After studying this chapter, you would be able to -

- **identify** the income which are chargeable to tax under the head “Income from other sources”.
- **identify** the admissible/ inadmissible deductions while computing income under this head.
- **examine** the circumstance(s) when amount paid or payable by a closely held company to the shareholder, being a beneficial owner or the concern in which such shareholder has the substantial interest would be deemed as dividend.
- **examine** the circumstances when any sum of money or property transferred without consideration or for inadequate consideration would be taxable in the hands of recipient and the exceptions thereto.
- **examine** the taxability in case of bond washing transactions and dividend stripping.
- **compute** the income under the head “Income from Other Sources” after allowing the deductions available thereunder.
8.1 INTRODUCTION

Any income, profits or gains includible in the total income of an assessee, which cannot be included under any of the preceding heads of income, is chargeable under the head 'Income from other sources'. Thus, this head is the residuary head of income and brings within its scope all the taxable income, profits or gains of an assessee which fall outside the scope of any other head. Therefore, when any income, profit or gain does not fall precisely under any of the other specific heads but is chargeable under the provisions of the Act, it would be charged under this head.

8.2 INCOMES CHARGEABLE UNDER THIS HEAD [SECTION 56]

(1) Income chargeable only under the head ‘Income from other sources’:

(i) Dividend income

The term ‘dividend’ as used in the Act has a wider scope and meaning than under the general law.

**Dividend [covered by sections 2(22)(a) to (e)]:**

According to section 2(22), the following receipts are deemed to be dividend:

(a) Distribution of accumulated profits, entailing the release of company’s assets - Any distribution of accumulated profits, whether capitalised or not, by a company to its shareholders is dividend if it entails the release of all or any part of its assets.

For example, if accumulated profits are distributed in cash it is dividend in the hands of the shareholders. Where accumulated profits are distributed in kind, for example by delivery of shares etc. entailing the release of company’s assets, the market value of such shares on the date of such distribution is deemed dividend in the hands of the shareholder.

(b) Distribution of debentures, deposit certificates to shareholders and bonus shares to preference shareholders - Any distribution to its shareholders by a company of debenture, debenture stock or deposit certificate in any form, whether with or without interest, and any distribution of bonus shares to preference shareholders to the extent to which the company possesses accumulated profits, whether capitalised or not, will be deemed as dividend.

The market value of such bonus shares is taxable in the hands of the preference shareholder.

In the case of debentures, debenture stock etc., their value is to be taken at the market rate and if there is no market rate they should be valued according to accepted principles of valuation.

**Note:** Bonus shares given to equity shareholders are not treated as dividend.
(c) **Distribution on liquidation** - Any distribution made to the shareholders of a company on its liquidation, to the extent to which the distribution is attributable to the accumulated profits of the company immediately before its liquidation, whether capitalised or not, is deemed to be dividend income.

**Note:** Any distribution made out of the profits of the company after the date of the liquidation cannot amount to dividend. It is a repayment towards capital.

Accumulated profits include all profits of the company up to the date of liquidation whether capitalised or not. But where liquidation is consequent to the compulsory acquisition of an undertaking by the Government or by any corporation owned or controlled by the Government, the accumulated profits do not include any profits of the company prior to the 3 successive previous years immediately preceding the previous year in which such acquisition took place subject to certain exceptions.

(d) **Distribution on reduction of capital** - Any distribution to its shareholders by a company on the reduction of its capital to the extent to which the company possessed accumulated profits, whether capitalised or not, shall be deemed to be dividend.

(e) **Advance or loan by a closely held company to its shareholder** - Any payment by a company in which the public are not substantially interested of any sum by way of advance or loan to any shareholder who is the beneficial owner of 10% or more of the equity capital of the company will be deemed to be dividend to the extent of the accumulated profits. If the loan is not covered by the accumulated profits, it is not deemed to be dividend.

**Advance or loan by a closely held company to a specified concern** - Any payment by a company in which the public are not substantially interested to any concern (i.e. HUF / Firm / AOP / BOI / Company) in which a shareholder, having the beneficial ownership of atleast 10% of the equity shares is a member or a partner and in which he has a substantial interest (i.e. atleast 20% share of the income of the concern) will be deemed to be dividend.

Also, any payments by such a closely held company on behalf of, or for the individual benefit of any such shareholder will also deemed to be dividend. However, in both cases the ceiling limit of dividend is the extent of accumulated profits.

**Exceptions:** The following payments or loan given would not be deemed as dividend:

(i) If the loan is granted in the ordinary course of its business and lending of money is a substantial part of the company’s business, the loan or advance to a shareholder or to the specified concern is not deemed to be dividend.

(ii) Where a loan had been treated as dividend and subsequently the company declares and distributes dividend to all its shareholders including the borrowing shareholder, and the
dividend so paid is set off by the company against the previous borrowing, the adjusted amount will not be again treated as a dividend.

**Other exceptions**

Apart from the exceptions cited above, the following also do not constitute "dividend" -

(i) Any payment made by a company on purchase of its own shares from a shareholder in accordance with the provisions of section 77A of the Companies Act, 1956;

(ii) any distribution of shares on demerger by the resulting companies to the shareholders of the demerged company (whether or not there is a reduction of capital in the demerged company).

**Year of accrual of dividend**

Section 8 provides that deemed dividend under section 2(22) declared by a company or distributed or paid by it shall be deemed to be the income of the previous year in which it is declared, distributed or paid, as the case may be. Any interim dividend shall be deemed to be the income of the previous year in which the amount is unconditionally made available to the member who is entitled to it.

**Basis of charge of dividend**

Any income by way of dividends, referred to under section 115-O, is excluded from the total income of the shareholder [Section 10(34)].

Under section 115-O, any dividend declared, distributed or paid by a domestic company, whether out of current or accumulated profits, shall be charged to additional income-tax at a flat rate of 15% in addition to normal income-tax chargeable on the income of the company. This is known as corporate dividend tax. Dividend distribution tax is not leviable on deemed dividend under section 2(22)(e). Hence, the same will be taxed in the hands of the shareholder.

Dividends received from a company, other than a domestic company, is still liable to tax in the hands of the shareholder. For example, dividend received from a foreign company is liable to tax in the hands of the shareholder.

It may, however, be noted that the exemption available under section 10(34) would not be allowable in respect of dividend income chargeable to tax in accordance with the provisions of section 115BBDA, even if the dividend distribution tax is paid by the domestic company on such amount of dividend.

**Tax on certain dividends received from domestic companies (Section 115BBDA)**

(i) Any income by way of aggregate dividend in excess of ₹ 10 lakh shall be chargeable to tax in the case of **specified assessee** who is resident in India, at the rate of 10%.
(ii) **Meaning of certain terms**

<table>
<thead>
<tr>
<th>Term</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>Specified assessee</td>
<td>A person other than</td>
</tr>
<tr>
<td></td>
<td>- domestic company</td>
</tr>
<tr>
<td></td>
<td>- a fund or institution or trust or any university or other educational institution or any hospital or other medical institution referred to in section 10(23C)(iv)/(v)/(vi)/(via)</td>
</tr>
<tr>
<td></td>
<td>- a trust or institution registered under section 12A or 12AA</td>
</tr>
<tr>
<td>Dividend</td>
<td>Includes dividend referred under section 2(22)(a) to (d) but shall not include sub-clause (e) thereof.</td>
</tr>
</tbody>
</table>

(iii) Further, the taxation of dividend income in excess ₹ 10 lakh shall be on gross basis i.e., no deduction in respect of any expenditure or allowance or set-off of loss shall be allowed to the assessee in computing the income by way of dividends.

(iv) Accordingly, exemption available under section 10(34), in respect of dividend received by a shareholder from a domestic company would not apply to income by way of dividend chargeable to tax under section 115BBDA.

**Illustration 1**

A Ltd., a domestic company, declared dividend of ₹ 170 lakh for the year F.Y.2016-17 and distributed the same on 10.7.2017. Mr. X, holding 10% shares in A Ltd., receives dividend of ₹ 17 lakh in July, 2017. Mr. Y, holding 5% shares in A Ltd., receives dividend of ₹ 8.50 lakh. Discuss the tax implications in the hands of A Ltd., Mr. X and Mr. Y, assuming that Mr. X and Mr. Y have not received dividend from any other domestic company during the year.

**Solution**

(i) The dividend of ₹ 170 lakh declared and distributed in the P.Y.2017-18 is subject to dividend distribution tax under section 115-O in the hands of A Ltd. First of all, the dividend received has to be grossed up by applying the rate of 15%. The gross dividend is ₹ 200 lakhs [₹ 170 lakhs x 100/85]. Dividend distribution tax @17.304% is ₹ 34.068 lakhs.

(ii) In the hands of Mr. X, dividend received upto ₹ 10 lakh would be exempt under section 10(34). ₹ 7 lakh, being dividend received in excess of ₹ 10 lakh, would be taxable @10% as per section 115BBDA. Such dividend would not be exempt under section 10(34). Therefore,
tax payable by Mr. X on dividend of ₹ 7 lakh under section 115BBDA would be ₹ 72,100 [i.e., 10% of ₹ 7 lakh + cess @3%].

(iii) In the hands of Mr. Y, the entire dividend of ₹ 8.50 lakh received would be exempt under section 10(34), since only dividend received in excess of ₹ 10 lakh would be taxable under section 115BBDA.

**Chargeability of Dividend in the hands of the shareholder**

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**Illustration 2**

*Dhaval is in business of manufacturing customized kitchen equipments. He is also the Managing Director and held nearly 65% of the paid-up share capital of Aarav (P) Ltd. A substantial part of the business of Dhaval is obtained through Aarav (P) Ltd. For this purpose, Aarav (P) Ltd. passed on the advance received from its customers to Dhaval to execute the job work entrusted to him.*
The Assessing Officer held that the advance money received by Dhaval is in the nature of loan given by Aarav (P) Ltd. to him and accordingly is deemed dividend within the meaning of provisions of section 2(22)(e) of the Income-tax Act, 1961. The Assessing Officer, therefore made the addition by treating advance money as the deemed dividend income of Dhaval.

Examine whether the action of the Assessing Officer is tenable in law.

Solution

As per section 2(22)(e), in case a company, not being a company in which the public are substantially interested, makes payment of any sum by way of advance or loan to a shareholder holding not less than 10% of voting power/share capital of the company, then, the payment so made shall be deemed to be dividend in the hands of such shareholder to the extent to which the company possesses accumulated profits.

In the present case, Dhaval is holding 65% of the paid-up capital of Aarav (P) Ltd. Aarav (P) Ltd. has passed on advance received from its customers to Dhaval for execution of job work entrusted to Dhaval.

Since Aarav (P) Ltd. is not a company in which public are substantially interested, the applicability of the provisions of section 2(22)(e) in respect of such transaction has to be examined. In CIT v. Rajkumar (2009) 318 ITR 462 (Del.), it was held that trade advance given to the shareholder which is in the nature of money transacted to give effect to a commercial transaction, would not be deemed to be dividend in the hands of the shareholder under section 2(22)(e). The Delhi High Court ruling in CIT v. Ambassador Travels (P) Ltd. (2009) 318 ITR 376 also supports the above view.

In the present case, the payment is made to Dhaval by Aarav (P) Ltd. for execution of work is in the course of commercial business transaction and therefore, it shall not be deemed as dividend in the hands of Dhaval under section 2(22)(e). Hence, the action of the Assessing Officer is not tenable in law.

Illustration 3

MNO Ltd. is a company in which the public are not substantially interested. K is a shareholder of the company holding 15% of the equity shares. The accumulated profits of the company as on 31.3.2017 amounted to ₹10,00,000. The company lent ₹1,00,000 to K by an account payee bank draft on 1.10.2017. The loan was not connected with the business of the company. K repaid the loan to the company by an account payee bank draft on 30.3.2018. Examine the effect of the borrowal and repayment of the loan by K on the computation of his total income for the assessment year 2018-19.
Solution

As per section 2(22)(e), any payment by a company, in which the public are not substantially interested, by way of advance or loan to a shareholder, being a person who is the beneficial owner of shares holding not less than 10% of the voting power, shall be treated as dividend to the extent to which the company possesses accumulated profits.

In the instant case, MNO Ltd. is a company in which the public are not substantially interested. The company has accumulated profits of ₹ 10,00,000 on 31.3.2017. The loan given by the company to K was not in the course of its business. K holds more than 10% of the equity shares in the company. Therefore, assuming that K has voting power equivalent to his shareholding, section 2(22)(e) comes into play and the sum of ₹ 1,00,000, representing the amount lent by the company to K, is includible as dividend in the total income of K for the assessment year 2018-19.

Under section 2(22)(e), the liability arises the moment the loan is borrowed by the shareholder and it is immaterial whether the loan is repaid before the end of the accounting year or not. Therefore, the repayment of loan by K to the company on 30.3.2018 will not affect the taxability of the sum of ₹ 1,00,000 as dividend in his hands.

(ii) Casual Income

Casual income means income in the nature of winning from lotteries, crossword puzzles, races including horse races, card games and other games of any sort, gambling, betting etc. Such winnings are chargeable to tax at a flat rate of 30% under section 115BB.

(iii) Any sum of money or value of property received without consideration or for inadequate consideration to be subject to tax in the hands of the recipient [Section 56(2)(x)]

(a) In order to prevent the practice of receiving sum of money or the property without consideration or for inadequate consideration, section 56(2)(x) brings to tax any sum of money or the value of any property received by any person without consideration or the value of any property received for inadequate consideration.

(b) Sum of Money: If any sum of money is received without consideration, and the aggregate value of which exceeds ₹ 50,000, the whole of the aggregate value of such sum is chargeable to tax.

(c) Immovable property:

1. If an immovable property is received

   a. Without consideration, the stamp duty value of such property would be taxed as the income of the recipient if it exceeds ₹ 50,000.
b. For a consideration, which is less than the stamp duty value of the property by an amount exceeding ₹50,000, the difference between the stamp duty value and the consideration shall be chargeable to tax in the hands of the assessee as “Income from other sources”.

II. Value of property to be considered where the date of agreement is different from date of registration: Taking into consideration the possible time gap between the date of agreement and the date of registration, the stamp duty value may be taken as on the date of agreement instead of the date of registration, if the date of the agreement fixing the amount of consideration for the transfer of the immovable property and the date of registration are not the same, provided whole or part of the consideration has been paid by way of an account payee cheque or an account payee bank draft or by use of electronic clearing system (ECS) through a bank account on or before the date of agreement.

III. If the stamp duty value of immovable property is disputed by the assessee, the Assessing Officer may refer the valuation of such property to a Valuation Officer. In such a case, the provisions of section 50C and section 155(15) shall, as far as may be, apply for determining the value of such property. As per section 50C, if such value is less than the stamp duty value, the same would be taken for determining the value of such property, for computation of income under this head in the hands of the buyer.

(d) Movable Property: If movable property is received

1. **without consideration**, the aggregate fair market value of such property on the date of receipt would be taxed as the income of the recipient, if it exceeds ₹50,000.

2. **for a consideration which is less than the fair market value of the property by an amount exceeding ₹50,000**, and the difference between the aggregate fair market value and such consideration exceeds ₹50,000, such difference would be taxed as the income of the recipient.

(e) Applicability of section 56(2)(x): The provisions of section 56(2)(x) would apply only to property which is the nature of a capital asset of the recipient and not stock-in-trade, raw material or consumable stores of any business of the recipient. Therefore, only transfer of a capital asset, without consideration or for inadequate consideration would attract the provisions of section 56(2)(x).
(f) The table below summarizes the scheme of taxability of gifts –

<table>
<thead>
<tr>
<th>Nature of asset</th>
<th>Taxable value</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Money</td>
<td>Without consideration, the whole amount if the same exceeds ₹ 50,000.</td>
</tr>
<tr>
<td>2 Movable property</td>
<td>(i) Without consideration: The aggregate fair market value of the property, if it exceeds ₹ 50,000.</td>
</tr>
<tr>
<td></td>
<td>(ii) Inadequate consideration: The difference between the aggregate fair market value and the consideration, if such difference exceeds ₹ 50,000.</td>
</tr>
<tr>
<td>3 Immovable property</td>
<td>(i) Without consideration: The stamp value of the property, if it exceeds ₹ 50,000.</td>
</tr>
<tr>
<td></td>
<td>(ii) Inadequate consideration: The difference between the stamp duty value and the consideration, if such difference exceeds ₹ 50,000.</td>
</tr>
</tbody>
</table>

(g) **Non-applicability of section 56(2)(x):** However, any sum of money or value of property received in the following circumstances would be outside the ambit of section 56(2)(x) -

(i) from any relative; or

(ii) on the occasion of the marriage of the individual; or

(iii) under a will or by way of inheritance; or

(iv) in contemplation of death of the payer or donor, as the case may be; or

(v) from any local authority as defined in the Explanation to section 10(20); or

(vi) from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in section 10(23C); or

(vii) from any trust or institution registered under section 12AA; or

(viii) by any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in Section 10(23C)(iv)/(v)/(vi)/(via).  

(ix) by way of transaction not regarded as transfer under clause (i) or clause (vi) or
clause (via) or clause (viiia) or clause (vib) or clause (vic) or clause (vicb) or clause (vid) or clause (vii) of section 47.

(x) from an individual by a trust created or established solely for the benefit of relative of the individual.

(h) **Meaning of certain terms:**

<table>
<thead>
<tr>
<th>Term</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property</td>
<td>A capital asset of the assessee, namely,-</td>
</tr>
<tr>
<td></td>
<td>(a) immovable property being land or building or both,</td>
</tr>
<tr>
<td></td>
<td>(b) shares and securities,</td>
</tr>
<tr>
<td></td>
<td>(c) jewellery,</td>
</tr>
<tr>
<td></td>
<td>(d) archaeological collections,</td>
</tr>
<tr>
<td></td>
<td>(e) drawings,</td>
</tr>
<tr>
<td></td>
<td>(f) paintings,</td>
</tr>
<tr>
<td></td>
<td>(g) sculptures,</td>
</tr>
<tr>
<td></td>
<td>(h) any work of art or bullion.</td>
</tr>
<tr>
<td>Relative</td>
<td>(a) In case of an individual –</td>
</tr>
<tr>
<td></td>
<td>(i) spouse of the individual;</td>
</tr>
<tr>
<td></td>
<td>(ii) brother or sister of the individual;</td>
</tr>
<tr>
<td></td>
<td>(iii) brother or sister of the spouse of the individual;</td>
</tr>
<tr>
<td></td>
<td>(iv) brother or sister of either of the parents of the individual;</td>
</tr>
<tr>
<td></td>
<td>(v) any lineal ascendant or descendant of the individual;</td>
</tr>
<tr>
<td></td>
<td>(vi) any lineal ascendant or descendant of the spouse of the individual;</td>
</tr>
<tr>
<td></td>
<td>(vii) spouse of any of the persons referred to above.</td>
</tr>
<tr>
<td></td>
<td>(b) In case of Hindu Undivided Family, any member thereof.</td>
</tr>
</tbody>
</table>

(i) **Rules for determination of fair market value of the movable property [Rule 11UA]**

(I) **Valuation of jewellery, archeological collections, drawings, paintings, sculptures or any work of art**

a. the fair market value of jewellery, archeological collections, drawings, paintings, sculptures or any work of art (artistic work) shall be estimated to be the price which it would fetch if sold in the open market on the valuation date;

b. in case the jewellery or the artistic work, as the case may be, is received by the way of purchase on the valuation date, from a registered dealer, the
invoice value of the jewellery or artistic work shall be the fair market value;

c. In case the jewellery or artistic work, as the case may be, is received by any other mode and the value of the jewellery or artistic work exceeds ₹ 50,000, then, the assessee may obtain the report of registered valuer in respect of the price it would fetch if sold in the open market on the valuation date.

(II) Valuation of shares and securities

a. Fair market value of quoted shares and securities

(i) If received by transaction through any recognized stock exchange - if the quoted shares and securities are received by way of transaction carried out through any recognized stock exchange, the fair market value of such shares and securities shall be the transaction value as recorded in such stock exchange;

(ii) If received by transaction other than through any recognized stock exchange - if such quoted shares and securities are received by way of transaction carried out other than through any recognized stock exchange, the fair market value of such shares and securities shall be,-

(1) if securities or shares are traded on any recognized stock exchange on valuation date: the lowest price of such shares and securities quoted on any recognized stock exchange on the valuation date, and

(2) if securities or shares are not traded on any recognized stock exchange on valuation date: the lowest price of such shares and securities on any recognized stock exchange on a date immediately preceding the valuation date when such shares and securities were traded on such stock exchange

b. Fair market value of unquoted equity shares

The fair market value of unquoted equity shares

\[
= (A+B+C+D-L) \times (PV)/(PE), \text{ where,}
\]

\[A = \text{book value of all the assets (other than jewellery, artistic work, shares, securities and immovable property) in the balance-sheet as reduced by,-}\]

(i) any amount of income-tax paid, if any, less the amount of income-tax refund claimed, if any; and

(ii) any amount shown as asset including the unamortised amount of deferred expenditure which does not represent the value of any asset;
INCOME FROM OTHER SOURCES  

\[ B = \text{the price which the jewellery and artistic work would fetch if sold in the open market on the basis of the valuation report obtained from a registered valuer;} \]

\[ C = \text{fair market value of shares and securities as determined in the manner provided in this rule;} \]

\[ D = \text{the value adopted or assessed or assessable by any authority of the Government for the purpose of payment of stamp duty in respect of the immovable property;} \]

\[ L = \text{book value of liabilities shown in the balance sheet, but not including the following amounts, namely -} \]

(i) the paid-up capital in respect of equity shares;

(ii) the amount set apart for payment of dividends on preference shares and equity shares where such dividends have not been declared before the date of transfer at a general body meeting of the company;

(iii) reserves and surplus, by whatever name called, even if the resulting figure is negative, other than those set apart towards depreciation;

(iv) any amount representing provision for taxation, other than amount of income-tax paid, if any, less the amount of income-tax claimed as refund, if any, to the extent of the excess over the tax payable with reference to the book profits in accordance with the law applicable thereto; (v) any amount representing provisions made for meeting liabilities, other than ascertained liabilities;

(v) any amount representing contingent liabilities other than arrears of dividends payable in respect of cumulative preference shares;

\[ PV = \text{the paid-up value of such equity shares;} \]

\[ PE = \text{total amount of paid up equity share capital as shown in the balance-sheet;} \]

(c) **fair market value of unquoted shares and securities other than equity shares** in a company which are not listed in any recognized stock exchange shall be estimated to be price it would fetch if sold in the open market on the valuation date and the assessee may obtain a report from a merchant banker or an accountant in respect of such valuation.
Note: For meaning of certain expressions/terms used in determination of Fair Market Value, please refer Para 4 – “Consideration received in excess of FMV of shares issued by a closely held company to be treated as income of such company, where shares are issued at a premium [Section 56(2)(viib)]”

Tax implications on transfer of immovable property for inadequate consideration

In the hands of the seller

If Land & Building are held as stock-in-trade

Section 43CA will apply

Is date of agreement different from the date of transfer?

Yes

Is whole or part of the consideration received otherwise than by way of cash on or before the date of agreement?

Yes

Stamp Duty Value on the date of transfer is the full value of consideration

No

Stamp Duty Value on the date of agreement is the full value of consideration

No

If Land & Building are held as Capital Asset

Section 50C will apply

Is date of agreement different from the date of transfer?

Yes

Is whole or part of the consideration received by way of A/c payee cheque/Bank Draft or ECS through Bank A/c on or before the date of agreement?

Yes

No

No

No
Illustration 4

Mr. A, a dealer in shares, received the following without consideration during the P.Y.2017-18 from his friend Mr. B, -

(1) Cash gift of ₹75,000 on his anniversary, 15th April, 2017.

(2) Bullion, the fair market value of which was ₹60,000, on his birthday, 19th June, 2017.

(3) A plot of land at Faridabad on 1st July, 2017, the stamp value of which is ₹5 lakh on that date. Mr. B had purchased the land in April, 2008.
Mr. A purchased from his friend Mr. C, who is also a dealer in shares, 1000 shares of X Ltd. @ ₹ 400 each on 19th June, 2017, the fair market value of which was ₹ 600 each on that date. Mr. A sold these shares in the course of his business on 23rd June, 2017.

Further, on 1st November, 2017, Mr. A took possession of property (building) booked by him two years back at ₹ 20 lakh. The stamp duty value of the property as on 1st November, 2017 was ₹ 32 lakh and on the date of booking was ₹ 23 lakh. He had paid ₹ 1 lakh by account payee cheque as down payment on the date of booking.

On 1st March, 2018, he sold the plot of land at Faridabad for ₹ 7 lakh.

Compute the income of Mr. A chargeable under the head “Income from other sources” and “Capital Gains” for A.Y.2018-19.

Solution

Computation of “Income from other sources” of Mr. A for the A.Y.2018-19

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Cash gift is taxable under section 56(2)(x), since it exceeds ₹ 50,000</td>
<td>75,000</td>
</tr>
<tr>
<td>(2) Since bullion is included in the definition of property, therefore, when bullion is received without consideration, the same is taxable, since the aggregate fair market value exceeds ₹ 50,000</td>
<td>60,000</td>
</tr>
<tr>
<td>(3) Stamp value of plot of land at Faridabad, received without consideration, is taxable under section 56(2)(x)</td>
<td>5,00,000</td>
</tr>
<tr>
<td>(4) Difference of ₹ 2 lakh in the value of shares of X Ltd. purchased from Mr. C, a dealer in shares, is not taxable as it represents the stock-in-trade of Mr. A. Since Mr. A is a dealer in shares and it has been mentioned that the shares were subsequently sold in the course of his business, such shares represent the stock-in-trade of Mr. A.</td>
<td>-</td>
</tr>
<tr>
<td>(5) Difference between the stamp duty value of ₹ 23 lakh on the date of booking and the actual consideration of ₹ 20 lakh paid is taxable under section 56(2)(x) as ₹ 1 lakh is paid on the date of booking by account payee cheque.</td>
<td>3,00,000</td>
</tr>
</tbody>
</table>

Income from Other Sources 9,35,000
Computation of “Capital Gains” of Mr. A for the A.Y.2018-19

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sale Consideration</td>
<td>7,00,000</td>
</tr>
<tr>
<td>Less: Cost of acquisition [deemed to be the stamp value charged to tax under section 56(2)(x) as per section 49(4)]</td>
<td>5,00,000</td>
</tr>
<tr>
<td><strong>Short-term capital gains</strong></td>
<td>2,00,000</td>
</tr>
</tbody>
</table>

**Note** – The resultant capital gains will be short-term capital gains since for calculating the period of holding, the period of holding of previous owner is not to be considered.

**Illustration 5**

Discuss the taxability or otherwise of the following in the hands of the recipient under section 56(2)(x) the Income-tax Act, 1961 -

(i) Akhil HUF received ₹ 75,000 in cash from niece of Akhil (i.e., daughter of Akhil’s sister). Akhil is the Karta of the HUF.

(ii) Nitisha, a member of her father’s HUF, transferred a house property to the HUF without consideration. The stamp duty value of the house property is ₹ 9,00,000.

(iii) Mr. Akshat received 100 shares of A Ltd. from his friend as a gift on occasion of his 25th marriage anniversary. The fair market value on that date was ₹ 100 per share. He also received jewellery worth ₹ 45,000 (FMV) from his nephew on the same day.

(iv) Kishan HUF gifted a car to son of Karta for achieving good marks in XII board examination. The fair market value of the car is ₹ 5,25,000.

**Solution**

<table>
<thead>
<tr>
<th>Taxable/Non-taxable</th>
<th>Amount liable to tax (₹)</th>
<th>Reason</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Taxable</td>
<td>75,000</td>
<td>Sum of money exceeding ₹ 50,000 received without consideration from a non-relative is taxable under section 56(2)(x). Daughter of Mr. Akhil’s sister is not a relative of Akhil HUF, since she is not a member of Akhil HUF.</td>
</tr>
<tr>
<td>(ii) Non-taxable</td>
<td>Nil</td>
<td>Immovable property received without consideration by a HUF from its relative is not taxable under section 56(2)(x). Since Nitisha is a member of the HUF, she is a relative of the HUF. However, income from such asset would be included in the hands of Nitisha under 64(2).</td>
</tr>
</tbody>
</table>

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(iii) Taxable 55,000 As per provisions of section 56(2)(x), in case the aggregate fair market value of property, other than immovable property, received without consideration exceeds ₹ 50,000, the whole of the aggregate value shall be taxable. In this case, the aggregate fair market value of shares (₹ 10,000) and jewellery (₹ 45,000) exceeds ₹ 50,000. Hence, the entire amount of ₹ 55,000 shall be taxable.

(iv) Non-taxable Nil Car is not included in the definition of property for the purpose of section 56(2)(x), therefore, the same shall not be taxable.

Illustration 6

Mr. Hari, a property dealer, sold a building in the course of his business to his friend Mr. Rajesh, who is a dealer in automobile spare parts, for ₹ 90 lakh on 1.1.2018, when the stamp duty value was ₹ 150 lakh. The agreement was, however, entered into on 1.9.2017 when the stamp duty value was ₹ 140 lakh. Mr. Hari had received a down payment of ₹ 15 lakh by a crossed cheque from Mr. Rajesh on the date of agreement. Discuss the tax implications in the hands of Mr. Hari and Mr. Rajesh, assuming that Mr. Hari has purchased the building for ₹ 75 lakh on 12th July, 2016.

Would your answer be different if Hari was a share broker instead of a property dealer?

Solution

Case 1: Tax implications if Mr. Hari is a property dealer

<table>
<thead>
<tr>
<th>In the hands of Mr. Hari</th>
<th>In the hands of Mr. Rajesh</th>
</tr>
</thead>
<tbody>
<tr>
<td>In the hands of Hari, the provisions of section 43CA would be attracted, since the building represents his stock-in-trade and he has transferred the same for a consideration less than the stamp duty value on the date of agreement. Therefore, ₹ 65 lakh, being the difference between the stamp duty value on the date of agreement (i.e., ₹ 140 lakh) and the purchase price (i.e., ₹ 75 lakh), would be chargeable as business income in the hands of Mr. Hari.</td>
<td>Since Mr. Rajesh is a dealer in automobile spare parts, the building purchased would be a capital asset in his hands. The provisions of section 56(2)(x) would be attracted in the hands of Mr. Rajesh who has received immovable property, being a capital asset, for inadequate consideration. Therefore, ₹ 60 lakh, being the difference between the stamp duty value of the property on the date of registration (i.e., ₹ 150 lakh) and the actual consideration (i.e., ₹ 90 lakh) would be taxable under section 56(2)(x) in the hands of Mr. Rajesh, since the payment is made by crossed cheque and not account payee cheque/draft or ECS.</td>
</tr>
</tbody>
</table>
Case 2: Tax implications if Mr. Hari is a stock broker

<table>
<thead>
<tr>
<th>In the hands of Mr. Hari</th>
<th>In the hands of Mr. Rajesh</th>
</tr>
</thead>
<tbody>
<tr>
<td>In case Mr. Hari is a stock broker and not a property dealer, the building would represent his capital asset and not stock-in-trade. In such a case, the provisions of section 50C would be attracted in the hands of Mr. Hari and ₹ 75 lakh, being the difference between the stamp duty value on the date of registration (i.e., ₹ 150 lakh) and the purchase price (i.e., ₹ 75 lakh) would be chargeable as short-term capital gains. It may be noted that under section 50C, the option to adopt the stamp duty value on the date of agreement can be exercised only if whole or part of the consideration has been received on or before the date of agreement by way of account payee cheque or draft or by use of ECS through a bank account on or before the date of agreement. In this case, since the payment is made by crossed cheque, the option cannot be exercised.</td>
<td></td>
</tr>
<tr>
<td>There would be no difference in the taxability in the hands of Mr. Rajesh, whether Mr. Hari is a property dealer or a stock broker. Therefore, the provisions of section 56(2)(x) would be attracted in the hands of Mr. Rajesh who has received immovable property, being a capital asset, for inadequate consideration. Therefore, ₹ 60 lakh, being the difference between the stamp duty value of the property on the date of registration (i.e., ₹ 150 lakh) and the actual consideration (i.e., ₹ 90 lakh) would be taxable under section 56(2)(x) in the hands of Mr. Rajesh.</td>
<td></td>
</tr>
</tbody>
</table>

Note: As per section 43CA, stamp duty value on the date of agreement can be adopted, if whole or part of consideration is received otherwise than by way of cash on or before the date of agreement.

However, both section 50C and 56(2)(x) permit adoption of stamp value duty on the date of agreement only if whole or part of consideration is received/paid, as the case may be by way of account payee cheque or account payee bank draft or by use of ECS through a bank account.

(iv) Consideration received in excess of FMV of shares issued by a closely held company to be treated as income of such company, where shares are issued at a premium [Section 56(2)(viib)]

(a) Section 56(2)(viib) brings to tax the consideration received from a resident person by a company, other than a company in which public are substantially interested, which is in excess of the fair market value (FMV) of shares.

(b) Such excess is to be treated as the income of a closely held company taxable under section 56(2) under the head “Income from Other Sources”, in cases where...
consideration received for issue of shares exceeds the face value of shares i.e. where shares are issued at a premium.

(c) However, these provisions would not be attracted where consideration for issue of shares is received:

(1) by a Venture Capital Undertaking (VCU) from a Venture Capital Fund (VCF) or Venture Capital Company (VCC); or

(2) by a company from a class or classes of persons as notified by the Central Government for this purpose.

(d) Fair market value of the shares shall be the higher of, the value as may be –

a. determined in accordance with the prescribed method; or

b. substantiated by the company to the satisfaction of the Assessing Officer, based on the value of its assets on the date of issue of shares.

For the purpose of computation of FMV, the value of assets would include the value of intangible assets being goodwill, know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature.

(e) Rules for determination of fair market value of unquoted equity shares [Rule 11UA(2)]

The fair market value of unquoted equity shares shall be the value, on the valuation date, of such unquoted equity shares as determined in the following manner under (a) or (b), at the option of the assessee, namely:-

(I) \[
\text{The fair market value of unquoted equity shares} = \frac{(A - L) \times (P \times V)}{E} , \text{where,}
\]

\[A = \text{Adjusted book value of assets i.e., book value of assets in the balance sheet as reduced by certain specified deductions, namely, -}
\]

(i) any amount of tax paid as deduction or collection at source; or

(ii) advance tax payment reduced by the amount of tax claimed as refund under the Income-tax Act, 1961; and

(iii) any amount shown in the balance-sheet as asset including the unamortised amount of deferred expenditure which does not represent the value of any asset.

\[L = \text{Adjusted book value of liabilities, i.e., book value of liabilities shown in the Balance Sheet drawn up on the valuation date but not including the following amounts: -}
\]
(i) the paid-up capital in respect of equity shares;

(ii) the amount set apart for payment of dividends on preference shares and equity shares where such dividends have not been declared before the date of transfer at a general body meeting of the company;

(iii) reserves and surplus, by whatever name called, even if the resulting figure is negative, other than those set apart towards depreciation;

(iv) any amount representing provision for taxation, other than amount of tax paid as deduction or collection at source or as advance tax payment as reduced by the amount of tax claimed as refund under the Income-tax Act, 1961, to the extent of excess over the tax payable with reference to the book profits in accordance with the law applicable thereto;

(v) any amount representing provisions made for meeting liabilities, other than ascertained liabilities;

(vi) any amount representing contingent liabilities other than arrears of dividends payable in respect of cumulative preference shares.

PE = Total amount of paid up equity share capital as shown in Balance Sheet.

PV = the paid up value of such equity shares.

(ii) the fair market value of the unquoted equity shares determined by a merchant banker or an accountant as per Discounted Free Cash Flow Method.

Meaning of certain expressions, used in determination of Fair Market Value, amended [Rule 11U]

<table>
<thead>
<tr>
<th>Term</th>
<th>Meaning</th>
<th>In any other case</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accountant</td>
<td><strong>For the purpose Rule 11UA(2)</strong></td>
<td>Meaning as assigned in the Explanation below section 288(2) i.e., Chartered Accountant within the meaning of the Chartered Accountants Act, 1949.</td>
</tr>
<tr>
<td></td>
<td>A fellow of the Institute of Chartered Accountants of India within the meaning of the Chartered Accountants Act, 1949, who is not appointed by the company as an auditor under –</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>(i)</strong> section 44AB of the Income-tax Act, 1961 or</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>(ii)</strong> section 224 of the Companies Act, 1956¹.</td>
<td></td>
</tr>
</tbody>
</table>

¹Section 139 of the Companies Act, 2013
<table>
<thead>
<tr>
<th>Balance Sheet</th>
<th>For the purpose Rule 11UA(2)</th>
<th>In any other case</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>“Balance sheet”, in relation to any company, means, the balance sheet of such company (including the notes annexed thereto and forming part of the accounts)-</td>
<td>“Balance sheet”, in relation to any company, means the balance sheet of such company (including the notes annexed thereto and forming part of the accounts) –</td>
</tr>
<tr>
<td></td>
<td>- as drawn up on the valuation date</td>
<td>- as drawn up on the valuation date</td>
</tr>
<tr>
<td></td>
<td>- which has been audited by the auditor of the company appointed under section 224 of the Companies Act, 1956.</td>
<td>- which has been audited by the auditor appointed under section 224 of the Companies Act, 1956.</td>
</tr>
<tr>
<td></td>
<td>Where the balance sheet on the valuation date is not drawn up, the expression “Balance Sheet” in relation to any company, would mean the balance sheet (including the notes annexed thereto and forming part of the accounts) drawn up as on a date immediately preceding the valuation date which has been approved and adopted in the annual general meeting of the shareholders of the company;</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Quoted shares or securities</th>
<th>A share or security quoted on any recognized stock exchange with regularity from time to time, where the quotations of such shares or securities are based on current transaction made in the ordinary course of business</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unquoted shares and securities</td>
<td>Shares and securities which is not a quoted shares or securities</td>
</tr>
<tr>
<td>Merchant banker</td>
<td>Category I merchant banker registered with Securities and Exchange Board of India established under section 3 of the Securities and Exchange Board of India Act, 1992</td>
</tr>
</tbody>
</table>
## Examples:

<table>
<thead>
<tr>
<th>Co.</th>
<th>No. of shares</th>
<th>Face value of shares (₹)</th>
<th>FMV of shares (₹)</th>
<th>Issue price of shares (₹)</th>
<th>Applicability of section 56(2)(viib)</th>
</tr>
</thead>
<tbody>
<tr>
<td>A (P) Ltd.</td>
<td>10,000</td>
<td>100</td>
<td>120</td>
<td>130</td>
<td>The provisions of section 56(2)(viib) are attracted in this case since the shares are issued at a premium (i.e., issue price exceeds the face value of shares). The excess of the issue price of the shares over the FMV would be taxable under section 56(2)(viib). ₹ 1,00,000 [10,000 × ₹ 10 (₹ 130 - ₹ 120)] shall be treated as income in the hands of A (P) Ltd.</td>
</tr>
<tr>
<td>B (P) Ltd.</td>
<td>20,000</td>
<td>100</td>
<td>120</td>
<td>110</td>
<td>The provisions of section 56(2)(viib) are attracted since the shares are issued at a premium. However, no sum shall be chargeable to tax in the hands of B (P) Ltd. under the said section as the shares are issued at a price less than the FMV of shares.</td>
</tr>
<tr>
<td>C (P) Ltd.</td>
<td>30,000</td>
<td>100</td>
<td>90</td>
<td>98</td>
<td>Section 56(2)(viib) is not attracted since the shares are issued at a discount, though the issue price is greater than the FMV.</td>
</tr>
<tr>
<td>D (P) Ltd.</td>
<td>40,000</td>
<td>100</td>
<td>90</td>
<td>110</td>
<td>The provisions of section 56(2)(viib) are attracted in this case since the shares are issued at a premium. The excess of the issue price of the shares over the FMV would be taxable under section 56(2)(viib). Therefore, ₹ 8,00,000 [40,000 × ₹ 20 (₹ 110 - ₹ 90)] shall be treated as income in the hands of D (P) Ltd.</td>
</tr>
</tbody>
</table>
(v) **Interest received on compensation/enhanced compensation deemed to be income in the year of receipt and taxable under the head “Income from Other Sources” [Sections 56(2)(viii)]**

(a) As per section 145(1), income chargeable under the head “Profits and gains of business or profession” or “Income from other sources”, shall be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee.

(b) Further, the Hon’ble Supreme Court has, in *Rama Bai v. CIT (1990) 181 ITR 400*, held that arrears of interest computed on delayed or on enhanced compensation shall be taxable on accrual basis. The tax payers are facing genuine difficulty on account of this ruling, since the interest would have accrued over a number of years, and consequently the income of all the years would undergo a change.

(c) Therefore, to remove this difficulty, clause (b) of section 145A provides that the interest received by an assessee on compensation or on enhanced compensation shall be deemed to be his income for the year in which it is received, irrespective of the method of accounting followed by the assessee.

(d) Section 56(2)(viii) provides that income by way of interest received on compensation or on enhanced compensation referred to in clause (b) of section 145A shall be assessed as “Income from other sources” in the year in which it is received.

(vi) **Advance forfeited due to failure of negotiations for transfer of a capital asset to be taxable as “Income from other sources” [Section 56(2)(ix)]**

(a) Prior to A.Y.2015-16, any advance retained or received in respect of a negotiation for transfer which failed to materialise is reduced from the cost of acquisition of the asset or the written down value or the fair market value of the asset, at the time of its transfer to compute the capital gains arising therefrom as per section 51. In case the asset transferred is a long-term capital asset, indexation benefit would be on the cost so reduced.

(b) With effect from A.Y.2015-16, section 56(2)(ix) provides for the taxability of any sum of money, received as an advance or otherwise in the course of negotiations for transfer of a capital asset. Such sum shall be chargeable to income-tax under the head ‘Income from other sources’, if such sum is forfeited and the negotiations do not result in transfer of such capital asset.

(c) In order to avoid double taxation of the advance received and retained, section 51 has been amended to provide that where any sum of money received as an advance or otherwise in the course of negotiations for transfer of a capital asset, has been included
in the total income of the assessee for any previous year, in accordance with section 56(2)(ix), such amount shall not be deducted from the cost for which the asset was acquired or the written down value or the fair market value, as the case may be, in computing the cost of acquisition.

(d) It may be noted that advance received and forfeited upto 31.3.2014 has to be reduced from cost of acquisition while computing capital gains, since such advance would not have been subject to tax under section 56(2)(ix). Only the advance received and forfeited on or after 1.4.2014 would be subject to tax under section 56(2)(ix). Hence, such advance would not be reduced from the cost of acquisition for computing capital gains.

(2) Income chargeable under the head “Income from other sources” only if not chargeable under the head “Profits and gains of business or profession” -

(i) Any sum received by an employer-assessee from his employees as contributions to any provident fund, superannuation fund or any other fund for the welfare of the employees.

(ii) Income from letting out on hire, machinery, plant or furniture.

(iii) Where letting out of buildings is inseparable from the letting out of machinery, plant or furniture, the income from such letting.

(iv) Interest on securities

However, the following interest income arising to certain persons would be exempt under section 10(15):

(a) Income by way of interest, premium on redemption or other payment on notified securities, bonds, annuity certificates or other savings certificates is exempt subject to such conditions and limits as may be specified in the notification.

It may be noted that interest on Post Office Savings Bank Account which was so far fully exempt would henceforth be exempt from tax for any assessment year only to the extent of:

(1) ₹ 3,500 in case of an individual account.

(2) ₹ 7,000 in case of a joint account.

(b) Interest on securities held by the Issue Department of Central Bank of Ceylon constituted under the Ceylon Monetary Law Act, 1949.

(c) Interest payable —

(1) by public sector companies on certain specified bonds and debentures subject to the conditions which the Central Government may specify by notification, including
the condition that the holder of such bonds or debentures registers his name and holding with that company;

Accordingly, the Central Government has specified tax free bonds issued by India Infrastructure Company Ltd. and tax free, secured, redeemable, non-convertible Bonds of the Indian Railway Finance Corporation Ltd. (IRFCL), National Highways Authority of India (NHAI), Rural Electrification Corporation Ltd. (RECL), Housing and Urban Development Corporation Ltd. (HUDCL), Power Finance Corporation (PFC), Jawaharlal Nehru Port Trust, Dredging Corporation of India Limited, Ennore Port Limited and The Indian Renewable Energy Development Agency Limited, the interest from which would be exempt under this section.

(2) by Government of India on deposit made by an employee of the Central or State Government or a public sector company in accordance with the scheme as may be notified of the moneys due to him on account of his retirement while on superannuation or otherwise. It is significant that this scheme is not applicable to non-Government employees.

The term ‘industrial undertaking’ means any undertaking which is engaged in:

(i) the manufacture or processing of goods; or
(ii) the manufacture of computer software or recording of programmes on any disc, tape, perforated media or other information device; or
(iii) the business of generation or generation and distribution of electricity or any other form of power; or
(iv) the business of providing telecommunication services; or
(v) mining; or
(vi) construction of ships, or
(vii) the business of ship-breaking; or
(viii) the operation of ships or aircrafts or construction or operation of rail systems.

For the purposes of the clause, “interest” shall not include interest paid on delayed payment of loan or default if which is more than 2% p.a. over the rate of interest payable in terms of such loan. Interest would include hedging transaction charges on account of currency fluctuation.

(d) **Bhopal Gas Victims** - Section 10(15)(v) provides exemption in respect of interest on securities held by the Welfare Commissioner, Bhopal Gas Victims, Bhopal, in the Reserve Bank’s Account No. SL/DH 048. Recently, in terms of an order of the Supreme...
Court to finance the construction of a hospital at Bhopal to serve the victims of the gas leak, the shares of the Union Carbide Indian Ltd., have been sold. The scope of the above exemption has been extended to interest on deposits for the benefit of the victims of the Bhopal Gas Leak disaster. Such deposits can be held in such account with the RBI or with a public sector bank as the Central Government may notify in the Official Gazette.

(e) Interest on Gold Deposit Bond issued under the Gold Deposit Scheme, 1999 or deposit certificates issued under the Gold Monetization Scheme, 2015 notified by the Central Government.

(f) Interest on bonds, issued by –
(1) a local authority; or
(2) a State Pooled Finance Entity

and specified by the Central Government by notification in the Official Gazette.

“State Pooled Finance Entity” means such entity which is set up in accordance with the guidelines for the Pooled Finance Development Scheme notified by the Central Government in the Ministry of Urban Development.

Accordingly, the Central Government has specified the “Tax-free Pooled Finance Development Bonds” under Pooled Finance Development Fund Scheme of Government of India, interest from which would be exempt under section 10(15).

(3) Keyman Insurance Policy

Any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy is chargeable under the head “Income from other sources” if such income is not chargeable under the head “Profits and gains if business or profession” or under the head “Salaries” i.e. if such sum is received by any person other than the employer who took the policy and the employee in whose name the policy was taken.

(4) Residual Income

Any income chargeable to tax under the Act, but not falling under any other head of income shall be chargeable to tax under the head “Income from other sources” e.g. Salary received by an MPs/MLAs will not be chargeable to income-tax under the head ‘Salary’ but will be chargeable as “Income from other sources” under section 56.

Interest from non-SLR Securities of Banks: Whether chargeable under the head “Profits and gains of business or profession” or “Income from other sources”? [Circular No. 18, dated 2.11.2015]

The issue addressed by this circular is whether in the case of banks, expenses relatable to
8.28 DIRECT TAX LAWS

investment in non-SLR securities need to be disallowed under section 57(i), by considering interest on non-SLR securities as “Income from other sources.”

Section 56(1)(id) provides that income by way of interest on securities shall be chargeable to income-tax under the head "Income from Other Sources", if the income is not chargeable to income-tax under the head "Profits and Gains of Business and Profession".

The CBDT clarified that the investments made by a banking concern are part of the business of banking. Therefore, the income arising from such investments is attributable to the business of banking falling under the head "Profits and Gains of Business and Profession".

8.3 BOND WASHING TRANSACTIONS AND DIVIDEND STRIPPING [SECTION 94]

(1) A bond-washing transaction is a transaction where securities are sold some time before the due date of interest and reacquired after the due date is over. This practice is adopted by persons in the higher income group to avoid tax by transferring the securities to their relatives/friends in the lower income group just before the due date of payment of interest. In such a case, interest would be taxable in the hands of the transferee, who is the legal owner of securities. In order to discourage such practice, section 94(1) provides that where the owner of a security transfers the security just before the due date of interest and buys back the same immediately after the due date and interest is received by the transferee, such interest income will be deemed to be the income of the transferor and would be taxable in his hands.

(2) In order to prevent the practice of sale of securities-cum-interest, section 94(2) provides that if an assessee who has beneficial interest in securities sells such securities in such a manner that either no income is received or income received is less than the sum he would have received if such interest had accrued from day to day, then income from such securities for the whole year would be deemed to be the income of the assessee.

(3) Section 94(7) provides that where

(i) any person buys or acquires any securities or unit within a period of three months prior to the record date and

(ii) such person sells or transfers –

(a) such securities within a period of three months after such date, or

(b) such unit within a period of nine months after such date and

(iii) the dividend or income on such securities or unit received or receivable by such person is exempted,
then, the loss, if any, arising therefrom shall be ignored for the purposes of computing his income chargeable to tax. Such loss should not exceed the amount of dividend or income received or receivable on such securities or unit.

8.4 APPLICABLE RATE OF TAX IN RESPECT OF CASUAL INCOME [SECTION 115BB]

(1) This section provides that income by way of winnings from lotteries, crossword puzzles, races including horse races or card games and other games of any sort or from gambling or betting of any form would be taxed at a flat rate of 30% plus surcharge, if applicable, plus education cess plus secondary and higher education cess.

(2) No expenditure or allowance can be allowed from such income.

(3) Deduction under Chapter VI-A is not allowable from such income.

(4) Adjustment of unexhausted basic exemption limit is also not permitted against such income.

8.5 DEDUCTIONS ALLOWABLE [SECTION 57]

The income chargeable under the head “Income from other sources” shall be computed after making the following deductions:

(1) In the case of dividends (other than dividends referred to in section 115-O) or interest on securities, any reasonable sum paid by way of commission or remuneration to a banker or any other person for the purpose of realising such dividend or interest on behalf of the assessee.

(2) Where the income consists of recovery from employees as contribution to any provident fund etc. in terms of clause (x) of section 2(24), then, a deduction will be allowed in accordance with the provisions of section 36(1)(va) i.e. to the extent the contribution is remitted before the due date under the respective Acts.

(3) Where the income to be charged under this head is from letting on hire of machinery, plant and furniture, with or without building, the following items of deductions are allowable in the computation of such income:

   (i) the amount paid on account of any current repairs to the machinery, plant or furniture.

   (ii) the amount of any premium paid in respect of insurance against risk of damage or destruction of the machinery or plant or furniture.

   (iii) the normal depreciation allowance in respect of the machinery, plant or furniture, due thereon.
(4) In the case of income in the nature of family pension, a deduction of a sum equal to 33-1/3 percent of such income or ₹ 15,000, whichever is less, is allowable. For the purposes of this deduction “family pension” means a regular monthly amount payable by the employer to a person belonging to the family of an employee in the event of his death.

The family pension received by the widow or children or nominated heirs, of a member of the armed forces (including para-military forces) of the Union, where the death of such member has occurred in the course of operational duties, in specified circumstances would, however, be exempt under section 10(19).

(5) Any other expenditure not being in the nature of capital expenditure laid out or expended wholly and exclusively for the purpose of making or earning such income.

(6) 50% of income by way of compensation/enhanced compensation received chargeable to tax under section 56(2)(viii). No deduction would be allowable under any other clause of section 57 in respect of such income.

Illustration 8

Interest on enhanced compensation received by Mr. G during the previous year 2017-18 is ₹ 5,00,000. Out of this interest, ₹ 1,50,000 relates to the previous year 2012-13, ₹ 1,65,000 relates to previous year 2013-14 and ₹ 1,85,000 relates to previous year 2014-15. Discuss the tax implication, if any, of such interest income for A.Y.2018-19.

Solution

The entire interest of ₹ 5,00,000 would be taxable in the year of receipt, namely, P.Y.2017-18.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest on enhanced compensation taxable u/s 56(2)(viii)</td>
<td>5,00,000</td>
</tr>
<tr>
<td>Less: Deduction under section 57(iv) @50%</td>
<td>2,50,000</td>
</tr>
<tr>
<td>Interest chargeable under the head “Income from other sources”</td>
<td>2,50,000</td>
</tr>
</tbody>
</table>

Note - The Supreme Court held in CIT v. Rajendra Prasad Moody [1978] 115 ITR 519, that in order to claim deduction under section 57 in respect of any expenditure, it is not necessary that income should in fact have been earned as a result of the expenditure. In this view of the matter, the Court held that the interest on money borrowed for investment in shares which had not yielded any taxable dividend was admissible as a deduction under section 57 under the head, “Income from other sources”.

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8.6 DEDUCTIONS NOT ALLOWABLE [SECTION 58]

No deduction shall be made in computing the “Income from other sources” of an assessee in respect of the following items of expenses:

(1) In the case of any assessee:
   (i) any personal expense of the assessee;
   (ii) any interest chargeable to tax under the Act which is payable outside India on which tax has not been paid or deducted at source.
   (iii) any payment taxable in India as salaries, if it is payable outside India unless tax has been thereon or deducted at source.

(2) In addition to these disallowances, section 58(2) specifically provides that the disallowance of payments to relatives and associate concerns and disallowance of payment or aggregate of payments exceeding ₹10,000 made to a person during a day otherwise than by account payee cheque or draft or use of Electronic clearing system through a bank account covered by section 40A will be applicable to the computation of income under the head ‘Income from other sources’ as well.

(3) 30% of expenditure shall not be allowed, in respect of a sum which is payable to a resident and on which tax is deductible at source, if
   - such tax has not been deducted or;
   - such tax after deduction has not been paid on or before the due date of return specified in section 139(1).

(4) No deduction in respect of any expenditure or allowance in connection with income by way of earnings from lotteries, cross word puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever shall be allowed in computing the said income.

The prohibition will not, however, apply in respect of the income of an assessee, being the owner of race horses, from the activity of owning and maintaining such horses. In respect of the activity of owning and maintaining race horses, expenses incurred shall be allowed even in the absence of any stake money earned. Such loss shall be allowed to be carried forward in accordance with the provisions of section 74A.

8.7 DEEMED INCOME CHARGEABLE TO TAX [SECTION 59]

The provisions of section 41(1) are made applicable, so far as may be, to the computation of income under this head. Accordingly, where a deduction has been made in respect of a loss,
expenditure or liability and subsequently any amount is received or benefit is derived in respect of such expenditure incurred or loss or trading liability allowed as deduction, then it shall be deemed as income in the year in which the amount is received or the benefit is accrued.

**8.8 METHOD OF ACCOUNTING [SECTION 145]**

Income chargeable under the head “Income from other sources” has to be computed in accordance with the cash or mercantile system of accounting regularly employed by the assessee. However, deemed dividend under section 2(22)(e) is chargeable to tax on payment basis under section 8, irrespective of the method of accounting followed by the assessee.

Under section 145(2), the Central Government is empowered to notify in Gazette from time to time, income computation and disclosure standards to be followed by any class of assesses or in respect of any class of income.

Accordingly, Central Government has notified ten ICDSs to be followed by all assesses (other than an individual or a HUF who is not required to get his accounts of the previous year audited in accordance with the provisions of section 44AB) following the mercantile system of accounting, for the purpose of computation of income chargeable to income-tax under the head “Profits and gains from business or profession” or “Income from other sources”.

Text of notified ICDSs is given as an Annexure at the end of this module.
Question 1

Parimal, Managing Director of Heavens Engg. Pvt. Ltd. holds 70% of its paid up capital of ₹ 20 Lacs. The balance as at 31.03.2017 in General Reserve was ₹ 6 Lacs. The company on 1.07.2017 gave an interest-free loan of ₹ 5 Lacs to its Supervisor having salary of ₹ 4,000 p.m., who in turn on 15.8.2017 advanced the said amount of loan so taken from the company to Shri Parimal. The Assessing Officer had taxed the amount of advance in the hands of Parimal. Is the action of Assessing Officer correct?

Answer

The company had advanced a loan to an employee who in turn had advanced the same to the Managing Director of the company holding 70% of its capital. By virtue of the provisions of section 2(22)(e), the same shall be treated as the payment by a company in which public are not substantially interested, on behalf of, or for individual benefit of any such shareholder (who holds not less than 10% of the voting power), to the extent to which the company possesses accumulated profits.

In this case, the company has reserves of ₹ 6 Lacs on 31st March of the preceding year and the amount of loan advanced on 1st July is ₹ 5 Lacs. Therefore, the payment is to be treated as deemed dividend. The amount of interest-free loan of ₹ 5 Lacs given by the company to the supervisor who in turn had given the same to Mr. Parimal, shall be construed as the amount given for the benefit of Mr. Parimal and is treated as deemed dividend chargeable to tax in the hands of Mr. Parimal. This has been held by the Supreme Court in the case of L. Alagusundaram Chettiar v. CIT (2001) 252 ITR 893.

Question 2

HLI Private Limited is a company with three shareholders H (40%), L (20%) and I on behalf of his HUF (40%). I (HUF) is a Hindu Undivided Family whose members are Mr. I, Mrs. I and their two sons, G and J. The company gave a loan of ₹ 9 lakhs to I (HUF) on 30th April, 2017, on which date the accumulated profits of the company was ₹ 6 lakhs. What is the tax consequence of this transaction?

Answer

The issue under consideration in this case is whether, where the Karta is a shareholder (on behalf of his HUF) of a company in which public are not substantially interested, the loan advanced by the company to the HUF would constitute deemed dividend under section 2(22)(e) to the extent to which the company possesses accumulated profits.

There are two views on the basis of which this question can be answered.
First view

Section 2(22)(e) would be attracted if the loan is given by a company in which public are not substantially interested to a shareholder, being a person who is the beneficial owner of shares holding not less than 10% of voting power.

On a plain reading of section 2(22)(e), it appears that the said provision would be attracted only if the person to whom the loan is given is a registered shareholder as well as beneficial owner.

If this view is taken, then section 2(22)(e) would not be attracted in this case, since the registered shareholder is Mr. I (on behalf of his HUF), whereas the beneficial owner is his HUF.

Therefore, loan given to the HUF would not be deemed as dividend by applying section 2(22)(e).

**Note** – This view was taken by the Supreme Court in Rameshwarlal Sanwarmal v. CIT (1980) 122 ITR 1 (SC).

Second view

Section 2(22)(e) would be attracted if the loan is given by a company in which public are not substantially interested to a shareholder, being a person who is the beneficial owner of shares holding not less than 10% of voting power.

Even though on a plain reading of section 2(22)(e), it appears that the said provision would be attracted only if the person to whom the loan is given is a registered shareholder as well as beneficial owner, the Delhi High Court, in CIT v. National Travel Services (2012) 347 ITR 305/(2011) 202 Taxman 327, has taken a view that where loan is given by a company to a firm, being the beneficial owner of shares held in the name of its partners, provisions of section 2(22)(e) would be attracted, since the essential condition to be satisfied is that of beneficial ownership and it is not necessary that the beneficial owner has to be a registered shareholder.

If this view is adopted, then section 2(22)(e) would get attracted in this case. The loan to the HUF, being the beneficial owner, would be deemed as dividend in the hands of the HUF.

It would, however, be taxable only to the extent to which the company possesses accumulated profits on the date of loan i.e., in this case, ₹ 6 lakh.

Question 3

Mr. Santhanam holding 25% voting power in VKS Manufacturing Private Limited permitted his own land to be mortgaged to a bank for enabling the company to obtain a loan. Mr. Santhanam requested the company to release the property from the mortgage. The company failed to do so, but for retaining the benefit of bank loan it gave an advance of ₹ 10 lakhs to Mr. Santhanam, which was authorized by a resolution passed by the Board of Directors. The company's accumulated profit on the date of payment of advance was ₹ 50 lakhs. The Assessing Officer proposes to tax the amount of ₹ 10 lakhs by invoking the provision of section 2(22)(e).

Is the proposition of the Assessing Officer correct in law?
Answer

The issue under consideration is whether loan or advance given to a shareholder by the company, in return of an advantage or benefit conferred on the company by the shareholder, can be deemed as dividend under section 2(22)(e) of the Income-tax Act, 1961 in the hands of the shareholder.

The facts of the case are similar to the facts in Pradip Kumar Malhotra v. CIT (2011) 338 ITR 538, wherein the above issue came up before the Calcutta High Court.

The High Court observed that the phrase "by way of advance or loan" appearing in section 2(22)(e) must be construed to mean those advances or loans which a shareholder enjoys simply on account of being a person who is the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) holding not less than 10% of the voting power.

In case such loan or advance is given to such shareholder as a consequence of any further consideration received from such a shareholder which is beneficial to the company, such advance or loan cannot be a deemed dividend within the meaning of the Act.

Thus, gratuitous loan or advance given by a company to a shareholder, who is the beneficial owner of shares holding not less than 10% of the voting power, would come within the purview of section 2(22)(e) to the extent of accumulated profits of the company but not the cases where the loan or advance is given in return for an advantage conferred upon the company by such shareholder.

In this case, advance of ₹ 10 lakhs was given by VKS Manufacturing (P) Ltd. to Mr. Santhanam holding 25% of voting power in lieu of non-release of his personal property from mortgage thereby enabling the company to retain the benefit of loan obtained from bank. Therefore, applying the rationale of the Calcutta High Court ruling in Pradip Kumar Malhotra’s case, such advance cannot be brought within the purview of section 2(22)(e), since it was not in the nature of gratuitous advance but was given to protect the interest of the company.

The proposition of the Assessing Officer to tax the amount of ₹ 10 lakhs by invoking the provisions of section 2(22)(e) in this case is, therefore, not correct.

Question 4

An enterprise engaged in manufacturing of steel balls discontinued its activities and decided to lease out its factory building, plant and machinery and furniture from 1.4.2017 on a consolidated lease rent of ₹ 50,000 per month. Compute the income for Assessment Year 2018-19 of the assessee from following information:
(i) Interest received on deposits  1,00,000
(ii) Brokerage paid on hundi loan taken  2,000
(iii) Interest paid on hundi and other loans which were given as deposits on interest to others  75,000
(iv) Expenses incurred on repairs of building, plant and machinery  15,000
(v) Fire insurance premium of plant and machinery and furniture  12,000
(vi) Depreciation for the year  1,47,500
(vii) Legal fees paid to an advocate for drafting and registering the lease agreement  1,500
(viii) Factory licence fees paid for the year  1,000
(ix) There is unabsorbed depreciation of ₹ 2,75,000 of the Assessment Years 2016-17 and 2017-18.
(x) Interest paid includes an amount of ₹ 25,000 remitted to a non-resident outside India on which tax was not deducted at source.

**Answer**

The income derived from leased assets shall be chargeable to tax as 'Income from other sources' under section 56(2)(iii) but the computation thereof shall be made after allowing deductions specified under sections 30, 31 and 32 subject to section 38. This is as per the provisions of section 57(ii) and 57(iii).

<table>
<thead>
<tr>
<th>Computation of income under the head “Income from other sources”</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
</tr>
<tr>
<td>(A) Lease Rent for 12 months @ ₹ 50,000 p.m.</td>
</tr>
<tr>
<td>Less: Expenses and deductions allowable under section 57(ii) &amp; 57(iii):</td>
</tr>
<tr>
<td>Repairs</td>
</tr>
<tr>
<td>Fire Insurance Premium</td>
</tr>
<tr>
<td>Legal expenses for drafting of lease agreement</td>
</tr>
<tr>
<td>Factory Licence fee</td>
</tr>
<tr>
<td>Depreciation for the year</td>
</tr>
<tr>
<td>Unabsorbed depreciation of earlier assessment years – eligible for deduction <strong>(Note 1)</strong></td>
</tr>
</tbody>
</table>

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INCOME FROM OTHER SOURCES

<table>
<thead>
<tr>
<th>(B)</th>
<th>Interest on Deposits</th>
<th>1,48,000</th>
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<tbody>
<tr>
<td>Less:</td>
<td>Expenses allowable under section 57(i)</td>
<td></td>
</tr>
<tr>
<td>Brokerage</td>
<td>₹ 2,000</td>
<td></td>
</tr>
<tr>
<td>Interest on hundi loans (Note 2)</td>
<td>₹ 50,000</td>
<td>52,000</td>
</tr>
<tr>
<td>Total Income</td>
<td></td>
<td>1,96,000</td>
</tr>
</tbody>
</table>

Note:

1. Unabsorbed depreciation of ₹ 2,75,000 pertains to earlier assessment years. The unabsorbed depreciation shall form part of the current year depreciation and can be set off against any other head of income. Accordingly, the amount of ₹ 2,75,000 is adjustable / allowed to be set off against 'Income from other sources'.

2. Since deposits are made by investing amount received on hundi and other loans, the interest on hundi and other loans would be eligible for deduction from the income arising on such deposits.

3. Interest paid to non-resident is not eligible for deduction as the tax has not been deducted at source.

Question 5

In July 2017, Mr. Pervez employed as Marketing Manager in a Pharma company, received a Maruti car as gift from a distributor of the company. The value of the gifted car is estimated at ₹ 2,60,000. Is the value of car taxable as income? If so, under what head it is taxable?

Answer

Mr. Pervez, an employee of a Pharma company, has received a car as a gift from a distributor of the company. Since there is no employer-employee relationship in this case between the distributor and Mr. Pervez, the value of gift is not a perquisite chargeable to tax under the head “Salaries”.

Section 56(2)(x), brings within its scope the value of any property received by any person. For this purpose, “property” means immovable property being land or building or both, shares and securities, jewellery, archaeological collections, drawings, paintings, sculptures, any work of art or bullion.

Therefore, for the purpose of attracting the provisions of section 56(2)(x) for chargeability under the head “Income from Other Sources”, an individual should be in receipt of property as defined therein. Since, car is not included in the definition of “property”, the provisions of section 56(2)(x) would not be attracted in the hands of Mr. Pervez.
1. **What are the tests for determining “substantial part of business” of lending company for the purpose of application of exclusion provision under section 2(22)?**

**CIT v. Parle Plastics Ltd.** (2011) 332 ITR 63 (Bom.)

**High Court’s Observations:** Under section 2(22), “dividend” does not include, *inter alia*, any advance or loan made to a shareholder by a company in the ordinary course of its business, where the lending of money is a substantial part of the business of the company. The expression used in the exclusion provision of section 2(22) is "substantial part of the business". Sometimes a portion which contributes a substantial part of the turnover, though it contributes a relatively small portion of the profit, would be termed as a substantial part of the business. Similarly, a portion which is relatively small as compared to the total turnover, but generates a large portion, say, more than 50% of the total profit of the company would also be a substantial part of its business. Percentage of turnover in relation to the whole as also the percentage of the profit in relation to the whole and sometimes even percentage of manpower used for a particular part of the business in relation to the total manpower or work force of the company would be required to be taken into consideration for determining the substantial part of business. The capital employed for a specific division of a company in comparison to total capital employed would also be relevant to determine whether the part of the business constitutes a substantial part.

In this case, 42% of the total assets of the lending company were deployed by it by way of loans and advances. Further, if the income earned by way of interest is excluded, the other business had resulted in a net loss. These factors were considered in concluding that lending of money was a substantial part of the business of the company.

**High Court’s Decision:** Since lending of money was a substantial part of the business of the lending company, the money given by it by way of advance or loan to the assessee could not be regarded as a dividend, as it had to be excluded from the definition of "dividend" by virtue of the specific exclusion in section 2(22).

2. **Can repair and renovation expenses incurred by a company in respect of premises leased out by a shareholder having substantial interest in the company, be treated as deemed dividend?**

**CIT v. Vir Vikram Vaid** (2014) 367 ITR 365 (Bom)

**Facts of the case:** The assessee holds more than 75% of equity shares in a company and is the executive director of the company. In his personal capacity, he is the owner of certain premises in which he was carrying on a proprietary business. Subsequently, the assessee ceased to carry on the business of proprietary concern and hence, let out the premises to the company. The company incurred ₹ 2.51 crores towards construction and improvement of factory premises, which it continued to use otherwise than as the owner of the premises. The Assessing Officer held that the amounts spent by the company towards repair and renovation
is taxable as deemed dividend in the hands of the assessee. In the alternative, the said amount was to be treated as a perquisite taxable in the hands of the assessee.

**Appellate Authorities’ Views:** The Commissioner (Appeals) noted the assessee’s submission that he had leased out the said premises for a rent lower than the prevailing market rate with an understanding that all expenditure for its upkeep and maintenance would be spent by the company on account of the assessee having stopped business activities. According to the Commissioner (Appeals), the assessee failed to substantiate his claim. The Commissioner (Appeals) was of the view that all the conditions provided under section 2(22)(e) for deemed dividend were satisfied. On the other hand, the Tribunal concluded that the payment was neither a deemed dividend nor a perquisite chargeable to tax.

**High Court’s Observations:** The challenge before the High Court by the Revenue was only with regard to applicability of section 2(22)(e) in this case. The High Court observed that no money had been paid by way of advance or loan to the shareholder who has substantial interest in the company. Further, the amount spent was towards repairs and renovation of the premises owned by the assessee but occupied by the company as lessee. There is no dispute that the company had taken on rent the aforesaid premises.

The High Court observed that the expenditure incurred by virtue of repairs and renovation on the premises cannot be brought within the definition of advance or loan given to the shareholder having substantial interest in the company, though he is the owner of the premises. It cannot be treated as payment by the company on behalf of the shareholder or for the individual benefit of such shareholder. If held in such manner, it is a mere assumption not tenable in law.

**High Court’s Decision:** The High Court, accordingly, held that the repair and renovation expenses in respect of premises occupied by the company cannot be treated as deemed dividend in the hands of shareholder being the owner of the building.

3. **Can the loan or advance given to a shareholder by the company, in return for an advantage conferred on the company by the shareholder, be deemed as dividend under section 2(22)(e) in the hands of the shareholder?**

**Pradip Kumar Malhotra v. CIT (2011) 338 ITR 538 (Cal.)**

**Facts of the case:** In the present case, the assessee, a shareholder holding substantial voting power in the company, permitted his property to be mortgaged to the bank for enabling the company to take the benefit of loan. The shareholder requested the company to release the property from the mortgage. On failing to do so and for retaining the benefit of loan availed from bank, the company gave advance to the assessee, which was authorized by a resolution passed by its Board of Directors.

**Issue:** The issue under consideration is whether the advance given by the company to the assessee-shareholder by way of security deposit for keeping his property as mortgage on behalf of company to reap the benefit of loan, can be treated as deemed dividend within the meaning of section 2(22)(e).
High Court’s Observations: In the above case, the Calcutta High Court observed that, the phrase “by way of advance or loan” appearing in section 2(22)(e) must be construed to mean those advances or loans which a shareholder enjoys simply on account of being a person who is the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) holding not less than 10% of the voting power. In case such loan or advance is given to such shareholder as a consequence of any further consideration which is beneficial to the company received from such a shareholder, such advance or loan cannot be said to be deemed dividend within the meaning of the Act. Thus, gratuitous loan or advance given by a company to a shareholder, who is the beneficial owner of shares holding not less than 10% of the voting power, would come within the purview of section 2(22)(e) but not to the cases where the loan or advance is given in return to an advantage conferred upon the company by such shareholder.

High Court’s Decision: In the present case, the advance given to the assessee by the company was not in the nature of a gratuitous advance; instead it was given to protect the interest of the company. Therefore, the said advance cannot be treated as deemed dividend in the hands of the shareholder under section 2(22)(e).

4. Would the provisions of deemed dividend under section 2(22)(e) be attracted in respect of financial transactions entered into in the normal course of business?

CIT v. Ambassador Travels (P) Ltd. (2009) 318 ITR 376 (Del.)

Under section 2(22)(e), loans and advances made out of accumulated profits of a company in which public are not substantially interested to a beneficial owner of shares holding not less than 10% of the voting power or to a concern in which such shareholder has substantial interest is deemed as dividend. However, this provision would not apply in the case of advance made in the course of the assessee’s business as a trading transaction.

The assessee, a travel agency, has regular business dealings with two concerns in the tourism industry dealing with holiday resorts.

High Court’s Observations & Decision: The High Court observed that the assessee was involved in booking of resorts for the customers of these companies and entered into normal business transactions as a part of its day-to-day business activities.

The High Court, therefore, held that such financial transactions cannot under any circumstances be treated as loans or advances received by the assessee from these concerns for the purpose of application of section 2(22)(e).

5. Can winnings of prize money on unsold lottery tickets held by the distributor of lottery tickets be assessed as business income and be subject to normal rates of tax instead of the rates prescribed under section 115BB?

CIT v. Manjoo and Co. (2011) 335 ITR 527 (Kerala)

High Court’s Observations: On the above issue, the Kerala High Court observed that winnings from lottery is included in the definition of income by virtue of section 2(24)(ix).
Further, in practice, all prizes from unsold tickets of the lotteries shall be the property of the organising agent. Similarly, all unclaimed prizes shall also be the property of the organising agent and shall be refunded to the organising agent.

The High Court contended that the receipt of winnings from lottery by the distributor was not on account of any physical or intellectual effort made by him and therefore cannot be said to be "income earned" by him in business. The said view was taken on the basis that the unsold lottery tickets cease to be stock-in-trade of the distributor because, after the draw, those tickets are unsaleable and have no value except waste paper value and the distributor will get nothing on sale of the same except any prize winning ticket if held by him, which, if produced will entitle him for the prize money. Hence, the receipt of the prize money is not in his capacity as a lottery distributor but as a holder of the lottery ticket which won the prize. The Lottery Department also does not treat it as business income received by the distributor but instead treats it as prize money paid on which tax is deducted at source.

Further, winnings from lotteries are assessable under the special provisions of section 115BB, irrespective of the head under which such income falls. Therefore, even if the argument of the assessee is accepted and the winnings from lottery is taken to be received by him in the course of his business and as such assessable as business income, the specific provision contained in section 115BB, namely, the special rate of tax i.e. 30% would apply.

**High Court's Decision:** The High Court, therefore, held that the rate of 30% prescribed under section 115BB is applicable in respect of winnings from lottery received by the distributor.