



Taxing of deemed Income and how far it is justified

Narayan Jain, LL.M., *Advocate*

1. Introduction

It was way back in 1961, when the Income Tax Act was enacted, the Government first deemed it fit to presume or deem certain transactions as income, profit or gains in the hands of the assessee. The government "deems" it fit to see income even where there may be not be really any income. The menace has been growing over the years. Even on a search in the website of Income tax department we find more than 100 sections dealing with deemed income and the ambit is being enlarged every year. Income is defined under Section 2(24) of the Income Tax Act which is an inclusive definition of income. This means that the Act specifically defines certain nature of receipts which are regarded as income of the assessee and there could be certain other nature of receipts which, though may or may not be in the nature of income, may also be regarded as or deemed as the income of the assessee.

2. Notional Income or Deemed Income

One of the basic concepts of taxation is that a person can be taxed in respect of his real income, and not in respect of notional income that one could possibly have earned. The purpose of income tax is to levy a tax on a person's income. The whole objective is to tax what a person earns. Unfortunately, our tax laws contain numerous provisions for taxation of notional income, which are not in consonance with the basic concept of taxing real income.

Some of the provisions of deemed income are measures to prevent tax avoidance. For instance, the provision deeming the stamp duty valuation to be the sale consideration of the property for the purposes of computation of capital gains on sale of an immovable property is to check the practice of receipt of sale consideration for properties partly in black money. Such measures are, therefore, justifiable considering the purpose for which they have been enacted. There are certain receipts which are not real income but with the deeming fiction in the Act, are regarded as income and these kinds of income too are subject to income tax. Therefore, it is extremely important to understand the provisions of deemed income. Let us examine a few of them in this article.

3. Section 2(22)(e): deemed dividend

If a Company (which is not a company in which public are substantially interested) makes any payment by way of loan or advance to a shareholder, who holds not less than 10% of the voting power in the company, such receipt will be deemed to be dividend income in hands of the receiving shareholder. This section also covers instances where, if such company gives loans or advance to any concern in which such shareholder is a member/partner beneficially holding at least 20% of its income, such receipt will also be deemed to be dividend income for the receiving shareholder. However, the amount of such deemed dividend will be restricted to the accumulated profits in the company. Thus,

if a Pvt. Ltd. Company gives a temporary loan to one of its shareholders (say Mr. A) holding more than 10% of voting power, the said amount will be deemed as dividend income in the hands of Mr. A. Further, if a Pvt. Ltd. Company gives temporary loan to another company in which Mr. A owns more than 20% shares, the amount shall also be deemed as dividend income in the hands of Mr. A. Therefore, even if such shareholder has received temporary money from the company which he has returned to the company after a certain period of time, the receipt will be deemed to be his dividend and he will be required to pay tax on such 'deemed income'.

4. Section 7 : Incomes to be deemed to be received in the previous year

As per sec. 7 these include-(a) the annual accretion to the balance (or Interest) at the credit of employee participating in recognised provident fund account to the prescribed extent as per Rule 6A of Part A of Fourth schedule (b) Transferred balance in a recognised provident fund to the prescribed extent as per Rule 11(4) of Part A of Fourth schedule generally in case of reorganisation of unrecognised provident fund; (c) Contribution made by the Central Government or any other employer to the account of the employee under a pension scheme referred to in section 80CCD.

5. Section 17(2): Sweet equity shares and other perquisites

Section 17(2) enumerates certain perquisites which are to be taxed in the hands of the employee. Section 17(2)(vi) provides to tax as income the value of any specified security or sweet equity shares allotted or transferred directly or indirectly, by the employer, free of cost or at the concessional rate to the assessee. (It will be taxed as per relevant rules)

6. Section 23(4) and 23(5) : House or Flat in occupation of the owner or held as stock in trade

Section 23(2) provides that where the property consists of a house or part of a house which (a) is in the occupation of the owner for the purposes of his own residence; or (b) cannot actually be occupied by the owner by reason of the fact that owing to his employment, business or profession carried on at any other place, he has to reside at that other place in a building not belonging to him, **the annual value of such house or part of the house shall be taken to be nil.**

Section 23(4) provides deeming Where the property referred to in sub-section (2) consists of more than two houses (w.e.f. asst year 2010-21) —

- (a) the provisions of that Sec. 23(2) shall apply only in respect of 2 of such houses, which the assessee may, at his option, specify in this behalf;
- (b) the annual value of the house or houses, *other than the 2 houses* in respect of which the assessee has exercised an option under clause (a), shall be determined under sub-section (1) **as if such house or houses had been let.**

Section 23 (5) provides that where the property consisting of any building or land appurtenant thereto is held as stock-in-trade and the property or any part of the property is not let during the whole or any part of the previous year, the annual value of such property or part of the property, for the period up to 2 years (w.e.f. asst year 2010-21) from the end of the financial year in which the certificate of completion of construction of the property is obtained from the competent authority, shall be taken to be *nil*. **This means that after the end of the said period of 2 years from the end of financial year in which the certificate of completion of construction of the property is obtained, the**

income will be deemed from such property held as stock in trade.

under Head Income from Other Sources in current Financial Year.

7. Deeming provisions of Section 41 and Sec. 59

The caption of section 41(1) is 'Profits Chargeable to tax'. The section falls under Chapter IV – Computation of Income from Business or Profession. In business there are circumstances where a person might have incurred a liability but later on he need not have to pay it for one or other reason. The Income Tax Act brings to tax such liabilities which are no more payable. Section 41(1) brings in to its ambit benefit in cash or in kind obtained by a person by remission or cessation of liability. The only condition is that the person must have obtained a deduction or allowance in his computation of income for the said liability in any previous years. A person may write back liability in his books of accounts unilaterally, i.e. without consent of the payee or many a times a liability remains in existence continuously over reasonably long time and the payee does not write it back in his books of account then also section 41(1) comes into operation and benefit is brought back to taxation by income tax department.

Section 59: Provisions of section 59 are akin to provisions of section 41. It provides that the provisions of section 41(1) shall apply, so far as may be, in computing the income of an assessee under section 56, as they apply in computing the income of an assessee under the head "Profits and gains of business or profession". As per Sec 59 where Assessee had claimed any deduction or allowance in any previous years but later on he has received any amount of such allowances or Deduction in current financial year then such allowances shall be deemed to be Income of current financial year under Head Income from Other Sources. Where Assessee had incurred any liability in past but successor of Assessee get remission of such liability than such remission shall be deemed to be Income of Successor

8. Section 43CA – Deemed sale consideration on Transfer of Immovable Property by developers/ promoters

Section 43CA, inserted by the Finance Act, 2013, applicable from FY 2013-14, provides that the profits on transfer of immovable property (land or building or both) held as stock-in-trade shall be computed on the basis of the stamp duty value adopted or assessed or assessable by any authority of a State Government for the purpose of payment of stamp duty. It is in line with Section 50C which is applicable for immovable property held in the nature of "capital asset" (discussed hereinafter). It has several complications for real estate developers following the percentage completion method. Section 43CA is applicable to all categories of assessee who deal in immovable property, as their business, being land or building or both. Thus, the provision of this section is applicable to Individual, Firm, HUF, Company or any other category of assessee. Further the section is applicable to all kind of immovable properties being Land or Building or both, held as stock in trade. It may be a commercial unit/ space/ shop/ flat, residential flat or plot, industrial building or plot, or agricultural land whether in rural or urban area etc. It is also applicable in case of transfer of ownership of immovable property even without registration of sale deed but by way of execution of sale agreement / Power of Attorney or by way of transfer with the regulatory authority or in any other manner. Section 43CA(3) further provides to adopt stamp duty value of the property assessable as on the date of entering into sale agreement instead of the value assessed as on the date of transfer of the property, where the date of agreement fixing the value of consideration for transfer of the asset and the date of registration of such transfer of asset are not the same.

Section 43CA(4) provides that stamp duty value of the property assessable as on the date of entering into sale agreement may be taken in a case where the amount of consideration or a part thereof has been received by any mode other than cash on or before the date of agreement for transfer of the asset.

Safe Harbour Rule : As per amendment made by the Finance Act, 2020, w.e.f. asst. year 2021-22 the difference between actual consideration and stamp duty valuation or fair market value to the extent of 10% shall be ignored for the purpose of computing income under section 43CA as well as section 50C. (Earlier for asst year 2019-20 and 2020-21 the permitted difference was upto 5 per cent).

In order to boost demand in the real-estate sector and giving benefit to the home buyers, Finance Ministry further increased the safe harbour from 10% to 20% under section 43CA for the period from 12th November, 2020 to 30th June, 2021 in respect of only primary sale of residential units of value up to Rs. 2 crore. Consequential relief by increasing the safe harbour from 10% to 20% has also been allowed to buyers of these residential units under section 56(2)(x) of the Act for the said period. Therefore, for these transactions, circle rate shall be deemed as sale/purchase consideration only if the variation between the agreement value and the circle rate is more than 20%. However it may be noted that the said concession of 20% does not apply under section 50C. The Government should consider extending the date for such concession for sale of flats etc. till 31st March, 2022 and it should be allowed to apply for promoters as well as others.

In view of the continued pandemic, it is suggested that the date for safe harbour should be extended till at least 31st March, 2022 and should be applied even for the purpose of section 50C.

9. Section 50C – Deemed sale consideration on Transfer of Immovable Property

Section 50C was introduced by Finance Act, 2002 w.e.f 1.4.2003 which prescribes provisions of deemed income in the case of transfer of land or building or both held in the nature of “capital asset”. Where an assessee transfers/sells an **Immovable Property (land or building or both)** as his capital asset and the sale proceeds received or accrued as a result of such transfer is less than the "stamp duty value" of the property, adopted/ assessed or assessable by the stamp duty valuation authority of State Government, then the stamp duty value of the IP adopted/ assessed or assessable will be deemed to be the full value of consideration received on transfer of such **Immovable Property**. It has however been stated in 3rd proviso to sec. 50C with effect from assessment year 2021-22 that if the stamp duty value is more only upto 10% of the sale consideration then the deeming fiction will not apply. The limit was only 5% for asst year 2019-20 and 2020-21.

The assessee has an option to dispute/appeal the value adopted by the stamp valuation authority before the appellate authority or apply to the Assessing Officer to refer the valuation of the property to a Valuation Officer. Accordingly, the value derived at by the appellate authority or the departmental valuation officer (DVO), as the case may be, will be considered as the final sale consideration for this transaction.

10. Section 50B(2)(ii): Slump Sale

The government has brought in amendment to Section 50B(2) to discourage tax avoidance schemes in case of slump sale. Section 50B(2) as amended by the Finance Act, 2021 with effect retrospectively w.e.f. asst year 2020-21, provides in relation to capital assets being an undertaking or division transferred by way of such slump sale-

- (i) The net worth of the undertaking or the division as the case may be, shall be

deemed to be the cost of acquisition and the cost of improvement for the purpose of section 48 and 49 and no regard shall be given to the provisions contained in the second proviso to sec. 48.

- (ii) Fair market value of the capital assets as on the date of transfer, calculated in the prescribed manner, shall be deemed to be the full value of consideration received or accruing as a result of transfer of such capital asset.

Sub section 3 provides that every assessee in the case of slump sale shall furnish a report in the prescribed form i.e. Form No. 3CEA from a Chartered Accountant before the specified date referred to in section 44AB indicating the computation of net worth of the undertaking or the division, as the case may be, and certifying that the net worth of the undertaking or the division has been correctly taken in accordance with provisions of section 50B.

In a situation where the sale consideration of the asset being transferred is lower than the deemed fair value so determined, then for the purpose of computing capital gains, the actual sale consideration is replaced by such deemed fair value. Till financial year 2019-20, for the purpose of business transfer pursuant to a slump sale, the tax law did not provide for any deemed fair valuation mechanism and thus, predominantly sale value disclosed by the seller would be the considered for computing capital gain tax.

Rule 11UAE for Computation of Fair Market Value of Capital Assets for the purposes of section 50B : CBDT vide Notification No.68/2021 dated 24/05/2021 notified Rule 11UAE of the Income Tax Rules, 1962 to compute the Fair Market Value (FMV) of Capital Assets for the purposes of section 50B of the Income-tax Act, 1961 for the purpose of computing the capital gains in case of an exchange of assets in a slump sale. For the purpose of clause (ii) of sub-section (2) of section 50B, the fair market value of the capital assets shall be the FMV1 determined

under sub-rule (2) or FMV2 determined under sub-rule (3), whichever is higher.

11. Section 56(2)(viib) – Issue of shares by Company – deemed income

When a Company (in which public are not substantially interested) receives any consideration, from a resident, for issue of shares exceeding the fair market value (FMV) of the share(s), the excess amount so received will be regarded as income of the company. The Company can arrive at the FMV of the shares of the company by calculating the same at Networth or Book value of the company. If the shares are issued at a price which is higher than the Net worth of the company, the same needs to be justified and supported by a valuation report as valued and certified by a certified valuer. The method of valuation is prescribed under Rule 11UA of the Income Tax Rules. In such cases, the company has actually received money against issue of its own shares at a premium, which essentially is a 'Capital Account transaction'. The company does not earn any income when it issues share at a premium. However, by virtue of deeming fiction, the premium which is received in excess of the FMV of the shares of the company so determined will be deemed to be income of the company and tax will be payable on the same by the company. Therefore, it is important for the company to get their shares valued from a registered valuer whenever it issues share at a premium, higher than the FMV of the shares. It may be noted that this deeming fiction does not apply when the shares are issued to a non-resident.

12. Section 56(2)(ix) – Forfeiture of advance money on failed negotiation

If an assessee has received any sum of money during the course of negotiation for transfer of a capital asset, which is in the nature of advance and if the negotiation does not result into a deal of transfer of the capital asset and if the

assessee forfeits the advance money so received, the money so received will be deemed to be the income of the assessee. Earlier, this advance receipt would go on to reduce the cost of the capital asset but now the section is amended to state that the advance so received and forfeited will be regarded as the income of the assessee.

13. Section 56(2)(x)

Section 56(2)(x), has come into effect from asst. year 2017-18 (in place of Section 56(2)(vii). It provides that receipt of the sum of money or the property received by a person without any consideration or upon crossing a particular threshold would be liable to tax in the hands of the receiver under the head 'Income from other sources'. The taxation on gifts received by an Individual/ HUF is also governed by the provisions of clause (x) in Section 56(2) of the Income Tax Act.

Under the erstwhile provision of section 56(2)(vii), any sum of money or any property received without any consideration by any Individual or HUF was chargeable to income tax. Section 56(2)(viiia), applicable upto asst year 2017-18, was applicable only to the Firm and Closely held company. Whereas, sec. 56(2)(x) is applicable to all kinds of the assessees.

The following receipts are to be taxed as deemed income:

- a) Any sum of money that is received without consideration, in aggregate exceeding Rs.50,000 during the financial year
- b) Any immovable property without any consideration, the stamp duty value of which exceeds Rs.50,000
- c) Any immovable property with the consideration which is less than stamp duty value by an amount exceeding Rs.50,000
- d) Any movable property (as defined and specified) without consideration where

aggregate fair market value whereof exceeds Rs.50,000

- e) Any movable property (as defined and specified) for consideration which is less than fair market value by an amount exceeding Rs.50,000

Exceptions to Section 56(2)(x): Provision of section 56(2)(x) would not apply to any sum of money or any property received from any relative. Meaning of Relative as defined in section 56(2)(vii). **Provisions of 56(2)(x) would also not be applicable to any sum of money or any property that is received from a relative as defined above and also under the following circumstances:**

- a) On the occasion of an individual's marriage
- b) By a will or by way of inheritance
- c) In the contemplation of death of the payer or donor, as the case may be;
- d) From any local authority that as defined in the Explanation to clause (20) of section 10
- e) From any fund/ foundation/ other educational institution/ university/ hospital/ other medical institution/ any trust or institution referred to in under section 10(23C)
- f) From or by any trust or institution that is registered under section 12A or section 12AA or section 12AB
- g) By any trust or fund or any institution or university or other educational institution or hospital or any other medical institution referred to in sub-clause (iv)/ (v)/ (vi) or sub-clause (vii) of section 10(23C)
- h) by way of transaction not regarded as transfer under clause (i)/(iv)/ (v)/ (vi)/ (vii) / (viii)/ (ix)/ (x)/ (xi)/ (xii)/ (xiii)/ (xiv)/ (xv)/ (xvi)/ (xvii)/ (xviii)/ (xix)/ (xx)/ (xxi)/ (xxii)/ (xxiii)/ (xxiv)/ (xxv)/ (xxvi)/ (xxvii)/ (xxviii)/ (xxix)/ (xxx) of section 47;

- i) From any individual by a trust created or established solely for the benefit of relative of the individual.
- j) from such class of persons and subject to such conditions as may be prescribed.

14. Sec. 56(2)(x)(c): Transfer of property other than Immovable Property

Where an assessee transfers Shares (other than shares quoted on recognised stock exchange), for a consideration which is less than Fair Market Value (FMV) of the share, such FMV shall be deemed to be full value of consideration received as a result of such transfer. The FMV of the shares shall be determined in accordance with Rule 11UA of the Income Tax Rules. The FMV in normal circumstances be calculated at "Net Worth" or "book value" of the company. Again, in such a case, a shareholder is required to pay tax on the amount which he has neither actually received nor is he going to receive in future but on the amount which he is deemed to have received based on certain valuation principals.

15. Sections 68 to 69D

Sections 68 to 69D are also provisions of deemed income and deal with Tax Treatment of Cash Credit, Unexplained investments, Unexplained money, Amount of investments not fully disclosed in books of account, Unexplained expenditure and Amount borrowed or repaid on hundi in cash under **section 68, Section 69, Section 69A, Section 69B, Section 69C and Section 69D** respectively. As per section 68, any sum found credited in the books of a taxpayer, for which he offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, may be charged to income-tax as the income of the taxpayer of that year. In case of a taxpayer being a closely held company (i.e., not being a company in which the public are substantially interested), if the sum so credited consists of share application money, share capital, share premium or any such

amount by whatever name called, any explanation offered by such company shall be deemed to be not satisfactory if prescribed conditions are not fulfilled.

Section 68 -As per section 68, any sum found credited in the books of a taxpayer, for which he offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, may be charged to income-tax as the income of the taxpayer of that year. In case of a taxpayer being a closely held company (i.e., not being a company in which the public are substantially interested), if the sum so credited consists of share application money, share capital, share premium or any such amount by whatever name called, any explanation offered by such company shall be deemed to be not satisfactory if prescribed conditions are not fulfilled.

In case of a taxpayer being a closely held company (i.e., not being a company in which the public are substantially interested), if the sum so credited consists of share application money, share capital, share premium or any such amount by whatever name called, any explanation offered by such company shall be deemed to be not satisfactory, unless:

- (a) the person, being a resident in whose name such credit is recorded in the books of such company, also offers an explanation about the nature and source of such sum so credited; and
- (b) such explanation in the opinion of the Assessing Officer has been found to be satisfactory.

The above provisions of share application money, share capital, etc., shall not apply if the person, in whose name such sum is recorded, is a venture capital fund or a venture capital company as referred to in section 10(23FB).

Conditions to be satisfied for applicability of section 68: Following conditions can be stated to attract the applicability of section 68 : Assessee

has maintained 'books; there has to be credit of amounts in the books maintained by the taxpayer of a sum during the year and the taxpayer offers no explanation about the nature and source of such credit found in the books or the explanation offered by the taxpayer in the opinion of the Assessing Officer is not satisfactory. If all these conditions exist, sum so credited may be charged to tax as income of the taxpayer of that year. Provisions applicable in case of closely held company have already been discussed above.

Sec. 69 Unexplained investments : Where in a year the taxpayer has made investments which are not recorded in the books of account, if any, maintained by him for any source of income, and he offers no explanation about the nature and source of the investments or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, then the value of the investments may be deemed to be the income of the taxpayer of such year.

Sec. 69A Unexplained money, etc.: Where in any year the taxpayer is found to be the owner of any money, bullion, jewellery or other valuable article and such money, bullion, jewellery or valuable article is not recorded in the books of account, if any, maintained by him for any source of income, and the taxpayer offers no explanation about the nature and source of acquisition of the money, bullion, jewellery or other valuable article, or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, then the money and the value of the bullion, jewellery or other valuable article may be deemed to be the income of the taxpayer for such year.

Sec. 69B Amount of investments, etc., not fully disclosed in books of account: Where in any year the taxpayer has made investments or is found to be the owner of any bullion, jewellery or other valuable article, and the Assessing Officer finds that the amount expended on making such investments or in acquiring such bullion, jewellery or other valuable article exceeds the amount recorded in this behalf in the books of account maintained by the taxpayer for any

source of income, and the taxpayer offers no explanation about such excess amount or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, then the excess amount may be deemed to be the income of the taxpayer for such year.

Sec. 69C Unexplained expenditure, etc.: Where in any year the taxpayer has incurred any expenditure and he offers no explanation about the source of such expenditure or part thereof, or the explanation, if any, offered by him is not, in the opinion of the Assessing Officer, satisfactory, then the amount covered by such expenditure or part thereof, as the case may be, may be deemed to be the income of the taxpayer for such year. It may be noted that the aforesaid unexplained expenditure which is deemed to be the income of the taxpayer by virtue of section 69C shall not be allowed as a deduction under any head of income.

Sec. 69D Amount borrowed or repaid on hundi: Where any amount is borrowed on a hundi from, or any amount due thereon is repaid to, any person otherwise than through an account-payee cheque drawn on a bank, the amount so borrowed or repaid shall be deemed to be the income of the person borrowing or repaying the such amount. It will be treated as income for the year in which it was borrowed or repaid, as the case may be. However, it should be noted that if any amount borrowed on a hundi has been treated as income of any person by virtue of section 69D, then such person shall not be liable to be assessed again in respect of the same amount on repayment thereof. Amount repaid shall include the amount of interest paid on the amount borrowed.

16. Section 115BBE: Tax rates applicable to amount charged to tax by virtue of sections 68, 69, 69A, 69B, 69C and 69D

As per Section 115BBE, income tax shall be calculated at 60% where the total income of assessee includes following income:

- a) Income referred to in Section 68, Section 69, Section 69A, Section 69B, Section 69C or Section 69D and reflected in the return of income furnished under Section 139; or
- b) Which is determined by the Assessing Officer and includes any income referred to in Section 68, Section 69, Section 69A, Section 69B, Section 69C or Section 69D, if such income is not covered under clause (a).

Such tax rate of 60% will be further increased by 25% surcharge, 4% Education Cess i.e., the final tax rate now comes out to be 78% (including cess). Provided that 6% (10 per cent of tax of 60 per cent) penalty under section 271AAC may be imposed if the addition is made by the A.O.. However as per sec. 271AAC(2), it shall not be levied when the income under Section 68, 69, etc., has been included in return of income and tax has been paid on or before the end of relevant previous year.

No deduction in respect of any expenditure or allowance [or set off of any loss] shall be allowed to the assessee in computing his income referred to in clause (a) of sub-section (1) of Section 115BBE.

17. Several other provisions for deemed income

In addition to above there are many other provisions in Income tax Act which include Income deemed to be received or accrued as incorporated in the scope of Income in Section 5; income deemed to accrue or arise in India (Sec. 9) determination of Arm's Length Price (ALP) for transfer of goods, services and technology between Associated enterprises in International transactions (contained in Chapter X of Income Tax Act), Specified domestic transactions in section 92BA where the transactions are generally between related parties and aggregate of such transactions entered into by the assessee in the previous year exceeds Rs.50 crore; GAAR (Se. 95 to 102), MAT under sec. 115JB, AMT under sec. 115JC as well as other provisions. Section 292C

provides for Presumptions as to assets, books of account found in course of search under sec. 132 and survey under sec. 133A.

18. Taxation of Real Income

In landmark case of *Poona Electric Supply Co. Ltd v. Commissioner Of Income-Tax*, [1965] 57 ITR 521(SC) : 1965 SCR (3) 818, the Supreme Court held that Income-tax is a tax on the real income. It was observed: "As a business concern the real profit of the appellant had to be ascertained on the principles of commercial accountancy. As a licensee governed by the statute its "clear profit" was ascertained in terms of the statute and the schedule annexed thereto. The two profits are for different purposes-one for commercial and tax purposes and the other for statutory purposes in order to maintain a reasonable level of rates. The amounts for which deduction was claimed were a part of the excess amount paid to the assessee and reserved to be returned to the consumers. They did not form part of the assessee's real profits, and therefore, to arrive at the taxable income of the assessee from the business, under s. 10(1) of the Income-tax Act, 1922 the said amounts had to be deducted from its total income. The income tax is a tax on the real income, that is the real profits arrived at on commercial principles subject to the provisions of the Income-tax Act. The real profit can be ascertained only by making the permissible deductions. There is a clear cut distinction between deductions made for ascertaining the profits and distributions made out of profits. It is a question of fact to be found on the relevant circumstances, having regard to business principles. Another distinction that should be borne in mind is that between the real and the statutory profits, that is between the commercial profits and statutory profits. The latter are statutorily fixed for a specified purpose. The real profit of a businessman under s. 10(1) of the Income tax Act, 1922 cannot, obviously include the amounts returned by him by way of rebate to the consumers, under statutory compulsion, from the statutory profits.

Other relevant decisions / decision followed and cited in many cases including the following:

- a) *Raja Bejoy Singh Dudhuria v. The Commissioner Of Income-Tax (1933) 35 BOMLR 811*: The Bombay High Court emphasized the concept of real income in the context of payment of income tax. Lord Macmillan, speaking for the Bench said that the only 'the real income' of the taxpayer is to be taxed.
- b) *Ratilal Daftari v. CIT, [1959] 36 ITR 18 (Bom)*
- c) *Murlidhar Himatsingha v. CIT [1966] 62 ITR 323 (SC)*, the decision in *Ratilal Daftari* was approved and it was reiterated that for purposes of assessment, the real income of the assessee has to be reached, which remains after deducting the amount that may be said to have been diverted and that what constitutes his real income only could be assessed.
- d) *Godhra Electricity Co. Ltd. (1997) 225 ITR 746 (SC)*;
- e) *CIT v. Sujata v. Manohar and G.B. Pattanaik (1999) 236 ITR 315 (SC)*;
- f) *Acit, Central Circle-7, New Delhi. v. Anil Kumar Sharma, B3, Agcr Enclave, New Karkardooma, New Delhi*
- g) *H.K. Kashiparekh & Co. Ltd. v. CIT [1960] 39 ITR 706 (Trib.)*
- h) *State Bank of Travancore v. CIT, [1986] 158 ITR 102 (SC)*. The real income theory was accepted by the Apex Court.
- i) *Southern Technologies Limited v. Joint CIT, Coimbatore [2010] 320 ITR 577 (SC)*
- j) *CIT v. Shoorji Vallabhdas & Co. 46 ITR 144 (SC)*;
- k) *CIT v. Chemosyn Ltd 371 ITR 427 (Bom)*
- l) *CIT v. Chamanlal Mangaldas & Co. 39 ITR 8 (SC)*
- m) *CIT v. Chamanlal Mangaldas & Co. 29 ITR 987 (Bom)*
- n) *CIT v. Harivallabhadas Kalidas & Co. 39 ITR 1 (SC)*
- o) *CIT v. Virtual Soft Systems Ltd 404 ITR 409 (SC)*
- p) *CIT v. Lakshmi Machine Works 290 ITR 667 (SC)*
- q) *Miss Dhun Dadbhoy Kapadia v. CIT 63 ITR 651 (SC)*
- r) *CIT v. Bokaro Steel Ltd 236 ITR 315 (SC)*

19. Deeming provision has to be interpreted strictly

It is settled principle of interpretation of tax statute that a deeming provision has to be interpreted strictly in terms of the language employed. It is also a cardinal principle of interpretation of taxing statute that a deeming fiction over a deeming fiction cannot be applied.

20. Notional Income or Deemed Income should not be taxed, Real income should only be taxed

The Government should find out the ways of curbing the trend of tax avoidance. It would do well if only real income is taxed under Income Tax Act. The Courts have also held in many cases that Real income should only be taxed. Therefore growing of taxing of deemed or notional income is not justified.

(Narayan Jain is former National Vice President of AIFTP and author of the books "How to Handle Income Tax Problems" and "Income Tax Pleading & Practice" with CA Dilip Loyalka).

