

UNIT X DIRECT AND INDIRECT TAXES

CHAPTER

32

DIRECT TAXES



Learning Objectives

To enable the students to

- know the meaning of direct tax and its types
- understand the term income tax and its features
- explain the basic concepts of Income tax
- understand the heads of Income, Gross Total Income and Total Income

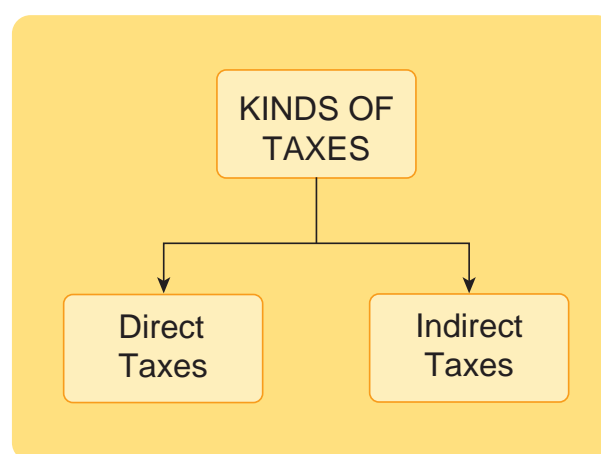
32.01 Meaning of Tax

Tax is a compulsory contribution to state revenue by the Government. It is levied on the income or profits from business of individuals and institutions. It may be added to the price of goods, services or transactions. Tax is the basic source of revenue to the Government. This revenue is utilised for the expenses of civil administration, internal and external security, building infrastructure, etc.

Types of Taxes

There are two types of taxes – direct taxes and indirect taxes.

- Direct Tax:** If a tax levied on the income or wealth of a person and is paid by that person (or his office) directly to the



Government, it is called direct tax e.g. Income-Tax, Wealth Tax, Capital Gains Tax, Securities Transaction Tax, Fringe Benefits Tax (from 2005), Banking Cash Transaction Tax (for Rs.50,000 and above - from 2005), etc. In India all direct taxes are levied and administered by Central Board of Direct Taxes.

- Indirect Tax:** If tax is levied on the goods or services of a person (seller). It is collected from the buyers and is paid by seller to the Government. It is called indirect tax. e.g. GST.

32.02 Income Tax

Income tax is a direct tax under which tax is calculated on the income, gains or profits earned by a person such as individuals and other artificial entities (a partnership firm, company, etc.)

Basic Concepts of Income Tax

i. Assessee[(Sec. 2(7))]

Assessee means a person by whom any tax or any other sum of money is payable under this Act. It includes every person in respect of whom any proceeding has been taken for the assessment of his income or assessment of fringe benefits.

ii. Person[Sec.2 (31)]

The term 'person' includes the following

- (i) an individual,
- (ii) a Hindu Undivided Family (HUF),
- (iii) a company,
- (iv) a firm,
- (v) an Association Of Persons or a Body Of Individual, whether incorporated or not,
- (vi) a local authority, and
- (vii) every artificial juridical person e.g., an idol or deity.



Structure of Indian Taxation System

Indian taxation system is one of the largest systems in the world. The authority to levy tax is derived from the Indian constitution and is well-structured. The tax administration has clear demarcation between Central Government and State Governments and then between State Governments and Local Bodies. Article 246 (Seventh Schedule) of the Indian constitution contains the legislative powers (including taxation) of the Union government and the State Governments.

iii. Assessment Year (A.Y)[Sec.2 (9)]

The term has been defined under section 2(9). The year in which tax is paid is called the assessment year. It normally consisting of a period of 12 months commencing on 1st April every year and ending on 31st March of the following year.

iv. Previous Year (P.Y)[Sec.(3)]

The year in which income is earned is called previous year. It is also normally consisting of a period of 12 months commencing on 1st April every year and ending on 31st March of the following year. It is also called as financial year immediately following the assessment year.

v. Income [Sec.2 (24)]

Income includes the followings;

- i. Profits and gains of business or profession.
- ii. Dividend
- iii. Voluntary contribution received by a charitable / religious trust or university/ education institution or hospital/ electoral trust[w.e.f.01.04.2010]
- iv. Value of perquisite or profit in lieu of salary taxable u/s 17 and social allowance or benefit specifically granted either to meet personal expenses or for performance of duties of an office or an employment of profit.
- v. Export incentives, like duty drawback, cash compensatory support, sale of licenses, etc.,
- vi. Interest, salary, bonus, commission or remuneration earned by a partner of a firm from such firm.
- vii. Capital gain chargeable u/s 45.

- viii. Profits and gains from the business of banking carried on by a co-operative society with its members.
- ix. Winning from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever.
- x. Deemed income u/s 41 or 59.
- xi. Sums received by an assessee from his employees towards welfare fund contribution such as provident fund, superannuation fund, etc.
- xii. Amount received under key man insurance policy including bonus thereon.
- xiii. Amount received under agreement for-
(a) not carrying out activity in relation to any business, or (b) not sharing any know-how, patent, copyright etc.
- xiv. Benefit or perquisite received from a company, by a director or a person holding substantial interest or a relative of the director or such person.
- xv. Gift as defined u/s 56 (2)(vi), and others.

vi. Agricultural Income (Section 2(1A))

Any rent or revenue derived from land which is situated in India and is used for agriculture purposes. Agricultural income is fully exempted from tax u/s 10(1) and as such does not form part of total income.

Heads of Income [Sec. 14]

Section 14 of Income Tax Act 1961 provides for the computation of total income of an assessee which is divided under five heads of income. Each head of income has its own

method of computation.

These five heads are;

- (i) Income from 'Salaries' [Sections 15-17];
- (ii) Income from 'House Property' [Sections 22-27];
- (iii) Income from 'Profits and Gains of Business or Profession' [Sections 28-44];
- (iv) Income from 'Capital Gains' [Sections 45-55]; and
- (v) Income from 'Other Sources' [Sections 56-59].

Gross Total Income (GTI) [Section 80B (5)]

Income from all the above five heads of income shall be computed separately according to the provisions given in the Act. Income computed under these heads shall be aggregated after adjusting past and present losses and the total so arrived at is known as 'Gross Total Income'.

Income	₹
(i) Income from 'Salaries'	XXXX
(ii) Income from 'House Property'	XXXX
(iii) Income from 'Business or Profession'	XXXX
(iv) Income from 'Capital Gains'	XXXX
(v) Income from 'Other Sources'	XXXX
Gross Total Income (GTI)	XXXX

Total Income (T.I.) [Sections 2 (45)]

Out of Gross Total Income, Income tax Act 1961 allows certain deductions under section 80. After allowing these deductions the figure which we arrive at is called 'Total Income' and on this figure tax liability is computed at the prescribed rates.

Gross Total Income	XXXX
Less: Deductions (Sec.80C to 80U)	XXXX
Total Income (T.I.)	XXXX

80C Deductions; Contribution to Provident Fund, life Insurance Premium, Children's Tuition Fees, Health Insurance Premium, Investment in National Savings Certificate, interest paid for home loans, etc.

Income Tax Slab Rate for Individual - Illustration

As per the Assessment Year 2021-22

TOTAL INCOME (Rs)	Income Tax Rate
Upto 5,00,000	Nil
5,00,001 – 7,50,000	10%
7,50,001 – 10,00,000	15%
10,00,001 – 12,50,000	20%
12,50,001 – 15,00,000	25%
Above 15,00,000	30%

Key Terms

Direct Tax	Indirect Tax
Assessment Year	Previous Year
Assessee	Person
Agricultural Income	



Exercise

I. Choose the Correct Answer

1. Income Tax is

- a) a business tax
- b) a direct tax
- c) an indirect tax
- d) none of these



2. Period of assessment year is

- a) 1st April to 31st March
- b) 1st March to 28th Feb
- c) 1st July to 30th June
- d) 1st Jan. to 31st Dec.

3. The year in which income is earned is known as

- a) Assessment Year
- b) Previous Year
- c) Light Year
- d) Calendar Year

4. The aggregate income under five heads is termed as

- a) Gross Total Income
- (b) Total Income
- (c) Salary Income
- (d) Business Income

5. Agricultural income earned in India is

- a) Fully Taxable
- b) Fully Exempted
- c) Not Considered for Income
- d) None of the above

Answers

1. b 2. a 3. b 4. b 5. b



II. Very Short Answer Questions

1. What is Income Tax?
2. What is meant by Previous year?
3. What is an assessment year?

III. Short Answer Questions

1. List out the five heads of income.
2. Write short notes on:
 - a) Direct tax
 - b) Indirect tax
3. Who are all included in the term person?

IV. Long Answer Questions

1. Elucidate any five features of Income Tax.

Reference

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