during the previous year ended on 31st March, 2026. Determine the income liable to tax for the assessment year 2026-27 if Mr. Y is (a) resident and ordinary resident (b) resident and not ordinary resident, and (c) non-resident in India during the previous year ended on 31st March, 2026.

- (i) Honorarium received from Government of India (Travelling and other incidental expenses of Rs. 7,000 were incurred in this connection)- Rs. 20,000

- (ii) Profits earned from a business in Tamilnadu controlled from Pakistan - Rs. 50,000
- (iii) Profits earned from a business in U.K. controlled from Delhi - Rs. 30,000
- (iv) Profits earned from a business in U.S.A. controlled from Pakistan and amount deposited in a bank there - Rs. 40,000
- (v) Income from a house property in France, received in India - Rs. 10,000
- (vi) Past untaxed foreign income brought into India during the year - Rs. 25,000
- (vii) Dividends from a German company credited to his account in Pakistan - Rs. 35,000
- (viii) Agricultural income from Burma not remitted to India - Rs. 40,000
- (ix) Pension for services rendered in India, but received in Pakistan - Rs. 30,000

**Solution:**

Computation of Income liable to tax of Mr. Y is given below:

<i>Particular</i>	<i>Resident &amp; Ordinarily Resident (Rs.)</i>	<i>Resident but not Ordinarily Resident (Rs.)</i>	<i>Non-Resident (Rs.)</i>
Honorarium received from Govt. of India	20,000	20,000	20,000
Profits earned from a business in Tamilnadu controlled from Pakistan (Income accrue or arise in India)	50,000	50,000	50,000
Profit earned from a business in U.K. controlled from Delhi (Income accrue or arise outside India from a business controlled from India)	30,000	30,000	-
Profits earned from a business in USA controlled from Pakistan and amount deposited in a Bank there (Income accrue outside India)	40,000	-	-
Income from a house property in France, received in India (Income received in India)	10,000	10,000	10,000
Past untaxed foreign income brought into India during the year (Not taxable as profit of past years, also remittance is irrelevant)	-	-	-
Dividends from a foreign company credited to his account in Pakistan (Income accrue outside India)	35,000	-	-
Agricultural income from Burma not remitted to India (Income accrue outside India)	40,000	-	-

Pension for Services rendered in India, but received in Pakistan (Income deemed to accrue or arise in India)	30,000	30,000	30,000
<b>Total</b>	<b>2,55,000</b>	<b>1,40,000</b>	<b>1,10,000</b>

Computation of Tax Liability includes following steps:

1. Determine the category of person
2. Determine the residential status of the person as per section 6
3. Calculate the Total income as per the provisions
4. Calculate the tax on income.

### COMPUTATION OF TAXABLE INCOME AND TAX LIABILITY OF AN ASSESSEE

Income tax is a charge on the assessee's income. Income Tax law lays down the provisions for computing the taxable income on which tax is to be charged. Taxable income of an assessee shall be calculated in the following manner.

1. Determine the residential status of the person as per section 6 of the Income tax Act, 1961.
2. Calculate the income as per the provisions of respective heads of income. Section 14 classifies the income under five heads.
  - (i) Income from salaries
  - (ii) Income from House Property
  - (iii) Profits and gains of business or Profession
  - (iv) Capital Gains
  - (v) Income from other sources.
3. Only net income after considering all the deductions and allowances given under the respective heads is taxed.
4. Exclude the income exempt under section 10 of the Act.
5. Aggregate of incomes computed under the 5 heads of income after applying clubbing provisions and making adjustments of set off and carry forward of losses is known as Gross Total Income.
6. Deduct therefrom the deductions admissible under Sections 80C to 80U (if applicable). The balance is called Total income.
7. The total income is rounded off to the nearest multiple of Rupees ten. (Section 288A)
8. Add agriculture income (if any) in the total income calculated in (6) above. Then calculate tax on the aggregate as if such aggregate income is the Total Income.
9. Calculate income tax on the net agricultural income as increased by Rs. 2,50,000/3,00,000/5,00,000 as the case may be, as if such increased net agricultural income were the total income.
10. The amount of income tax determined under (9) above will be deducted from the amount of income tax determined under (8) above.

11. Calculate income tax on capital gains under Section 112, and on other income at specified rates.
12. The balance of amount of income tax left as per (10) above plus the amount of income tax at (11) above will be the income tax in respect of the total income.
13. Deduct the following from the amount of tax calculated under (12) above.
  - Rebate under section 87A (if applicable).
  - Tax deducted and collected at source.
  - Advance tax paid.
  - Double taxation relief (Section 90 or 91).
14. The balance of amount left after deduction of items given in (13) above, shall be the net tax payable or net tax refundable for the assessee. Net tax payable/refundable shall be rounded off to the nearest multiple of Ten rupees (Section 288B).
15. Along with the amount of net tax payable, the assessee shall have to pay penalties or fines, if any, imposed on him under the Income-tax Act.

For calculation of income, amount received is classified under 5 heads of income; it is then to be adjusted with reference to the provisions of the Income Tax laws in the following manner.

<i>Particulars</i>	<i>Amount (Rs.)</i>
<b>Income under the head :</b>	
+ Income from Salaries	XXX
+ Income from House Property	XXX
+ Profits and gains of business or profession	XXX
+ Capital gains	XXX
+ Income from other sources	XXX
<b>Adjustment in respect of :</b>	
+ Clubbing of Income	XXX
– Set off and carry forward of losses	(XXX)
<b>= Gross Total Income</b>	XXX
– Deductions under section 80C to 80U (or Chapter VIA)	(XXX)
<b>= Total Income</b>	XXX

Tax on Total Income	XXX
Less : Rebate & Relief	(XXX)
Add : Interest u/s 234A/B/C	XXX
Total Tax Liability	XXX
Less : TDS / Advance Tax	(XXX)
Net Tax Payable / Refundable	XXX

#### LESSON ROUND-UP

- Tax is the financial charge imposed by the Government on income, commodity or activity. Government imposes two types of taxes namely Direct taxes and Indirect taxes. Direct tax is one where burden of tax is directly on the payer. While Indirect tax is paid by the person other than the person who utilizes the product or service.
- The Income tax Act contains the provisions for determination of taxable income, determination of tax liability, procedure for assessment, appeal, penalties and prosecutions.
- Every year a Budget is presented before the parliament by the Finance Minister. One of the important components of the Budget is the Finance Bill. The Bill contains various amendments such as the rates of income tax and other taxes. When the Finance Bill is approved by both the houses of parliament and receives the assent of President, it becomes the Finance Act.
- To levy income tax, one must have the understanding of the various concepts related to the charge of tax like previous year, assessment year, Income, total income, person etc. These are summarized below:
- **Income:** No precise definition of the word 'Income' is available under the Income-tax Act, 1961. The definition of Income as given in Section 2(24) of the Act starts with the word includes therefore the list is inclusive not exhaustive.
- **Assessee:** In common parlance every tax payer is an assessee. However, the word assessee has been defined in Section 2(7) of the Act according to which assessee means a person by whom any tax or any other sum of money (i.e. interest, penalty etc.) is payable under the Act.
- **Person:** Income-tax is charged in respect of the total income of the previous year of every person. Hence, it is important to know the definition of the word person.
- **Assessment year** means the period of twelve months commencing on 1st April every year.
- **Previous year:** Income earned in a year is taxable in the next year. The year in which income is earned is known as previous year.
- **Computation of Income:** Income tax is a charge on the assessee's income. Income Tax law lays down the provisions for computing the taxable income on which tax is to be charged.
- Total income of an assessee cannot be computed unless the person's residential status in India during the previous year is known. According to the residential status, the assessee can either be;

- (i) Resident in India, or
  - (ii) Non-resident in India.
- Section 6 of the Income-tax Act prescribes the tests to be applied to determine the residential status of all tax payers for purposes of income-tax. There are three alternative tests to be applied for individuals, two for companies and Hindu Undivided Families and firms, associations of persons, bodies of individuals and artificial juridical persons.
  - **Residential status of Individual:** The residential status of individual is determined on the basis of number of days he / she is physically present in India.
  - **Residential status of HUF :** The test to be applied to determine the residential status of a HUF, Firm or other Association of Persons is based upon the control and management of the affairs of the assessee concerned. A HUF, firm or other association of persons is said to be resident in India within the meaning of Section 6(2) in any previous year, if during that year the control and management of its affairs is situated wholly or partly in India during the relevant previous year. If the control and management of its affairs is situated wholly outside India during the relevant previous year, it is considered non-resident.
  - A HUF can be “not ordinarily resident” If manager/karta has been a not ordinarily resident in India in the previous year in accordance with the tests applicable to individuals.
  - Firms, association of persons, local authorities and other artificial juridical persons can be either resident (ordinarily resident) or non-resident in India but they cannot be not ordinarily resident in India.
  - Residential status of Company: All Indian companies within the meaning of Section 2(26) of the Act are always resident in India regardless of the place of effective management. In the case of a foreign company, the place of effective management (POEM) is the basis on which the company’s residential status is determinable.
  - Basis of charge: Section 4 of the Act imposes a charge of tax on the total or taxable income of the assessee. The meaning and scope of the expression of total income is contained in Section 5. The total income of an assessee cannot determined unless we know the residential status in India during the previous year. The scope of total income and consequently the liability to income-tax also depends upon the following facts:
    - i. whether the income accrues or is received in India or outside,
    - ii. the exact place and point of time at which the accrual or receipt of income takes place, and
    - iii. the residential status of the assessee.

### TEST YOURSELF

*(These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.)*

#### Multiple Choice Questions ‘MCQs’

1. Person is defined under section \_ of the Income Tax Act, 1961
  - (a) 2 (31)
  - (b) 2 (7)

(c) 2 (9)

(d) 3

Answer: (a)

2. Association of persons consists of .....

(a) Individuals (only)

(b) Company

(c) Any Person other than (a)

(d) Any kind of person

Answer: (d)

3. Body of Individuals consists of .....

(a) Individuals (only)

(b) Company

(c) Any Person other than (a)

(d) Any kind of person

Answer: (a)

4. Income is defined under section ..... of the Income Tax Act, 1961

(a) 2 (31)

(b) 2 (24)

(c) 2 (9)

(d) 3

Answer: (b)

5. Which of the following is not a revenue receipt?

(i) Compensation received for the loss of a capital asset

(ii) Compensation received for damage to or loss of a trading asset.

(iii) Profits on purchase and sale of shares by a share broker on his own account.

(iv) Income from letting out buildings owned by a company to its employees etc.

(a) i only

(b) i and ii both

(c) i , ii, and iii

(d) All of the above

Answer: (a)

6. The incidence of tax on income under the Income tax Act, 1961 is linked with residential status of an assessee. Ram, an individual brought into India during the previous year 2026-27 past untaxed profits of Rs. 2,00,000 of the business in UK. State in which case amount of Rs. 2,00,000 brought into India be put to tax in A.Y. 2026-27 when Ram is (a) Resident and Ordinary resident (R&OR); (b) Resident and not Ordinary resident (R&NOR) and (c) Non-Resident (NR).

(a) Taxable in case of R&OR and R&NOR

- (b) Taxable in case of R&OR and Non Resident
- (c) Not taxable in all R&OR; R&NOR and Non-Resident
- (d) Taxable in all R&OR; R&NOR and Non-Resident

Answer: (c)

7. Radhika during the previous year 01.04.2025 to 31.03.2026 received (1) Dividend from XYZ Ltd of UK, a Foreign Company of Rs. 12,00,000 (2) Agriculture income from land in Rajasthan of Rs. 50,000 (3) Short term capital gain on sale of shares of Indian company received in London of Rs. 60,000. Total Income of Radhika when she is a Resident and not Ordinarily Resident (R&NOR) for Assessment Year 2026-27 shall be :

- (a) Rs. 13,10,000
- (b) Rs. 60,000
- (c) Rs. 1,10,000
- (d) Rs. 12,00,000

Answer: (b)

8. Sita Raman born in U.K. is a foreign citizen. His father Radha Raman was born in Rajasthan in 1960 and mother Geeta was born in South Africa in 1965. His grandfather was also born in Rajasthan in 1935. Sita Raman for the first time to see historical places comes to India on 25th November, 2024 and remained till June, 2025 for 200 days. Residential status for assessment year 2026-27 of Sita Raman shall be :

- (a) Resident and Ordinarily Resident
- (b) Not Ordinarily Resident
- (c) Non-Resident
- (d) None of the above

Answer: (c)

9. The definition of Income as per section 2(24) of the Income tax Act, 1961 is ..... :

- (a) Inclusive
- (b) Exhaustive
- (c) Exclusive
- (d) Descriptive

Answer: (a)

10. A & Co. received Rs. 2 lacs as compensation from B & Co. for premature termination of contract of agency. Amount so received is ..... :

- (a) Capital receipt & taxable
- (b) Capital receipt & not taxable
- (c) Revenue receipt & taxable
- (d) Revenue receipt & not taxable

Answer: (a)

11. If Karta is ROR in India but control & management of HUF is situated partly outside India in PY, HUF is:
- (a) ROR
  - (b) RNOR
  - (c) NR
  - (d) None of the above

Answer: (a)

#### Descriptive Questions:

1. Determining the Residential Status of an assessee is the First Step for computing the tax liability of an assessee. How?
2. Explain the term POEM 'Place of Effective Management'?
3. Define the term 'Business Connection'?
4. Distinguish between the Capital and Revenue Receipt?
5. Capital Receipt will also be taxable if it is expressly provided in the Act. Explain with examples.
6. Income may be legal as well as illegal for tax purposes. Explains.
7. Explain the term 'Active Business outside India' as define in guiding principles of 'POEM'.

#### LIST OF FURTHER READINGS

- **Direct Taxes Law and Practice**

**Author :** Dr. Vinod K. Singhania & Dr. Kapil Singhania

**Publisher :** Taxmann

- **Direct Taxes Ready Reckoner with Tax Planning**

**Author :** Dr. Girish Ahuja & Dr. Ravi Gupta

**Publisher :** Wolters Kluwer

#### OTHER REFERENCES

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- **Income Tax Rules, 1962:** <https://www.incometaxindia.gov.in/Pages/rules/income-tax-rules-1962.aspx>
- **Circulars:** <https://www.incometaxindia.gov.in/Pages/communications/circulars.aspx>
- **Notifications:** <https://www.incometaxindia.gov.in/Pages/communications/notifications.aspx>