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FACULTY OF COMMERCE AND MANAGEMENT

COURSE: B.COM III SEM.

SUBJECT: Income Tax Laws and Practice

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LECTURE: 4

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LECTURE-4

FUNDAMENTAL CONCEPTS OR DEFINITIONS

1. Assessment year: [Sec.2 (9)]

The term assessment year means the period of 12 months commencing on the first day of April every year. Thus, the assessment year always begins on 1st April and ends on 31st March every year. This period is also known as the financial year.

3. Previous Year [sec. 3]

The year in which income is earned is termed as the previous year. Income tax is charged on the total income of the previous year, and the income earned during the previous year is assessed to tax at the rates and as per the provisions applicable for the assessment year relevant to the previous year. In other words, the income chargeable to tax in the assessment year is the one actually earned in the previous year.

5. Financial year to be the previous year [sec.3 (1)]:

It should be noted that financial year is the previous year for tax purpose only, and the assessee is free to follow an accounting year different from the financial year. However, is the assessee‟s accounting year is different from the financial year; he will still be required to maintain accounts for every financial year for the purpose of submitting the income tax returns.

6. Previous year for a new source of income:

Where a new source of income comes into being in a financial year either by way of set up of new business or profession or otherwise, the period of the first previous year will begin (i) with the date of setting up of the business or profession; or (ii) the date on which new source of income comes into existence and will end with the said financial year. Therefore, in such cases the first previous year may be less than 12 months.

7. Income [Sec.2 (24)]:

The concept of income is very important as it is the income that is taxed under the income tax act. The definition of income under this act is a very wide and includes profits and gains, dividends, voluntary contributions, perquisites, allowances, discharge of an obligation, compensation receipts, profits on sale of license, cash assistance received against exports, recovery of loss or expenditure, recovery of bad debts, any wins from lottery, cross word puzzles, races, card games, gambling, betting etc.

8. Heads of Income: [sec.14]

For the purpose of charge of income tax, all incomes are classified under five heads of income, namely, Salaries, House property, profits and gains of business or profession, Capital gains and income from other sources.

9. Exempted Incomes [Sec.10 and Sec.86]

These incomes are either fully or partially exempted from income tax and therefore, to the extent of exemption, do not form a part of the total income and hence are not taxable

10. Deductions from income:

Income tax act allows certain specific reductions to be made from the income of an assessee while computing the total income. These reductions are termed as deductions. **Two type of deductions** have been provided under the act, i.e. deductions from the specific **heads of income** and deductions from **gross total income**.

11. Gross total income [Sec.80B (5)]

The aggregate of net taxable income under various heads of income is termed as Gross total income. This aggregation is not a mathematical process but a legal concept. It is computed after allowing for the deductions specific to various heads of income, set off of losses and allowances or set off of carry forward losses and allowances and clubbing of income of any other person that may be liable to be included in assesses total income.

12. Total Income [Sec.2 (45)]

Total income, computed in accordance with sec.5 according to residential status, is arrived at after allowing deductions under Sec.80CCC to 80U from the gross total income. The charge of income tax is on total income of an assessee. Incomes exempted from income tax do not form a part of total income.

13. Computation of tax liability:

Income tax is a charge on total income of previous year and is calculated by applying rates of tax prescribed for the relevant assessment year to the total income of the previous year. The net tax liability is then computed by allowing any rebates of relief due to the assessee, adding the surcharge, education cess and giving credit for any tax paid in advance of deducted at source.

14. Rates of Income tax:

The rates of income tax are prescribed every year by the finance act which follows a combination of flat and slab rates for charging tax on total income.

15. Rebate [sec.87]

Rebate is a reduction allowed in the amount of income tax computed in case of certain types of assessee.

16. Relief from tax [sec.89]

Where an assessee receives arrears of salary or advance of salary or profits in lieu of salary during previous year and it becomes taxable during the same previous year by virtue of a provision of the income tax act there by causing the assessee to be taxed at a higher rate than he would otherwise have been assessed, relief may be allowed under Rule 21A from tax so computed at the higher rate. The act provides for the relief only in case of arrears of salary or salary received in advance or family pension.

17. Deduction v/s Rebates v/s Relief:

While the basic purpose of all the three is to benefit the assessee by reducing the incidence of tax, they differ greatly in the way they achieve their common objective and the conditions under which they pass on the relief. While the deductions reduce the amount of income chargeable to tax, rebates and relief reduces the amount of tax computed on the chargeable income.

18. Surcharge:

Surcharge is a charge levied on the amount of income tax computed under the act. This is levied by the government to raise revenue for special purpose for the union and accrues wholly to the central government. In simple terms surcharge is tax on income tax.

19. Surcharge v/s Income tax:

Income tax is a charge on total income while surcharge is a levy on income tax. First, income tax is computed on total income at prescribed rates and then surcharge is worked out on the amount of income tax so computed to arrive at the total tax liability.

20. Education and SHEC:

Education cess and secondary and higher education cess are levied on the aggregate of income tax and surcharge. These are fully assigned to the central government to enable it to finance universalized basic education. Income tax v/s surcharge v/s Education cess: Income tax is levied on total income. Surcharge is levied on income tax. Education cess and SHEC are charged on the aggregate of income tax and surcharge.