Southern India Regional Council of
The Institute of Chartered Accountants of India

Back to Basic – Educational Series - Income tax:

Important Exemptions and Deductions

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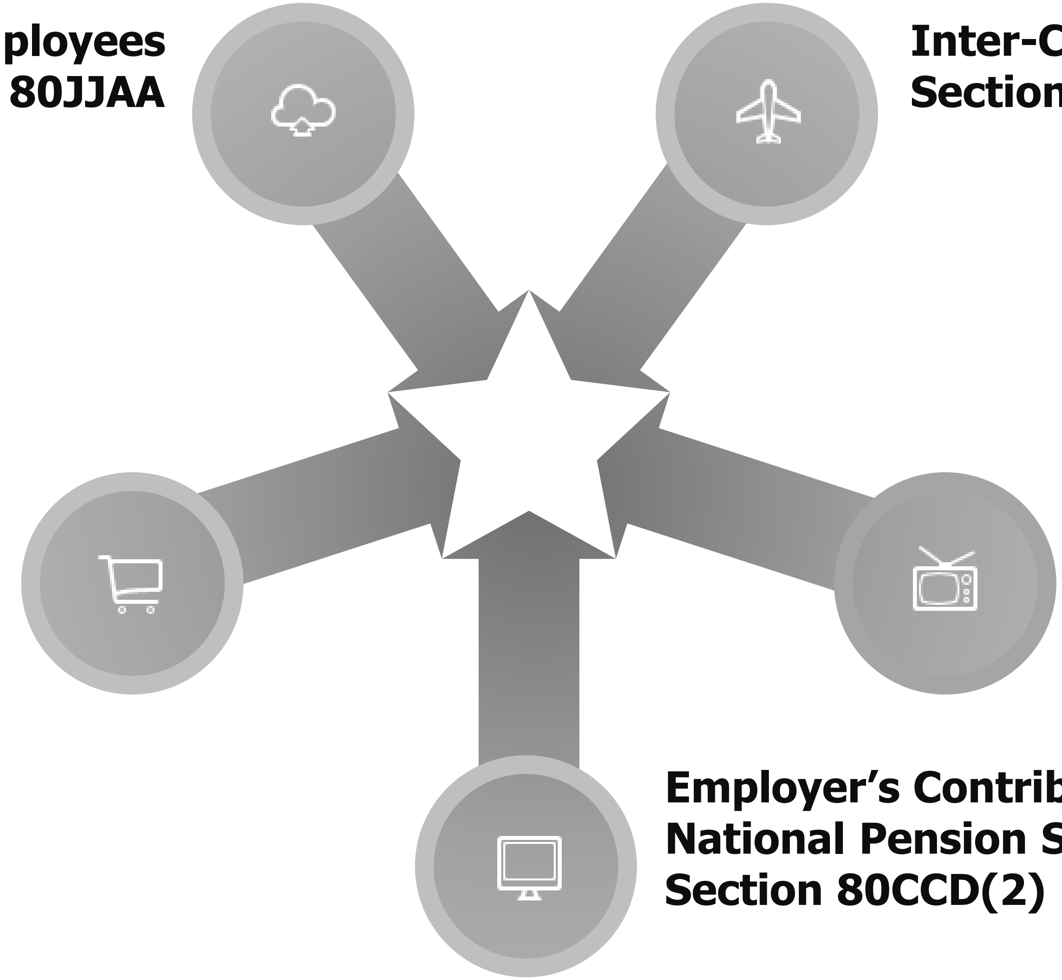
Deductions


Employment of new employees
Section 80JJAA
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Section 80-IAC
Employer’s Contribution to
National Pension Scheme (NPS)
Section 80CCD(2)

Employment of new employees

- Eligibility of deduction in case of an assessee engaged in “Profession”

  Memorandum to Finance Bill, 2016: *With a view to extend this employment generation incentive to all sectors*
- Computation of eligible deduction under Section 80JJAA:

Particulars	Case I	Case II	Case III Rs. Crores
Profits & Gains from Business (PGBP)	25	25	(10)
Brought forward losses adjusted	-	(25)	-
Net PGBP	25	-	(10)
Income from Other Sources	20	20	20
Gross Total Income	45	20	10
Deduction as computed u/s 80JJAA	40	40	40
Eligible Deduction u/s 80JJAA	?	?	?

- Deduction in respect of two subsequent years (Carried forward deduction)
- Carried forward deduction, in case of events in Year 2:
  - Amalgamation
  - Demerger

Employment of new employees

- **Interpretations w.r.t. embargo, in case of business formed by splitting up/ reconstruction of existing business, acquired business etc.**
  - Deduction qua-organization **vs.** qua-business undertaking
  - Subsequent years of business that was originally acquired by business purchase/ slump sale etc.
- **Furnishing of the report of accountant:**
  - Condition for claim of deduction v. procedural aspect
  - Delayed filing of Form 10DA.
  - Report not filed in Year 1/ filed belatedly. Deduction for the subsequent two years?
- **Reckoning of increase in employees:**

Particulars	Year 1	Year 2
Opening Head Count	100	105 ?
PY C/f of <240 days		25
Additions >240 days	20	30
Additions <240 days	25	-
Deletions	(15)	(40)
Closing Head Count	130	120

- **Interpretations w.r.t. 'additional employee':**
  - In case of employee employed < 240 days in year 1, condition should again be tested in Year 2?
  - Whether the employee should necessarily remain in the payroll at the end of the year?

Employment of new employees

- **Computation of total emoluments per month & implications in the deduction:**
  - Condition w.r.t total emoluments < 25,000 to be looked at in which year?
    - Carried forward benefit
    - Employee deemed to be additional employee for the year (by virtue of employed < 240 days in previous year)
  - In case of salary increment during the year? For example, total emoluments:
    - First 10 months - < 25,000
    - Last 2 months - > 25,000
    - 12 months average < 25,000

- **Indicative verification of documents for Form 10DA:**
  - Payroll registers (date of joining, date of exit, emoluments (with details of components)
  - HR records for increments/ change in pay structure
  - Appointment/ increment letters
  - Resignation letters/ approvals reckoning date of exit
  - Bank Statements evidencing salary disbursements
  - Provident fund working, challan evidencing payments
  - Documentation of positions taken in claim of deduction under Section 80JJAA along with basis
  - Possibility of complete disclosures

Inter-Corporate Dividends

- Eligibility to claim deduction under Section 80M:

Example: X Ltd. receives dividend of Rs. 100 crores from its subsidiary Y Ltd. and distributes dividend of Rs. 80 crores to its shareholders. The details of the transaction is tabulated below:

Particulars	Case I	Case II
Dividend received from Y Ltd. (Rs. in Crores)	100	100
Due date for furnishing ROI of X Ltd.	31st Oct	31st Oct
Date of declaration of dividend by X Ltd.	20th Sept	25th Sept
Date of payment by X Ltd. to its shareholders	29th Sept	3rd Oct
Is X ltd eligible for deduction under Section 80M to the extent of dividend paid to its shareholders	?	?

- ***Punjab Distilling Industries Ltd (SC) (57 ITR 1) –*** The expression 'distribution' connotes something actual and not notional. It can be physical; it can also be constructive. One may distribute amounts between different shareholders either by crediting the amount due to each one of them in their respective accounts or by actually paying to each one of them the amount due to him.

- *Declaration/ Payment/ Distribution* – Section 8

Inter-Corporate Dividends

- Amount of deduction under Section 80M:

Particulars	Amount Rs. in Crores
Gross dividend received	100
Less: Deduction u/s 57 of the Act (say interest on funds borrowed to for investment)	(20)
Net dividend included in GTI	80
Dividend declared to shareholders (within the due date prescribed under Section 80M)	85
Eligible deduction under Section 80M r.w. Section 80AB	80

- Relevance of Section 80AB of the Act – Net income principle.
- ***Distributors (Baroda) (P.) Ltd (SC) (155 ITR 120) –*** Intent of the legislature was to give relief to such amount of dividend which has suffered tax in the hands of the company receiving dividend.

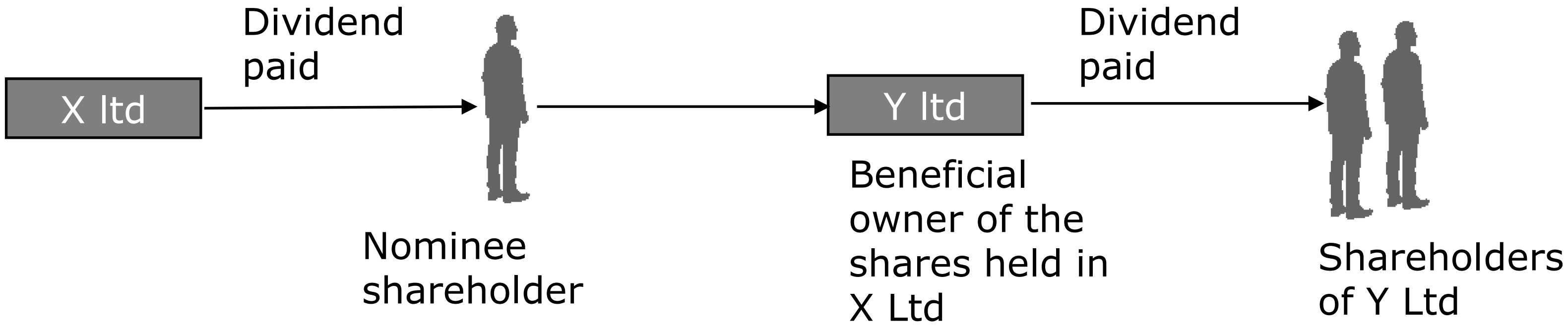
Inter-Corporate Dividends

- **Interplay between Section 115BBD and Section 80M**
  - Whether the non-obstante clause in Section 115BBD (until AY 2022-23) prohibited a domestic company from claiming a deduction under Section 80M in respect of dividends received from a foreign company?
  - Is deduction under Section 80M a deduction in respect of an **expenditure or allowance**?

    CIT vs Williamson Financial Services (SC) (165 Taxman 638) - Deductions under Chapter VIA or not deductions under particular source of income but from the gross total income.

- **Registered owner vs Beneficial owner of shares** – If the dividends are taxed in the hands of the beneficial owner of the shares (being a domestic company), will it be eligible to claim deduction under Section 80M?

  In the example below, can Y ltd claim deduction under Section 80M? - ***Indian Iron Steel Co Ltd*** **(*Calcutta HC*)** ***(156 ITR 314)***



Inter-Corporate Dividends

- **Applicability of Section 80M to Deemed Dividends u/s 2(22) of the Act:**
  - If the income of a domestic company distributing dividends to its shareholders, includes income by the way of deemed dividends u/s 2(22) of the Act, will it be eligible to claim deduction under Section 80M?
  - Definition of dividend u/s 2(22) of the Act includes deemed dividends.
  - Decision of ***Calcutta HC in the case of Jai Hind Investment Industries (P.) Ltd (6 taxman 361).***
- **Set off of business loss with dividend income:**

Particulars	Amount Rs. in Crores
Current year loss under the head PGBP	(50)
Current year dividend income	150
Current year interest income	20
Gross total income	**120**
Eligible deduction under Section 80M if received and distributed is 100 Crores (read with Section 80A)	120

- CBDT circular no. 58 dated 15 April 1971 – Clarification w.r.t. erstwhile Section 80M.

Eligible Start-up

- **Section 80-IAC – Salient aspects:**
  - Eligible startup engaged in eligible business
  - **Deduction:** 100% of the PGBP for 3 consecutive AYs within 10 years of incorporation.

  ! Opting for Section 115BAA bars deduction u/s 80-IAC.

  MAT Provisions applicable.

  - **Key Conditions:**
    - Not formed by splitting up, reconstruction etc. of existing business
    - Not formed by transfer of existing P&M by more than 20% of total value of P&M (except imported P&M)
    - Furnishing of accountant's report (Form 10CCB)

- **"Eligible Startup":**
  - Co./ LLP
  - Incorporated between FY 2016-17 & 2023-24
  - Total turnover <= Rs. 100 Crore (in the year of claim of deduction)
  - Holds Start-up approval

- **"Eligible business":** *engaged in innovation, development or improvement of products or processes or services or a scalable business model with a high potential of employment generation or wealth creation*

- **Other Key Aspects (IT Act):**
  - Angel Tax exemption
  - Deferment of taxation of ESOPS in the hands of employees
  - Relaxation form c/f of loss in case of change in shareholding

Employer’s Contribution to NPS

- **Section 80CCD(2)– Salient aspects:**
  - **Deduction:** Employer’s contribution to NPS to the extent of 10% of Salary plus DA (up to 14% in case of Government employees)
  - Deemed to be the income of the taxpayer in the year in which he closure/ opting out of the NPS Account

    Exception: in case of receipt by nominee in the event of death of the subscriber.

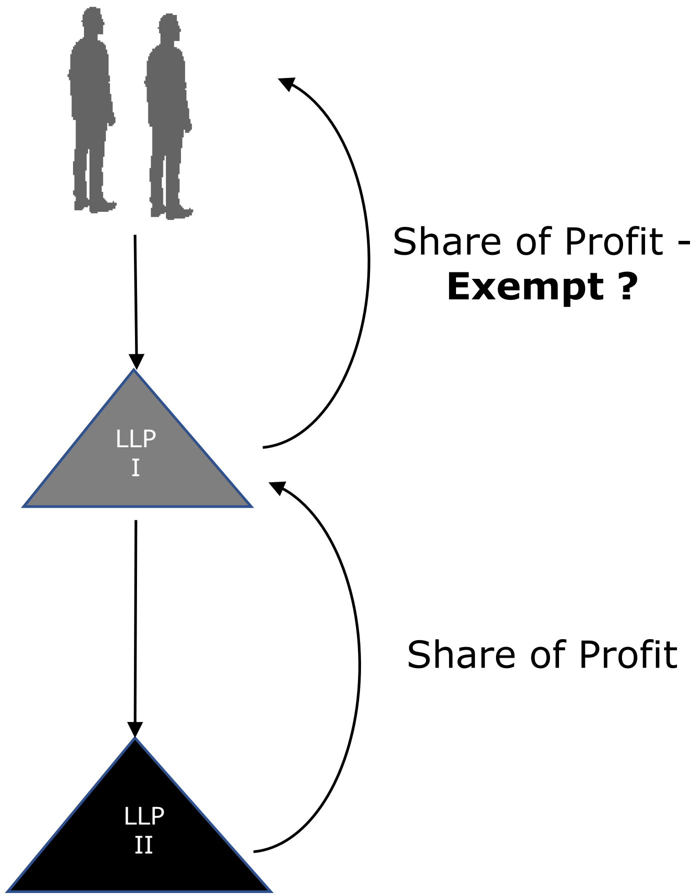
    Deemed to be the income of the taxpayer in the year in which he closure/ opting out of the NPS Account

- **Tax implications:**
  - Lump sum withdrawal (upto 60%) - Exempt u/s 10(12A)
  - Partial withdrawal (for specific reasons under the scheme) (up to 25%) – Exempt u/s 10(12B)
  - Amount used for purchase of annuity plan is not taxable. Pension received from the annuity plan purchased is taxable.

Exemptions/Deduction

1. Share of Profit from a firm
   Section 10(2A)
2. Short-stay exemption
   Section 10(6)(vi)
3. Amount received under Life insurance policy
   Section 10(10D)
4. Income from buy-back
   Section 10(34A)
5. Income chargeable to Equalisation levy
   Section 10(50)
6. Tax deduction for SEZ Units
   Section 10AA: Select issues
7. Other exemptions

Share of Profit from a firm



- *10. In computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included—*

  *(2A) in the case of a person being a partner of a firm **<u>which is separately assessed as such</u>**, his share in the total income of the firm.*

- **CBDT Circular No. 8/ 2014**:

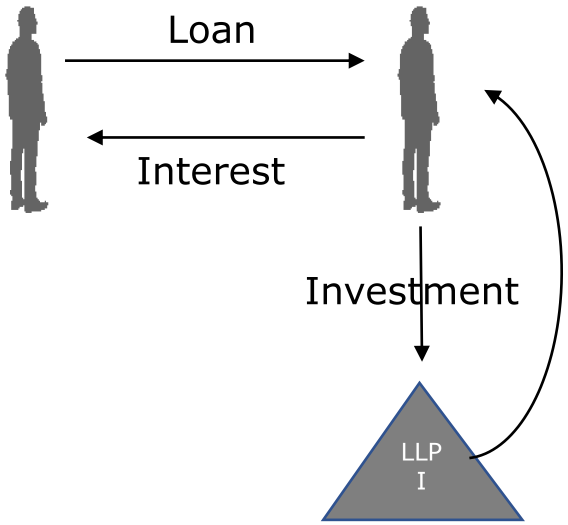
  The income of a firm is to be taxed in the hands of the firm only and the same can under no circumstances be taxed in the hands of its partners. Accordingly, the entire profit credited to the partners' accounts in the firm would be exempt from tax in the hands of such partners, even if the income chargeable to tax becomes NIL in the hands of the firm on account of any exemption or deduction as per the provisions of the Act.

- **Vidya investment and Trading Co P Ltd v. UOI** (2014) 367 ITR 33 (Kar)**.**

Share of Profit from a firm

Aspects for discussion	Reference
Share of Profits from Partnership firm situated outside India	• Definition of “firm” u/s 2(23) r.w. Partnership Act, 1932 • Canoro Resources Ltd (2009) 313 ITR 2 (AAR)
Interest on capital / remuneration disallowed in the hands of the firm	Explanation to Section 10(2A): *For the purposes of this clause, the share of a partner in the total income of a firm separately assessed as such shall, notwithstanding anything contained in any other law, be **<u>an amount which bears to the total income of the firm</u>** the same proportion as the amount of his share in the profits of the firm in accordance with the partnership deed bears to such profits ;*
Adjustments during assessment/ other proceedings in the hands of the firm/ the partner	Section 155(1), (1A): *the Assessing Officer may amend the order of assessment of the partner … … provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the financial year in which the final order was passed in the case of the firm.*

Share of Profit from a firm



1. Interest on Capital
2. Remuneration
3. Share of Profit

Rs. in Crores

Particulars	Year 1	Year 2
Share of Profit	-	20
Interest on capital	12	12
Interest on loan (proceeds invested in the firm)	15	15

- **Section 14A(1):**

  Notwithstanding anything to the contrary contained in this Act, for the purposes of computing the total income under this Chapter, no deduction shall be allowed in respect of expenditure incurred by the assessee ***in relation to income*** *which does not form part of the total income under this Act.*

- **Explanation (inserted by Finance Act 2022)**

  For the removal of doubts, it is hereby clarified that notwithstanding anything to the contrary contained in this Act, the provisions of this section shall apply and shall be deemed to have always applied in a case where the income, not forming part of the total income under this Act, has not accrued or arisen or has not been received during the previous year relevant to an assessment year and the expenditure has been incurred during the said previous year in relation to such income not forming part of the total income.

Short-stay exemption

- **Section 10(6)(vi):**

  In computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included—

  in the case of an individual who is ***not a citizen of India****,—*

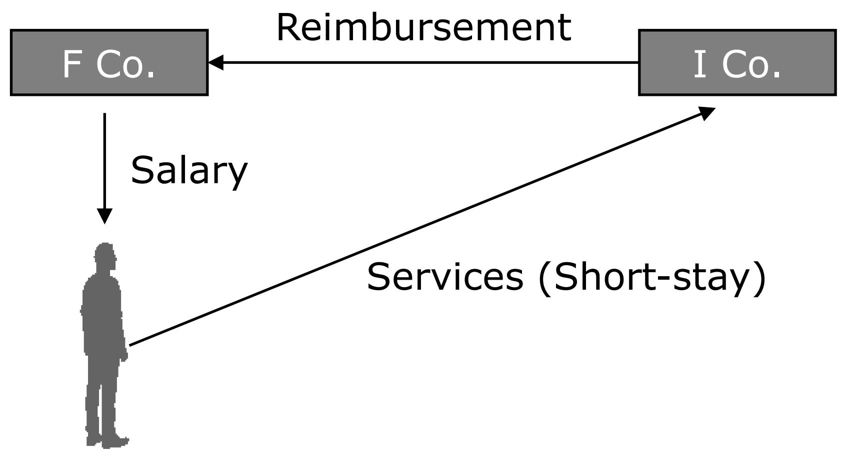
  the remuneration received by him as an ***employee of a foreign enterprise*** *for services rendered by him during his stay in India, provided the following conditions are fulfilled—*

  (a) the foreign enterprise is not engaged in any trade or business in India ;

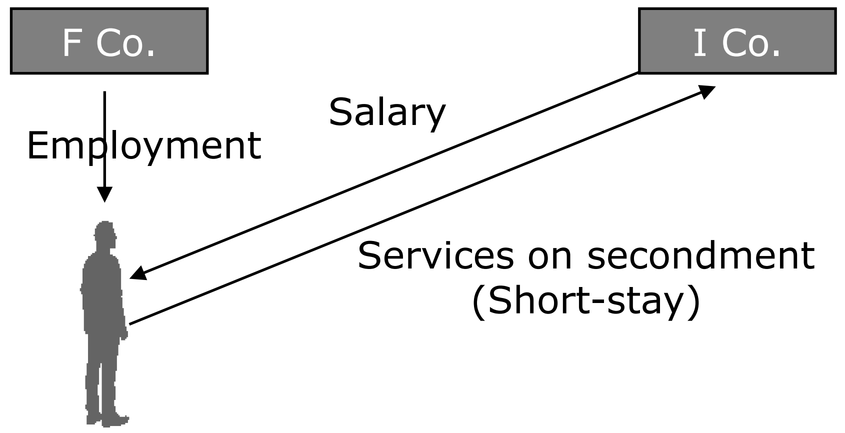
  (b) his stay in India does not exceed in the ***aggregate a period of ninety days in such previous year*** *; and*

  (c) such remuneration is not liable to be deducted from the income of the employer chargeable under this Act ;

- Bharat Heavy Electricals (2001) 252 ITR 218 (Del)



- Case Study:



Amount received under Life insurance policy

<table>
<tr><th>Particulars</th><th>Maturity Amount</th><th>Death benefit</th></tr>
<tr><td>Sum received from LIP on the death of the dependent with disability, in case of LIP under specific schemes for maintenance of such disabled dependent</td><td>N.A.</td><td>Taxable</td></tr>
<tr><td>Sum received under key-man insurance policy (including policies assigned)</td><td>Taxable</td><td>Taxable</td></tr>
<tr><td>Policies issued between April 2003 to March 2012 with premium in any year > 20% of sum assured (SA) *</td><td rowspan="4">Taxable</td><td rowspan="4">Exempt</td></tr>
<tr><td>Policies issued after March 2012 with premium in any year > 10%# of SA *</td></tr>
<tr><td>Policies issued after March 2023 with premium in any year > Rs. 5 Lakhs %</td></tr>
<tr><td>ULIP issued after Jan 2021 with premium in any year > Rs. 2.5 Lakhs @</td></tr>
<tr><td>Other amounts received under Life Insurance Policy</td><td colspan="2">Exempt</td></tr>
</table>

* excluding any premium agreed to be returned and amounts in excess of sum assured (example, bonus)

In case of persons with severe disabilities/ specified diseases, the threshold is relaxed to 15%, in case of Policies issued after March 2023.

% In case of persons with multiple LIPs, exemption limited to LIPs with aggregate premium of up to Rs. 5 Lakhs in any previous year.

@ In case of persons with multiple ULIPs, exemption limited to ULIPs with aggregate premium of up to Rs. 2.50 Lakhs in any previous year.

Amount received under Life insurance policy

Rs. Lakhs

Life Insurance Policy			A	B	C
Unit linked Insurance Policy	**X**	**Y**			
Date of issue	1 Apr 21	1 Apr 23	1 Apr 24	1 Apr 24	1 Apr 24
Annual premium	1.0	1.0	1.0	1.5	3.0
Sum assured	10.0	10.0	10.0	15.0	30.0
Consideration received on surrender as on 1 July 2033	6.0		6.0		
Consideration received on maturity as on 1 Nov 2034		12.0		18.0	34.0
Taxability of sum received	Exempt *		Exempt #	Taxable @	Exempt %

* Aggregate ULIP premium (for each of the years FY 2021-22 to FY 2033-34/ 2034-35) < Rs. 2.50 Lakhs.

LIP: Amount of premium paid does not exceed 10% of the sum assured in all the cases.

FY 2033-34: Aggregate amount of premium paid for LIP A & C in any of the years (FY 2024-25 to FY 2033-34 does not exceed Rs. 5 Lakhs.

% **FY 2034-35:** Aggregate amount of premium paid for LIP A & C in any of the years does not exceed Rs. 5 Lakhs (Considering LIP A & C is more beneficial than LIP A & B to the taxpayer).

@ Aggregate amount of premium paid for LIP A, B & C exceeds Rs. 5 Lakhs. Hence, not eligible for exemption for LIP B. However, had the taxpayer not claimed exemption for LIP A in FY 2033-34, he would be eligible for exemption for LIP B&C in FY 2034-35.

Reference: CBDT Circular No. 15 of 2013 (Example 13).

Amount received under Life insurance policy

- **Taxation of sum received under keyman insurance policy:**
  - Profits in lieu of salary - Section 17(3)
  - Profits & Gains from business or Profession – Section 28(vi)
  - Income from Other Sources - 56(2)(iv)
  - Carved out from exemption under Section 10(10D)

- **Matters for discussion:**
  - Year of taxation – Assignment vs. Surrender or Matuirity
  - Taxable amount – Gross amount received vs. permissibility of any deduction

Income from buy-back

- Income distributed by a domestic company on buy-back of shares from the shareholders – Subject to buy-back tax @ 20% plus surcharge and cess u/s 115QA.

- **Buy-back**: purchase by a company of its own shares in accordance with the **provisions of any law for the time being in force** relating to companies

- **Distributed income:** consideration paid by the company on buy-back of shares as reduced by the amount, which was received by the company for issue of shares, determined in the prescribed manner.

- Tax to be discharged by the Company. No credit to the shareholders.

- **Section 10(34A):**

  In computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included—

  any income arising to an assessee, being a shareholder, on account of buy back of shares by the company as referred to in section 115QA;

- Taxation of Buy-back of shares by a foreign company/ Capital reduction etc.
  - Dividend - Section 2(22)(d)
  - Capital Gains – Section 46A

- Redemption of Preference Shares?
- Applicability of Section 56(2)(x) ?

  Vora Financial Services (P.) Ltd. [2018] 171 ITD 646 (Mumbai Trib.) - S.56(2)(viia)

  Venture Lighting India Ltd. (ITA No. 3171/CHNY/2019)

Income chargeable to Equalisation levy

- Applicability of equalization levy:

Particulars	Rate of levy	Mechanism	Remarks
Consideration **received/ receivable** by a non-resident from a resident/ Indian PE of a NR: Online advertising, Provision of digital advertising space, Related services	6%	To be deducted by the payer.	Exceptions: - NR has a PE in India and income effectively connected with such PE - Payment not in connection with the business/ profession of the recipient - Aggregate consideration <= Rs. 1 Lakh. - Taxable as Royalty/ FTS u/ IT Act/ DTAA.
Consideration **received/ receivable** by a non-resient e-commerce supplier for e-commerce supply or services to a person resident in India, buyer’s IP located India etc.	2%	To be collected by the e-commerce operator	Exceptions: - NR has a PE in India and income effectively connected with such PE - Advertising (covered by above provisions) - Gross receipts of e-commerce supplier < Rs. 2 Crore - Taxable as Royalty/ FTS u/ IT Act/ DTAA.

Income chargeable to Equalisation levy

- Non-residents engaged in business through digital medium having business connection/ significant economic presence in India.

- Section 10(50):

  In computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included—

  *any income arising from any specified service provided on or after the date on which the provisions of Chapter VIII of the Finance Act, 2016 comes into force or arising from any e-commerce supply or services made or provided or facilitated on or after the 1st day of April, 2020 and **chargeable to equalisation levy** under that Chapter.*

  Explanation 1.—For the removal of doubts it is hereby clarified that the income referred to in this clause shall not include and shall be deemed never to have been included any income which is chargeable to tax as royalty or fees for technical services in India under this Act read with the agreement notified by the Central Government under section 90 or section 90A.

Tax exemption for SEZ Units – Select issues

- **Salient aspects of Section 10AA:**
  - Manufacturing/ Service
  - Begins operations in SEZ between FY 2005-06 to FY 2019-20
  - Exemption:

Period	Tax exemption
First 5 years	100% of the profits from export
6 – 10 years	50% of the profits from export
11 – 15 years	50% of the profits from export, subject to , subject to transfer to **SEZ reinvestment reserve** and conditions to be fulfilled.

  - Reinvestment reserve to be utilized for buying new plant & machinery (to be put to use within 3 years of creation of reserve)

- **Matters for discussion:**
  - Requirement of creation of earmarked funds for reinvestments?
  - Reinvestment in new P&M only within the SEZ unit? or can be carried out in other units/ expansion projects etc.?
  - Exemption withdrawn and opted for Section 115BAA. Applicable tax rate?

Thank you!

Credits

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