CHAPTER 3

PROFITS AND GAINS OF BUSINESS OR PROFESSION



LEARNING OUTCOMES

After studying this chapter, you would be able to -

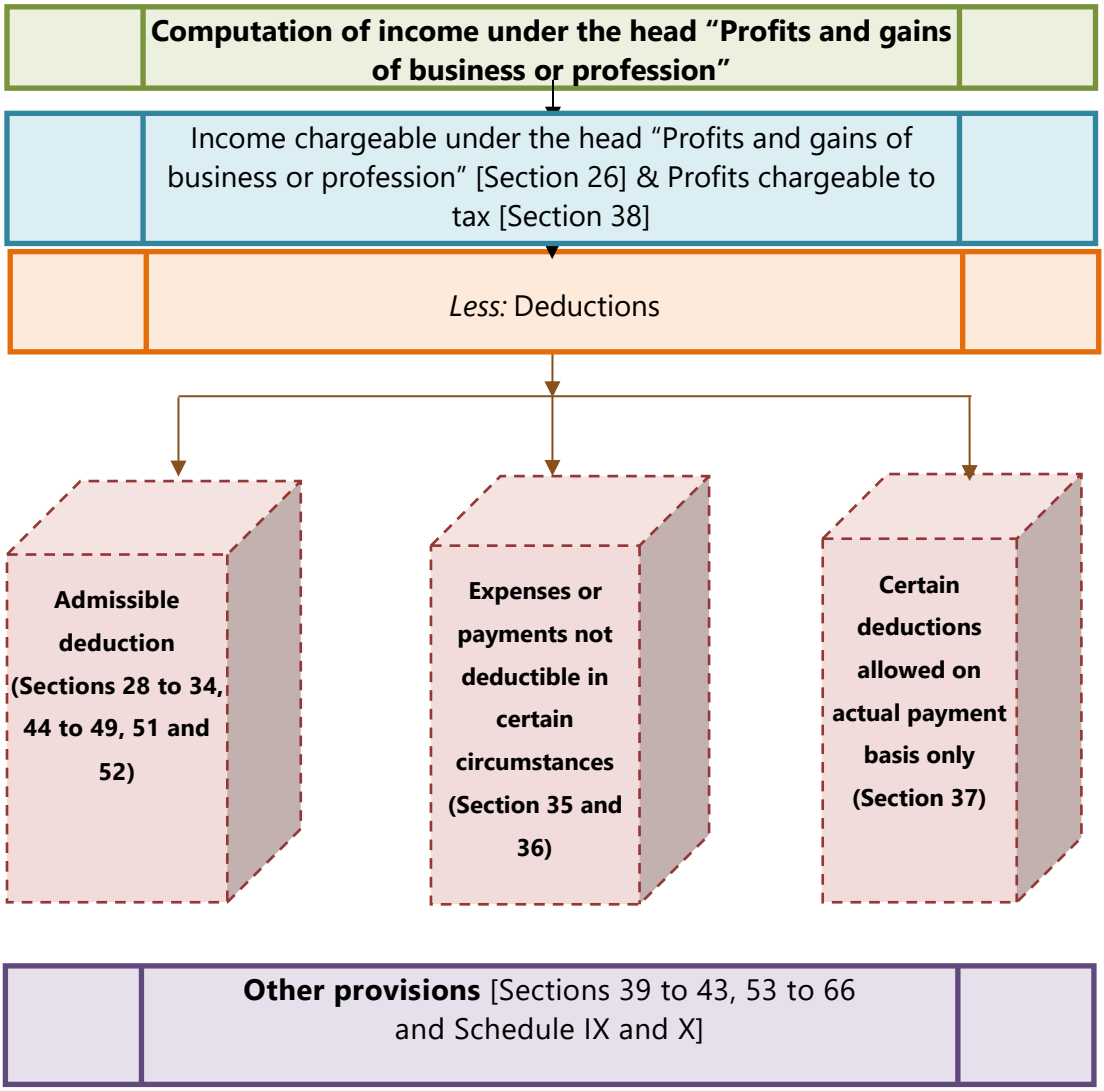
- **examine** whether a particular income would be chargeable to tax under the head "Profits and gains of business or profession" by analysing the provisions of section 26;
- **comprehend** the "Income Computation and Disclosure Standards" (ICDSs) and analyse and apply these standards to determine the income chargeable to tax under this head;
- **analyse and apply** the provisions of sections 28 to 34, 44 to 49, 51 and 52 to determine whether any particular expenditure/ payment would be admissible as deduction while computing income under this head;
- **analyse and apply** the conditions contained under sections 35 & 36 to determine whether a particular expenditure/ payment would be admissible/ inadmissible as deduction while computing income under this head;
- **analyse and apply** the provisions of section 37 to allow/ disallow expenditures specified therein, in respect of which deduction is admissible only on actual payment;
- **examine** when certain receipts are deemed as income under section 38 chargeable to tax under this head;

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- **appreciate** the provisions of section 62 relating to maintenance of books of account and identify the assessees, who are compulsorily required to maintain books of account;
- **appreciate** the provisions of section 63, listing the circumstances when an assessee is compulsorily required to get the books of account audited under Income-tax Act, 2025;
- **examine** the presumptive tax provisions contained in section 58 to determine whether an assessee engaged in a business, profession or plying, hiring or leasing goods carriages can opt for such presumptive taxation schemes;
- **compute** income under this head applying the charging and deeming provisions, allowing the permissible deductions and disallowing the impermissible deductions.

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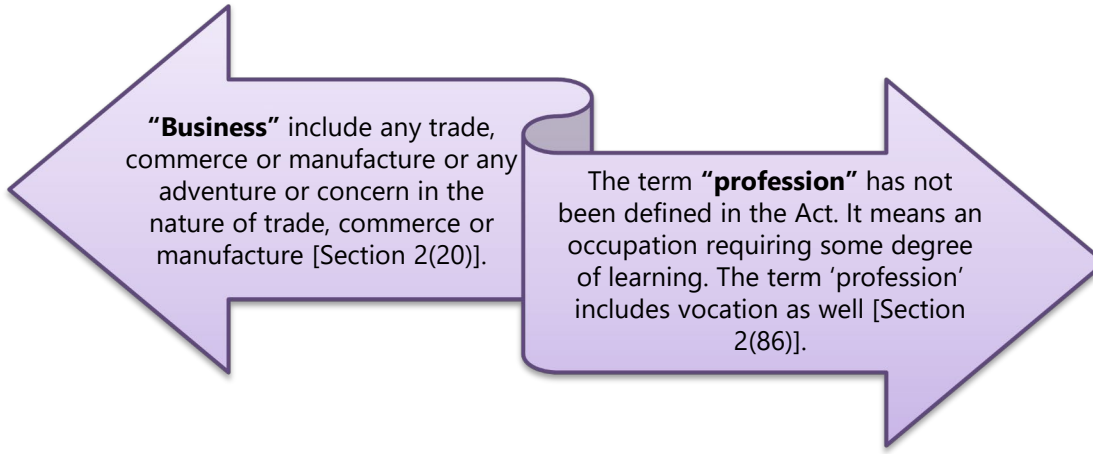
CHAPTER OVERVIEW



3.1 MEANING OF 'BUSINESS' AND 'PROFESSION'

The income chargeable to tax under this head is in respect of the profits and gains of **any business or profession**, carried on by an assessee at any time during the tax year.

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Particulars	Explanation
Examples of Profession	Painter, doctor, lawyer, architect, auditor, author, astrologer etc. are persons who can be said to be carrying on a profession and not business.
Meaning of Business	Business generally involves continuous exercise of an activity with a profit motive. Even a single trade venture may also be treated as business.
Tax treatment of business, profession and vocation	For income-tax purposes, it is generally immaterial whether a person carries on a business, profession or vocation, since profits from all are taxed under the same head "Profits and Gains of Business or Profession". However, differences exist in provisions relating to tax audit and presumptive taxation, where threshold limits and rates vary for business and profession.

Meaning of 'Profits

(1) **Profits in cash or in kind:** Profits may be realised in money or in money's worth, i.e., in cash or in kind. Where profit is realised in any form other than cash, the cash equivalent of the receipt on the date of receipt must be taken as the value of the income received in kind.

(2) **Capital receipts:** Capital receipts are not generally to be taken into account while computing profits under this head.

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(3) **Voluntary receipts:** Payment voluntarily made by persons who were under no obligation to pay anything at all would be income in the hands of the recipient, if they were received in the course of a business or by the exercise of a profession or vocation. Thus, any amount paid to a lawyer by a person who was not a client, but who has been benefited by the lawyer's professional service to another would be assessable as the lawyer's income.

(4) **Income from distinct businesses:** The profits of each distinct business must be computed separately but the tax chargeable under this section is not on the separate income of every distinct business but on the aggregate profits of all the businesses carried on by the assessee.

(5) **Computation of profits:** Profits should be computed after deducting the losses and expenses incurred for earning the income in the regular course of the business, profession, or vocation unless the loss or expenses is expressly or by necessary implication, disallowed by the Act. The charge is not on the gross receipts but on the profits and gains.

(6) **Legality of income:** The illegality of a business, profession or vocation does not exempt its profits from tax. The revenue is not concerned with the taint of illegality in the income or its source. Thus, income tax is not restricted in its application to lawful business only.

However, expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law would not be allowable as deduction while computing profits of such business.



Mr. X carries on an illegal betting business and earns a profit of ₹ 10,00,000 during the tax year. Even though the business is illegal, the income earned from such activity is still taxable under the head "Profits and Gains of Business or Profession".

3.2 METHOD OF ACCOUNTING

Section 276 of the Income-tax Act, 2025 provides for the method of accounting. Section 276(1) requires income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" to be computed as per either the cash or mercantile system of accounting

Method of accounting [Section 276]

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regularly employed by the assessee, subject to the provisions of section 276(2).

However, as per section 278, certain income would be taxable in the following manner:

(i) **Interest on compensation or enhanced compensation:** Interest received by an assessee on compensation or on enhanced compensation, shall be deemed to be the income of the tax year in which it is received. [Such income is taxable under the head "Income from other sources"]

(ii) **Claim for escalation of price in a contract or export incentives**: The claim for escalation of price in a contract or export incentives shall be deemed to be the income of the tax year in which reasonable certainty of its realisation is achieved.

(iii) **Subsidy or grant or cash incentive etc.:** Income referred to in section 2(49)(w) i.e., assistance in the form of a subsidy or grant or cash incentive or duty drawback or waiver or concession or reimbursement, by whatever name called, by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee shall be deemed to be the income of the tax year in which it is received, if not charged to income tax for any earlier tax year.

Under section 276(2), the Central Government is empowered to notify **income computation and disclosure standards (ICDSs)** to be followed by any class of assessees or in respect of any class of income. The Central Government had, vide ***Notification No. S.O.3079(E) dated 29.9.2016*****,** notified ten ICDSs in terms of section 145(2) of the Income-tax Act, 1961.

The notified ICDSs have to be followed by all assessees (other than an individual or a Hindu undivided family who is not required to get his accounts of the tax year audited in accordance with the provisions of section 63) following the mercantile system of accounting, for the purposes of computation of income chargeable to income-tax under the head "Profits and gains of business or profession" or "Income from other sources".

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The ten notified ICDSs are:

ICDS I:	Accounting Policies
ICDS II:	Valuation of Inventories
ICDS III:	Construction Contracts
ICDS IV:	Revenue Recognition
ICDS V:	Tangible Fixed Assets
ICDS VI:	The Effects of Changes in Foreign Exchange Rates
ICDS VII:	Government Grants
ICDS VIII:	Securities
ICDS IX:	Borrowing Costs
ICDS X:	Provisions, Contingent Liabilities and Contingent Assets

Cardinal features of Notified ICDSs

(1) Applicability: All the notified ICDSs are applicable for computation of income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and **not** for the purpose of maintenance of books of accounts. This is stated in the Preamble at the beginning of each ICDS.

(2) Position in case of conflict with the Income-tax Act, 2025: In the case of conflict between the provisions of the Income-tax Act, 2025 and the notified ICDSs, the provisions of the Act shall prevail to that extent. This is also stated in the Preamble at the beginning of each ICDS.

(3) Scope Paragraph: Each of the ten notified ICDSs has a scope paragraph explaining what exactly the ICDS deals with. In some standards, the scope paragraph also specifies what the ICDS does not deal with.

(4) Disclosure Requirements: All ICDSs (except ICDS VI on Effects of changes in foreign exchange rates and ICDS VIII on Securities) contain specific disclosure requirements. The last paragraph(s) of these ICDSs is on disclosure.

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Salient Features of the notified ICDSs

ICDS I: Accounting Policies

- This ICDS deals with significant accounting policies.
- While it recognizes the fundamental accounting assumptions of going concern, consistency and accrual, it does not recognize the concepts of "materiality" and "prudence" in selection of accounting policies.
- Treatment and presentation of transactions have to be governed by their substance and not merely by the legal form.
- Marked to market loss or an expected loss is not to be recognized unless recognition of such loss is in accordance with the provisions of any other ICDS.

ICDS II: Valuation of Inventories

- "Inventories" has been defined to mean assets held for –
  - sale in the ordinary course of business;
  - in the process of production for such sale;
  - in the form of materials or supplies to be consumed in the production process or in the rendering of services.
- This ICDS requires inventory to be valued at cost or net realizable value, whichever is lower.
- This ICDS requires disclosure of the accounting policies adopted in measuring inventories including the cost formulae used and the total carrying amount of inventories and its classification appropriate to a person.

ICDS III: Construction Contracts

- This ICDS is required to be applied in determination of income for a construction contract of a contractor.
- It recognizes percentage of completion method (POCM) for recognizing contract revenue and contract costs associated with a construction contract.
- However, contract revenue and contract costs associated with the construction contract, which commenced on or before 31.3.2016 but not completed by the said date, can be recognised based on the method regularly followed by the person prior to the year 2016-17.
- This ICDS also contains certain disclosure requirements, like the amount of contract revenue recognized as revenue in the period, the methods used to determine the stage of completion of contracts in progress etc.

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ICDS IV: Revenue Recognition

- This ICDS deals with the bases for recognition of revenue arising in the course of the ordinary activities of a person from –
  - the sale of goods;
  - the rendering of services;
  - the use by others of the person's resources yielding interest, royalties or dividends.
- It does not, however, deal with the aspects of revenue recognition which are dealt with by other ICDSs.
- "Revenue" is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of a person from the sale of goods, from the rendering of services, or from the use by others of the person's resources yielding interest, royalties or dividends. In an agency relationship, the revenue is the amount of commission and not the gross inflow of cash, receivables or other consideration.
- This ICDS also contains a provision wherein the revenue from sale of goods could be recognized when there is reasonable certainty of its ultimate collection.
- Revenue from service transactions is required to be recognized on the basis of percentage completion method. However, revenue can be recognised on a straight line basis over a specific period of time, when services are provided by an indeterminate number of acts over such period.
- Revenue from service contracts with duration of not more than 90 days to be recognised when the rendering of services under that contract is completed or substantially completed.
- This ICDS contains certain disclosure requirements, like the amount of revenue from service transactions recognized as revenue during the tax year, the method used to determine the stage of completion of service transactions in progress, information relating to service transactions in progress at the end of the tax year etc.

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ICDS V: Tangible Fixed Assets

- This ICDS deals with the treatment of tangible fixed assets.
- "Tangible fixed asset" is an asset being land, building, machinery, plant or furniture held with the intention of being used for the purpose of producing or providing goods or services and is not held for sale in the normal course of business.
- This ICDS provides the components of actual cost of such assets and valuation of such assets in special cases.
- The fair value of a tangible fixed asset acquired in exchange for shares or other securities or another asset shall be its actual cost.
- The ICDS also provides that depreciation on such assets and income arising on transfer of such assets shall be computed in accordance with the provisions of the Income-tax Act.
- The ICDS also contains disclosure requirements in respect of such assets, like the description of asset or block of assets, rate of depreciation, actual cost or written down value, as the case may be, additions or deductions during the year with dates, depreciation allowable and written down value at the end of the year.

ICDS VI: The Effects of changes in foreign exchange rates

- This ICDS deals with treatment of transactions in foreign currencies, translating the financial statements of foreign operations and treatment of foreign currency transactions in the nature of forward exchange contracts.
- This ICDS requires exchange differences arising on settlement of monetary items or conversion thereof at last day of the tax year to be recognized as income or as expense in that tax year.
- In respect of non-monetary items, exchange differences arising on conversion thereof as at the last day of the tax year shall not be recognized as income or as expense in that tax year.
- At the last day of each tax year, foreign currency monetary items shall be converted into reporting currency by applying the closing rate.
- Non-monetary items in a foreign currency shall be converted into reporting currency by using the exchange rate at the date of the transaction.

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- Non-monetary item being inventory which is carried at net realisable value denominated in a foreign currency shall be reported using the exchange rate that existed when such value was determined.
- The ICDS contains provisions for initial recognition, conversion at the last date of the tax year and recognition of exchange differences. These provisions shall be subject to the provisions of section 42 of the Income-tax Act, 2025 and Rule 206 of the Income-tax Rules 2026.

ICDS VII: Government Grants

- This ICDS deals with the treatment of government grants. It recognizes that government grants are sometimes called by other names such as subsidies, cash incentives, duty drawbacks etc.
- This ICDS does not deal with Government assistance other than in the form of Government grants and Government participation in the ownership of the enterprise.
- It requires recognition of Government Grants when there is a reasonable assurance that the person shall comply with the conditions attached to them and the grants shall be received. However, it also states that recognition of Government grant shall not be postponed beyond the date of actual receipt.
- This ICDS requires Government grants relatable to depreciable fixed assets to be reduced from actual cost/WDV. It further provides that where the Government grant is not directly relatable to the asset acquired, then a pro-rata reduction of the amount of grant should be made in the same proportion as such asset bears to all assets with reference to which the Government grant is so received.
- The standard requires grants relating to non-depreciable fixed assets to be recognized as income over the same period over which the cost of meeting such obligations is charged to income.
- The standard also requires Government grants receivable as compensation for expenses or losses incurred in a previous financial year or for the purpose of giving immediate financial support to the person with no further related costs to be recognized as income of the period in which it is receivable.
- All other Government Grants have to be recognized as income over the periods necessary to match them with the related costs which they are intended to compensate.

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- The standard contains certain disclosure requirements, like nature and extent of Government grants recognized during the tax year as income, nature and extent of Government grants not recognized during the tax year as income and reasons thereof etc.

ICDS VIII: Securities

- This ICDS deals with securities.
- There are two parts. Part A deals with securities held as stock-in-trade. Part B deals with securities held by a scheduled bank or public financial institutions formed under a Central or a State Act or so declared under the Companies Act, 1956 or the Companies Act, 2013.
- It requires securities (referred to in Part A) to be recognized at actual cost on acquisition, which shall comprise of its purchase price and include acquisition charges like brokerage, fees, tax, duty or cess.
- The actual cost of a security (referred to in Part A) acquired in exchange for other securities or another asset shall be the fair value of the security so acquired.
- Subsequently, at the end of any tax year, securities held as stock-in-trade have to be valued at actual cost initially recognized or net realizable value at the end of that tax year, whichever is lower.
- It goes on to provide that such comparison of actual cost initially recognized and net realizable value has to be done category-wise and not for each individual security.
- Where actual cost initially recognized cannot be ascertained by reference to specific identification, use of "First in First Out" method or "Weighted Average Cost" formula is permitted for subsequent measurement of securities held as stock-in-trade (other than unlisted or unquoted securities) referred to in Part A.
- Securities referred to in Part B to be classified, recognised and measured in accordance with the extant guidelines issued by the RBI in this regard. Any claim for deduction in excess of the said guidelines will not be taken into account. To this extent, the provisions of ICDS VI on the effect of changes in foreign exchange rates relating to forward exchange contracts would not apply.

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ICDS IX: Borrowing Costs

- This ICDS deals with the treatment of borrowing costs. It does not deal with the actual or imputed cost of owners' equity and preference share capital.
- It requires borrowing costs which are directly attributable to the acquisition, construction or production of a qualifying asset to be capitalized as part of the cost of that asset. Other borrowing costs have to be recognized in accordance with the provisions of the Act.
- Qualifying asset has been defined to mean –
- land, building, machinery, plant or furniture, being tangible assets;
- know-how, patents, copyrights, trade marks, licences, franchises or any other business or commercial rights of similar nature, being intangible assets;
- inventories that require a period of twelve months or more to bring them to a saleable condition.
- This ICDS requires capitalization of specific borrowing costs and general borrowing costs.
- This ICDS provides the formula for capitalization of borrowing costs when funds are borrowed generally and used for the purpose of acquisition, construction or production of a qualifying asset.
- For the purpose of computing the amount of borrowing costs to be capitalized, in a case where the funds are not borrowed specifically for the purposes of acquisition, construction or production of a qualifying asset, a qualifying asset would be such asset that necessarily require a period of 12 months or more for its acquisition, construction or production.
- It also provides as to when capitalization of borrowing costs would commence and cease.
- It requires disclosure of the accounting policy adopted for borrowing costs and the amount of borrowing costs capitalized during the year.

ICDS X: Provisions, Contingent Liabilities and Contingent Assets

- This ICDS deals with Provisions, Contingent Liabilities and Contingent Assets. However, it does not deal with provisions, contingent liabilities and contingent assets –

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- resulting from financial instruments,
- resulting from executory contracts,
- arising in insurance business from contracts with policyholders and
- covered by another ICDS.

It also does not deal with recognition of revenue dealt with by ICDS on Revenue Recognition.

- ♦ The ICDS specifies the conditions for recognition of a provision, namely, existence of a present obligation as a result of a past event, reasonable certainty that outflow of resources embodying economic benefits will be required to settle the obligation and making a reliable estimate of the amount of the obligation.
- ♦ It provides that a person shall not recognize a contingent liability or a contingent asset. However, it requires contingent assets to be assessed continually. When it becomes reasonably certain that inflow of economic benefit will arise, the asset and related income have to be recognized in the tax year in which the change occurs.
- ♦ It contains provisions for measurement and review of a provision and asset and related income.
- ♦ It also provides that a provision shall be used only for expenditures for which the provision was originally recognized.
- ♦ The ICDS also contains specific disclosure requirements in respect of each class of provision, asset and related income recognized.

Clarification on Income Computation and Disclosure Standards (ICDS) notified under section 276(2) – [Circular No. 10/2017, dated 23-03-2017]

The CBDT has, vide this circular, issued the following clarifications on various issues related with ICDS:

S. No.	Question	Answer
1.	Preamble of ICDS I states that this ICDS is applicable for computation of income	As stated in the Preamble, ICDS is not meant for maintenance of books of accounts or preparing financial

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	chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and not for the purposes of maintenance of books of account. However, Para 1 of ICDS I states that it deals with significant accounting policies. Accounting policies are applied for maintenance of books of accounts and preparing financial statements. What is the interplay between ICDS I and maintenance of books of accounts?	statements. Persons are required to maintain books of accounts and prepare financial statements as per accounting policies applicable to them. For example, companies are required to maintain books of account and prepare financial statements as per requirements of Companies Act, 2013. The accounting policies mentioned in ICDS-I being fundamental in nature shall be applicable for computing income under the heads "Profits and gains of business or profession" or "Income from other sources".
2.	Certain ICDS provisions are inconsistent with judicial precedents. Whether these judicial precedents would prevail over ICDS?	The ICDS have been notified after due deliberation and after examining judicial views for bringing certainty on the issues covered by it. Certain judicial pronouncements were pronounced in the absence of authoritative guidance on these issues under the Act for computing Income under the head "Profits and gains of business or profession'' or "Income from other sources". Since certainty is now provided by notifying ICDS, the provisions of ICDS shall be applicable to the transactional issues dealt therein.
3.	Does ICDS apply to non-corporate taxpayers who are not required to maintain books of account and/or those who are covered by presumptive scheme	ICDS is applicable to specified persons having income chargeable under the head 'Profits and gains of business or profession' or 'Income from other sources'. Therefore, the relevant

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	of taxation like section 58 and section 61 of the Income-tax Act, 2025?	provisions of ICDS shall also apply to the persons computing income under the relevant presumptive taxation scheme. For example, for computing presumptive income of a partnership firm under Table: Sl. No. 1 of section 58(2), the provisions of ICDS on Construction Contract or Revenue recognition shall apply for determining the receipts or turnover, as the case may be.
4.	If there is conflict between ICDS and other specific provisions of the Income-tax Rules governing taxation of income, which provisions shall prevail?	ICDS provides general principles for computation of income. In case of conflict, if any, between the provisions of Rules and ICDS, the provisions of Rules, which deal with specific circumstances, shall prevail.
5.	ICDS is framed on the basis of accounting standards notified by Ministry of Corporate Affairs (MCA) vide Notification No. GSR 739(E) dated 7th December, 2006 under section 211(3C) of erstwhile Companies Act, 1956. However, MCA has notified in February, 2015 a new set of standards called 'Indian Accounting Standards' (Ind-AS). How will ICDS apply to companies which adopted Ind-AS?	ICDS shall apply for computation of taxable income under the head "Profit and gains of business or profession" or "Income from other sources" under the Income-tax Act. This is irrespective of the accounting standards adopted by companies i.e. either Accounting Standards or Ind-AS.
6.	Whether ICDS shall apply to computation of Minimum Alternate Tax (MAT) or Alternate	MAT under section 206(1) of the Act is computed on 'book profit' that is net profit as shown in the Profit and Loss

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	Minimum Tax (AMT) under section 206 of the Income-tax Act, 2025?	Account prepared under the Companies Act subject to certain specified adjustments. Since, the provisions of ICDS are applicable for computation of income under the regular provisions of the Act, the provisions of ICDS shall not apply for computation of MAT. AMT under section 206(2) of the Act is computed on adjusted total income which is derived by making specified adjustments to total income computed as per the regular provisions of the Act. Hence, the provisions of ICDS shall apply for computation of AMT.
7.	Whether the provisions of ICDS shall apply to Banks, Non-banking financial institutions, Insurance companies, Power sector etc.?	The general provisions of ICDS shall apply to all persons unless there are sector specific provisions contained in the ICDS or the Act. For example, ICDS VIII contains specific provisions for banks and certain financial institutions, and Schedule XIV of the Act contains specific provisions for Insurance business.
8.	Para 4(ii) of ICDS-I provides that Mark to Market (MTM) loss or an expected loss shall not be recognized unless the recognition is in accordance with the provisions of any other ICDS. Whether similar consideration applies to recognition of MTM gain or expected incomes?	Same principle as contained in ICDS-I relating to MTM losses or an expected loss shall apply mutatis mutandis to MTM gains or an expected profit.

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9.	ICDS-I provides that an accounting policy shall not be changed without 'reasonable cause'. The term 'reasonable cause' is not defined. What shall constitute 'reasonable cause'?	Under the Act, 'reasonable cause' is an existing concept and has evolved well over a period of time conferring desired flexibility to the taxpayer in deserving cases.
10.	Which ICDS would govern derivative instruments?	ICDS -VI (subject to para 3 of ICDS-III) provides guidance on accounting for derivative contracts such as forward contracts and other similar contracts. For derivatives, not within the scope of ICDS-VI, provisions of ICDS-I would apply.
12.	Since there is no specific scope exclusion for real estate developers and Build -Operate-Transfer (BOT) projects from ICDS IV on Revenue Recognition, please clarify whether ICDS-III and ICDS-IV should be applied by real estate developers and BOT operators. Also, whether ICDS is applicable for leases.	At present, there is no specific ICDS notified for real estate developers, BOT projects and leases. Therefore, relevant provisions of the Act and ICDS shall apply to these transactions as may be applicable.
13.	The condition of reasonable certainty of ultimate collection is not laid down for taxation of interest, royalty and dividend. Whether the taxpayer is obliged to account for such income even when the collection thereof is uncertain?	As a principle, interest accrues on time basis and royalty accrues on the basis of contractual terms. Subsequent non-recovery in either cases can be claimed as deduction. Further, the provision of the Act shall prevail over the provisions of ICDS.
14.	Whether ICDS is applicable to revenues which are liable to tax on gross basis like interest,	Yes, the provisions of ICDS, also apply for computation of these incomes on

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	royalty and fees for technical services for non-residents u/s 207 of the Income-tax Act, 2025?	gross basis for arriving at the amount chargeable to tax.
15.	Para 8 of ICDS-V states expenditure incurred on commissioning of project, including expenditure incurred on test runs and experimental production shall be capitalized. It also states that expenditure incurred after the plant has begun commercial production i.e., production intended for sale or captive consumption shall be treated as revenue expenditure. What shall be the treatment of expense incurred after the conduct of test runs and experimental production but before commencement of commercial production?	As clarified in Para 8 of ICDS-V, the expenditure incurred till the plant has begun commercial production, that is, production intended for sale or captive consumption, shall be treated as capital expenditure.
18.	If the taxpayer sells a security on 30th April 2026. The interest payment dates are December and June. The actual date of receipt of interest is on 30th June 2026 but the interest on accrual basis has been accounted as income on 31st March 2026. Whether the taxpayer shall be permitted to claim deduction of such interest i.e. offered to tax but not received while computing the capital gain?	Yes, the amount already taxed as interest income on accrual basis shall be taken into account for computation of income arising from such sale.

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19.	Para 9 of ICDS-VIII on securities requires securities held as stock-in-trade shall be valued at actual cost initially recognised or net realisable value (NRV) at the end of that tax year, whichever is lower. Para 10 of Part-A of ICDS-VIII requires the said exercise to be carried out category wise. How the same shall be computed?	For subsequent measurement of securities held as stock-in-trade, the securities are first aggregated category wise. The aggregate cost and NRV of each category of security are compared and the lower of the two is to be taken as carrying value as per ICDS-VIII. This is illustrated below –

Security	Category	Cost	NRV	Lower of cost or NRV	ICDS Value
A	Share	100	75	75	
B	Share	120	150	120	
C	Share	140	120	120	
D	Share	200	190	190	
	Total	**560**	**535**	**505**	535
E	Debt Security	150	160	150	
F	Debt Security	105	90	90	
G	Debt Security	125	135	125	
H	Debt Security	220	230	220	
	Total	**600**	**615**	**585**	**600**
Securities Total		**1160**	**1150**	**1090**	**1135**

20.	There are specific provisions in the Act read with Rules under which a portion of borrowing cost may get disallowed under sections like 14, 37, 35(b)(i), 35(b)(ii), 36(2), etc. of the Income-tax Act, 2025. Whether	Since specific provisions of the Act override the provisions of ICDS, it is clarified that borrowing costs to be considered for capitalization under ICDS IX shall exclude those borrowing costs which are disallowed under specific provisions of the Act.

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	borrowing costs to be capitalized under ICDS-IX should exclude portion of borrowing costs which gets disallowed under such specific provisions?	Capitalization of borrowing cost shall apply for that portion of the borrowing cost which is otherwise allowable as deduction under the Act.
21.	Whether bill discounting charges and other similar charges would fall under the definition of borrowing cost?	The definition of borrowing cost is an inclusive definition. Bill discounting charges and other similar charges are covered as borrowing cost.
22.	How to allocate borrowing costs relating to general borrowing as computed in accordance with formula provided under Para 6 of ICDS-IX to different qualifying assets?	The capitalization of general borrowing cost under ICDS-IX shall be done on asset by-asset basis.
24.	Expenditure on most post-retirement benefits like provident fund, gratuity, etc. are covered by specific provisions. There are other post-retirement benefits offered by companies like medical benefits. Such benefits are covered by AS-15 for which no parallel ICDS has been notified. Whether provision for these liabilities are excluded from scope of ICDS X?	It is clarified that provisioning for employee benefit which are otherwise covered by AS 15 shall continue to be governed by specific provisions of the Act and are not dealt with by ICDS-X.
25.	ICDS-I requires disclosure of significant accounting policies and other ICDS requires specific disclosures. Where is the taxpayer required to make such disclosures specified in ICDS?	Net effect on the income due to application of ICDS is to be disclosed in the Return of income. The disclosures required under ICDS shall be made in the tax audit report in Form 26. However, there shall not be any separate disclosure requirements for persons who are not liable to tax audit.

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Notified ICDS and Corresponding AS and IND AS

ICDS	Corresponding AS	Corresponding IND AS
ICDS I - Accounting Policies	AS – 1 Disclosure of Accounting Policies	Ind AS 1 - Presentation of Financial Statements
ICDS II - Valuation of Inventories	AS - 2 Valuation of Inventories (Revised)	Ind AS – 2 Inventories
ICDS III - Construction Contracts	AS 7 – Construction Contracts	Ind AS 115 – Revenue from Contracts with Customers
ICDS IV - Revenue Recognition	AS 9 – Revenue Recognition	Ind AS 115 - Revenue from Contracts with Customers
ICDS V - Tangible Fixed Assets	AS 10 – Property, Plant and Equipment (Revised)	Ind AS 16 Property, Plant and Equipment
ICDS VI - The Effects of changes in foreign exchange rates	AS 11 – The Effects of Changes in Foreign Exchange Rates (Revised)	Ind AS 21 – The Effects of Changes in Foreign Exchange Rates
ICDS VII - Government Grants	AS 12 - Accounting for Government Grants	Ind AS 20 – Accounting for Government Grants and Disclosure of Government Assistance
ICDS VIII - Securities	AS 13 - Accounting for Investments (Revised)	Ind AS 40 – Investment Property, Ind AS109 – Financial Instruments, Ind AS 105 – Non-current Assets held for Sale and Discontinued Operations
ICDS IX - Borrowing Costs	AS 16 - Borrowing Costs	Ind AS 23 - Borrowing Costs
ICDS X - Provisions, Contingent Liabilities and Contingent Assets	AS 29 - Provisions, Contingent Liabilities and Contingent Assets (Revised)	Ind AS 37 - Provisions, Contingent Liabilities and Contingent Assets

Student may note that the text of the notified ICDSs has been given as Annexure 1 at the end of this Module.

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Method of Accounting in Certain Cases [Section 277]

Section 277 provides that for the purpose of determining the income chargeable under the head "Profits and gains of business or profession":

Valuation of Inventory

(a) the valuation of inventory shall be **made at lower of actual cost or net realizable value** computed as per the notified ICDS i.e., ICDS II "Valuation of inventories".

(b) the valuation of purchase and sale of goods or services and of inventory shall be adjusted to **include the amount of any tax, duty, cess or fee actually paid or incurred by the assessee** to bring the goods or services to the place of its location and condition as on the date of valuation.

(c) **inventory being securities not listed** on a recognised stock exchange or **listed but not quoted** on a recognised stock exchange with regularity from time to time, shall be valued **at actual cost initially recognised** as per the notified ICDS i.e., ICDS VIII: Securities.

(d) **inventory being listed and quoted securities**, shall be valued at **lower of actual cost or net realisable value** as per the notified ICDS i.e., ICDS VIII: Securities.

However, inventories being securities held by a scheduled bank or public financial institution shall be valued as per the notified ICDS after taking into account the extant guidelines issued by the RBI [Section 277(2)].

The comparison of actual cost and net realisable value of securities shall be done category-wise [Section 277(3)].

3.3 INCOME CHARGEABLE UNDER THIS HEAD [SECTION 26]

The income referred to in section 26(2) shall be chargeable to tax as income under the head 'profits and gains of business or profession'. These incomes are as under:

(1) Income from business or profession: Income arising to any person by way of profits and gains from the business or profession carried on by him at any time during the tax year.

Exception

If an assessee is **engaged in the business of letting out of residential houses**, the income generated from

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letting out of a residential house or a part of it shall not be chargeable under the head "Profits and gains of business or profession" and would be chargeable under the head "Income from house property".



Chennai Properties and Investments Ltd. v. CIT (2015) 373 ITR 673 (SC); Rayala Corporation (P) Ltd. v. Asstt. CIT (2016) 386 ITR 500 (SC); and Raj Dadarkar and Associates v. ACIT (2017) 394 ITR 592 (SC)

Issue: Would rental income from the business of leasing out properties be taxable under the head "Income from house property" or "Profits and gains from business or profession"?

Analysis & Decision: In Chennai Properties and Investments Ltd. v. CIT (2015) 373 ITR 673, the Supreme Court observed that holding of the properties and earning income by letting out of these properties is the main objective of the company. Further, in the return of income filed by the company and accepted by the Assessing Officer, the entire income of the company is comprised of income from letting out of such properties. The Supreme Court, accordingly, held that such income was taxable as business income. Likewise, in Rayala Corporation (P) Ltd. v. Asst. CIT (2016) 386 ITR 500, the Supreme Court noted that the assessee was engaged only in the business of renting its properties and earning rental income therefrom and accordingly, held that such income was taxable as business income. However, in Raj Dadarkar and Associates v. ACIT (2017) 394 ITR 592, on account of lack of sufficient material to prove that substantial income of the assessee was from letting out of property, the Supreme Court held that the rental income has to be assessed as "Income from house property".

Note: *Section 26(4) of the Income-tax Act, 2025 provides that the income from* ***letting out of a residential house or a part of it*** *by the owner would be chargeable to tax under the head "Income from house property" and will no longer be considered under the head* ***"Profits and gains of business or profession" even though the main business of the assessee is to let out the residential house properties.*** *Accordingly, the rationale of the above rulings hold good only in respect of letting out of commercial properties.*

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(2) **Any compensation or other payment due to or received by** any person, by whatever name called,

(i) wholly or substantially managing the affairs -

(a) of an Indian company or

(b) in India, of any other company; or

(ii) holding an agency in India for any part of the business activities of any other person; or

(iii) for any contract relating to business,

in connection with the termination of his management, office, agency or contract, as the case may be, or modification of terms and conditions relating thereto.

(3) **Any compensation or payment due to or received by** any person, for vesting of the management of any property or business, in the Government including any corporation owned or controlled by the Government under any law in force.

(4) **Income from specific services performed for its members by a trade, professional or business:** Income derived by any trade, professional or similar associations from specific services rendered by them to their members. It may be noted that this forms an exception to the general principle of mutuality governing the assessment of income of mutual associations such as chambers of commerce, stock brokers' associations etc.

As a result, a trade, professional or similar association performing specific services for its members is to be deemed as carrying on business in respect of these services and on that assumption the income arising therefrom is to be subjected to tax. For this purpose, it is not necessary that the income received by the association should definitely or directly be related to these services.

(5) **Incentives received or receivable by assessee carrying on export business:** Following incentives received or receivable by an assessee:

- Profits on sale of import licence,
- Cash assistance against export,
- Duty drawback,
- Duty remission, or

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- any other export incentive

(6) Value of any benefit or perquisite: The value of any benefit or perquisite arising from business or the exercise of any profession, whether –

- convertible into money or not or
- in cash or in kind or partly in cash and partly in kind



If a company provides rent free residential accommodation to a lawyer in consideration of professional services rendered by him to the company, the value of such accommodation would be assessable in the hands of the said lawyer as his income under the head "Profits and gains or business or profession".

(7) Sum due to, or received by, a partner of a firm: Any interest, salary, bonus, commission or remuneration, by whatever name called, which is due to or received by a partner of a firm from such firm will be deemed to be income from business. However, if any interest, salary, bonus, commission or remuneration by whatever name called, or any part thereof has not been allowed as deduction under section 35(e) in the computation of the income of the firm, the income to be taxed in the hands of partner shall be reduced to the extent of the amount disallowed in the hands of firm.



A firm pays interest to a partner at 20% p.a. simple interest to a partner. The allowable rate of interest is 12% p.a. Hence, the excess 8% paid will be disallowed in the hands of the firm. Since excess interest has suffered tax in the hands of the firm due to disallowance, the same will not be taxed in the hands of the partner. However, the interest allowed to the extent of 12% p.a. in the hands of firm will be taxed in the hands of partner.

Exemption of share income of a partner [Section 11 read with Table: Sl. No. 2 of Schedule III]

Entry at Sl. No. 2 in Schedule III exempts from tax a partner's share in the total income of the firm. In other words, the partner's share in the total income of the firm determined in accordance with the profit-sharing ratio will be exempt from tax.

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(8) Any sum whether received or receivable, in cash or kind, under an agreement

(i) **for not carrying out any activity** in relation to any business or profession.

However, the following sums received or receivable would not be chargeable to tax under the head "profits and gains from business or profession":

(a) any sum, received on account of transfer of the right to manufacture, produce or process any article or thing or right to carry on any business or profession, which is chargeable under the head "Capital gains".

(b) any sum received as compensation from the multilateral fund of the Montreal Protocol on Substances that Deplete the Ozone layer under the United Nations Environment Programme, as per the terms of agreement entered into with the Government of India.

(ii) **for not sharing** any know-how, patent, copyright, trade-mark, licence, franchise or any other business or commercial right of similar nature, or information or technique likely to assist in the manufacture or processing of goods or provision for services.

Meaning of certain terms

Section	Term	Meaning
66(1)	**Agreement**	Agreement includes any arrangement or understanding or action in concert, - (A) whether or not such arrangement, understanding or action is formal or in writing; or (B) whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings;
66(29)	**Service**	Service means a service of any description which is made available to potential users and includes the provision of services in connection with business of any industrial or commercial nature such as accounting, banking, communication, conveying of news or information, advertising,

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		entertainment, amusement, education, financing, insurance, chit funds, real estate, construction, transport, storage, processing, supply of electrical or other energy, boarding and lodging.

(9) Any sum received under a Keyman insurance policy: Any sum received by the assessee, as an employer, under a Keyman insurance policy including the sum allocated by way of bonus on such policy will be taxable as income from business.

(10) Fair market value of inventory on its conversion/ treatment as capital asset: Fair market value of inventory as on the date on which it is converted into or treated as a capital asset, determined in the prescribed manner, would be chargeable to tax as business income[1].

(11) Sum received on account of capital asset referred under section 46: Any sum which is received or receivable, in cash or kind, when -

(i) a capital asset other than land or goodwill or financial instrument, is demolished, destroyed, discarded or transferred and

(ii) the whole of the expenditure on it has been allowed as a deduction under section 46 of the Income-tax Act, 2025 or under section 35AD of the Income-tax Act, 1961.



Where a specified person, being a partner of a firm or member of other AOP/BOI, receives during the tax year, any stock in trade from a specified entity, being a firm or other AOP/BOI, in connection with the dissolution or reconstitution of such specified entity, then, the specified entity would be deemed to have transferred such stock in trade to the specified person in the year in which such stock-in-trade is received by the specified person. Profit and gains arising from such deemed transfer would be deemed to be the income of such specified entity of the tax year in which such stock-in-trade was received by specified person and chargeable to income-tax under the "Profit and gains of business or profession" [Section 8]. For detailed discussion on section 8, refer Chapter 4 – "Capital Gains".

[1] *Rule 57 prescribes the manner of determination of fair market value (FMV) of the inventory on the date of conversion. For detailed reading of Rule 57 of the Income-tax Rules, 2026, refer to* ***Annexure 2*** *at the end of this module.*

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CIT v. K and Co. (2014) 364 ITR 93 (Del)

Issue: Whether interest income on margin money deposited with bank for obtaining bank guarantee to carry on business, is taxable under the head 'Profits and Gains from Business or Profession' or under the head 'Income from other sources'?

Analysis & Decision: The interest income from the deposits made by the assessee is inextricably linked to the business of the assessee and such income, therefore, cannot be treated as income under the head 'Income from other sources'. The margin money requirement was an essential element for obtaining the bank guarantee. If the assessee had not furnished bank guarantee, it would not have got the contract.

Therefore, the interest income received on funds kept as margin money for obtaining the bank guarantee would be taxable under the head "Profits and gains of business or profession".

3.4 SPECULATION BUSINESS

Section 26(3) specifically provides that where an assessee carries on speculative business, that business of the assessee must be deemed as distinct and separate from any other business. This becomes necessary because section 113 provides that losses in speculation business unlike other businesses, cannot be set-off against the profits of any business other than a speculation business.



Likewise, a loss in speculation business carried forward to a subsequent year can be set-off only against the profit and gains of any speculation business in the subsequent year. Profits and losses resulting from speculative transactions must, therefore, be treated as separate and distinct from profits and gains of business and profession from any other business.

As per section 113(5), where any part of the business of a company consists of purchase and sale of the shares of other companies, then such company shall be deemed to be carrying on speculation business to the extent to which the business consists of the purchase and sale of such shares.

However, this deeming provision under section 113(5) does not apply to the following companies –

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If its gross total income consists of mainly income chargeable under the heads "Income from house property", "Capital gains" or "Income from other sources"

OR

its principal business is of trading in shares or banking or granting of loans and advances

Accordingly, if these companies as mentioned above carry on the business of purchase and sale of shares of other companies, they would not be deemed to be carrying on speculation business [Section 113(6)].

Meaning of Speculative Transaction



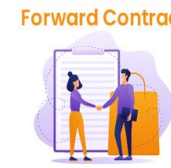
"Speculative transaction" means a transaction in which a contract for the purchase or sales of any commodity including stocks and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips **other than the following transactions**:

(i) **Hedging contract in respect of raw materials or merchandise:** A contract in respect of raw materials or merchandise entered into by a person in the course of his manufacturing or merchandising business to guard against loss through future price fluctuations in respect of his contracts for the actual delivery of goods manufactured by him or merchandise sold by him.



(ii) **Hedging contract in respect of stocks and shares:** A contract in respect of stocks and shares entered into by a dealer or investor therein to guard against loss in his holdings of stocks and shares through price fluctuation.

(iii) **Forward contract:** A contract entered into by a member of a forward market or stock exchange in the course of any transaction in the nature of jobbing or arbitrage to guard against any loss which may arise in the ordinary course of his business as a member.



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(iv) A specified derivative transaction: A specified derivative transaction means any transaction in respect of

- ♦ trading in derivatives or
- ♦ trading in commodity derivatives (other than agricultural commodity derivatives) which is chargeable to commodities transaction tax under Chapter VII of the Finance Act, 2013 or
- ♦ trading in agricultural commodity derivatives

if such transactions are carried out electronically on screen-based systems of a recognised stock exchange

(i) through a stock broker or such other intermediary[i]; or

(ii) by banks or mutual funds; and

if such transactions are supported by a time-stamped contract note issued by the intermediary to every client indicating in the contract note -

(i) the unique client identity number allotted under any law in force and

(ii) permanent account number;

Accordingly, the above (i) to (iv) forms of transactions shall not be deemed to be speculative transactions.

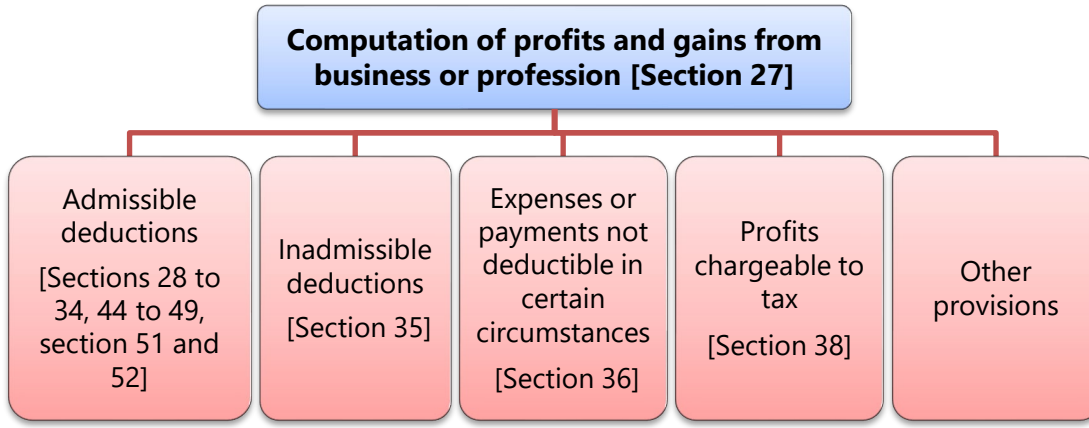
Examples of speculative and non-speculative transactions

Speculative transaction	Non-speculative transaction
Buying and selling shares without taking physical delivery.	Purchases of raw materials through a forward contract and takes actual delivery of goods on maturity of the contract.
Commodity contract for gold and settles the contract by payment of price difference without actual delivery of gold.	Hedging contract entered into by a cotton mill to guard against loss from price fluctuations in raw cotton.

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3.5 MANNER OF COMPUTING PROFITS AND GAINS OF BUSINESS OR PROFESSION [SECTION 27]

According to section 27, the profits and gains of any business or profession are to be as per the provisions contained in sections 28 to 60, except section 58. It must, however, be remembered that in addition to the specific allowances and deductions stated in sections 28 to 33, the Act further permits allowance of items of expenses under the residuary section 34(1), which extends the allowance to items of business expenditure not covered by sections 28 to 33, where these are allowable according to accepted commercial practices.



3.6 ADMISSIBLE DEDUCTIONS

Rent, rates, taxes, repairs and insurance [Section 28]

Section 28 allows following deductions in respect of premises, machinery, plant or furniture used by the assessee for the purposes of his business or profession.

- **Insurance premium:** Any premium paid in respect of insurance against risk of damage or destruction thereof.

Note **-** The premium may even take the form of contribution to a trade association which undertakes to indemnify and insure its members against

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loss; such premium or contribution would be deductible as an allowance under this section even if a part of it is returnable to the insured in certain circumstances.

It does not matter if the payment of the claim will endure to the benefit of someone other than the owner.

- **Land revenue, local rates or municipal taxes paid**
- **Rent paid, when the premises are occupied by the assessee as tenant**
- **Amount paid for repairs to the premises:**
  - **When the premises are occupied by the assessee otherwise than as a tenant** - Amount paid on account of current repairs to the premises
  - **When the premises are occupied by the assessee as a tenant -** Amount paid on account of cost of repairs, where he has undertaken to bear the cost of repairs to the premises
- **Amount paid for repairs to machinery, plant or furniture -** The amount paid on account of current repairs to machinery, plant or furniture.

Note: *Cost of repairs and current repairs in the nature of capital expenditure is not allowed as deduction.*

- **Premises, building, machinery, plant or furniture used partly for business:** Where the premises, building, machinery, plant or furniture is partly used or not wholly and exclusively used for the purposes of the business or profession, then only a fair proportionate part of the expenses as determined by the Assessing Officer, having regard to the usage for the purposes of the business or profession, will be allowed as a deduction [Section 28(2)].

Usage of the asset: In order to claim this deduction, the assets must have been used for purposes of the assessee's own business the profits of which are being taxed. The word 'used' has to be read in a wide sense so as to include active as well as passive use.

Repairs exclude replacement or reconstruction: The term 'repairs' will include renewal or renovation of an asset but not its replacement or reconstruction.

The deduction allowable under this section is only of current repairs but not arrears of repairs for earlier years even though they may still rank for a deduction under section 34(1).

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Deductions related to employee welfare [Section 29]

Section 29 allows following deductions in the case of an assessee, being an employer in relation to employee welfare:

(i) Contributions to provident fund and superannuation funds [Section 29(1)(a)]

Contribution to the employees' recognised provident fund or an approved superannuation fund is allowable subject to

- the limits laid down for recognizing the provident fund or approving superannuation fund and
- such specified conditions, for cases where the contributions are not made annually either as fixed amounts, or annual contributions fixed on some definite basis by reference to the income chargeable under the head "Salaries" or the contributions or to the number of members of the fund.

(ii) Employer's contribution for an employee under a Pension Scheme referred to in section 124 [Section 29(1)(b)]

- Section 29(1)(b) provides that the employer's contribution for an employee under a Pension Scheme as referred to in section 124 would be allowed as deduction while computing business income.
- However, deduction would be restricted to **14% of the salary** of the employee in the tax year.

Salary, for this purpose, includes dearness allowance, if the terms of employment so provide, but excludes all other allowances and perquisites.

ILLUSTRATION 1

X Ltd. contributes 20% of basic salary for each employee under a pension scheme referred to in section 124. Dearness Allowance is 40% of basic salary and it forms part of pay of the employees.

Compute the amount of deduction allowable under section 29(1)(b), if the basic salary of the employees aggregate to ₹ 10 lakhs.

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SOLUTION

Computation of deduction u/s 29(1)(b)

Particulars	₹
Basic Salary	10,00,000
Dearness Allowance@40% of basic salary [DA forms part of pay]	4,00,000
Salary for the purpose of section 29(1)(b) (Basic Salary + DA)	**14,00,000**
Actual contribution (20% of basic salary i.e., 20% of ₹10 lakhs)	2,00,000
Permissible deduction under section 29(1)(b) [14% of (basic salary *plus* dearness pay) = 14% of ₹ 14,00,000 = ₹ 1,96,000]	**1,96,000**

(iii) Contribution towards an approved gratuity fund and provision for payment of gratuity [Section 29(1)(c), 29(1)(d) and 29(2)]

Following deductions are available with respect to the contribution towards gratuity:

Contribution to an approved gratuity fund is allowable u/s 29(1)(c) subject to the condition that the gratuity fund should be for exclusive benefit of the employees under an irrevocable trust.

Any provision made for the purpose of making contribution towards approved gratuity fund or for the purpose of payment of any gratuity that has become payable during the tax year is allowable u/s 29(1)(d).

However, by virtue of section 29(2) –

- No deduction shall be allowed for any provision made for the payment of gratuity to the employees on their retirement or termination for any reason unless it is covered by section 29(1)(d); and
- In case deduction has been allowed for any provision made u/s 29(1)(d), then no deduction shall be allowed on actual payment made from such provision.

(iv) Amount received by assessee-employer as contribution from his employees towards their welfare fund to be allowed only if such amount is credited on or before due date of filing of return of income

Section 29(1)(e) provides that deduction in respect of any sum received by the employer as contribution from his employees towards any welfare fund of such

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employees (including employee's contribution to Provident Fund, Superannuation Fund and ESIC Contribution) will be allowed as deduction only if such sum is credited by the employer assessee to the employee's account in the relevant fund on or before the **due date of filing of return of income under section 263(1) for the tax year.**



Any sum received by the employer assessee from his employees as contribution to any PF or superannuation fund or any fund for the welfare of such employees shall be treated as income under clause (o) of section 2(49). The same is allowed as deduction in the hands of employer assessee, if the amount is deposited in the respective fund on or before the "due date of filing of return of income u/s 263(1)".

No deduction will be allowed in respect of any sum paid by the assessee as an employer towards

- setting up or formation of,
- or as contribution to,

any fund, trust, company, association of persons, body of individuals, society registered under the Societies Registration Act, 1860, or other institution for any purpose.

However, where such sum is paid, for the purposes and to the extent provided in section 29(1)(a), 29(1)(b) or 29(1)(c), or as required by or under any other law in force, then deduction will not be denied.

Deduction on certain premium [Section 30]

Following premiums paid by the assessee are allowed as deduction:

(i) Insurance premium for stock or stores [Section 30(a)] - If insurance policy has been taken out against risk of damage or destruction of the stock or stores of the business or profession, the premia paid is deductible.

(ii) Insurance premium paid by a Federal Milk Co-operative Society [Section 30(b)] - Deduction is allowed in respect of the amount of premium paid by a Federal Milk Co-operative Society to effect or to keep in force an insurance on the life of the cattle owned by a member of a co-operative society, being

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a primary society engaged in supply of milk raised by its members to such Federal Milk Co-operative Society.

(iii) Premium paid by employer for health insurance of employees [Section 30(c)] - This clause seeks to allow a deduction to an employer in respect of premium paid by him through any mode of payment other than cash to effect or to keep in force an insurance on the health of his employees in accordance with a scheme framed by

(a) the General Insurance Corporation of India and approved by the Central Government; or

(b) any other insurer and approved by the IRDA.

Deduction for bad debt and provision for bad and doubtful debt [Section 31]

(i) Deduction in respect of Provision for Bad and Doubtful Debts in case of specified banks [Section 31(1)]

Deduction in respect of provision for bad and doubtful Debts is allowed to Banks, NBFCs and Financial Institutions. The amount mentioned in column (C) is allowed as deduction to the corresponding assessee specified in column B as per the Table below:

Sl. No.	Specified assessee	Amount of deduction
A	B	C
1.	(a) A scheduled bank, other than a bank incorporated by or under the laws of a country outside India; or (b) a non-scheduled bank; or (c) a co-operative bank, other than (i) a primary agricultural credit society; or (ii) a primary co-operative agricultural and rural development bank	(a) an amount **not more than 8.5%** of the total income of the tax year computed before making any deduction under this clause and Chapter VIII, And **an additional amount up to 10%** of the aggregate average advances made by rural

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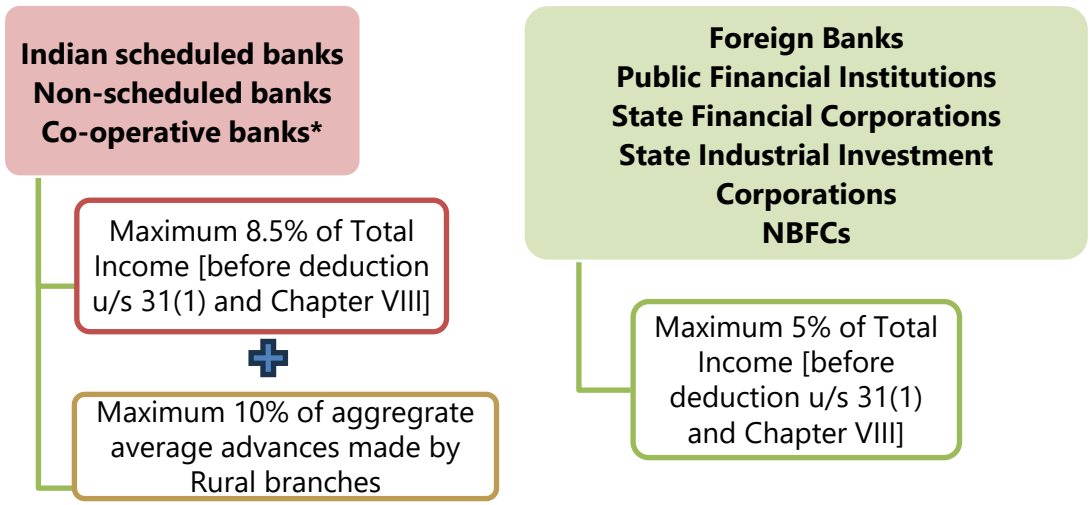
		branches computed in the prescribed manner; (b) a scheduled bank or a non-scheduled bank as mentioned in (a) and (b) of column B, at its option, an additional amount in excess of (a) above but not more than the **income from redemption of securities** as per a scheme framed by the Central Government, when such income has been disclosed in the return of income under gains of "business or profession."
2.	(a) A bank incorporated by or under the laws of a country outside India (i.e. a Foreign Bank); or (b) a public financial institution or a State Financial Corporation or a State Industrial Investment Corporation; or (c) a non-banking financial company.	**Not more than 5%** of the total income of a tax year computed before making any deduction under this clause and Chapter VIII.

Meaning of certain terms

Term	Meaning
Scheduled Bank	"Scheduled bank" has the same meaning as assigned to it in section 2(*e*) of the Reserve Bank of India Act, 1934. It refers to the State Bank of India or any of its subsidiaries or any of the nationalised banks and would

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	also include any other bank which is listed in the Second Schedule to the Reserve Bank of India Act, 1934.
Non-Scheduled Bank	This refers to a banking company as defined in section 5(c) of the Banking Regulation Act, 1949 which is not a scheduled bank.
Rural branch	A branch of a scheduled bank or a non-scheduled bank situated in a place which has a population of not more than 10,000 according to the last preceding census of which the relevant figures have been published before the first day of the tax year.



** other than a primary agricultural credit society or primary co-operative agricultural and rural development bank*

(ii) Deduction in respect of Bad Debts [Section 31(2)]

While section 31(1) discussed above provides for deduction in respect of "Provision for Bad and Doubtful Debts", deduction on account of "Bad Debt" is governed by provisions of section 31(2).

Any amount of bad debt or part of it is allowed as deduction in the tax year in

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which such amount is written off as irrecoverable in the accounts of the assessee subject to the conditions that

I. **debt has been taken into account in computing the income of the assessee of the tax year in which such debt is written off**, or of an earlier tax year, or should represent money lent by the assessee in the ordinary course of his business of banking or money lending carried on by the assessee.

Any bad debt written off as irrecoverable shall not include any provision for bad and doubtful debt, meaning thereby that for the purposes of section 31(2), the deduction for bad debts is available only when debt has been actually written off in the accounts and mere a provision for bad debts shall not be treated as actual write off of debt [Section 31(3)(a)].



Circular no. 12/2016, dated 30-05-2016

The CBDT has, ***clarified vide Circular no. 12/2016, dated 30-05-2016,*** *that claim for any debt or part of it in any tax year, shall be admissible, if it is written off as irrecoverable in the books of accounts of the assessee for that tax year and it fulfils the stipulated conditions.*

However, no such requirement is there in law that the assessee has to establish that the debt has, in fact, become irrecoverable.

II. **Deduction of differential amount of debts due as bad debts in the year of recovery, to the extent of deficiency in recovery:** If the amount ultimately recovered on any such debt or part of debt is less than the difference between the debt or part and the amount so deducted, the deficiency can be claimed as deduction in the tax year in which the ultimate recovery is made.

III. **Deductions for bad debt in case of an assessee for which provisions for bad and doubtful debts is allowable under section 31(1):** In case of an assessee for which provisions for bad and doubtful debts is allowable under section 31(1), deduction for bad debt written off shall be allowed

- only to the amount which exceeds the credit balance in the provision for bad and doubtful debts account made under section 31(1).
- such amount shall be allowed only when the assessee has debited any

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amount of bad debt or part thereof in that tax year to the provision for bad and doubtful debts account made under section 31(1) and

- only one account shall be made in respect of provisions for bad and doubtful debt u/s 31(1) and such account shall be related to all types of advances, including advances made by rural branches.

Amount of debt taken into account in computing the income of the assessee on the basis of notified ICDSs to be allowed as deduction in the tax year in which such debt or part thereof becomes irrecoverable [Section 31(3)]

(i) Under section 31(2), deduction is allowed in respect of the amount of any bad debt or part of it which is written off as irrecoverable in the accounts of the assessee for the tax year.

(ii) Therefore, writing off in the books of account is an essential condition for claim of bad debts under section 31(2).

(iii) In this regards, section 31(3)(b) provides that the amount of bad debt or part of it, which has been taken into account in computing the income of the assessee of the tax year in which such debt has become irrecoverable or of an earlier tax year on the basis of notified ICDSs without recording it in the accounts is to be allowed as deduction in the tax year in which such debt or part of it becomes irrecoverable and such bad debt or part of it shall be deemed to be written off as irrecoverable in the accounts for the purpose of section 31(2).

(iv) If a debt, which has not been recognized in the books of account but has been taken into account in the computation of income as per the notified ICDSs, has become irrecoverable, it can still be claimed as bad debts under section 31(2) since **it shall be deemed that the debt has been written off as irrecoverable in the account.** This is because some ICDSs require recognition of income at an earlier point of time (prior to the point of time such income is recognised in the books of account). Consequently, if the whole or part of such income, recognised at an earlier point of time for tax purposes, becomes irrecoverable, it can be claimed as bad debts on account of section 31(3)(b).

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Where the amount of such debt or part thereof has been taken into account in computing the income of the assessee **(on the basis of ICDSs without recording the same in the accounts)**

of the tax year in which such debt has become irrecoverable **(or)** of an earlier tax year

Such debt or part of it shall be allowed **in the tax year in which such debt or part thereof becomes irrecoverable**

(and)

It shall be **deemed that such debt or part thereof has been written off as irrecoverable in the accounts**

(iii) Recovery of a bad debt subsequently [Section 38(1)(d)]

If a deduction has been allowed in respect of a bad debt under section 31(2), and subsequently the amount recovered in respect of such debt exceeds than the difference between such debt and the amount allowed, the excess shall be deemed to be the profits and gains of business or profession and will be chargeable to income-tax in the tax year in which recovery is made.

It does not matter whether the business or profession in respect of which deduction has been made is in existence in that year or not.



For T.Y. 2025-26, bad debts of ₹ 40,000 was allowed by the Assessing Officer out of total bad debts of ₹ 75,000. Subsequently, ₹ 44,000 is recovered during T.Y. 2026-27.

Since Bad debt recovered i.e., ₹ 44,000 exceeds ₹ 35,000, being the difference between debt and debt allowed, the excess ₹ 9,000 would be deemed to be the profits and gains of business or profession of T.Y. 2026-27 and will be chargeable to income-tax in the T.Y. 2026-27 in which it is recovered.

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Other Deductions [Section 32]

This section authorises deduction of certain specific expenses. The items of expenditure and the conditions under which such expenditures are deductible are:

(i) Bonus and Commission [Section 32(a)]

These are deductible in full provided the sum paid to the employees as bonus or commission shall not be payable to them as profits or dividends if it had not been paid as bonus or commission.

It is a provision intended to safeguard against a private company or an association escaping tax by distributing a part of its profits by way of bonus amongst the members, or employees of their own concern instead of distributing the money as dividends or profits.

(ii) Interest on borrowed capital [Section 32(b)]

Deduction of interest is allowed in respect of capital borrowed for the purposes of business or profession in the computation of income under the head "Profits and gains of business or profession".

Capital may be borrowed for several purposes like for acquiring a capital asset, or to pay off a trading debt or loss etc. The scope of the expression 'for the purposes of business' is very wide. Capital may be borrowed in the course of the existing business as well as for acquiring assets for extension of existing business.

However as per section 32(b)(i), deduction in respect of any amount of interest, in respect of capital borrowed for acquisition of an asset, whether capitalised in the books of account or not, for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use shall not be allowed.

Further as per section 32(b)(ii), recurring subscriptions paid periodically by shareholders or subscribers in Mutual Benefit Societies fulfilling the conditions as may be prescribed, shall be deemed to be capital borrowed.

Meaning of interest [Section 2(59)]

Interest" means interest payable in any manner for moneys borrowed or debt incurred (including a deposit, claim or other similar right or obligation) and includes

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service fee or any other charges for the moneys borrowed or debt incurred or for any credit facility that has not been utilized.

Section 39(4) (Table: SI No. 13) provides that interest relatable to a period after the asset is first put to use cannot be capitalised. Interest in respect of capital borrowed for any period from the date of borrowing to the date on which the asset was first put to use should, therefore, be capitalised.

(iii) Contribution by a public financial institution to Credit guarantee fund trust for small industries [Section 32(c)]

Section 32(c) provides for deduction of contribution paid by a public financial institution to the credit guarantee fund trust for small industries notified by the Central Government.

(iv) Discount on Zero Coupon Bonds (ZCBs) [Section 32(d)]

Section 32(d) provides deduction for the discount on ZCB on pro rata basis having regard to the period of life of the bond to be calculated in the manner prescribed where -

Discount = The amount received or receivable by an infrastructure capital company/ infrastructure capital fund/ public sector company/ scheduled bank on issue of the bond - the amount payable by such company or fund or bank on maturity or redemption of the bond.
Period of life of the bond = The period commencing from the date of issue of the bond and ending on the date of the maturity or redemption of such bond.

Meaning of Infrastructure Capital Company [Section 2(55)]

"Infrastructure capital company" means a company which makes investments by way of acquiring shares or providing long-term finance to **-**

(1) any enterprise or undertaking wholly engaged –

(a) in the business of

(i) developing/ operating and maintaining/ developing, operating and maintaining any infrastructure facility fulfilling the specified conditions

(ii) providing telecom services, whether basic or cellular

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(iii) developing, developing and operating or maintaining and operating an industrial park or special economic zone notified by the Central Government

(iv) generating, transmitting or distributing power or undertaking substantial renovation and modernization of the existing network of transmission or distribution lines.

(b) in any business of developing a SEZ.

(2) an undertaking developing and building -

(a) a housing project approved before 31.3.2008 by a local authority and commences or commenced development and construction on or after 1.10.98 and completes or completed development and construction within the time specified.

(b) a project for constructing a hotel of not less than three-star category as classified by the Central Government or

(c) a project for constructing a hospital with at least 100 beds for patients.

Meaning of Infrastructure Capital Fund [Section 2(56)]

Infrastructure capital fund means a fund operating under a trust deed registered under the provisions of the Registration Act, 1908 established to raise monies by the trustees for investment by way of acquiring shares or providing long-term finance to enterprises or undertakings referred to in section 2(55) mentioned above.

(v) Special deduction to specified entities engaged in eligible business [Section 32(e)]

(a) Under this section, an amount carried to a special reserve created and maintained by a specified entity is allowed as deduction.

(b) **Amount of deduction:** The quantum of deduction, however, **should not exceed 20%** of the profits derived from eligible business computed under the head "Profits and gains of business or profession" (before making any deduction under this clause).

However, when the aggregate amount carried to such reserve account exceeds twice the amount of paid up share capital and general reserve of the specified entity, no deduction shall be allowed in respect of such excess.

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In simple terms, quantum of deduction shall be the least of the following

(i) Amount transferred to special reserve

(ii) 20% of profit derived from eligible business (before this deduction)

(iii) 200% of paid up capital and general reserve *less* aggregate amount carried to Special Reserve account.

Amount withdrawal from special reserve [Section 38(1)(e)]

Where a deduction has been allowed in respect of any special reserve created and maintain under section 32(e), and subsequently the amount is withdrawn from such special reserve then such amount shall be deemed to be the profits and gains of business or profession and will be chargeable to income-tax in the tax year in which such amount is withdrawn.

If the amount is withdrawn in a tax year in which the business is no longer in existence, the taxability would arise in the above manner as though the business is in existence in that tax year.

(c) **Eligible business for specified entities:** The eligible business for different entities specified are given in the table below –

	Specified entity	Eligible business
1.	(a) a public financial institution as specified in section 2(72) of the Companies Act, 2013 (b) a financial corporation which is a public sector company (c) a banking company (d) a co-operative bank (other than a primary agricultural credit society or a primary co-operative	Business of providing long-term finance for - (i) industrial or agricultural development or (ii) development of infrastructure facility in India; or (iii) development of housing in India.

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	agricultural and rural development bank)	
2.	A housing finance company	Business of providing long-term finance for the construction or purchase of residential house in India.
3.	Any other financial corporation including a public company	Business of providing long-term finance for development of infrastructure facility in India.

(d) **Infrastructure facility** mean -

(1) an infrastructure facility i.e.,



(i) a road including toll road, a bridge or a rail system;

(ii) a highway project including housing or other activities being an integral part of the highway project;

(iii) a water supply project, water treatment system, irrigation project, sanitation and sewerage system or solid waste management system; and

(iv) a port, airport, inland waterway or inland port or a navigational channel in the sea

(2) any other public facility of a similar nature as may be notified by the CBDT in this behalf in the Official Gazette and which fulfils the prescribed conditions;



Notification of public facilities as infrastructure facility for the purpose of section 32(e) [Notification No. 188/2006, dated 20.7.2006]

The following public facilities have been notified by the CBDT as infrastructure facility for purposes of section section 32(e) -

(i) Inland Container Depot and Container Freight Station notified under the Customs Act, 1962

(ii) Mass Rapid Transit system

(iii) Light Rail Transit system

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(iv)	Expressways
(v)	Intra-urban or semi-urban roads like ring roads or urban by-passes or flyovers
(vi)	Bus and truck terminals
(vii)	Subways
(viii)	Road dividers
(ix)	Bulk Handling Terminals which are developed or maintained or operated for development of rail system
(x)	Multilevel Computerized Car Parking.



(3) an undertaking providing telecommunication services, an undertaking developing, developing and operating, maintaining and operating an industrial park or SEZ notified by the Central Government, an undertaking generating, distributing or transmitting power, substantial renovation and modernization of existing network of transmission or distribution lines); and

(4) an undertaking developing and building housing projects approved by a local authority.

Meaning of Long term finance

As per section 66(10), long-term finance means any loan or advance where the terms under which moneys are loaned or advanced provide for repayment along with interest thereof during a period of not less than 5 years.

(vi) Expenditure incurred by entities established under any Central, State or Provincial Act [Section 32(f)]

Any expenditure, not being capital expenditure, incurred by a corporation or a body corporate, by whatever name called, if –

(i) it is constituted or established by a Central, State or Provincial Act;

(ii) such corporation or body corporate is notified by the Central Government for this purpose having regard to the objects and purposes of the Act;

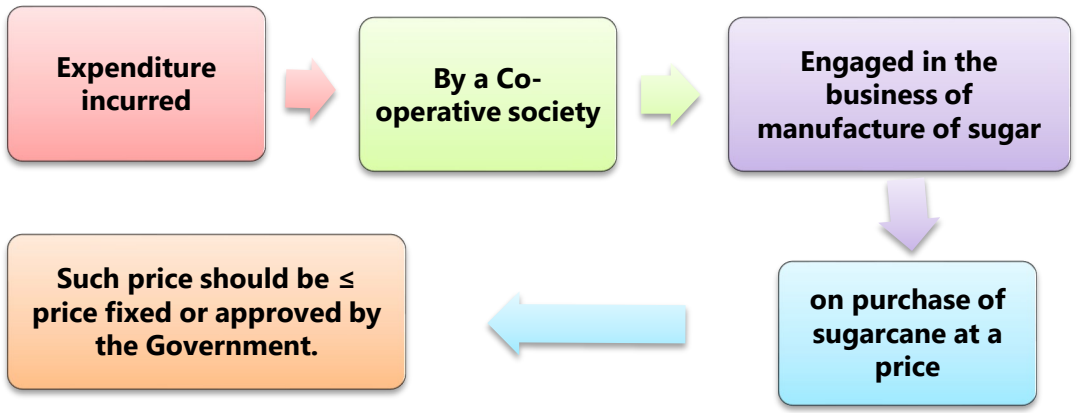
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(iii) the expenditure is incurred for the objects and purposes authorised by the Act under which it is constituted and established.

The Central Government has notified the Oil Industry Development Board for the purpose of deduction under section 32(f).

(vii) Amount of expenditure incurred by a co-operative society for purchase of sugarcane at price fixed by the Government [Section 32(g)]

Section 32(g) provides for deduction of the expenditure incurred by a co-operative society engaged in the business of manufacture of sugar, on purchase of sugarcane at a price equal to or less than the price fixed or approved by the Government.





Circular no. 18/2021 dated 25.10.2021

The CBDT has, vide Circular no. 18/2021 dated 25.10.2021, clarified that the phrase 'price fixed or approved by the Government' includes price fixation by State Governments through State level Acts/Orders or other legal instruments that regulate the purchase price for sugarcane, including State Advised Price, which may be higher than the Statutory Minimum Price/ Fair and Remunerative Price fixed by the Central Government.

(viii) Marked to market loss [Section 32(h)]

Marked to market loss or other expected loss as computed as per the ICDS notified under section 276(2), shall be allowed as deduction. ICDS I provides that marked to

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market losses would not be allowed unless the same is in accordance with any other ICDS. Therefore, only marked to market losses specifically permitted under any other ICDS would be allowable as deduction under section 32(h).

(ix) Expenses on family planning by a company [Section 32(i)]

Any expenditure of revenue nature *bona fide* incurred by a company for the purpose of promoting family planning amongst its employees will be allowed as a deduction in computing the company's business income;

- Where, the expenditure is of a capital nature, **one-fifth of such expenditure** will be deducted in the tax year in which it was incurred and the balance in each of the four immediately succeeding tax years.
- This deduction is **allowable only to companies** and not to other assessees.
- The assessee would be **entitled to carry forward and set off** the unabsorbed part of the allowance in the same way as unabsorbed depreciation.
- The capital expenditure on promoting family planning will be treated in the same way as capital expenditure for scientific research for purposes of dealing with the profit or loss on the sale or transfer of the asset including a transfer on amalgamation.

(x) Allowance for animals [Section 32(j)]

This clause grants an allowance in respect of animals used for the purposes of the business or profession otherwise than as stock-in-trade, where such animals have died or become permanently useless.

The amount of the allowance is the difference between the actual cost of the animals and the price realized on the sale of the animals themselves or their carcasses.

(xi) Amount of securities transaction tax and commodities transaction tax paid [Section 32(k)]

The amount of securities transaction tax and commodities transaction tax paid by the assessee during the year is allowed as deduction if

(a) the taxable securities transactions or taxable commodities transactions are entered into the course of the business during the tax year; and

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(b) the income arising from such taxable securities transactions or taxable commodities transactions is included in the income computed under the head "Profits and gains of business or profession".

Taxable commodities transaction

A 'taxable commodities transaction' means a transaction of sale of commodity derivatives or sale of commodity derivatives based on prices or indices of prices of commodity derivatives or option on commodity derivatives or option in goods in respect of commodities, other than agricultural commodities, traded in recognised stock exchange.

A "commodity derivative" means –

(a) A contract for delivery of goods which is not a ready delivery contract

(b) A contract for differences which derives its value from prices or indices of prices-

  (i) of such underlying goods; or

  (ii) of related services and rights, such as warehousing and freight; or

(c) with reference to weather and similar events and activities having a bearing on the commodity sector.

Depreciation [Section 33]

(i) Charge of depreciation mandatory



Section 33 allows a deduction in respect of depreciation resulting from the diminution or exhaustion in the value of certain capital assets.

Section 33(7) provides that deduction on account of depreciation shall be made compulsorily, whether or not the assessee has claimed the deduction in computing his total income.

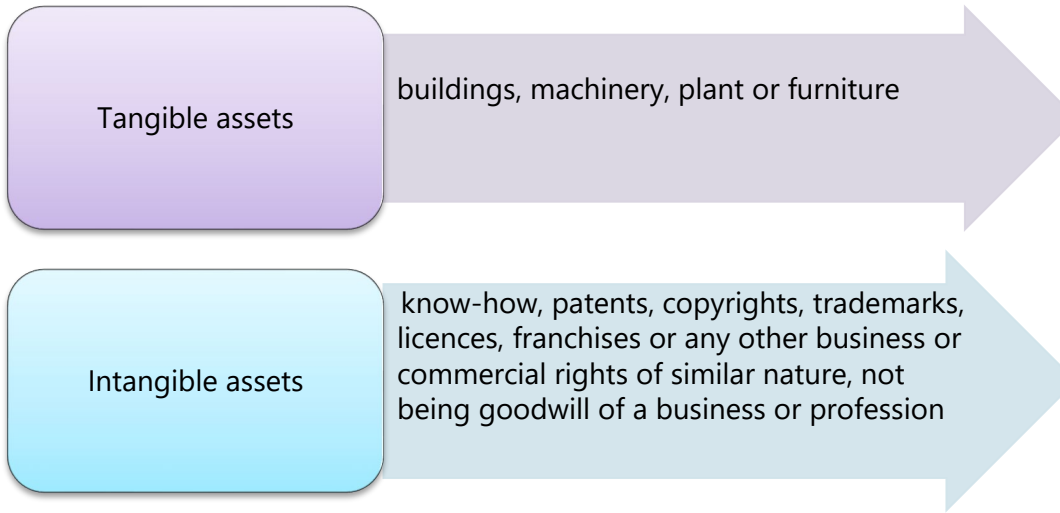
(ii) Conditions to be satisfied for allowance of depreciation

The allowance of depreciation which is regulated by Rule 25 of the Income-tax Rules, 2026, is subject to the following conditions which are cumulative in their application.

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(a) **The assets in respect of which depreciation is claimed must belong to either of the following categories, namely:**

Category of assets



- The depreciation in the value of any other capital assets cannot be claimed as a deduction from the business income.
- No depreciation is allowable on the cost of the land on which the building is erected because the term 'building' refers only to superstructure but not the land on which it has been erected.
- **Know-how [Section 33(12)(b)] -** 'Know-how' means any industrial information or technique likely to assist in the manufacture or processing of goods or in the working of a mine, oil-well or other sources of mineral deposits (including searching for discovery or testing of deposits for the winning of access thereto).
- The term 'plant' as defined in section 66(17) includes ships, vehicles, books, scientific apparatus and surgical equipment used for the purpose of the business or profession but does not include tea bushes or livestock or buildings or furniture and fittings.
- The word 'plant' does not include an animal, human body or stock-in-trade. Thus, plant includes all goods and chattels, fixed or movable, which a businessman keeps for employment in his business with some degree of durability.

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- The expression 'plant' includes part of a plant (e.g., the engine of a vehicle); machinery includes part of machinery and building includes a part of the building.
- Similarly, the term 'buildings' includes within its scope roads, bridges, culverts, wells and tubewells.

(b) **The assets should be actually used by the assessee wholly and exclusively for purposes of his business or profession during the tax year -** The asset must be put to use at any time during the tax year. The amount of depreciation allowance is not proportionate to the period of use during the tax year. If the asset is acquired during the tax year and is not put to use in the same year, then the depreciation shall not be allowed for such asset but the cost of such asset would be added to the block of asset.

Depreciation in case of lease or license

Depreciation would be allowable to the owner even in respect of assets which are actually worked or utilized by another person e.g., a lessee or licensee. The deduction on account of depreciation would be allowed under this section to the owner who has let on hire his building, machinery, plant or furniture provided that letting out of such assets is the business of the assessee. In other cases where the letting out of such assets does not constitute the business of the assessee, the deduction on account of depreciation would still be allowable under section 93(1)(c).



I.C.D.S. Ltd. v. CIT (2013) 350 ITR 527 (SC)

Issue: Can depreciation on leased vehicles be denied to the lessor on the ground that the vehicles are registered in the name of the lessee and that the lessor is not the actual user of the vehicles?

Analysis & Decision: Section 33 imposes a twin requirement of "ownership" and "usage for business" as conditions for claim of depreciation thereunder. As far as usage of the asset is concerned, the section requires that the asset must be used for the purposes of the business or profession. It does not mandate actual usage by the assessee itself. **In this case, the assessee did use the vehicles in the course of its leasing business. Hence, this**

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requirement of section 33 has been fulfilled, notwithstanding the fact that the assessee was not the actual user of the vehicles.

As long as the assessee-lessor has a right to retain the legal title against the rest of the world, he would be the owner of the asset in the eyes of law. In this regard, the following provisions of the lease agreement are noteworthy –

- The assessee is the exclusive owner of the vehicle at all points of time;
- The assessee is empowered to repossess the vehicle, in case the lessee committed a default;
- At the end of the lease period, the lessee was obliged to return the vehicle to the assessee;
- The assessee had a right of inspection of the vehicle at all times.

The proof of ownership lies in the lease agreement itself, which clearly points in favour of the assessee. **The assessee-lessor was, therefore, entitled to claim depreciation in respect of vehicles leased out since it has satisfied both the requirements of section 33, namely, ownership of the vehicles and its usage in the course of business.**

Use includes passive use in certain circumstances: One of the conditions for claim of depreciation is that the asset must be "used for the purpose of business or profession". Depreciation is allowed when asset is actually put to use and not ready to use. However, in certain circumstances, Courts have held that, an asset can be said to be in use even when it is "kept ready for use".

Use includes both active use and passive use



Stand by equipment and fire extinguishers can be capitalized if they are 'ready for use'.

Likewise, machinery spares which can be used only in connection with an item of tangible fixed asset and their use is expected to be irregular, has to be capitalised. Hence, in such cases, the term "use"

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embraces both active use and passive use. However, such passive use should also be for business purposes.

(c) **The assessee must own the assets, wholly or partly –** Depreciation is allowed only to the owner of the asset. If the assessee has taken an asset on lease, he, being the lessee, cannot avail depreciation in respect of such asset. On the other hand, the lessor will be entitled to depreciation on such asset as he is the owner.

Depreciation is allowable not only in respect of assets "wholly" owned by the assessee but also in respect of assets "partly" owned by him and used for the purposes of his business or profession.

Note - *In this connection, students may note that the section 33(6) provides that where the business or profession of the assessee is carried on in a building not owned by him but in respect of which the assessee holds a lease or other right of occupancy, and if any capital expenditure is incurred by the assessee for the purposes of the business or profession or the construction of any structure or any work by way of renovation, extension or improvement to the building, then depreciation will be allowed as if the said structure or work is a building owned by the assessee.*

(iii) Computation of Depreciation Allowance

Depreciation allowance will be calculated on the following basis:

(a) Power generation undertakings [Section 33(2)]: In the case of assets of an undertaking engaged in generation or generation and distribution of power, such percentage on the actual cost to the assessee as prescribed by Rule 25(3).



Rule 25(3) - As per this rule, the depreciation on the above-mentioned assets shall be calculated at the percentage of the actual cost at rates specified in Table in Appendix II of these rules. However, the aggregate depreciation allowed in respect of any asset for different tax years shall not exceed the actual cost of the asset. It is further provided that such an undertaking as mentioned above has the option of being allowed

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depreciation on the written down value of such block of assets as are used for its business at rates specified in Appendix I to these rules.

However, such option must be exercised before the due date for furnishing return under section 263(1)(c) for the tax year in which it begins to generate power.

It is further provided that any such option once exercised shall be final and shall apply to all subsequent tax years.

(b) Block of assets [Section 33(3)]: In the case of any block of assets, at such percentage of its written down value of the block, as may be prescribed by Rule 25(1).

Block of Assets

A "block of assets" is defined in section 2(17), as a group of assets falling within a class of assets comprising—

(a) tangible assets, being buildings, machinery, plant or furniture;

(b) intangible assets, being know-how, patents, copyrights, trademarks, licenses, franchises or any other business or commercial rights of similar nature, not being goodwill of a business or profession, in respect of which the same percentage of depreciation is prescribed.

Block of asset simply means "same class of assets with same rate of depreciation".



(1) When any building, machinery, plant or furniture is partly or not wholly and exclusively used for the business or profession of the assessee, the depreciation allowable would be restricted to a fair proportionate part thereof as determined by the Assessing Officer, having regard to the usage of such asset for the purpose of the business or profession [Section 33(3)(b)].

(2) When deduction of actual cost in respect of any machinery or plant has been allowed under section 54 i.e., in case of business of prospecting for mineral oil, no deduction for depreciation on such asset would be allowed [Section 33(3)(c)].

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(c) Asset used for less than 180 days [Section 33(4)]: The deduction for depreciation under section 33(2) and 33(3) would be restricted to 50% of the prescribed rate, if such asset is

- acquired by the assessee during the tax year; and
- is put to use for the purposes of business or profession for less than 180 days in that tax year.



This restriction applies only to the year of acquisition and not for subsequent years.

(d) Additional depreciation on Plant or Machinery acquired [Section 33(8) and 33(9)]: Apart from normal depreciation under section 33(3), an additional depreciation is also allowed to the assessee if the following conditions are satisfied:

Additional depreciation

- the assessee is engaged in the business of manufacture or production of any article or thing or in the business of generation or transmission or distribution of power.
- the assessee acquires and installs new machinery or plant
- the new machinery or plant is first put to use by the assessee for the purpose of business and
- the new machinery or plant (not being a ship or an aircraft)
  - was not used either within or outside India by any other person before its installation by the assessee
  - is not installed in any office premises or any residential accommodation, including accommodation in the nature of a guest house
  - is not in the nature of any office appliances or road transport vehicles

is not an asset on which the whole of the actual cost of which is allowed as a deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head "Profits and Gains of Business or Profession" of any tax year.

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Rate of additional depreciation - Additional depreciation is allowed

- @ 20% of the actual cost of new machinery or plant in the tax year when it is acquired and put to use in that tax year.
- @10% of the actual cost, if the new machinery or plant is acquired and put to use for less than 180 days in the relevant tax year, and balance 10% of the actual cost shall be allowed in the immediately succeeding tax year.

10%, if put to use for < 180 days



(1) Additional Depreciation is available only when assessee claims normal depreciation under section 33(3) i.e., in respect of Block of Assets. It is not available in case of assessee claiming normal depreciation based on actual cost of asset under section 33(2).

(2) In case of an individual, HUF, AoP (other than a co-operative society) or BoI or an artificial juridical person, additional depreciation is not allowable under the default tax regime under section 202(1). Additional depreciation would be allowable only if such person has exercised the option of shifting out of the default tax regime and pays tax as per the optional tax regime under the regular provisions of the Act.

(3) In case of companies and co-operative societies, additional depreciation would not be allowable if they opted for the special provisions u/s 200/201 and section 203/204, respectively. In other words, additional depreciation would be allowable only if companies and co-operative societies pay tax under the normal provisions of the Act.



Eligibility for grant of additional depreciation in the case of an assessee engaged in printing or printing and publishing [Circular No. 15/2016, dated 19-5-2016]

An assessee, engaged in the business of manufacture or production of an article or thing, is eligible to claim additional depreciation under section 33(8) in addition to the normal depreciation under section 33(3).

*The CBDT has, vide this Circular, clarified that the **business of printing or printing and publishing amounts to manufacture or production** of an article or thing and is, therefore, eligible for additional depreciation.*

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(e) Terminal depreciation [Section 33(10)]: In case of any tangible asset of power concern as covered under section 33(2) above, the difference between the WDV and the moneys payable including the scrap value, if any, shall be allowed as deduction if –

- such asset is sold, discarded, demolished or destroyed in the tax year (other than the tax year in which it is first put into use),
- the moneys payable together with the amount of scrap value, if any, is less than the WDV and
- such deficiency is actually written off in the books of the assessee.



Mahapower Ltd. purchased an asset on 20.7.2022. The actual cost of the asset was ₹ 100 lakhs. Mahapower Ltd. claimed depreciation @5% on the actual cost of the asset. WDV of the asset as on 1.4.2026 is ₹ 80 lakhs. On 15.5.2026, Mahapower Ltd. sold the asset for ₹ 55 lakhs. Deduction allowed as terminal depreciation u/s 33(10) for T.Y. 2026-27 is ₹ 25 lakhs (₹ 80 lakhs - ₹ 55 lakhs) if the deficiency of ₹ 25 lakhs is actually written off in the books of Mahapower Ltd.

Meaning of certain terms

Term	Meaning
Moneys payable	In respect of any tangible asset i.e., building, machinery, plant or furniture includes — (a) any insurance, salvage or compensation moneys payable in respect thereof; (b) where the building, machinery, plant or furniture is sold, the price for which it is sold.
Sold	Includes a transfer by way of exchange or a compulsory acquisition under any law for the time being in force. However, it does not include a transfer, in a scheme of amalgamation, of any asset by the amalgamating company to the amalgamated company where the

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	amalgamated company is an Indian company or a transfer of any asset by a banking company to a banking institution in a scheme of amalgamation of such banking company with the banking institution, sanctioned and brought into force by the Central Government.

(iv) Rates of depreciation

All assets have been divided into four main categories and rates of depreciation as prescribed by Rule 25(1) read with Appendix I of the Income-tax Rules, 2026 are given below:

PART A TANGIBLE ASSETS		
I	**Buildings**	
Block 1.	Buildings which are used mainly for residential purposes except hotels and boarding houses	5%
Block 2.	Buildings which are not used mainly for residential purposes and not covered by Block (1) above and (3) below	10%
Block 3.	Buildings for installing machinery and plant forming part of water supply project or water treatment system and which is put to use for the purpose of business of providing infrastructure facilities	40%
Block 4.	Purely temporary erections such as wooden structures	40%
II	**Furniture and Fittings**	
Block 1.	Furniture and fittings including electrical fittings ["Electrical fittings" include electrical wiring, switches, sockets, other fittings and fans, etc.]	10%
III	**Plant & Machinery**	
Block 1.	Motor cars other than those used in a business of running them on hire, acquired on or after 23.8.2019 but before 1.4.2020 and put to use before 1.4.2020	30%

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Block 2.	Motor cars other than those used in a business of running them on hire, acquired or put to use on or after 1-4-1990 [Other than motor cars mentioned in Block 1 above]	15%
Block 3.	Motor buses, motor lorries and motor taxis used in a business of running them on hire, acquired on or after 23.8.2019 but before 1.4.2020 and put to use before 1.4.2020	45%
Block 4.	Motors buses, motor lorries, motor taxis used in the business of running them on hire [Other than motor cars mentioned in Block 3 above]	30%
Block 5.	Moulds used in rubber and plastic goods factories	30%
Block 6.	Aeroplanes, Aeroengines	40%
Block 7.	Specified air pollution control equipments, water pollution control equipments, solid waste control equipment and solid waste recycling and resource recovery systems	40%
Block 8.	Plant & Machinery used in semi-conductor industry covering all Integrated Circuits (ICs) (other than mentioned in Block 7 Above)	30%
Block 9.	Life saving medical equipments	40%
Block 10.	Machinery and plant, acquired and installed on or after 1.9.2002 in a water supply project or a water treatment system and which is put to use for the purpose of business of providing infrastructure facility	40%
Block 11.	Containers made of glass or plastic used as re-fills	40%
Block 12	Energy Saving Devices (as specified)	40%
Block 13.	Renewable Energy Saving Devices (as specified) including the devices specified in (i) to (iii) below	40%
	(i) Electrically operated vehicles including battery powered or fuel-cell powered vehicles	40%
	(ii) Windmills and any specially designed devices which	40%

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	run on windmills installed on or after 1.4.2014	
	(iii) Any special devices including electric generators and pumps running on wind energy installed on or after 1.4.2014	40%
Block 14.	Windmills and any specially designed devices running on windmills installed on or before 31.3.2014 and any special devices including electric generators and pumps running on wind energy installed on or before 31.3.2014	15%
Block 15.	Computers including computer software (See Note below)	40%
Block 16.	Books (annual publications or other than annual publications) owned by assessees carrying on a profession	40%
Block 17.	Books owned by assessees carrying on business in running lending libraries	40%
Block 18.	Plant & machinery (General rate)	15%
IV	**Ships**	
Block 1.	Ocean-going ships	20%
Block 2.	Vessels ordinarily operating on inland waters not covered by Block 3 below	20%
Block 3.	Speed boats operating on inland water	20%
PART B INTANGIBLE ASSETS		
Know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature, not being goodwill of a business or profession		25%



Mobile phones and EPABX are not considered as computers and hence, not eligible for 40% rate of depreciation while computer accessories such as UPS, printers' scanners, etc. are eligible for 40% rate of depreciation. [CIT v. BSES Yamuna Powers Ltd (2013) 358 ITR 47 (Delhi)/ CIT v. Orient Ceramics and Industries Ltd. (2013) 358 ITR 0049 (Delhi)/ Federal Bank Ltd. v. ACIT (2011) 332 ITR 319 (Kerala)]

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Note: Students should refer to Income-tax Rules, 2026 for the detailed classification of assets under Rule 25 and the rate of depreciation applicable thereto.

(v) Increased rate of depreciation for certain assets [Rule 25(7)]

Where any new machinery or plant is installed during the tax year, for the purposes of business of manufacture or production of any article or thing and such article or thing -

a. is manufactured or produced by using any technology (including any process) or other know-how developed in, or

b. is an article or thing invented in,

a laboratory owned or financed by the Government or a laboratory owned by a public sector company or a University or an institution recognised in this behalf by the Secretary, Department of Scientific and Industrial Research, Government of India, such plant or machinery shall be treated as a part of block of assets qualifying for depreciation at the rate of 40 per cent of written down value

Conditions to be fulfilled:

1. The right to use such technology (including any process) or other know-how or to manufacture or produce such article or thing has been acquired from the owner of such laboratory or any person deriving title from such owner.
2. The return filed by the assessee for any tax year in which the said machinery is acquired, should be accompanied by a certificate from the Secretary, Department of Scientific and Industrial Research, Government of India to the effect that such article or thing is manufactured or produced by using such technology (including any process) or other know-how developed in such laboratory or such article or thing has been invented in that laboratory.
3. The machinery or plant is not used for the purpose of business of manufacture or production of any article or thing specified in the Schedule XIII.

The depreciation ordinarily allowable to an assessee in respect of any block of assets shall be calculated at the above specified rates on the WDV of such block of

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assets as are used for the purposes of the business or profession of the assessee at any time during the tax year.

ILLUSTRATION 2

XYZ (P) Ltd., engaged in manufacturing business since 2016, furnishes the following particulars:

	Particulars	***₹***
(1)	*Opening WDV of plant and machinery as on 1.4.2026*	*30,00,000*
(2)	*New plant and machinery purchased and put to use on 08.06.2026*	*20,00,000*
(3)	*New plant and machinery acquired and put to use on 15.12.2026*	*8,00,000*
(4)	*Computer acquired and installed in the office premises on 2.1.2027*	*3,00,000*

Compute the amount of depreciation and additional depreciation as per the Income-tax Act, 2025 for the T.Y. 2026-27. Assume that all the assets were purchased by way of account payee cheque and that the company does not opt for section 200.

SOLUTION

Computation of depreciation and additional depreciation for T.Y. 2026-27

Particulars	**Plant & Machinery (15%) (₹)**	**Computer (40%) (₹)**
Normal depreciation		
♦ @ 15% on ₹ 50,00,000 **[See Working Notes 1 & 2]**	7,50,000	-
♦ @ 7.5% (50% of 15%, since put to use for less than 180 days) on ₹ 8,00,000	60,000	-
♦ @ 20% (50% of 40%, since put to use for less than 180 days) on ₹ 3,00,000	-	60,000

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Additional Depreciation		
♦ @ 20% on ₹ 20,00,000 (new plant and machinery put to use for more than 180 days)	4,00,000	-
♦ @10% (50% of 20%, since put to use for less than 180 days) on ₹ 8,00,000	80,000	-
Total depreciation	**12,90,000**	**60,000**

Working Note:

Computation of written down value of Plant & Machinery

Particulars	Plant & Machinery (₹)	Computer (₹)
Written down value as on 1.4.2026	30,00,000	-
Add: Plant & Machinery purchased on 08.6.2026 (put to use for more than 180 days)	20,00,000	-
Add: Plant & Machinery acquired on 15.12.2026 (put to use for less than 180 days)	8,00,000	-
Computer acquired and installed in the office premises (put to use for less than 180 days)	-	3,00,000
Written down value as on 31.03.2027	**58,00,000**	**3,00,000**

Composition of plant and machinery included in the WDV

Particulars	Plant & Machinery (₹)	Computer (₹)
Plant and machinery put to use for 180 days or more [₹ 30,00,000 (WDV) + ₹ 20,00,000 (purchased on 8.6.2026)]	50,00,000	
Plant and machinery put to use for less than 180 days	8,00,000	-
Computers put to use for less than 180 days	-	3,00,000
	58,00,000	3,00,000

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Notes:

1. As per section 33(4) and 33(9)(b), where an asset acquired during the tax year is put to use for less than 180 days in that tax year, the amount of deduction allowable as normal depreciation and additional depreciation would be restricted to 50% of amount computed in accordance with the prescribed percentage.

   Therefore, normal depreciation on plant and machinery acquired and put to use on 15.12.2026 and computer acquired and installed on 02.01.2027, is restricted to 50% of 15% and 40%, respectively. The additional depreciation on the said plant and machinery is restricted to ₹ 80,000, being 10% (i.e., 50% of 20%) of ₹ 8 lakh.

2. As per section 33(9)(b), the balance additional depreciation of ₹ 80,000 being 50% of ₹ 1,60,000 (20% of ₹ 8,00,000) would be allowed as deduction in the T.Y.2027-28 if XYZ (P) Ltd. does not opt for the provisions of section 200.

3. As per section 33(8), additional depreciation is allowable, in the case of any new machinery or plant acquired by an assessee engaged, *inter alia,* in the business of manufacture or production of any article or thing, @20% of the actual cost of such machinery or plant.

   However, the new machinery or plant should not be installed in any office premises or any residential accommodation, including accommodation in the nature if a guest house.

   Accordingly, additional depreciation is not allowable on computer installed in the office premises.

ILLUSTRATION 3

A newly qualified Chartered Accountant, Mr. Dhaval, commenced practice and has acquired the following assets in his office during T.Y. 2026-27 at the cost shown against each item. Calculate the amount of depreciation that can be claimed from his professional income for T.Y.2026-27. Assume that all the assets were purchased by way of account payee cheque.

Sl. No.	Description	Date of acquisition	Date when put to use	Amount ₹
1.	Computer including computer software	27 Sept., 26	1 Oct., 26	35,000

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2.	*Computer UPS*	*2 Oct., 26*	*8 Oct., 26*	*8,500*
3.	*Computer printer*	*1 Oct., 26*	*1 Oct., 26*	*12,500*
4.	*Books (of which books being annual publications are of ₹ 12,000)*	*1 Apr., 26*	*1 Apr., 26*	*13,000*
5.	*Office furniture (Acquired from a practising C.A.)*	*1 Apr., 26*	*1 Apr., 26*	*3,00,000*
6.	*Laptop*	*26 Sep., 26*	*8 Oct., 26*	*43,000*

SOLUTION

Computation of depreciation allowable for T.Y.2026-27

Asset		Rate	Depreciation
Block 1	Furniture **[See working note below]**	10%	30,000
Block 2	Plant (Computer including computer software, computer UPS, laptop, computer printer & books)	40%	34,500
Total depreciation allowable			**64,500**

Working Notes:

Computation of depreciation

Block of Assets	₹
Block 1: Furniture – [Rate of depreciation - 10%]	
Put to use for more than 180 days [₹ 3,00,000@10%]	**30,000**
Block 2: Plant [Rate of depreciation - 40%]	
(a) Computer including computer software (put to use for more than 180 days) [₹ 35,000@40%]	14,000
(b) Computer UPS (put to use for less than 180 days) [₹ 8,500@20%] **[See Note below]**	1,700
(c) Computer Printer (put to use for more than 180 days) [₹ 12,500@40%]	5,000
(d) Laptop (put to use for less than 180 days) [₹ 43,000@20%] **[See Note below]**	8,600

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(e) Books (being annual publications or other than annual publications) (Put to use for more than 180 days) [₹ 13,000@40%]	5,200
	34,500

Note - *Where an asset is acquired by the assessee during the tax year and is put to use for the purposes of business or profession for a period for less than 180 days in that tax year, the deduction on account of depreciation would be restricted to 50% of the prescribed rate. In this case, since Mr. Dhaval commenced his practice in the T.Y. 2026-27 and acquired the assets during the same year, the restriction of depreciation to 50% of the prescribed rate would apply to those assets which have been put to use for less than 180 days in that year, namely, laptop and computer UPS.*

(vi) Depreciation in case of succession of firm/sole proprietary concern by a company or business reorganization, amalgamation or demerger of companies or succession of business otherwise than on death

As per section 33(5), depreciation allowable in the hands of

- predecessor and the successor in case of succession of firm/ sole proprietary concern by a company fulfilling the conditions mentioned in section 70(1)(zd) or (zf) or
- predecessor company and successor LLP in case of conversion of a private company or an unlisted public company into an LLP fulfilling the conditions mentioned in section 70(1)(ze) or
- predecessor and the successor in case of succession of business otherwise than on death
- amalgamating/ amalgamated company or demerged or resulting company in case of amalgamation or demerger of companies

shall not exceed the amount of depreciation calculated at the prescribed rates as if the succession, business reorganization, amalgamation or demerger had not taken place.

It is also provided that such amount of depreciation shall be allowed on *pro rata* basis based on **number of days for which the assets were used by them**.

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ILLUSTRATION 4

Sai Ltd. has a block of assets carrying 15% rate of depreciation, whose WDV as on 1.4.2026 was ₹ 40 lakhs. It purchased another asset (second-hand plant and machinery) of the same block on 01.11.2026 for ₹ 14.40 lakhs and put to use on the same day. Sai Ltd. was amalgamated with Shirdi Ltd. with effect from 01.01.2027.

You are required to compute the depreciation allowable to Sai Ltd. & Shirdi Ltd. for the tax year 2026-27 assuming that the assets were transferred to Shirdi Ltd. at ₹ 60 lakhs. Also assume that the plant and machinery were purchased by way of account payee cheque.

SOLUTION

Statement showing computation of depreciation allowable to Sai Ltd. & Shirdi Ltd. for T.Y. 2026-27

Particulars		₹
Opening WDV as on 1.4.2026		40,00,000
Addition during the T.Y. 2026-27 (used for less than 180 days)		14,40,000
Total		**54,40,000**
Depreciation on ₹ 40,00,000 @15%		6,00,000
Depreciation on ₹ 14,40,000 @7.5%		1,08,000
Total depreciation for the T.Y. 2026-27		**7,08,000**
Apportionment between two companies:		
(a)	Amalgamating company, Sai Ltd.	
	₹ 6,00,000 × 275/365	4,52,055
	₹ 1,08,000 × 61/151	43,629
		4,95,684
(b)	Amalgamated company, Shirdi Ltd.	
	₹ 6,00,000 × 90/365	1,47,945
	₹ 1,08,000 × 90/151	64,371
		2,12,316

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Notes:

(i) The aggregate deduction, in respect of depreciation allowable to the amalgamating company and amalgamated company in the case of amalgamation shall not exceed in any case, the deduction calculated at the prescribed rates as if the amalgamation had not taken place. Such deduction shall be allowed on *pro rata* basis based on **number of days for which the assets were used by them**.

(ii) The price at which the assets were transferred, i.e., ₹ 60 lakhs, has no implication in computing eligible depreciation.

(vii) Hire purchase

In the case of assets under the hire purchase system the allowance for depreciation would under *Circular No. 9 of 1943 R. Dis. No. 27(4) I.T. 43 dated 23-3-1943*, be granted as follows:

- In every case of payment purporting to be for hire purchase, production of the agreement under which the payment is made would be insisted upon by the department.
- Where the effect of an agreement is that the ownership of the asset is at once transferred on the lessee, the transaction should be regarded as one of purchase by instalments and consequently no deduction in respect of the hire amount should be made. This principle will be applicable in a case where the lessor obtains a right to sue for arrears of installments but has no right to recover the asset back from the lessee. Depreciation in such cases should be allowed to the lessee on the hire purchase price determined in accordance with the terms of hire purchase agreement.
- Where the terms of an agreement provide that the asset shall eventually become the property of the hirer or confer on the hirer an option to purchase an asset, the transaction should be regarded as one of hire purchase. In such case, periodical payments made by the hirer should for all tax purposes be regarded as made up of
  - (i) the consideration for hirer which will be allowed as a deduction in assessment, and
  - (ii) payment on account of the purchase price, to be treated as capital outlay and depreciation being allowed to the lessee on the initial value

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namely, the amount for which the hired assets would have been sold for cash at the date of the agreement.

The allowance to be made in respect of the hire should be the amount of the difference between the aggregate amount of the periodical payments under the agreement and the initial value as stated above. The amount of this allowance should be spread over the duration of the agreement evenly. If, however, agreement is terminated either by outright purchase of the asset or by its return to the seller, the deduction should cease as from the date of termination of agreement.

For the purpose of allowing depreciation, an assessee claiming deduction in respect of the assets acquired on hire purchase would be required to furnish a certificate from the seller or any other suitable documentary evidence in respect of the initial value or the cash price of the asset.

In cases where no such certificate or other evidence is furnished the initial value of the assets should be arrived at by computing the present value of the amount payable under the agreement at an appropriate per centum.

For the purpose of allowing depreciation the question whether in a particular case the assessee is the owner of the hired asset or not is to be decided on a consideration of all the facts and circumstances of each case and the terms of the hire purchase agreement. Where the hired asset is originally purchased by the assessee and is registered in his name, the mere fact that the payment of the price is spread over the specified period and is made in installments to suit the needs of the purchaser does not disentitle the assessee from claiming depreciation in respect of the asset, since the assessee would be the real owner although the payment of purchase price is made subsequent to the date of acquisition of the asset itself.

(viii) Carry forward and set-off of depreciation [Section 33(11)]

Section 33(11) provides for carry forward of unabsorbed depreciation. Where the profits and gains chargeable for the tax year before allowing the depreciation is less than such allowable depreciation, then

- if such profits and gains is not a loss, the deduction for depreciation shall be allowed to the extent of the available profits and gains

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- if such profits and gains is a loss, no deduction for depreciation shall be allowed.

The depreciation which has not been allowed, i.e., the unabsorbed depreciation shall be added to the allowable depreciation for the succeeding tax year and total amount shall be deemed to be eligible for deduction in that year and so on for succeeding tax years. The effect of this provision is that the unabsorbed depreciation shall be carried forward indefinitely till it is fully set off.



Profits and gains from business or profession of Mr. X for T.Y. 2026-27, before charging depreciation of ₹ 20 lakhs, was ₹ 16 lakhs. In such a case, after setting off the depreciation, the unabsorbed depreciation of T.Y. 2026-27 would be ₹ 4 lakhs. If profits and gains of business or profession for T.Y. 2027-28 before depreciation is ₹ 11 lakhs and depreciation allowance u/s 33 for the said tax year is ₹ 5 lakhs, then, the unabsorbed depreciation of ₹ 4 lakhs for the T.Y. 2026-27 would be added to the depreciation allowance of ₹ 5 lakhs. Consequently, ₹ 9 lakhs would be allowed to be set off against the profits of ₹ 11 lakhs and the taxable profits for T.Y. 2027-28 would be ₹ 2 lakhs.

Order of set-off

However, in the order of set-off of losses under different heads of income, effect shall first be given to current year depreciation then brought forward business losses (including loss from speculation business) and only then to unabsorbed depreciation.

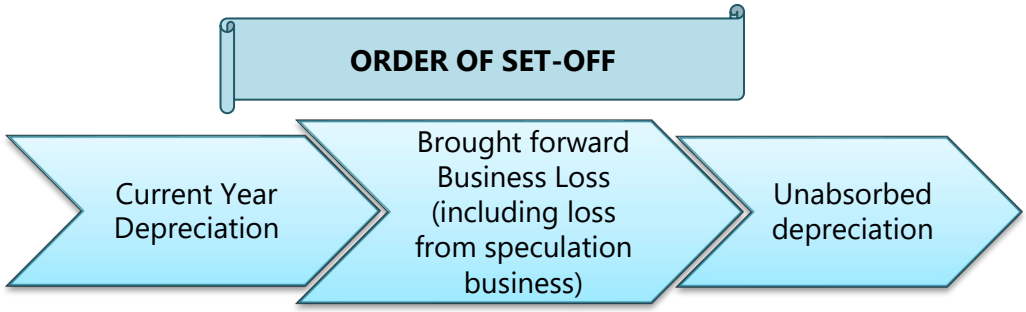
The provisions in effect are as follows:

- Since the unabsorbed depreciation forms part of the current year's depreciation, it can be set off against any other head of income except "Salaries".
- The unabsorbed depreciation can be carried forward for indefinite number of tax years.
- Set-off will be allowed even if the same business to which it relates is no longer in existence in the year in which the set-off takes place.

Current depreciation to be deducted first - The Supreme Court, in *CIT v. Mother India Refrigeration (P.) Ltd. [1985] 23 Taxman 8,* has categorically held that current depreciation must be deducted first before deducting the unabsorbed carried

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forward business losses of the earlier years in giving set off while computing the total income of any particular year.



(ix) Actual Cost [Section 39]

(a) Actual cost of an asset: The actual cost of an asset used for the purposes of the business or profession means the actual cost to the assessee, as reduced by the following amounts:

- part of cost of asset, if any, met by any other person or authority, directly or indirectly
- GST paid in respect of which credit of input tax has been claimed and allowed under the relevant law
- excise duty or additional duty leviable u/s 3 of the Customs Tariff Act, 1975 in respect of which a claim of credit has been made and allowed under the Central Excise Rules, 1944
- subsidy, grant or reimbursement, by whatever name called, if any, relatable to the acquisition of the asset, received, directly or indirectly, by the assessee from
  - the Central Government
  - a State Government
  - any authority established under any law or
  - any other person

(b) Proportionate amount if the subsidy, grant or reimbursement is not directly related to the asset acquired: In a case where the subsidy, grant or reimbursement referred in above diagram is not directly relatable to the asset acquired, the amount of reduction shall be :

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$$A \times \left(\frac{B}{C} \right)$$

where,

A = total amount of subsidy, grant or reimbursement not directly relatable to the asset;

B = cost of the asset acquired for which actual cost is to be determined;

C = cost of all the assets in respect of or in reference to which the subsidy or grant or reimbursement is so received.



ICDS VII requires Government grants relatable to depreciable assets to be reduced from actual cost of the asset/WDV of the block of asset. It further provides that where the Government grant is not directly relatable to the asset acquired, then a pro-rata reduction of the amount of grant should be made in the same proportion as such asset bears to all assets with reference to which the Government grant is so received.

(c) Payment exceeding ₹ 10,000 made in a day otherwise than by specified banking or online mode not included actual cost: The payment or aggregate of payment exceeding ₹ 10,000 in a day for acquisition of an asset or part thereof, made to a person in a mode otherwise than by specified banking or online mode, shall be excluded from the actual cost of that asset.

Meaning of "Specified Banking or Online Mode" [Section 66(32)]

Specified Banking or Online Mode mean transaction by

- an account payee cheque or
- an account payee bank draft or
- use of electronic clearing system through a bank account or
- through such other electronic mode, as may be prescribed.

As per Rule 48 of the Income-tax Rules, 2026, "other electronic modes of payment" are the following:

- Credit Card;
- Debit Card;
- Net Banking;

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- IMPS (Immediate Payment Service);
- UPI (Unified Payment Interface);
- RTGS (Real Time Gross Settlement);
- NEFT (National Electronic Funds Transfer);
- BHIM (Bharat Interface for Money) Aadhaar Pay, and
- Tier-III: Full KYC Central Bank Digital Currency wallets, P-CBDC, Wholesale/Cross-border CBDC.

(d) Actual cost in certain special situations [Section 39(4)]

S. No.	Specified circumstances	Actual cost to the assessee
1.	Where capital asset is transferred by the amalgamating company to the amalgamated Indian company in a scheme of amalgamation	Actual cost to the amalgamated company will be taken the same as it would have been if the amalgamating company had continued to hold such capital asset for the purposes of its own business.
2.	Where capital asset is transferred by a demerged company to the resulting Indian company in a demerger	Actual cost to resulting company shall be taken the same as it would have been if the demerged company had continued to hold such capital asset for the purpose of its own business. The actual cost shall not exceed the WDV of such capital asset in the hands of the demerged company.
3.	Where inventory is converted or treated as a capital asset	Fair market value of such inventory as on the date of its conversion into capital asset, as determined in the prescribed manner
4.	Where asset is acquired by the assessee by way of gift or inheritance	Actual cost to the previous owner *minus* depreciation allowable as if such asset was the only asset in the relevant block of assets.

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		Further, any expenditure incurred by the assessee such as expenditure on freight, installation etc. of such asset would also be includible in the actual cost.
5.	Where a building being the property of the assessee, is put to use for the purpose of business or profession during the tax year	Actual cost of the building as reduced by the depreciation – ♦ that would have been allowable had the building been used for the purpose of business or profession from the date of acquisition and ♦ calculated at the rates in force on the date on which such asset was put to use for the purpose of business or profession.
6.	Where capital asset is transferred by - a holding company to its wholly owned Indian subsidiary company or - a subsidiary company to its 100% holding company, being an Indian company	Actual cost to the transferee company shall be taken to be the same as it would have been if the transferor company had continued to hold such asset for the purposes of its own business.
7.	Where an asset, which previously belonged to the assessee and had been used by him for the purposes of his business or profession, is re-acquired by the assessee	(a) actual cost of the asset in the hands of assessee, when it was first acquired *minus* depreciation allowable to the assessee as if asset was the only asset in the relevant block of assets; or

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		(b) the actual price for which such asset is re-acquired by the assessee, whichever is lower
8.	Where an asset is acquired by the assessee from previous owner and subsequently asset is given back to the previous owner by way of lease, hire or otherwise and the asset was being used for the purpose of business or profession by the previous owner and depreciation has been claimed by the previous owner	Actual cost of the asset shall be the written down value of the said asset in the hands of the previous owner at the time of transfer by the previous owner.
9.	Where an asset is used in business after it ceases to be used for scientific research related to that business and a deduction is allowable u/s 33(3).	Actual cost of the asset as reduced by deduction allowed for the capital asset u/s 45(1)(a)(i) of the Income-tax Act, 2025 or u/s 35(1)(iv) of the Income-tax Act, 1961. ***Note -*** *Actual cost of such asset would be Nil as already 100% deduction would have been claimed under above mentioned sections 45(1)(a)(i) / 35(1)(iv)*
10.	Where the assessee had acquired an asset outside India, as a non- resident, and the asset is brought by him to India and put to use in his business or profession in India.	Actual cost of the asset as reduced by the depreciation ♦ that would have been allowable had the asset been used for the purpose of business or profession in India since the date of its acquisition and ♦ calculated at the rate in force

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11.	Where capital asset is acquired under the scheme of corporatisation of a recognised stock exchange approved by the SEBI ***Note:*** *Under the scheme of corporatization, recognised stock exchange gets converted into 'Company' from the status of being 'Association of persons' or 'Body of Individuals'.*	Actual cost of the asset, as if there was no corporatisation.
12(a)	Where deduction u/s 46 (capital expenditure of specified business) was allowed or allowable in respect of the capital asset (i) to the assessee; or (ii) to any person and the assessee acquires or receives such asset through special modes of acquisition from such person.	Actual cost shall be deemed to be nil.
	As per section 39(7), special modes of acquisition mean acquisition: (a) by way of a gift or will or an irrevocable trust or (b) upon distribution on the liquidation of a company or (c) by way of distribution of capital assets on total or partial partition of a HUF or (d) by way of any transfer of a capital asset by a holding company to its 100% subsidiary company, being an Indian company or (e) by way of any transfer of a capital asset by a subsidiary company to its 100% holding company, being an Indian company or (f) by way of any transfer of a capital asset by the amalgamating company to an amalgamated company in a scheme of	

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	amalgamation, if the amalgamated company is an Indian company or (g) by way of any transfer of a capital asset by the demerged company to the resulting company in a scheme of demerger, if the resulting company is an Indian company or (h) by way of any transfer of a capital asset or intangible asset by a firm to a company as a result of succession of the firm by a company in the business carried on by the firm (fulfilling the conditions prescribed) or (i) by way of any transfer of a capital asset or intangible asset by a private company or unlisted public company to a LLP as a result of conversion of the company into LLP (fulfilling the conditions prescribed) or (j) by way of any transfer of a capital asset or intangible asset by a sole proprietary concern to a company, where the sole proprietary concern is succeeded by a company (fulfilling the conditions specified).	
12(b)	Where deduction allowed u/s 46 in respect of a capital asset becomes deemed income as per section 46(9)(b) [on account of being used for a purpose other than specified business u/s 46].	Actual cost of the asset as reduced by the depreciation, ♦ that would have been allowable had the asset been used for the purpose of business since date of acquisition; and ♦ calculated at the rate in force
13.	Where any amount is paid or payable as interest in connection with the acquisition of an asset.	Actual cost shall not include so much of interest as is relatable to any period after such asset is first put to use.

(e) Acquisition of assets with the main purpose to reduce tax liability [Section 39(5) and 39(6)]

Where the asset is acquired by the assessee and before such acquisition, the asset was used by any other person for the purposes of his business and the Assessing Officer is satisfied that the main purpose of the transfer of the

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asset, directly or indirectly, was to reduce tax liability (by claiming depreciation with reference to an enhanced cost) , the actual cost of such asset shall be such an amount as may be determined by the Assessing Officer, having regard to all the circumstances of the case.

The determination of actual cost by the Assessing Officer shall be made with prior approval of the Joint Commissioner.

Provisions of this section shall apply irrespective of anything contained in the circumstances discussed above in section 39(4), except the case discussed at Sl. No. 8.

(x) Written down value [Section 41]

For the purposes of computation of income under the head "Profits and gains of business or profession", written down value means the following -

Situation	Amount of WDV
If the asset is acquired in the tax year	the actual cost to the assessee
If the asset is acquired before the tax year	Actual cost to the assessee less depreciation actually allowed under Income-tax Act 2025 or under Income-tax Act, 1961. Any depreciation carried forward u/s 33(11) is deemed to be depreciation actually allowed [Section 41(8)].
In case of block of assets	The written down value of block of assets shall be: [(A-D) + B – C] - E

(A)	W.D.V. of the block of assets in the immediately preceding tax year (T.Y. 2025-26)	xxx
(D)	Less: Depreciation actually allowed in respect of that block of assets in relation to the said immediately preceding tax year (i.e., in T.Y. 2025-26)	xxx

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Opening balance as on 1st April of the current T.Y. (i.e., on 1.4.2026)		xxx
Increased by		
(B)	Actual cost of any asset falling within that block, acquired during the tax year (i.e., T.Y. 2026-27)	xxx
Reduced by		
(C)	Money payable together with scrap value, if any, in respect of any asset falling within the block which is sold, transferred, demolished, destroyed or discarded during the tax year. However, such amount cannot exceed the amount in (A-D) + B.	xxx
(E)	**In case of slump sale**, actual cost of the asset (-) depreciation allowable under the Income-tax Act, 2025 or under the Income-tax Act, 1961 as if such asset was the only asset in the relevant block of asset.	xxx
W.D.V at the end of the year (i.e., as on 31.3.2026) on which depreciation is allowable		xxx

Where block of assets is transferred by a holding company its wholly owned Indian subsidiary company or by a subsidiary company to its 100% holding company, being an Indian company or by amalgamating company to amalgamated Indian company	the actual cost of the block of assets in the hands of transferee company or amalgamated company, as the case may be, shall be the same as WDV of the block of assets as in the case of the transferor company or amalgamating company in the immediately preceding tax year as reduced by depreciation actually allowed in respect of that block of asset in relation to that tax year.
Where block of assets is transferred by a demerged company to a resulting company	the written down value of the block of assets of the demerged company for the immediately preceding year shall be reduced by the written down value of the

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	assets transferred to the resulting company.
	the written down value of the block of assets for resulting company shall be the written down value of the assets transferred from the demerged company immediately before such demerger.
Where block of assets is transferred by a private company or unlisted public company to a LLP and the conditions in section 70(1)(ze) are satisfied	the actual cost of the block of assets in the hands of successor LLP shall be the written down value in the hands of said company as on the date of conversion of the company into LLP.
Where block of assets is transferred to a company by a recognised stock exchange in India under a scheme for corporatization approved by the SEBI	the written down value of the block of assets in the hands of such company shall be the written down value of the assets transferred immediately before such transfer.
In the case of a succession in business or profession otherwise than on death, where an assessment is made in the hands of successor under section 313(2)	the written down value of any asset or block of assets shall be the amount which would have been taken as its written down value, if the assessment had been made directly on the person succeeded to.
	Tapan succeeded his father's business due to retirement of his father. The WDV of the assets in the hands of Tapan would be the WDV of the assets in the hands of his father

(xi) Depreciation provided in the books of account deemed to be depreciation actually allowed

Section 33 provides that depreciation shall be allowed at the prescribed percentage on the written down value (WDV) of any block of assets. Section 41 provides that written down value in the case of assets acquired before the tax year means the

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actual cost to the assessee *less* all depreciation actually allowed to him under the Income-tax Act, 2025 or the Income-tax Act, 1961.

Persons who were exempt from tax were not required to compute their income under the head "Profits and gains of business or profession". However, when the exemption is withdrawn subsequently, such persons became liable to income-tax and hence, were required to compute their income for income-tax purposes. In this regard, a question arises as to the basis on which depreciation is to be allowed in respect of assets acquired during the years when the person was exempt from tax.

Accordingly, section 41(9) provides that where an assessee was not required to compute his total income for the purposes of this Act for any tax year or tax years preceding the tax year under consideration,-

(a) the actual cost of an asset has to be adjusted by the amount attributable to the revaluation of such asset, if any, in the books of account;

(b) the total amount of depreciation on such asset provided in the books of account of the assessee in respect of such tax year or years preceding the tax year under consideration shall be deemed to be the depreciation actually allowed under the Act and

(c) the depreciation actually allowed as above has to be adjusted by the amount of depreciation attributable to such revaluation of the asset.

(xii) Composite Income

Section 41(10) provides that where the income of an assessee is derived, in part from agriculture and in part from business chargeable to income-tax under the head "Profits and gains of business or profession", for computing the written down value of assets acquired before the tax year, the total amount of depreciation shall be computed as if the entire income is derived from the business of the assessee under the head "Profits and gains of business or profession" and the depreciation so computed shall be deemed to be the depreciation actually allowed under the Income-tax Act, 2025 or under the Income-tax Act, 1961.

Rule 271 prescribes the taxability of income from the manufacture of tea. Under the said Rule, income derived from the sale of tea grown and manufactured by seller shall be computed as if it were income derived from business, and 40% of such income shall be deemed to be income liable to tax.

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If the turnover is, say, ₹ 20 lakh, the depreciation ₹ 1 lakh and other expenses ₹ 4 lakh then, the income would be ₹ 15 lakh. Business income would be ₹ 6 lakh (being 40% of ₹ 15 lakh). In this case, ₹ 1 lakh, being the amount of depreciation would be deemed to have been actually allowed.

Accordingly, the WDV is required to be computed by deducting the full depreciation attributable to composite income i.e., ₹ 1 lakh.

ILLUSTRATION 5

Lights and Power Ltd., engaged in the business of generation of power, furnishes the following particulars pertaining to T.Y. 2026-27. Compute the depreciation allowable under section 33 for T.Y.2026-27 and the opening balance of written down value of the block of assets as on 01.04.2027, while computing his income under the head "Profits and gains of business or profession". The company has opted for the depreciation allowance on the basis of written down value. Assume that all the assets were purchased by way of account payee cheque and that the company has not opted for the special tax regimes under section 200 or under section 201.

	Particulars	***(₹)***
1.	*Opening Written down value of Plant and Machinery (15% block) as on 01.04.2026 (Purchase value ₹ 8,00,000)*	*5,78,000*
2.	*Purchase of second hand machinery (15% block) on 29.12.2026 for business purpose*	*2,00,000*
3.	*Machinery Y (15% block) purchased and installed on 12.07.2026 for the purpose of power generation*	*8,00,000*
4.	*Acquired and installed for use a new air pollution control equipment on 31.7.2026*	*2,50,000*
5.	*New air conditioner purchased and installed in office premises on 8.9.2026*	*3,00,000*
6.	*New machinery Z (15% block) acquired and installed on 23.11.2026 for the purpose of generation of power*	*3,25,000*
7.	*Sale value of an old machinery X, sold during the year (Purchase value ₹ 4,80,000, WDV as on 01.04.2026 ₹ 3,46,800)*	*3,10,000*

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SOLUTION

Computation of depreciation allowance under section 33 for the T.Y. 2026-27

Particulars	(₹)	Plant and Machinery (15%) (₹)	Plant and Machinery (40%) (₹)
Opening WDV as on 01.04.2026		5,78,000	-
Add: Plant and Machinery acquired during the year			
- Second hand machinery	2,00,000		
- Machinery Y	8,00,000		
- Air conditioner for office	3,00,000		
- Machinery Z	3,25,000	16,25,000	-
- Air pollution control equipment		-	2,50,000
		22,03,000	2,50,000
Less: Asset sold during the year		3,10,000	Nil
Written down value as on 31.3.2027 before charging depreciation		18,93,000	2,50,000
Normal depreciation			
40% on air pollution control equipment (₹ 2,50,000 x 40%)		-	1,00,000
Depreciation on plant and machinery put to use for less than 180 days@ 7.5% (i.e., 50% of 15%)			
♦ Second hand machinery (₹ 2,00,000 × 7.5%)	15,000		
♦ **Machinery Z (₹ 3,25,000 × 7.5%)**	**24,375**	**39,375**	

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15% on the balance WDV being put to use for more than 180 days (₹ 13,68,000 × 15%)		2,05,200	
Additional depreciation			
♦ Machinery Y (₹ 8,00,000 × 20%)	1,60,000		
♦ Machinery Z (₹ 3,25,000 × 10%, being 50% of 20%)	32,500	1,92,500	-
♦ Air pollution control equipment (₹ 2,50,000× 20%)		-	50,000
Total depreciation		**4,37,075**	**1,50,000**
WDV as on 1.4.2027 [WDV of T.Y. 2026-27 *less* depreciation for that year]		**14,55,925**	**1,00,000**

Notes:

(i) Power generation equipments qualify for claiming additional depreciation in respect of new plant and machinery.

(ii) Additional depreciation is not allowed in respect of second hand machinery and air conditioner installed in office premises.

(iii) The balance 50% additional depreciation in respect of Machinery Z of ₹ 32,500 (10% x ₹ 3,25,000) can be claimed as deduction in the subsequent tax year i.e., T.Y. 2027-28.

(xiii) Balancing Charge

Section 38(1)(b) read with section 38(2)(b) provides for the manner of calculation of the amount which shall be chargeable to income-tax as income of the business of the tax year in which the moneys payable for the tangible asset on which depreciation has been claimed and allowed under section 33(2), i.e., in the case of power undertakings, becomes due.

The balancing charge will be computed where any tangible asset which is owned by the assessee is sold, discarded, demolished or destroyed and the moneys payable for such asset, together with the scrap value exceeds the written down

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value of such assets. The balancing charge amount will be –

- moneys payable for such asset together with the scrap value - WDV of such assets, where the moneys payable for such asset together with the scrap value < the actual cost of such asset
- Actual cost of such asset – WDV of such asset, in any other case.

Section 38(5) makes it clear that the provisions of section 38(1)(b) shall apply in a tax year even if the business is no longer in existence.



Mahapower Ltd. purchased an asset on 20.7.2022. The actual cost of the asset was ₹ 100 lakhs. Mahapower Ltd. claimed depreciation @5% on the actual cost of the asset. WDV of the asset as on 1.4.2026 is ₹ 80 lakhs. On 15.5.2026, Mahapower Ltd. sold the asset for ₹ 90 lakhs. The balancing charge of ₹ 10 lakhs (₹ 90 lakhs - ₹ 80 lakhs) would be taxable as income u/s 38(1)(b).

Suppose, on 15.5.2026, Mahapower Ltd. sold the asset for ₹ 120 lakhs instead of ₹ 90 lakhs. The balancing charge of ₹ 20 lakhs (₹ 100 lakhs - ₹ 80 lakhs) would be taxable as income u/s 38(1)(b).

Amortisation of Preliminary Expenses [Section 44]

(i) Nature of expenditure: Section 44 provides for the amortisation of preliminary expenses incurred by Indian companies and other resident non-corporate taxpayers for the establishment of business concerns or the expansion of the business of existing concerns.

(ii) Applicable: This section applies

(a) only to Indian companies and resident non-corporate assessees,

(b) in the case of new companies to expenses incurred before the commencement of its business,

(c) in the case of extension of an existing undertaking to expenses incurred till the extension is completed,

(d) in the case of the setting up of a new unit - expenses incurred till the new unit commences production or operation.

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(iii) Amount eligible for deduction: Such preliminary expenditure incurred shall be allowed as deduction over a period of 5 years. In other words, 1/5th of such expenditure is allowable as a deduction for each of the five successive tax years beginning with the tax year in which the business commences or, the tax year in which the extension of the undertaking is completed, or the new unit commences production or operation, as the case may be.

(iv) Eligible expenses - The following expenditures are eligible for amortisation:

(I) Expenditure in connection with –

(a) the preparation of feasibility report

(b) the preparation of project report

(c) conducting market survey or any other survey necessary for the business of the assessee

(d) engineering services relating to the assessee's business

The assessee has to furnish a statement containing the particulars of above expenditure within one month prior to the due date for furnishing the return of income as specified under section 263(1) to the Director General of Income-tax (Systems) or any person authorised by him in the Form No. 5 in prescribed manner for each tax year [Rule 27].

(II) legal charges for drafting any agreement between the assessee and any other person for any purpose relating to the setting up to conduct the business of assessee.

(III) **Where the assessee is a company,** in addition to the above, expenditure incurred –

(a) by way of legal charges for drafting and printing of the Memorandum and Articles of Association of the company

(b) by way of fees for registering the company under the provisions of the Companies Act; 2013

(c) in connection with the issue, for public subscription, of the shares in or debentures of the company, being underwriting commission, brokerage and charges for drafting, typing, printing and advertisement of the prospectus; and

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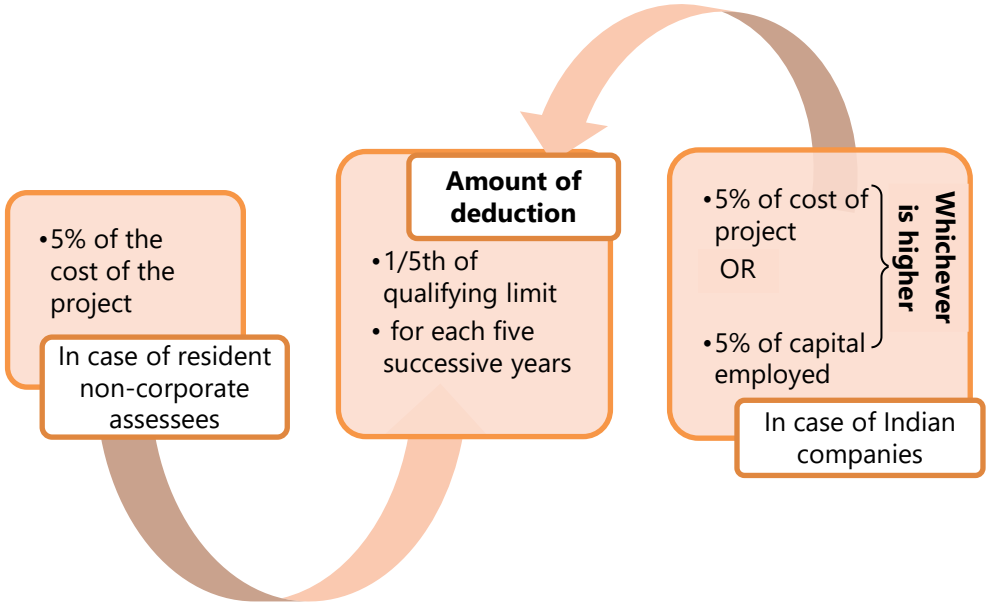
(IV) Such other items of expenditure (not being expenditure qualifying for any allowance or deduction under any other provision of the Act) as may be prescribed by the Board for the purpose of amortisation.

(v) Overall Limits - The maximum aggregate amount of the qualifying expenses that can be amortised is

In case of resident non-corporate assessee - 5% of the cost of the project

In the case of an Indian company – 5% of the cost of the project or 5% of the capital employed in the business of the company, at the option of the company.

The excess, if any, of the qualifying expenses shall be ignored.



Meaning of certain terms:

Terms	Meaning
Cost of the project	The actual cost of the fixed assets, being land, buildings, leaseholds, plant, machinery, furniture, fittings and railway sidings (including expenditure on the development of land and buildings) **(i) In case of expenses incurred before the commencement of business:** The actual cost as shown in the

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	books of the assessee as on the last day of the tax year in which the business of the assessee commences **(ii)** **In case of expenses incurred for extension of the business or setting up of a new unit:** The actual cost as shown in the books of the assessee as on the last day of the tax year in which either the extension of the undertaking is completed or, as the case may be, in so far as such fixed assets have been acquired or developed in connection with the extension of the undertaking or the setting up of the new unit.
Capital employed in the business of the company	**(i)** **In the case of new company**: The aggregate of the issued share capital, debentures and long-term borrowings as on the last day of the tax year in which the business of the company commences **(ii)** **In the case of extension of the business or the setting up of a new unit**: The aggregate of the issued share capital, debentures, and long-term borrowings as on the last day of the tax year in which the extension of the undertaking is completed or, as the case may be, the unit commences production or operation in so far as such capital, debentures and long-term borrowings have been issued or obtained in connection with the extension of the undertaking or the setting up of the new undertaking or the setting up of the new unit of the company.
Long-term borrowing	(i) Any moneys borrowed by the company from the Government or the Industrial Finance Corporation of India Limited or any other financial institution which is eligible for deduction under section 32(e) or any banking institution, or (ii) any moneys borrowed or debt incurred by it in a foreign country in respect of the purchase outside India of capital plant and machinery, where the tenure of moneys are borrowed or the debt is not less than 7 years.

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(vii) Audit of accounts: In case where the assessee is a person, other than a company or a co-operative society, the deduction would be allowable only

- if the accounts of the assessee for the year or years in which the expenditure is incurred have been audited by an Accountant before the date specified in section 63 i.e., one month prior to the due date for furnishing the return of income u/s 263(1); and
- the assessee has furnished for the first year in which the deduction is claimed, the report of such audit by such date in the prescribed form duly signed and verified by such accountant and setting forth such other particulars as may be prescribed.

Particulars	Due date of filing of return	Specified Date
Assessees (other than a company) subject to tax audit	31st October of the financial year succeeding the relevant T.Y.	30th September of the financial year succeeding the relevant T.Y.
	For T.Y.2026-27, on or before 31st October, 2027	For T.Y.2026-27, on or before 30th September, 2027.

(viii) Special provisions for amalgamation and demerger- If an undertaking of an Indian company is transferred, before the expiry of the period of five years, to another Indian company under a scheme of amalgamation, then

- no deduction will be admissible to the amalgamating company for the tax year in which the amalgamation takes place and
- the aforesaid provisions will continue to apply to the amalgamated company as they would have applied to the amalgamating company, as if the amalgamation had not taken place.

Likewise, in the scheme of demerger where the resulting company will be able to claim amortisation of preliminary expenses as if demerger had not taken

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place, and no deduction shall be allowed to the demerged company in the year of demerger.

(ix) **No other deduction under any provision of the Act:** It has been clarified that in case where a deduction under this section is claimed and allowed for any tax year in respect of any item of expenditure, the expenditure in respect of which deduction is so allowed shall not qualify for deduction under any other provision of the Act for the same or any other tax year.



Berger Paints India Ltd v. CIT (2017) 393 ITR 113 (SC)

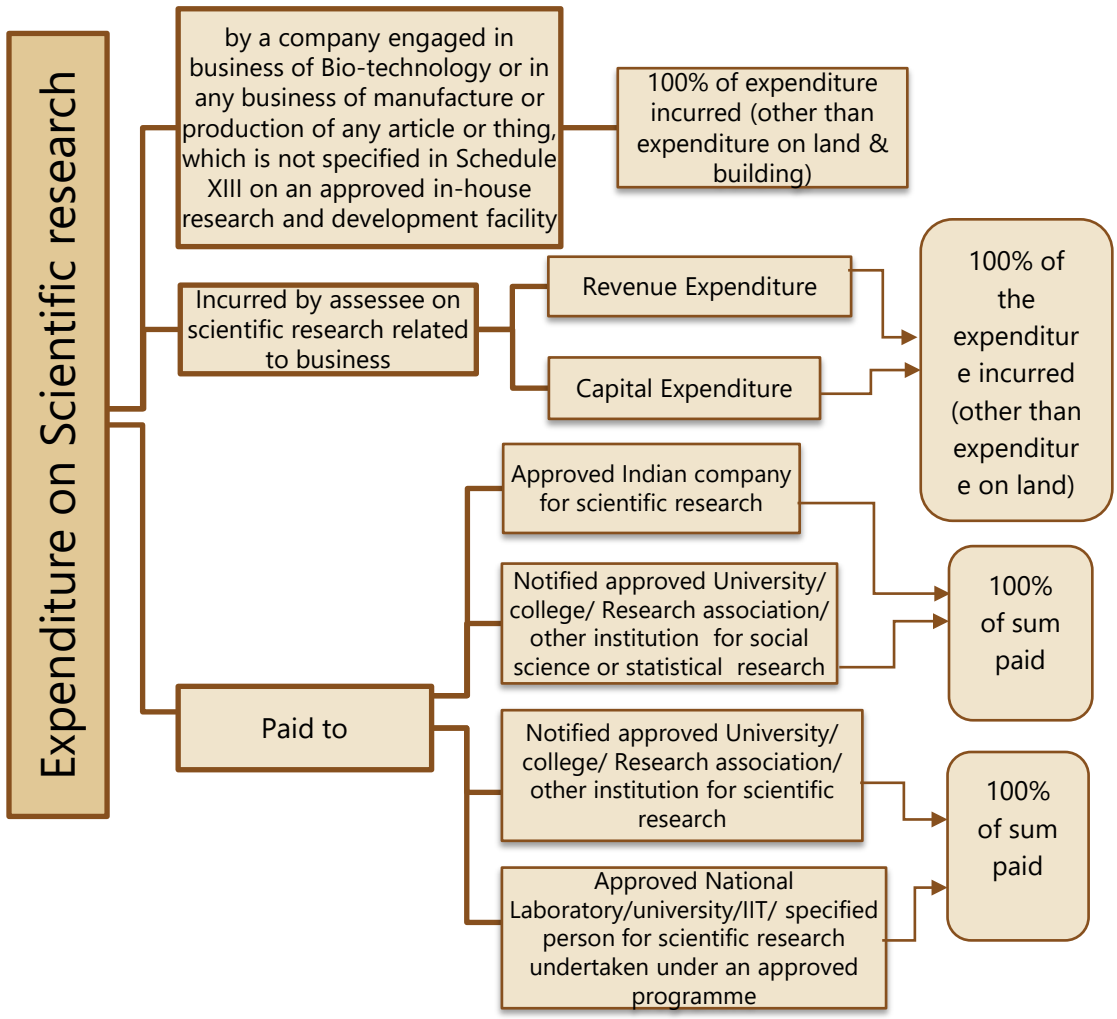
Issue: Whether "premium" on subscribed share capital is "capital employed in the business of the company" under section 44 to be eligible for a deduction?

Analysis & Decision: Share premium collected by the assessee on its subscribed issued share capital could not be part of "capital employed in the business of the company" for the purpose of section 44. If it were the intention of the legislature to treat share premium as being "capital employed in the business of the company", it would have been explicitly mentioned. Moreover, Sl. No. IV(i) in Form MGT- 7 read with section 92 of the Companies Act, 2013 dealing with capital structure of the company provides the break-up of "issued share capital" and "subscribed share capital" which does not include share premium at the time of subscription. **Hence, in the absence of the reference in section 44, share premium is not a part of the capital employed**. Also, section 52 of the Companies Act, 2013 requires a company to transfer the premium amount to be kept in a separate account called "securities premium account". **The assessee is, therefore, not entitled to claim deduction u/s 44 in relation to the premium amount received from shareholders at the time of share subscription.**

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Expenditure on Scientific Research [Section 45]

The deduction allowable under this section consists of –



Meaning of certain terms:

Term	Meaning
Scientific research	Any activities for the extension of knowledge in the fields of natural or applied science including agriculture, animal husbandry or fisheries.

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Scientific research expenditure	Expenditure incurred on scientific research would include all expenditure incurred for the prosecution or the provision of facilities for the prosecution of scientific research but does not include any expenditure incurred in the acquisition of rights in or arising out of scientific research.
Scientific research related to a business or a class of business	Scientific research related to a business or a class of business would include (i) any scientific research which may lead to or facilitate an extension of that business or all the business of that class; (ii) any scientific research of a medical nature which has a special relation to the welfare of the workers employed in that business or all the business of that class.

(I) Incurred by assessee related to his business [Section 45(1)]

(i) Revenue and capital expenditure: A deduction would be allowed for any expenditure, being in the nature of

- capital expenditure, but not on acquisition of land which is acquired as such or part of any property or
- revenue expenditure,

incurred on scientific research **related to the business of the assessee.**

(ii) Expenditure incurred on salary to research personnel and purchase of material prior to commencement of business: A deduction would also be allowed in the tax year in which the business is commenced in respect of the aggregate of expenditure (not being in the nature of capital expenditure), related to business, incurred on –

- salary to an employee engaged in such scientific research or
- purchase of materials used in such scientific research,

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where such expenditure is incurred within three years immediately preceding the commencement of business. The deduction will be limited to the extent certified by the prescribed authority as incurred on such research.

(iii) Capital Expenditure prior to commencement of business: Where any capital expenditure has been incurred prior to the commencement of the business, the aggregate of the expenditure so incurred within the three years immediately preceding the commencement of the business shall be deemed to have been incurred in the tax year in which the business is commenced and will rank for deduction as expenditure for scientific research incurred during the tax year.

(iv) Carry forward of deficiency: Capital expenditure incurred on scientific research which cannot be absorbed by the business profits of the relevant tax year shall be treated in the same manner as unabsorbed deprecation u/s 33(11) i.e., it can be carried forward to the immediately succeeding tax year and shall be treated as the allowance for that year. In effect, this means that there is no time bar on the period of carry forward. It shall be accordingly allowable for that tax year against any head of income other than salaries [Section 45(7)].

(v) No depreciation: Section 45(6) clarifies that no depreciation will be admissible on any expenditure represented wholly or partly by an asset which has been allowed as a deduction under section 45 whether in the year in which deduction under section 45 was allowed or in any other tax year.

(vi) Sale of asset representing expenditure of capital nature on scientific research: Section 38(1)(c) seeks to tax the profits arising on the sale of an asset representing expenditure of a capital nature on scientific research.

Where the asset representing expenditure of a capital nature on scientific research is sold **without having been used for other purposes**, and the sale proceeds together with the total deductions allowed under section 45(1)(a)(i) exceed the amount of capital expenditure, the excess or the amount of deduction so made, whichever is less, will be charged to tax as income of the business of the tax year in which the asset was sold.

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If capital expenditure incurred on building for scientific research in T.Y. 2026-27 is ₹ 3 lakhs, then deduction u/s 45(1)(a)(i) would have been ₹ 3 lakhs in that T.Y. If the asset is sold for ₹ 4 lakhs in T.Y.2027-28, ₹ 3 lakhs, being lower of sale proceeds of ₹ 4 lakhs together with total deduction of ₹ 3 lakhs – amount of capital expenditure of ₹ 3 lakhs and deduction u/s 45(1)(a)(i) of ₹ 3 lakhs, would be charged to tax u/s 38(1)(c) in the T.Y. 2027-28, being the year of sale.



Deduction under section 45(1) would be available to an assessee under the concessional tax regimes under section 200 to 204 as well as the regular provisions of the Act.

(II) Company engaged in Business of bio-technology or manufacturing of article or thing etc. [Section 45(2)]

A deduction would be allowed in respect of any expenditure on scientific research incurred (not being expenditure on land or building) by a company engaged in the business of

- bio-technology or
- manufacture or production of any article or thing, which is not specified in Schedule XIII

on in-house research and development facility as approved by the prescribed authority.

However, no deduction would be allowed to a company which is approved under section 45(3)(b).

"Expenditure on scientific research" in relation to drugs and pharmaceuticals shall include expenditure incurred on clinical drug trial, obtaining approval from any regulatory authority under any Central Act or State Act or Provincial Act and filing an application for a patent under the Patents Act, 1970.

No other deduction under the Act: No deduction will be allowed in respect of the above expenditure under any other provision of the Income-tax Act, 2025.

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In case of companies, deduction u/s 45(2) would not be allowable if they have opted for the special provisions u/s 200/201. In other words, deduction u/s 45(2) would be allowable only if they pay tax under the normal provisions of the Act.

(III) Amount contributed or paid to [Section 45(3)]:

(i) Amount contributed or paid to research association, university, college or other institution: Under section 45(3)(a), a deduction is allowed in respect of any sum paid to -

- a research association having the object of undertaking scientific research or to a university, college or institution to be used for scientific research
- a research association having the object of undertaking research in social science or statistical research or to a university, college or institution to be used for research in any social science or statistical research.

The above association university, college or other institution must be approved for this purpose and notified by the Central Government [Section 45(4)(b)].

(ii) Amount contributed or paid to approved Indian company for scientific research: A deduction is allowed in respect of any sum paid to a company.

Such deduction would be available only if

- the company is registered in India having the main object of scientific research and development and
- approved by the prescribed authority and should fulfill the other prescribed conditions [Section 45(3)(b)].

(iii) Amount contributed or paid to National Laboratory, etc.: A deduction is allowed under section 45(3)(c) in respect of any sum paid to a National Laboratory or University or Indian Institute of Technology or a specified person with a specific direction that the said sum shall be used for scientific research undertaken under a programme approved in this behalf by the prescribed authority.

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Specified Person means a person who is approved by the prescribed authority.

No other deduction under the Act: No deduction will be allowed in respect of the sum under any other provision of the Income-tax Act, 2025.

Notes:

- The expenditure under section 45(3) shall be allowed subject to such conditions and on furnishing of documents, as may be prescribed.
- Section 45(5) clarifies that the deduction to which an assessee (i.e. donor) is entitled on account of payment of any sum as above shall not be denied merely on the ground that subsequent to payment of such sum by the assessee, the approval granted to any of the aforesaid entities is withdrawn or the programme undertaken by entities as mentioned has been withdrawn.



(1) Deduction u/s 45(3) would be available to an individual, HUF, AoP (other than a co-operative society) or BoI or an artificial juridical person only if they exercise the option of shifting out of the default tax regime and pay tax as per the optional tax regime of the Act.

(2) In case of companies and co-operative societies, deduction u/s 45(3) would not be allowable if they have opted for the special provisions u/s 200/201 and section 203/204, respectively. In other words, deduction u/s 45(3) would be allowable only if they pay tax under the normal provisions of the Act.

(IV) In case of amalgamation

When an amalgamating company sells or otherwise transfers to the amalgamated Indian company, in a scheme of amalgamation, any asset representing capital expenditure on scientific research, the aforesaid provisions shall apply to the amalgamated company as they would have applied to the amalgamating company if the latter had not so sold or otherwise transferred the asset.

ILLUSTRATION 6

A Ltd., engaged in the business of manufacturing since 2015, furnishes the following particulars for the T.Y.2026-27. Compute the deduction allowable under section 45

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for T.Y.2026-27, while computing its income under the head "Profits and gains of business or profession", assuming that it does not opt for special tax regime under section 200.

	Particulars	***₹***
1.	*Amount paid to notified approved Indian Institute of Science, Bangalore, for scientific research*	*1,00,000*
2.	*Amount paid to IIT, Delhi for an approved scientific research programme*	*2,50,000*
3.	*Amount paid to X Ltd., a company registered in India which has as its main object scientific research and development, as is approved by the prescribed authority*	*4,00,000*
4.	*Expenditure incurred on in-house research and development facility as approved by the prescribed authority*	
	(a) Revenue expenditure on scientific research	*3,00,000*
	(b) Capital expenditure (including cost of acquisition of land ₹ 5,00,000) on scientific research	*7,50,000*

SOLUTION

Computation of deduction under section 45 for the T.Y.2026-27

Particulars	₹	Section	% of deduction	Amount of deduction (₹)
Payment for scientific research				
Indian Institute of Science	1,00,000	45(3)(a)	100%	1,00,000
IIT, Delhi	2,50,000	45(3)(c)	100%	2,50,000
X Ltd.	4,00,000	45(3)(b)	100%	4,00,000
Expenditure incurred on in-house research and development facility				
Revenue expenditure	3,00,000	45(2)	100%	3,00,000

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Capital expenditure (excluding cost of acquisition of land ₹ 5,00,000)	2,50,000	45(2)	100%	2,50,000
Deduction allowable under section 45				**13,00,000**

"Investment-linked tax incentives" for specified businesses [Section 46]

Section 46 provides deduction for the capital expenditure incurred, wholly and exclusively, for the purposes of such specified business carried on by him.

(i) Deduction for Capital Expenditure

100% of the capital expenditure incurred, wholly and exclusively, for the specified business carried on the assessee would be allowed as deduction to the assessee, at his option, during the tax year in which such expenditure is incurred.



Capital expenditure shall not include any expenditure

- ♦ *for which the payment or aggregate of payments made to a person in a day exceeds ₹ 10,000 is not through specified banking or online mode*
- ♦ *incurred on the acquisition of any land, goodwill or financial instrument.*

Meaning of "Specified Banking or Online Mode" [Section 66(32)]

Specified Banking or Online Mode mean transaction by

- an account payee cheque or
- an account payee bank draft or
- use of electronic clearing system through a bank account or
- through such other electronic mode, as may be prescribed.

As per Rule 48 of the Income-tax Rules, 2026, "other electronic modes of payment" are the following:

- ➢ Credit Card;
- ➢ Debit Card;
- ➢ Net Banking;

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- IMPS (Immediate Payment Service);
- UPI (Unified Payment Interface);
- RTGS (Real Time Gross Settlement);
- NEFT (National Electronic Funds Transfer);
- BHIM (Bharat Interface for Money) Aadhaar Pay, and
- Tier-III: Full KYC Central Bank Digital Currency wallets, P-CBDC, Wholesale/Cross-border CBDC.



In case of an individual/HUF/AoP/BoI carrying on specified business, deduction u/s 46 would be available only if such person exercises the option of shifting out of the default tax regime. If such person is paying concessional rates of tax under the default tax regime u/s 202(1), deduction u/s 46 would not be available.

A company/ cooperative society would not be eligible for deduction under section 46, if it has opted for the special provisions of section 200/201 or section 203/204, respectively.

(ii) Expenditure incurred prior to commencement of operation

Where the expenditure is incurred, wholly and exclusively, for the purpose of specified business prior to commencement of its operation and such expenditure is capitalised in the books of account as on the date of commencement of its operations, deduction would be allowed during the tax year in which the such business is commenced.

(iii) List of specified businesses

Specified businesses, for which deduction of capital expenditure is allowed under this section, are as follows:

(i) setting-up and operating 'cold chain' facilities for specified products

(ii) setting-up and operating warehousing facilities for storage of agricultural produce;

(iii) laying and operating a cross-country natural gas or crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of such network;

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(iv) building and operating a hotel of two-star or above category, anywhere in India;

(v) building and operating a hospital, anywhere in India, with at least 100 beds for patients;

(vi) developing and building a housing project under a notified scheme for slum redevelopment or rehabilitation framed by the Central Government or a State Government.

(vii) developing and building a housing project under a notified scheme for affordable housing framed by the Central Government or State Government;

(viii) production of fertilizer in India;

(ix) setting up and operating an inland container depot or a container freight station notified or approved under the Customs Act, 1962;

(x) bee-keeping and production of honey and beeswax;

(xi) setting up and operating a warehousing facility for storage of sugar;

(xii) laying and operating a slurry pipeline for the transportation of iron ore;

(xiii) setting up and operating a semiconductor wafer fabrication manufacturing unit, if such unit is notified by the Board in accordance with the prescribed guidelines;

(xiv) developing or maintaining and operating or developing, maintaining and operating a new infrastructure facility.



CIT v. Ceebros Hotels Private Limited [2018] 409 ITR 423 (Mad)

Issue: Can an assessee setting up a hotel claim deduction under section 46 for the relevant tax year, on the basis that it had commenced its operations and made an application for three-star category classification in beginning of the said tax year, even though the same was granted by the authority only in the next year due to the requirement of completion of inspection?

Analysis & Decision: As the application for three star category classification was granted with no discrepancy during inspection, the assessee could not be penalised for the delay on the part of the concerned authority (the Hotel and Restaurant Approval and Classification Committee, in the instant case) to complete inspection before the end of the financial year. Under section 46,

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deduction is available from the tax year in which the assessee commences operation of the specified business i.e., hotel business, in this case. Section 46 does not mandate that the date of the certificate has to be with effect from a particular date.

Thus, the assessee is entitled to claim the deduction under section 46 for the relevant tax year, since the provision which was introduced to encourage the establishment of hotels of a particular category is a beneficial provision, and hence, should be read and interpreted liberally.

(iv) Conditions to be fulfilled

For claiming deduction under section 46, the specified business should fulfill the following conditions –

General Conditions:	
To be fulfilled by every specified business	
(i)	it should not be set up by splitting up, or the reconstruction, of a business already in existence
(ii)	it should not be set up by the transfer to the specified business of machinery or plant previously used for any purpose In order to satisfy this condition, the total value of the plant or machinery so transferred should not exceed 20% of the value of the total plant or machinery used in such specified business. For the purpose of this condition, machinery or plant would not be regarded as previously used if it had been used outside India by any person other than the assessee provided the following conditions are satisfied: (a) such plant or machinery was not, at any time prior to the date of its installation by the assessee, used in India; (b) the plant or machinery was imported into India from a foreign Country; and (c) no deduction on account of depreciation in respect of such plant or machinery has been allowed to any person at any time prior to the date of installation by the assessee.

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Conditions required to be fulfilled by certain specified businesses:	
I. Business of laying and operating a cross-country natural gas or crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of such network	
(i)	Such business should be owned by a company formed and registered in India under the Companies Act, 2013 or by a consortium of such companies or by an authority or a board or a corporation established or constituted under any Central or State Act;
(ii)	It should have been approved by the Petroleum and Natural Gas Regulatory Board and notified by the Central Government in the Official Gazette
(iii)	It should have made not less than such proportion of its total pipeline capacity available for use on common carrier basis by any person other than the assessee or an associated person.
(iv)	It should fulfil any other prescribed condition.
II. Business of developing or operating and maintaining or developing, operating and maintaining a new infrastructure facility	
(i)	The business should be owned by a company registered in India or by a consortium of such companies or by an authority or a board or corporation or any other body established or constituted under any Central or State Act.
(ii)	The entity should have entered into an agreement with the Central Government or a State Government or a local authority or any other statutory body for developing or operating and maintaining or developing, operating and maintaining, a new infrastructure facility.

(v) No deduction under Chapter VIII-C

Where a deduction under this section is claimed and allowed in respect of the specified business for any tax year, no deduction under the provisions of Chapter VIII-C is permissible in relation to such specified business for the same or any other tax year.

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(vi) No deduction allowable under the Act in respect of expenditure for which deduction allowed under this section

The assessee cannot claim deduction in respect of such expenditure incurred for specified business under any other section in any tax year or under this section in any other tax year, if the deduction has been claimed and allowed to him under section 46.

(vii) Date of Commencement of specified businesses

S. No.	Specified business	Date of commencement of operations on or after
1.	Laying and operating a cross-country natural gas pipeline network for distribution, including storage facilities being an integral part of such network	1st April, 2007
2.	(a) building and operating anywhere in India, a hotel of two-star or above category as specified by the Central Government (b) building and operating a hospital with at least 100 beds for patients (c) notified scheme for slum redevelopment or rehabilitation housing projects	1st April, 2010
3.	(a) notified scheme for affordable housing projects and (b) production of fertilizer in a new plant or in a newly installed capacity in an existing plant	1st April, 2011
4.	(a) setting up and operating an inland container depot or a container freight station notified or approved under the Customs Act, 1962, (b) bee-keeping and production of honey and beeswax and (c) setting up and operating a warehousing facility for storage of sugar	1st April, 2012

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5.	(a) laying and operating a slurry pipeline for the transportation of iron ore (b) setting up and operating a semi-conductor wafer fabrication manufacturing unit	1st April, 2014
6.	developing or operating and maintaining or developing, operating and maintaining, any infrastructure facility	1st April, 2017
7.	In any other case, namely, setting and operating - (a) cold-chain facilities for specified products (b) warehousing facilities for storing agricultural produce	1st April, 2009

(viii) Meaning of certain terms

Term	Meaning
Cold chain facility	A chain of facilities for storage or transportation of agricultural and forest produce, meat and meat products, poultry, marine and dairy products, products of horticulture, floriculture and apiculture and processed food items under scientifically controlled conditions including refrigeration and other facilities necessary for the preservation of such produce.
Associated person	In relation to the assessee, means a person— (i) who participates directly or indirectly or through one or more intermediaries in the management or control or capital of the assessee; (ii) who holds, directly or indirectly, shares carrying not less than 26% of the voting power in the capital of the assessee; (iii) who appoints more than half of the Board of directors or members of the governing board, or one or more executive directors or executive members of the governing board of the assessee; or

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	(iv)	who guarantees not less than 10% of the total borrowings of the assessee.
Infrastructure facility	(i)	A road including toll road, a bridge or a rail system.
	(ii)	A highway project including housing or other activities being an integral part of the highway project.
	(iii)	A water supply project, water treatment system, irrigation project, sanitation and sewerage system or solid waste management system.
	(iv)	A port, airport, inland waterway, inland port or navigational channel in the sea.

(ix) Transfer of hotel built by the assessee

Where the assessee builds a hotel of two-star or above category as classified by the Central Government and subsequently, transfers the hotel operation to another person while retaining its ownership, the assessee shall be deemed to be carrying on the specified business of building and operating a hotel. Therefore, he would be eligible to claim investment-linked tax deduction under section 46.



Therefore, in effect, the assessee shall be deemed to be carrying on the specified business of building and operating hotel if –

(i) The assessee builds a hotel of two-star or above category;

(ii) Thereafter, he transfers the operation of the hotel to another person;

(iii) He, however, should continue to own the hotel.

(x) Other conditions contained under section 46

S. No.	Particulars	Condition
1.	**Transfer of goods and services**	Where any goods or services held for the purposes of the specified business are transferred to any other business carried on by the assessee, or vice versa, and the consideration for such transfer recorded

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		in the accounts of the specified business does not correspond to the market value of such goods or services as on the date of transfer then the profits and gains of the specified business shall be computed as if the transfer was made at market value of such goods or services as on that date.
2.	**Close connection between assessee and any other person**	Where due to the close connection between the assessee and the other person or for any other reason, it appears to the Assessing Officer that the profits of specified business is increased to more than the ordinary profits, the Assessing Officer shall compute the amount of profits of such eligible business as may be reasonably deemed to have been derived therefrom for allowing the deduction.
2.	**Audit of accounts**	The deduction shall be allowed to the assessee only if the accounts of the assessee for the relevant tax year have been audited by an accountant before the specified date referred to in section 63 and the assessee furnishes by that date the audit report in the prescribed form duly signed and verified by such accountant.
3.	**Asset to be used for specified business for eight years**	Section 46(9)(a) provides that any asset for which a deduction is claimed and allowed under section 46 shall be used only for the specified business for a period of 8 years beginning with the tax year in which such asset is acquired or constructed.

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4.	**Asset is used for any other business other than specified business during 8 years**	Section 46(9)(b) provides that if any asset for which a deduction is claimed and allowed under section 46 is **used for any purpose other than the specified business** during 8 years beginning with the tax year in which such asset is acquired or constructed, the total amount of deduction so claimed and allowed in any tax year(s), as reduced by the amount of depreciation allowable under section 33, as if no deduction had been allowed under section 46, shall be deemed to be income of the assessee chargeable under the head "Profits and gains of business or profession" of the tax year in which the asset is so used. In such a case, as per provisions of section 39(4)-Table Sl. No. 12(b), the actual cost of such asset for the assesse shall be the actual cost as reduced by the depreciation calculated at the rate in force that would have been allowable had the asset been used for the purpose of business since the date of its acquisition. However, the deeming provision under sub-section 9(b) shall not be applicable to a company which has become a sick industrial company[2], during the intervening period of eight years specified in sub-section 9(a).
5.	**Asset demolished, destroyed, discarded or**	If any asset on which a deduction under section 46[3] has been allowed, is

[2] *under section 17(1) of the Sick Industrial Companies (Special Provisions) Act, 1985*
[3] *or section 35AD of the Income-tax Act, 1961*

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	transferred for which a deduction has been allowed	demolished, destroyed, discarded or transferred, the sum received or receivable for the same is chargeable to tax under clause (k) of section 26(2). This does not take into account a case where asset on which deduction under section 46 has been allowed is used for any purpose other than the specified business by way of a mode other than the specified ones.

(xi) Set-off or carry forward and set-off of loss from specified business

As per section 114, the loss of an assessee claiming deduction under section 46 in respect of a specified business can be set-off against the profit of another specified business, irrespective of whether the latter is eligible for deduction under section 46.

Such loss can, however, be carried forward indefinitely for set-off against profits of the same or any other specified business but the assessee has to file return of income on or before the due date of filling return of income under section 263 for carry forward of losses from specified business.



A assessee can therefore, set-off the losses of a hospital or hotel which begins to operate after 1st April, 2010 and which is eligible for deduction section 46, against the profits of the existing business of operating a hospital (with atleast 100 beds for patients) or a hotel (of two-star or above category) started before 1st April, 2010, even if the latter is not eligible for deduction under section 46.

ILLUSTRATION 7

Mr. A commenced operations of the businesses of setting up a warehousing facility for storage of food grains, sugar and edible oil on 1.4.2026. He incurred capital expenditure of ₹80 lakhs, ₹60 lakhs and ₹50 lakhs, respectively, on purchase of land and building during the period January, 2026 to March, 2026 exclusively for the above businesses, and capitalized the same in its books of account as on 1st April, 2026. The cost of land included in the above figures is ₹50 lakhs, ₹40 lakhs and ₹30 lakhs,

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respectively. During the T.Y. 2026-27, he incurred capital expenditure of ₹ 20 lakhs, ₹ 15 lakhs & ₹ 10 lakhs, respectively, for extension/ reconstruction of the building purchased and used exclusively for the above businesses.

The profits from the business of setting up a warehousing facility for storage of food grains, sugar and edible oil (before claiming deduction under section 46 and section 33) for the T.Y. 2026-27 is ₹ 16 lakhs, ₹ 14 lakhs and ₹ 31 lakhs, respectively. Assume in respect of expenditure incurred, the payments are made by account payee cheque or use of ECS through bank account.

Compute the income under the head "Profits and gains of business or profession" for the T.Y.2026-27 and the loss to be carried forward, assuming that Mr. A is exercising the option of shifting out of the default tax regime and has fulfilled all the conditions specified for claim of deduction under section 46 and wants to claim deduction under section 46 and has not claimed any deduction under Chapter VIII-C.

SOLUTION

Computation of profits and gains of business or profession for T.Y. 2026-27

Particulars	₹ (in lakhs)
Profit from business of setting up of warehouse for storage of edible oil (before providing for depreciation under section 33)	31
Less: Depreciation under section 33	
10% of ₹ 30 lakh, being (₹ 50 lakh – ₹ 30 lakh + ₹ 10 lakh)	3
Income chargeable under "Profits and gains from business or profession"	**28**

Computation of income/loss from specified business under section 46

	Particulars	Food Grains	Sugar	Total
		₹ (in lakhs)		
(A)	**Profits from the specified business of setting up a warehousing facility (before providing deduction under section 46)**	**16**	**14**	30

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	***Less:* Deduction under section 46**			
(B)	Capital expenditure incurred prior to 1.4.2026 (i.e., prior to commencement of business) and capitalized in the books of account as on 1.4.2026 (excluding the expenditure incurred on acquisition of land) = ₹ 30 lakh (₹ 80 lakh – ₹ 50 lakh) and ₹ 20 lakh (₹ 60 lakh – ₹ 40 lakh)	30	20	50
(C)	Capital expenditure incurred during the T.Y.2026-27	20	15	35
(D)	**Total capital expenditure (B + C)**	**50**	**35**	**85**
(E)	**Deduction under section 46**			
	100% of capital expenditure (food grains/sugar)	50	35	85
	Total deduction u/s 46 for T.Y.2026-27	**50**	**35**	**85**
(F)	**Loss from the specified business of setting up and operating a warehousing facility (after providing for deduction under section 46) to be carried forward as per section 114 (A-E)**	**(34)**	**(21)**	**(55)**

Notes:

(i) Deduction of 100% of the capital expenditure is available under section 46 for T.Y.2026-27 in respect of specified business of setting up and operating a warehousing facility for storage of sugar and setting up and operating a warehousing facility for storage of agricultural produce where operations are commenced on or after 01.04.2012 or on or after 01.04.2009, respectively.

(ii) However, since setting up and operating a warehousing facility for storage of edible oils is not a specified business, Mr. A is not eligible for deduction under section 46 in respect of capital expenditure incurred in respect of such business.

(iii) Mr. A can, however, claim depreciation@10% under section 33 in respect of the capital expenditure incurred on buildings. It is presumed that the buildings were put to use for more than 180 days during the T.Y. 2026-27.

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(iv) Loss from a specified business can be set-off only against profits from another specified business. Therefore, the loss of ₹ 55 lakh from the specified businesses of setting up and operating a warehousing facility for storage of food grains and sugar cannot be set-off against the profits of ₹ 28 lakh from the business of setting and operating a warehousing facility for storage of edible oils, since the same is not a specified business. Such loss can, however, be carried forward indefinitely for set-off against profits of the same or any other specified business provided Mr. A file his return of income on or before the due date as specified u/s 263(1).

ILLUSTRATION 8

XYZ Ltd. commenced operations of the business of a new three-star hotel in Madurai, Tamil Nadu on 1.4.2026. The company incurred capital expenditure of ₹ 50 lakhs during the period January, 2026 to March, 2026 exclusively for the above business, and capitalized the same in his books of account as on 1st April, 2026. Further, during the T.Y. 2026-27, it incurred capital expenditure of ₹ 2 crores (out of which ₹ 1.50 crores was for acquisition of land) exclusively for the above business.

Compute the income under the head "Profits and gains of business or profession" for the T.Y.2026-27, assuming that XYZ Ltd. has fulfilled all the conditions specified for claim of deduction under section 46 and opted for claiming deduction under section 46; and has not claimed any deduction under Chapter VIII-C. The company is not opting for the concessional tax regime under section 200.

The profits from the business of running this hotel (before claiming deduction under section 46) for the T.Y.2026-27 is ₹ 25 lakhs. Assume that the company also has another existing business of running a four-star hotel in Coimbatore, which commenced operations fifteen years back, the profits from which are ₹ 120 lakhs for the T.Y.2026-27. Also, assume that expenditure incurred during the tax year 2026-27 were paid by account payee cheque or use of ECS through bank account.

SOLUTION

Computation of profits and gains of business or profession for T.Y. 2026-27

Particulars	₹ (in lakhs)
Profits from the specified business of new hotel in Madurai (before providing deduction under section 46)	25
***Less*: Deduction under section 46**	

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Capital expenditure incurred during the T.Y.2026-27 (excluding the expenditure incurred on acquisition of land) = ₹ 200 lakhs – ₹ 150 lakhs	50 lakhs	
Capital expenditure incurred prior to 1.4.2026 (i.e., prior to commencement of business) and capitalized in the books of account as on 1.4.2026	50 lakhs	
Total deduction under section 46 for T.Y.2026-27		100
Loss from the specified business of new hotel in Madurai		(75)
Profit from the existing business of running a hotel in Coimbatore		120
Net profit from business after set-off of loss of specified business against profits of another specified business under section 114.		**45**

ILLUSTRATION 9

ABC Ltd. is a company having two units – Unit A carries on specified business of setting up and operating a warehousing facility for storage of sugar; Unit B carries on non-specified business of operating a warehousing facility for storage of edible oil.

Unit A commenced operations on 1.4.2025 and it claimed deduction of ₹ 100 lakhs incurred on purchase of two buildings for ₹ 50 lakhs each (for operating a warehousing facility for storage of sugar) for T.Y. 2025-26. However, in February, 2027, Unit A transferred one of its buildings to Unit B.

Examine the tax implications of such transfer in the hands of ABC Ltd.

SOLUTION

Since the capital asset, in respect of which deduction of ₹ 50 lakhs was claimed, has been transferred by Unit A carrying on specified business to Unit B carrying on non-specified business in the T.Y.2026-27, the deeming provision under section 46(9)(b) is attracted during the T.Y. 2026-27.

Particulars	₹
Deduction allowed under section 46[4] for T.Y.2025-26	50,00,000
Less: Depreciation allowable for T.Y.2025-26 [10% of ₹ 50 lakhs]	5,00,000
Deemed income under section 46(7B)	**45,00,000**

[4] *Section 35AD of the Income-tax Act, 1961*

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ABC Ltd., however, can claim depreciation under section 33 on the building in Unit B for T.Y. 2026-27. For the purpose of claiming depreciation on building in Unit B, the actual cost of the building would be:

Particulars	₹
Actual cost to the assesse	50,00,000
Less: Depreciation allowable for T.Y.2025-26 [10% of ₹ 50 lakhs]	5,00,000
Actual cost in the hands of ABC Ltd. in respect of building in Unit B	**45,00,000**

Deduction in respect of expenditure incurred on notified agricultural extension project and skill development project [Section 47]

(i) Allowable deduction: Any expenditure incurred on

(a) agricultural extension project by any assessee; or

(b) any skill development project by a company,

is allowed as a deduction, in the tax year in which such expenditure is incurred. The project must be notified by the Board as per the guidelines issued by it.

(ii) No other deduction: In case deduction in respect of such expenditure is claimed and allowed for any tax year under this section, no deduction in respect of such expenditure shall be allowed under any other provisions of the Act for the same or any other tax year.



(1) While deduction for expenditure on agricultural extension project is available to all the assessees, deduction for expenditure on skill development project is available only to a company.

(2) Deduction is available for both revenue and capital expenditure excluding cost of any land or building.

(3) A company would not be eligible for deduction under section 47, if it has opted for the special provisions of section 200/201.

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(4) In case of an individual, HUF, AoP (other than a co-operative society) or BoI or an artificial juridical person, deduction u/s 47 in respect of expenditure on agricultural extension project would be available only if such person exercises the option of shifting out of the default tax regime. If such person is paying concessional rates of tax under the default tax regime u/s 202(1), such deduction would not be available.

A cooperative society would not be eligible for deduction us/ 47 in respect of expenditure on agricultural extension project, if it has opted for the special provisions of section 203/204.

Tea Development Account/ Coffee Development Account/ Rubber Development Account [Section 48 and Schedule IX]

This section provides for a deduction in the computation of the taxable profits in the case of an assessee carrying on business of growing and manufacturing tea or coffee or rubber in India.

The assessee shall be allowed a deduction on the basis of deposits into the special account or deposit account and computed as per the provisions of Schedule IX.

(i) Quantum of deduction: Schedule IX provides that the assessee shall be allowed **a deduction of lower of**:

(a) the amount or aggregate of the amounts deposited in the specified account and

(b) 40% of the profits of such business computed under the head 'Profits and gains of business or profession before making any deduction under this section.

The above deduction will be allowed before allowing set-off of brought-forward loss as per section 112.

(ii) Condition for claiming deduction: Deduction would be allowed if the assessee fulfils the below mentioned conditions –

(a) the assessee is carrying on the business of growing and manufacturing tea or coffee or rubber in India during the tax year,

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(b) where the assessee has before the expiry of six months from the end of the tax year or before the due date of furnishing the return of income, **whichever is earlier**, deposited any amount in the specified account, being

- a special account maintained with the National Bank in accordance with and for the purpose specified in the special scheme
- a deposit account in accordance with the scheme and for the purpose specified in the special scheme and

(c) the accounts of such business of the assessee for the relevant tax year have been audited by an accountant before the date specified in section 63 i.e., one month prior to the due date for furnishing return of income u/s 263, and the assessee furnishes by that date the report of such audit in the prescribed form duly signed and verified by such accountant.

Particulars	Due date of filing of return	Specified Date
Assessees (other than a company) subject to tax audit	31st October of the financial year succeeding the relevant T.Y.	30th September of the financial year succeeding the relevant T.Y.
	For T.Y.2026-27, on or before 31st October, 2027	For T.Y.2026-27, on or before 30th September, 2027.

Where the assessee is required by any other law to get his accounts audited, it shall be sufficient compliance with the requirement of audit if such assessee gets the accounts of such business audited under any such law before the date specified in section 63 and furnishes by that date the report of the audit and a further report in the prescribed form.

(iii) Non-eligibility of deduction in any other tax year: If any deduction has been allowed under section 48 in any tax year, no deduction shall be allowed in respect of such amount in any other tax year.

(iv) No deduction to partner of assessee-firm or member of assessee-AOP/ BOI: Where the assessee is a firm or any association of persons or any body of individuals, this deduction shall not be allowed in the computing the income of any of the partner or member of such firm, AOP or BOI.

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Amount withdrawn or utilised or released from the specified account at the time of closure

Any amount withdrawn or utilised or released from the specified account at the time of closure or otherwise shall be charged to tax as per the provisions of the Schedule IX.

(i) **Condition to withdraw the amount from special account or deposit account:** Any amount standing to the credit of the assessee in the specified account cannot be withdrawn except for the purposes specified in the special scheme or in the deposit scheme or in the circumstances specified.

Specified circumstances are:

(a) Closure of business

(b) Death of an assessee

(c) Partition of HUF

(d) Dissolution of a firm

(e) Liquidation of a company.

(ii) **Amount withdrawn on the closure of business or dissolution of a firm:** If any amount standing to the credit of the assessee in the specified account is withdrawn during any tax year on the closure of his business or dissolution of a firm, the whole of such withdrawal shall be deemed to be the profits and gains of business of that tax year and shall be charged to income-tax for that tax year, as if the business had not been closed or the firm had not been dissolved.

(iii) **Amount withdrawn and utilised for purchase of specified articles or thing would be chargeable to tax as business income:** If any amount standing to the credit of the assessee in the specified account is released by the National Bank or is withdrawn by the assessee from the Deposit account during any tax year and such amount is utilised for the purchase of specified articles or thing, then the whole of such amount so utilised shall be deemed to be the profits and gains of business of that tax year and shall be charged to income-tax for that tax year.

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Meaning of Specified articles or thing mean

Specified articles or thing mean

(a) any machinery or plant to be installed in any office premises or residential accommodation, including any accommodation in the nature of a guest house.

(b) any office appliances (other than computers)

(c) any machinery or plant, the whole of the actual cost of which is allowed as a deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head 'Profits and gains of business or profession' of any one tax year;

(d) any new machinery or plant to be installed in an industrial undertaking for the purpose of the business of construction, manufacture or production of any article or thing specified in the list in the Schedule XIII.

(iv) Consequences of non-utilisation of withdrawn amount: If any amount standing to the credit of the assessee

- in the specified account is released by the National Bank or
- is withdrawn by the assessee from the Deposit Account

during tax year for utilization for the purposes of such business as per the special scheme or deposit scheme and the same is not utilized either wholly or partly within that tax year, such unutilised amount shall be deemed to be profits and gains of business of that tax year and charged to income-tax for that tax year.

However, where amount is released during any tax year on closure of the account on the death of the assessee, partition of a HUF or liquidation of a company, the above restriction will not apply.

(v) Expenditure met for business purpose not available as a deduction: If the amount standing to the credit of the assessee in the specified account is utilised to incur any expenditure for the purpose of such business as per the specified scheme or deposit scheme, no deduction would be allowed against such expenditure in computing the business income.

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Asset acquired as per the special scheme or the deposit scheme is sold

Where any asset acquired as per the special scheme or the deposit scheme is sold or otherwise transferred in any tax year, the taxability will be in accordance with the provisions of Schedule IX.

(i) Consequences of sale or transfer: Where any asset

- ♦ is acquired in accordance with the special scheme or deposit scheme and
- ♦ is sold or transferred to any person in the tax year at any time before the expiry of 8 years from the end of the tax year in which it was acquired,

then, the part of cost which is relatable to the deduction allowed under section 48 shall be deemed to be profits and gains of business or profession of the tax year in which the asset is sold or transferred and shall be charged to income-tax for that tax year.

(ii) Exceptions: The above provisions on sale or transfer would not apply if the asset is sold or transferred -

(a) by the assessee to the specified person i.e., to Government, local authority, statutory corporation or a Government company.

(b) by a firm to a company in connection with the succession of a firm by such company provided –

- the provisions of special scheme or deposit scheme is applicable to the company in the same manner as it applied to the firm
- all the properties and liabilities of the firm relating to the business or profession immediately before the succession become the properties and liabilities of the company and
- all the shareholders of the company were partners of the firm immediately before the succession.

Meaning of National Bank: "National Bank" means the National Bank for Agricultural and Rural Development (NABARD).

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Site Restoration Fund [Section 49 and Schedule X]

This section provides for a deduction in the computation of the taxable profits in the case of an assessee carrying on a business of prospecting, extraction or producing petroleum or natural gas or both in India and who has an agreement with the Central Government for such business.

The assessee shall be allowed a deduction on the basis of deposits to special account or site restoration account and computed as per the provisions of Schedule X.

(i) Quantum of deduction: Schedule X provides that the assessee shall be allowed **a deduction of lower of**:

(a) the amount or aggregate of the amounts deposited by the assessee in the specified account and

(b) 20% of the profits of such business computed under the head 'Profits and gains of business or profession before making any deduction under this section.

The above deduction will be allowed before allowing set-off of brought-forward loss as per section 112.

Any interest credited in the specified account shall be deemed to be a deposit.

(ii) Condition for claiming deduction: Deduction would be allowed if the assessee fulfils the below mentioned conditions –

(a) the assessee is, during the tax year, carrying on the business consisting of the prospecting for, or extraction or production of, petroleum or natural gas or both in India and has entered into an agreement with the Central Government for such business,

(b) where the assessee has before the end of the tax year deposited any amount in the specified account, being

- a special account maintained with the SBI in accordance with and for the purpose specified in the special scheme
- a site restoration fund in accordance with and for the purpose specified in the deposit scheme and

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(c) the accounts of such business of the assessee for the relevant tax year have been audited by an accountant before the date specified in section 63 i.e., one month prior to the due date for furnishing return of income u/s 263, and the assessee furnishes by that date the report of such audit in the prescribed form duly signed and verified by such accountant.

Where the assessee is required by any other law to get his accounts audited, it shall be sufficient compliance with the requirement of audit if such assessee gets the accounts of such business audited under any such law before the date specified in section 63 and furnishes by that date the report of the audit and a further report in the prescribed form.

(iii) Non-eligibility of deduction in any other tax year: If any deduction has been allowed under section 49 in any tax year, no deduction shall be allowed in respect of such amount in any other tax year.

(iv) No deduction to partner of assessee-firm or member of assessee-AOP/ BOI: Where the assessee is a firm or any association of persons or any body of individuals, this deduction shall not be allowed in the computing the income of any of the partner or member of such firm, AOP or BOI.

Amount withdrawn or transferred from the specified account at the time of closure

Any amount withdrawn or transferred from the specified account at the time of closure or otherwise shall be charged to tax in the year in which the amount is transferred or withdrawn as per the provisions of Schedule X. The amount standing to the credit of the assessee in the specified account includes interest accrued to such accounts.

(i) Condition to withdraw the amount from special account or deposit account: Any amount standing to the credit of the assessee in the specified account cannot be withdrawn except for the purposes specified in the special scheme or in the deposit scheme.

(ii) No deduction: If any amount standing to the credit of the assessee in the specified account is utilised for the purchase of specified articles or thing, then such amount shall not be allowed as deduction.

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Meaning of Specified articles or thing

Specified articles or thing mean

(a) any machinery or plant to be installed in any office premises or residential accommodation, including any accommodation in the nature of a guest house.

(b) any office appliances (other than computers)

(c) any machinery or plant, the whole of the actual cost of which is allowed as a deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head 'Profits and gains of business or profession' of any one tax year;

(d) any new machinery or plant to be installed in an industrial undertaking for the purpose of the business of construction, manufacture or production of any article or thing specified in the list in the Schedule XIII.

(iii) Amount withdrawn on the closure of account: Where any amount standing to the credit of the assessee in the specified account is withdrawn on the closure of such account in any tax year, then the following amount shall be deemed to be the profits and gains of business for the tax year and shall be charged to income-tax for that tax year

$$A = B - C$$

A = deemed profits and gains of business or profession of that tax year

B = amount withdrawn from the specified account on its closure

C = amount payable to the Central Government by way of profit or production share as

Where any amount is withdrawn on closure of the specified account in a tax year in which the business of the assessee in no longer in existence, these provisions will apply as if the business is in existence in that tax year.

(iv) Consequences of non-utilisation of withdrawn amount: If any amount standing to the credit of the assessee

- in the specified account is released by the SBI or
- is withdrawn by the assessee from the site restoration account

during any tax year for utilization for the purposes of such business as per the special scheme or deposit scheme and the same is not utilized either

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wholly or partly within that tax year, such unutilised amount shall be deemed to be profits and gains of business of that tax year and charged to income-tax for that tax year.

(v) Expenditure met for business purpose not available as a deduction: If the amount standing to the credit of the assessee in the specified account is utilised to incur any expenditure for the purpose of such business as per the specified scheme or deposit scheme, no deduction would be allowed against such expenditure in computing the business income.

Asset acquired as per the special scheme or the deposit scheme is sold

Where any asset acquired as per the special scheme or the deposit scheme is sold or otherwise transferred in any tax year, the taxability will be in accordance with the provisions of Schedule X.

(i) Consequences of sale or transfer: Where any asset

- is acquired in accordance with the special scheme or deposit scheme and
- is sold or transferred to any person in the tax year at any time before the expiry of 8 years from the end of the tax year in which it was acquired,

then, the part of cost as is relatable to the deduction allowed under section 49 shall be deemed to be profits and gains of business or profession of the tax year in which the asset is sold or transferred and shall be charged to income-tax for that tax year.

(ii) Exceptions: The above provisions on sale or transfer would not apply if the asset is sold or transferred -

(a) by the assessee to the specified person i.e., to Government, local authority, statutory corporation or a Government company.

(b) by a firm to a company in connection with the succession of a firm by such company provided –

- the provisions of special scheme or deposit scheme is applicable to the company in the same manner as it applied to the firm
- all the properties and liabilities of the firm relating to the business or profession immediately before the succession become the properties and liabilities of the company and
- all the shareholders of the company were partners of the firm immediately before the succession.

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Amortisation of expenditure for prospecting of certain minerals [Section 51]

(i) **Eligible assessee:** This provision applies only to expenditure incurred by an Indian company or other resident non-corporate taxpayer. In order to qualify for amortisation, the assessee should be engaged in any operations relating to prospecting for or the extraction or production of any mineral.

(ii) **Eligible expenses** - The nature and kind of expenditure qualifying for amortisation are –

(i) It must have been incurred by the assessee at any time during the year of commercial production and any one or more of the four tax years immediately preceding that year,

(ii) It must be incurred wholly and exclusively on any operations relating to the prospecting for any mineral or group of certain minerals listed in the Schedule XII of the Income-tax Act, 2025 or on the development of a mine or other natural deposit of any mineral or group of associated minerals.

(iii) **Expenditure reimbursed by any other person to be reduced** - Any portion of the expenditure which is met directly or indirectly by any other person or authority and the sale, salvage, compensation or insurance moneys realised by the assessee in respect of any property or rights brought into existence as a result of the expenditure should be reduced from the amount of expenditure qualifying for amortisation.

(iv) **Expenditure not allowed for deduction:** The following items of expenditure do not qualify for amortisation at all viz.:

(a) any expenditure on the acquisition of the site of the source of any minerals or group of associated minerals stated above or of any right in or over such site;

(b) any expenditure on the acquisition of the deposits of such minerals or group of associated minerals or of any rights in or over such deposits; or

(c) any expenditure of a capital nature in respect of any building, machinery, plant or furniture for which depreciation allowance is permissible under section 33.

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(iv) Amount of deduction - The assessee will be allowed for each of ten relevant tax years, **a deduction of an amount equal to one-tenth** of the aggregate amount of the qualifying expenditure.

Thus, the deduction to be allowed for any relevant tax year is

(i) one-tenth of the expenditure as reduced by the expenditure not allowable as specified in (ii) and (iii) above or

(ii) such amount as will reduce to nil the income of the tax year arising from the commercial exploration of any mine or other natural deposit of the mineral or any one or more of the minerals in a group of associated minerals in respect of which the expenditure was incurred,

whichever is less.

(v) Carry forward of unabsorbed deduction: If any part of the instalment for a relevant tax year is not fully allowed, it shall be carried forward to the subsequent tax year, becoming part of the instalment of that tax year and such carrying forward may continue for each following tax year, but no instalment shall be carried forward beyond the 10th tax year from the tax year in which commercial production began.

(vi) Audit of accounts: Where the assessee is a person other than a company or co-operative society, the accounts of the assessee for the tax years in which expenditure are incurred have been audited by an accountant before the date specified in section 63 i.e., one month prior to the due date for furnishing return of income u/s 263, and the assessee furnishes for the first tax year in which deduction under section 51 is claimed, by that date, the report of such audit in the prescribed form duly signed and verified by such accountant.

(vii) Special provisions for amalgamation or demerger: In the case of amalgamation, such deduction would continue to be admissible to the amalgamated company as if the amalgamation had not taken place.

Likewise, in case of demerger where such deduction can be availed of by the resulting company as if the demerger had not taken place.

Further, no deduction will be admissible to the amalgamating/ demerged company in the year of amalgamation/ demerger.

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(viii) No other deduction allowed in respect of the expenditure for which deduction is claimed under this section: If a deduction is claimed and allowed for any tax year on account of amortisation of the expenses under section 51 in respect of any expenditure, such expenditure shall not again qualify for deduction from the profits and gains under any other provisions of the Act for the same or any other tax year.

Meaning of certain terms

Term	Meaning
Operation relating to prospecting	Any operation undertaken for the purpose of exploiting, locating or proving deposits of any minerals and includes any such operation which proves to be infructuous or abortive.
Year of commercial production	The tax year in which as a result of any operation relating to prospecting or commercial production of any material or one or more of the minerals in a group of associated minerals specified in Part A or Part B, respectively, of the Schedule XII commences.
Relevant tax year	Ten tax years beginning with the year of commercial production

Amortisation of expenditure for telecommunications services, amalgamation, demerger, scheme of voluntary retirement, etc. [Section 52]

Section 52 provides for deduction of certain specific expenditure incurred by the assessee during a tax year. The deduction is provided in equal instalments over a number of tax years, beginning from the initial tax year.

(i) Amount and Period of Deduction: The nature of expenditure eligible for deduction under this section, initial tax year and number of tax years for which each deduction is allowed has been mentioned in the table given below:

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Sl. No.	Nature of expenditure	Initial tax year	Number of tax years over which deduction of expenditure is allowable in equal instalments
1.	Expenditure incurred by an Indian company, wholly and exclusively for the purposes of amalgamation or demerger of an undertaking.	Tax year in which such amalgamation or demerger takes place.	5 tax years
2.	Amount paid to an employee in connection with his voluntary retirement as per any scheme of voluntary retirement.	Tax year in which such payment is made.	5 tax years
3.	Capital expenditure incurred and actually paid for acquiring any right to use spectrum for telecommunication services (spectrum fee).	Tax year in which, (a) the business to operate telecom services is commenced; or (b) spectrum fee is actually paid, whichever is later.	Number of years commencing from the initial tax year and ending in the tax year up to which the spectrum for which the fee is paid remains in force.

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4.	Capital expenditure incurred and actually paid for acquiring any right to operate telecommunication services (licence fee).	Tax year in which, (a) the business to operate telecom services is commenced; or (b) licence fee is actually paid, whichever is later.	Number of years commencing from the initial tax year and ending in the tax year up to which the licence for which the fee is paid remains in force.

(ii) Meaning of certain terms:

Term	Meaning
Actually paid	"Actually paid" means actual payment of expenditure irrespective of the tax year in which the liability for expenditure was incurred according to the method of accounting regularly employed by the assessee or payable in the prescribed manner.
	Rule 41 substantiates the meaning of the phrase 'actually paid' **(a) In a case where full upfront payment of spectrum fee has been made:** where an assessee has opted and been allowed by the Department of Telecommunications, Government of India to make full upfront payment of spectrum fee, the actual payment of expenditure irrespective of the tax year in which the liability for the expenditure was incurred according to the method of accounting regularly employed by the assessee; **(b) In a case where deferred payment is made:** where an assessee has opted and been allowed by the Department of Telecommunications, Government of India to make deferred payment,

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	the amount which would have been payable by the assessee had he opted for full upfront payment of spectrum fee irrespective of the tax year in which the liability for the expenditure was incurred according to the method of accounting regularly employed by the assessee. However, in case of deferred payment referred to in (b), where there is failure by the assessee to comply with any of the conditions specified by the scheme of the Department of Telecommunications, Government of India and the Department of Telecommunications terminates the allotment or assignment of spectrum, the Assessing Officer in exercise of power vested in him under section 52(5) of the Act, shall re-compute the total income of the assessee for the tax year in which the deduction has been claimed and granted to him by deeming that, (a) the total spectrum fee paid up to the date of termination is the amount "actually paid"; (b) the spectrum was in force up to the date of its termination for the purpose of determining the number of tax years as required by section 52(1)(Table: Sl. No. 3, Col. D) of the Act.
Equal instalments	1/ tax years mentioned in the above table

(iii) No depreciation: No depreciation shall be allowed in respect of the expenditure incurred on spectrum or licence, if the deduction under this section is claimed and allowed for any tax year.

(iv) deduction under any other section: No deduction shall be allowed under any other provision of the Act in respect of the expenditure incurred by an Indian company, wholly and exclusively for the purposes of amalgamation or

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demerger of an undertaking or amount paid to an employee in connection with his voluntary retirement as per any scheme of voluntary retirement.

Special Provision for voluntary retirement payments mentioned in SI. No. 2 of the table above

In case of amount paid to an employee in connection with his voluntary retirement as per any voluntary retirement scheme, where a specified business reorganisation takes place before the expiry of the period of 5 tax years over which deduction of expenditure is allowable, then

(1). the benefit of deduction shall continue to available to the successor entity as they would have applied to the predecessor entity if such reorganization had not taken place and

(2). no deduction shall be allowed to the predecessor entity under this section for the tax year in which such reorganisation takes place.

Specified business reorganisation means

(i) amalgamation of an Indian company and its undertaking with another Indian company; or

(ii) demerger of an undertaking of an Indian company to another company; or

(iii) succession of a firm or proprietorship concern to a company fulfilling conditions as laid down in section 70(1)(zd); or

(iv) conversion of a private company or unlisted public company to a LLP fulfilling conditions laid down in section 70(1)(ze).

Special Provision in respect of spectrum or licence mentioned in SI. No. 3 and 4 of the table above

(i) Transfer of spectrum or licence

Where a deduction has been claimed in this section in respect of a spectrum or licence and subsequently such spectrum or licence is transferred, following provisions shall apply:

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	Transaction	Manner of deduction
(1)	**Transfer of spectrum or licence**	
	Case 1: Licence or spectrum is transferred and proceeds of the transfer < the expenditure though incurred, but remaining unallowed	The expenditure remaining unallowed, as reduced by the proceeds of the transfer, shall be allowed in respect of the tax year in which the licence or spectrum is transferred. **Amount of deduction** = Expenditure remain unallowed – Sale proceeds
	Case 2: Licence or spectrum is transferred, whether in whole or in part, and the proceeds of the transfer > the amount of the expenditure though incurred, but remaining unallowed	The excess amount shall be chargeable to tax as profits and gains of business in the tax year in which the licence or spectrum has been transferred. However, the excess should not exceed the difference between the expenditure incurred to obtain the licence or spectrum and the amount of expenditure remaining unallowed.
		Taxable as profits and gains from business and profession = Sale proceeds - Expenditure remain unallowed **OR** Expenditure allowed till date Whichever is less
		If the licence/spectrum is transferred in a tax year in which the business is no longer in existence, the taxability would arise in the above manner as if the business is in existence in that tax year.
	Case 3: Licence or spectrum is transferred,	No deduction for such expenditure shall be allowed in the tax year in which

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	whether in whole or in part, and the proceeds of the transfer ≥ the amount of the expenditure incurred remaining unallowed	licence/ spectrum is transferred or in respect of any subsequent tax year(s). Amount of deduction = NIL
	Case 4: Where a part of the licence/ spectrum is transferred and the case is not covered under Case 2 above i.e., the proceeds of transfer of a part of the licence does not exceed the amount of expenditure remaining unallowed	Expenditure though incurred but remaining unallowed would be amortised in the following manner – (i) subtracting the proceeds of transfer from the expenditure remaining unallowed; and (ii) dividing the remainder by the number of relevant tax years which have not expired at the beginning of the tax year during which the licence or spectrum is transferred. **Amount of deduction** = Expenditure remaining unallowed **less** proceeds of transfer/ Remaining no of T.Ys
(2)	**Transfer of spectrum or licence in a scheme of amalgamation or demerger**	
	Licence or spectrum is sold or otherwise transferred by the amalgamating company or demerged company, in a scheme of amalgamation or demerger, to the amalgamated Indian company or resulting Indian company	The provisions of cases (1), (2), (3) and (4) above shall not apply to the amalgamating or demerged company; and all the provisions of this section shall continue to apply to the amalgamated or resulting company as it would have applied to the amalgamating or demerged company, as if the transfer had not taken place.

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(ii) Consequences of failure to comply with the conditions after grant of deduction for licence: In case any deduction has been claimed and granted in respect of an expenditure on licence in a tax year and subsequently there is failure on part of the assessee to comply with any of the provisions of this section, then,

- the deduction shall be deemed to have been wrongly allowed;
- the Assessing Officer may recompute the total income of the assessee for the said tax year and make the necessary rectification. This is notwithstanding anything contained in the Income-tax Act, 2025;
- the period of four years specified under section 287(8) for rectification of mistake apparent from record would be reckoned from the end of the tax year in which such the failure takes place.

ILLUSTRATION 10

X Ltd., providing telecommunication services, acquired a telecom licence at cost of ₹ 50 lakhs on 01.04.2024 for a period of 10 years. Assuming the telecom licence is transferred by X Ltd. in T.Y. 2026-27, say for: (a) ₹ 32 lakhs; (b) ₹ 43 lakhs or (c) ₹ 52 lakhs, and if:

(i) Whole of the license is transferred

(ii) Part of the license is transferred.

Explain, how the transfer shall be dealt with under the Income-tax Act, 2025 and the amount, if any, deductible for T.Y. 2026-27.

SOLUTION

(i) Whole of the license is transferred:

Particulars	₹ (in lakhs)
Cost of the licence	50
Less: Deduction u/s 52[5] for T.Y. 2024-25	5
	45
Less: Deduction u/s 52[6] for T.Y. 2025-26	5

[5] *under section 35ABB of the Income-tax Act, 1961*
[6] *under section 35ABB of the Income-tax Act, 1961*

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Expenditure remaining unallowed	40
(a) If transferred for ₹ 32 lakhs	
Proceeds from transfer	32
Deduction allowed u/s 52 in T.Y. 2026-27 (Expenditure remaining unallowed **as reduced by** the proceeds of transfer)	8
(b) If transferred for ₹ 43 lakhs	
Proceeds from transfer	43
Taxable as profits and gains from business and profession (Lesser of: ₹ 3 lakhs i.e., Proceed from transfer - Expense remain unallowed i.e. ₹ 43 lakhs - ₹ 40 lakhs **or** ₹ 10 lakhs i.e., expense allowed till date)	3
(c) If transferred for ₹ 52 lakhs	
Proceeds from transfer	52
Taxable as profits and gains from business and profession (Lesser of: ₹ 12 lakhs i.e., Proceed from transfer - Expense remain unallowed i.e. ₹ 52 lakhs - ₹ 40 lakhs or ₹ 10 lakhs i.e., expense allowed till date)	10
Short Term Capital Gains (₹ 52 lakhs - ₹ 40 lakhs - ₹ 10 lakhs)	2

(ii) Part of the license is transferred:

Particulars	₹ (in lakhs)
Cost of the licence	50
Less: Deduction u/s 52[7] for T.Y. 2024-25	5
	45
Less: Deduction u/s 52[8] for T.Y. 2025-26	5
Expenditure remaining unallowed	**40**
(a) If transferred for ₹ 32 lakhs	
Proceeds from transfer	32

[7] *under section 35ABB of the Income-tax Act, 1961*
[8] *under section 35ABB of the Income-tax Act, 1961*

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	Deduction allowed u/s 52 in T.Y. 2026-27 [₹ 40 lakhs - ₹ 32 lakhs)/ 8 years	1
(b)	**If transferred for ₹ 43 lakhs**	
	Proceeds from transfer	43
	Taxable as profits and gains from business and profession (Lesser of: ₹ 3 lakhs i.e., Proceeds from transfer - Expense remaining unallowed i.e. ₹ 43 lakhs - ₹ 40 lakhs **or** ₹ 10 lakhs i.e., expense allowed till date)	3
(**c**)	**If transferred for ₹ 52 lakhs**	
	Proceeds from transfer	52
	Amount taxable as profits and gains from business and profession (Lesser of: ₹ 12 lakhs i.e., Proceeds from transfer - Expense remaining unallowed i.e. ₹ 52 lakhs - ₹ 40 lakhs **or** ₹ 10 lakhs i.e., expense allowed till date)	10
Short Term Capital Gains (₹ 52 lakhs - ₹ 40 lakhs - ₹ 10 lakhs)		2

General conditions for allowable deductions [Section 34]

(i) **Revenue expenditure incurred for purposes of carrying on the business, profession or vocation:** This is a residuary section under which only business expenditure is allowable but not the business losses, e.g., those arising out of embezzlement, theft, destruction of assets, misappropriation by employees etc. The deduction is limited only to the amount actually expended and does not extend to a reserve created against a contingent liability.

(ii) **Conditions for allowance**: By virtue of section 34(1), following conditions should be fulfilled in order that a particular item of expenditure may be deductible under this section:

(a) The expenditure should **not** be of the nature specified in **sections 28 to 33, 44 to 49, 51and 52**

(b) It should **not** be in the nature of **any personal expenses** of the assessee.

(c) It should have been laid out or expended wholly and exclusively for the purposes of such business or profession.

(d) It should **not** be in the nature of **capital expenditure**.

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CIT v. Orient Ceramics and Industries Ltd. (2013) 358 ITR 49 (Delhi)

Issue: What is the nature of expenditure incurred on glow-sign boards displayed at dealer outlets - capital or revenue?

Analysis & Decision: The expenditure on glow sign boards displayed at dealer outlets is revenue in nature due to the following reasons-

(i) The expenditure incurred by the assessee on glow sign boards does not bring into existence an asset or advantage for the enduring benefit of the business, which is attributable to the capital.

(ii) The glow sign board is not an asset of permanent nature. It has a short life.

(iii) The materials used in the glow sign boards decay with the effect of weather. Therefore, it requires frequent replacement. Consequently, the assessee has to incur expenditure on glow sign boards regularly in almost each year.

(iv) The assessee incurred expenditure on the glow sign boards with the object of facilitating the business operation and not with the object of acquiring asset of enduring nature.



Mahle Anand Filter Systems Pvt. Ltd. v. ACIT [2023] 456 ITR 29 (SC)

Issue: Can foregoing a security deposit to settle a dispute be considered a revenue expenditure?

Analysis & Decision: When the assessee sought to vacate certain leased premises, disputes arose, and to end the dispute with the lessor, the assessee agreed not to claim the security deposit of ₹ 5.8 crores. The Apex Court affirmed the decision of the High Court which held that the amount of ₹ 5.8 crores could not be treated as revenue expenditure merely because it was paid in the course of a dispute. It is evident that the character of the amount was of a capital nature and remained so although assessee decided to forgo ₹ 5.8 crores (the security deposit).

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CIT v. ITC Hotels Ltd. (2011) 334 ITR 109 (Kar.)

Issue: Would the expenditure incurred on issue and collection of convertible debentures be treated as revenue expenditure or capital expenditure?

Decision: The expenditure incurred on the issue and collection of debentures would be treated as revenue expenditure even in case of convertible debentures, i.e., the debentures which had to be converted into shares at a later date.



PCIT vs. Adadyn Technologies (P.) Ltd. [2024] 465 ITR 409 (SC)

Issue: Whether the expenses incurred by the Assessee towards development of software for advertisement, which, due to technological development, had to be abandoned, can be claimed as revenue expenditure allowable?

Facts of the case: The assessee is a company engaged in the business of rendering customized internet advertising services to advertisers which could be used on the Desktop. In order to develop its software, assessee had incurred certain expenditure. Due to rapid change in the technology, the application sought to be developed by the assessee had become obsolete and the assessee abandoned further development.

Decision: The High Court held that since the product having been abandoned, the assessee shall not get any enduring benefit. In substance, assessee has incurred expenditure in these two years to develop a software but due to change in technology, it had to abandon the product. In effect, it had lost money spent on this product. Accordingly, the High Court held that the assessee shall not get any enduring benefit and therefore, the expenditure was to be treated as revenue in nature.



CIT v. Priya Village Roadshows Ltd. (2011) 332 ITR 594 (Delhi)

Issue: Would expenditure incurred on feasibility study conducted for examining proposals for technological advancement relating to the existing business be classified as a revenue expenditure, where the project was abandoned without creating a new asset?

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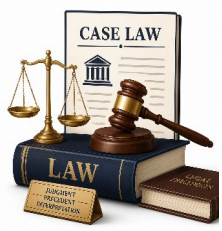
Analysis & Decision: Since the feasibility studies were conducted by the assessee for the existing business with a common administration and common fund and the studies were abandoned without creating a new asset, the expenses were of revenue nature.



National Co-operative Development Corporation v. CIT (2020) 427 ITR 288 (SC)

Issue: Is source of funds from which expenditure is incurred for the purpose of business relevant for the purpose of allowability of deduction under section 34(1)?

Analysis & Decision: In case of an assessee carrying on business, it is relevant to see whether an outlay constitutes an expenditure "for the purpose of business" as used in section 34(1), for the purpose of claiming deduction thereunder. **The source of funds from which the expenditure is made is not relevant.** Every application of income towards the business objective of the assessee is a business expenditure. There can be an amount treated as a capital receipt while the same amount expended may be a revenue expenditure.



Shanti Bhushan v. CIT (2011) 336 ITR 26 (Delhi)

Issue: Can the expenditure incurred on heart surgery of an assessee, being a lawyer by profession, be allowed as business expenditure under section 28, by treating it as current repairs considering heart as plant and machinery, or under section 34, by treating it as expenditure incurred wholly and exclusively for the purpose of business or profession?

Analysis & Decision: Though the definition of "plant" as per the provisions of section 66(17) is inclusive in nature, such plant must have been used as a business tool which is not true in case of heart. Therefore, the **heart cannot be said to be plant for the business or profession of the assessee. Therefore, the expenditure on heart surgery is not allowable as repairs to plant under section 28.**

Also, **there is no direct nexus between the expenses incurred by the assessee on the heart surgery and his efficiency in the professional field**. **Therefore, the claim for allowing the said expenditure under section 34 is also not tenable.** Hence, the heart surgery expenses shall **not** be allowed as a business expenditure of the assessee under the Income-tax Act.

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CIT v. Neelavathi & Others (2010) 322 ITR 643 (Karn)

Issue: Can payment to police personnel and gundas to keep away from the cinema theatres run by the assessee be allowed as deduction?

Analysis & Decision: Any payment made to the police illegally amounts to bribe and such illegal gratification cannot be considered as an allowable deduction. Similarly, any payment to a gunda as a precautionary measure so that he shall not cause any disturbance in the theatre run by the assessee is an illegal payment for which no deduction is allowable under the Act.



Honda Siel Cars India Ltd. v. CIT (2017) 395 ITR 713(SC)

Issue: Whether technical fee paid under a technical collaboration agreement for setting up a joint venture company in India is to be treated as revenue or capital expenditure, where, upon termination of the agreement, the joint venture would come to an end?

Analysis & Decision: If a limited right to use technical know-how is obtained for a limited period for improvising existing business, the expenditure is revenue in nature. However, if technical know-how is obtained for setting up a new business, the position may be different.

The very purpose of the technical collaboration agreement, in this case, was to set up the Joint Venture. The collaboration included not only transfer of technical information, but, complete assistance, actual, factual and on the spot, for establishment of plant, machinery, etc. so as to set up a manufacturing unit. Upon termination of technical collaboration agreement, the joint venture itself would come to an end. Therefore, in this case, **technical fee is capital in nature since upon termination of technical collaboration agreement, the joint venture itself would come to an end.**



Sharp Business System. V. CIT (2025) 2025 INSC 1481

Issue: Whether a non-compete fee paid by an assessee to its joint venture partner, as consideration for the latter refraining from competing in the same business, constitutes allowable revenue expenditure under section 34, or whether the same is to be treated as capital expenditure on account of the enduring benefit it confers upon the assessee?

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Analysis & Decision: The assessee, a joint venture between Sharp Corporation, Japan and Larsen & Toubro Limited (L&T), was engaged in importing, marketing and selling electronic office products in India. It paid ₹ 3 Cr. to L&T as non-compete fee, being consideration for L&T not setting up or undertaking competing business activities. The Assessing Officer treated the said payment as capital expenditure and made an addition to the assessee's income. This was affirmed by the CIT(A), ITAT and the Delhi High Court, all of which held the expenditure to be capital in nature.

The Supreme Court reversed the view of the courts and held that the non-compete fee paid by the assessee is an allowable revenue expenditure under section 34. The Court reasoned that the payment was made purely to enable the assessee to operate its existing business more efficiently and profitably, without resulting in the acquisition of any capital asset or the creation of a new profit-earning apparatus. The non-compete arrangement did not bring into existence any new asset or business structure; it merely removed a competitive obstacle from the assessee's existing commercial field.

The Court further elucidated that the length of time over which an enduring benefit may accrue to the payer is not determinative of the character of the expenditure. Where a payment facilitates the more efficient and profitable conduct of the existing business without touching the fixed capital structure, it retains its revenue character even if the benefit persists over a period of time. Accordingly, the expenditure was held to be deductible under section 34(1).

(iii) Following expenditures are not considered as "laid out or expended wholly and exclusively for business or profession of the assessee" and accordingly are not allowed as deduction u/s 34(1):

(a) an expenditure incurred for any purpose which is an offence or is prohibited by law; or

(b) an expenditure incurred on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013; or

(c) an expenditure incurred on advertisement in any souvenir, brochure, tract, pamphlet or the like, published by a political party.

An expenditure incurred for any purpose which is an offence or is prohibited by law, as mentioned in (a) above, shall include expenditure incurred for -

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(i) any purpose which is an offence under, or is prohibited by, any law in force in or outside India; or

(ii) providing a benefit or perquisite in any form to a person, who may or may not be carrying on a business or exercising a profession, when its acceptance by the person is in violation of any law or rule or regulation or guideline governing the conduct of that person; or

(iii) compounding an offence under any law in force in or outside India; or

(iv) settling proceedings initiated in relation to contravention under any law notified by the Central Government in this behalf.



Notification no. 38/2025 dated 23.4.2025

The Central Government has, vide notification no. 38/2025 dated 23.4.2025, notified that any expenditure incurred to settle proceedings initiated in relation to contravention or defaults under the following laws shall not be deemed to have been incurred for the purpose of business or profession and no deduction or allowance shall be made in respect of such expenditure –

(a) the Securities and Exchange Board of India Act, 1992;

(b) the Securities Contracts (Regulation) Act, 1956;

(c) the Depositories Act, 1996;

(d) the Competition Act, 2002.



Expenses incurred in providing freebies to medical practitioner by pharmaceutical and allied health sector industry are in violation of the provisions of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations. Hence, such expenditure is considered to be expenses prohibited by the law and not allowed in the hands of such pharmaceutical or allied health sector industry or other assessee which has provided aforesaid freebie.

The Supreme Court, in Apex Laboratories Pvt. Ltd. v. DCIT (2022) 442 ITR 1, held that the incentives (or "freebies") given by the pharmaceutical company, to the doctors, had a direct result of exposing the recipients to the odium of sanctions, leading to a ban on their practice of medicine. Those sanctions are mandated by law, as they are embodied in the code of conduct and ethics, which are normative,

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and have legally binding effect. The conceded participation of the assessee – Pharmaceutical company, i.e., the provider or donor, was plainly prohibited, as far as their receipt by the medical practitioners was concerned. That medical practitioners were forbidden from accepting such gifts, or "freebies" was no less a prohibition on the part of their giver, or donor, i.e., pharmaceutical company.

Thus, pharmaceutical companies' gifting freebies to doctors is clearly "prohibited by law" and not allowed to be claimed as a deduction under section 34(1). Doing so would wholly undermine public policy.



Millennia Developers (P) Ltd. v. DCIT (2010) 322 ITR 401 (Karn.)

Issue: Is the amount paid by a construction company as regularization fee for violating building bye-laws allowable as deduction?

Analysis & Decision: The assessee, a private limited company carrying on business activity as a developer and builder, claimed the amount paid by way of regularization fee for the deviations made while constructing a structure and for violating the plan sanctioned in terms of the building bye-laws, approved by the municipal authorities as per the provisions of the Karnataka Municipal Corporations Act, 1976.

As per the provisions of the Karnataka Municipal Corporations Act, 1976, **the amount paid to compound an offence is obviously a penalty and hence, does not qualify for deduction under section 34**. Merely describing the payment as a compounding fee would not alter the character of the payment.



CIT v. Kap Scan and Diagnostic Centre P. Ltd. (2012) 344 ITR 476 (P&H)

Issue: Can the commission paid to doctors by a diagnostic centre for referring patients for diagnosis be allowed as a business expenditure under section 34 or would it be treated as illegal and against public policy to attract disallowance?

Analysis & Decision: As per the Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002, no physician shall give, solicit, receive,

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or offer to give, solicit or receive, any gift, gratuity, commission or bonus in consideration of a return for referring any patient for medical treatment.

The demanding as well as paying of such commission is bad in law. It is not a fair practice and is opposed to public policy and should be discouraged. Thus, **the commission paid to doctors for referring patients for diagnosis is not allowable as business expenditure.**

Important clarifications/Circulars



Expenditure incurred on Keyman insurance policy [Circular no. 762/1998 dated 18.02.1998]

CBDT clarifies that the premium paid on the Keyman Insurance Policy is allowable as business expenditure.

The High Court of Punjab and Haryana has, in the case of *M/s. Ramesh Steels, ITA No. 437 of 2015*, vide judgement dated 2.2.2016, reiterating the above view, held that, "the said policy when obtained to secure the life of a partner to safeguard the firm against a disruption of the business is equally for the benefit of the partnership business which may be effected as a result of premature death of a partner. Thus, the premium on the Keyman Insurance Policy of partner of the firm is wholly and exclusively for the purpose of business and is allowable as business expenditure".

In view of the above, the CBDT has clarified that in case of a firm, premium paid by the firm on the Keyman Insurance Policy of a partner, to safeguard the firm against a disruption of the business, is an admissible expenditure under section 34 of the Income-tax Act, 2025.



Treatment of expenditure incurred for development of roads/ highways in Build-Operate-Transfer (BOT) agreements [Circular No. 09/2014, dated 23.04.2014]

The CBDT has, vide this Circular, clarified the tax treatment of expenditure incurred on development and construction of infrastructural facilities like roads/highways on Build-Operate-Transfer (BOT) basis with right to collect toll - whether the same is entitled to depreciation under section 33 of Income-tax Act, 2025 or can be amortized by treating it as an allowable business expenditure under the relevant provisions of the Income-tax Act.

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Generally, the BOT basis projects are entered into between the developer and the government or the notified authority, on the following terms:

(i) In such projects, the developer, in terms of concessionaire agreement with Government or its agencies, is required to construct, develop and maintain the infrastructural facility of roads/highways which, *inter alia*, includes laying of road, bridges, highways, approach roads, culverts, public amenities etc. at its own cost and its utilization thereof for a specified period.

(ii) The possession of land is handed over to the assessee (i.e., the developer) by the Government/ notified authority for the purpose of construction of the project without any actual transfer of ownership. The assessee, therefore, has only a right to develop and maintain such asset. It also enjoys the benefits arising from the use of asset through collection of toll for a specified period, without having actual ownership over such asset. Therefore, the rights in the land remain vested with the Government/ notified agencies.

(iii) Since the assessee does not hold any rights in the project except recovery of toll fee to recoup the expenditure incurred, it cannot be treated as an owner of the property, either wholly or partly, for purposes of allowability of depreciation under section 33(1)(b). Thus, claim of depreciation on toll ways is not allowable due to non-fulfillment of ownership criteria in such cases.

(iv) Where the assessee incurs expenditure on a project for development of roads/highways, it is entitled to recover cost incurred towards development of such facility (comprising of construction cost and other pre-operative expenses) during construction period. Further, expenditure incurred by the assessee on such BOT projects brings to it an enduring benefit in the form of right to collect the toll during the period of agreement.

The Supreme Court, in *Madras Industrial Investment Corporation Ltd. vs. CIT [1997] 225 ITR 802,* allowed the spreading over of liability over a number of years on the ground that there was continuing benefit to the company over a period. Therefore, analogously, expenditure incurred on an infrastructure project for development of roads/highways under BOT agreement may be treated as having been made/ incurred for the purposes of business or profession of the assessee and same shall be allowed to be spread during the tenure of concessionaire agreement.

In view of the above, the CBDT clarifies that the cost of construction on development of infrastructure facility, being roads/highways under BOT projects,

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may be amortized and claimed as allowable business expenditure under the Act in the following manner:

(i) The amortization allowable may be computed at the rate which ensures that the whole of the cost incurred in creation of infrastructural facility of road/highway is amortised evenly over the period of concessionaire agreement after excluding the time taken for creation of such facility.

(ii) Where an assessee has claimed any deduction out of initial cost of development of infrastructure facility of roads/highways under BOT projects in earlier years, the total deduction so claimed for the tax years prior to tax year under consideration may be deducted from the initial cost of infrastructure facility of roads/highways and the cost so reduced shall be amortised equally over the remaining period of toll concessionaire agreement.

The clarification given in this Circular is applicable only to those infrastructure projects for development of road/highways on BOT basis where ownership is not vested with the assessee under the concessionaire agreement.

ILLUSTRATION 11

Isac limited is a company engaged in the business of biotechnology. The net profit of the company for the financial year ended 31.03.2027 is ₹ 35,25,890 after debiting the following items:

S. No.	Particulars	₹
1.	*Purchase price of raw material used for the purpose of in-house research and development*	*11,80,000*
2.	*Purchase price of asset used for in-house research and development*	
	(a) Land	*5,00,000*
	(b) Building	*3,00,000*
3.	*Expenditure incurred on notified agricultural extension project*	*25,50,000*
4.	*Expenditure on notified skill development project:*	

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	(a) Purchase of land	*40,00,000*
	(b) Expenditure on training for skill development	*32,50,000*
5.	*Expenditure incurred on advertisement in the souvenir published by a political party*	*75,000*
6.	*Expenditure incurred on issue of right shares*	*80,000*
7.	*Expenditure incurred on issue of debentures*	*50,000*
8.	*Penalty paid under GST Act*	*35,000*
9.	*Interest paid on loan taken from bank for payment of advance income-tax*	*60,000*
10.	*Provision for loss of subsidiary*	*85,000*

Compute the income under the head "Profits and gains of business or profession" for the T.Y. 2026-27 of Isac Ltd. assuming that the company does not opt for the provisions of section 200.

SOLUTION

Computation of income under the head "Profits and gains of business or profession" for the T.Y.2026-27

Particulars	₹	₹
Net profit as per profit and loss account		**35,25,890**
Add: **Items debited to profit and loss account, but to be disallowed**		
Purchase price of raw material used for the purpose of in-house research and development – qualifies for 100% deduction u/s 45(2)	-	
Purchase price of land used in in-house research and development - being capital expenditure not allowable as deduction under section 45	5,00,000	
Purchase price of building used in in-house research and development - being capital		

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	expenditure, 100% of which is allowable as deduction u/s 45(1)	-	
	Expenditure incurred on notified agricultural extension project – 100% deduction is allowed under section 47	-	
	Expenditure incurred on notified skill development project - Purchase of land - being capital expenditure not qualifying for deduction under section 47	40,00,000	
	Expenditure incurred on notified skill development project - Expenditure on training for skill development – 100% deduction is allowed under section 47	-	
	Expenditure incurred on advertisement in the souvenir published by a political party not allowed as deduction as per section 34(2)(c)	75,000	
	Expenditure incurred on issue of right shares not allowed as deduction since expenses is of capital nature	80,000	
	Expenditure incurred on issue of debentures [allowable]	-	
	Penalty paid under GST Act - Not allowed as deduction	35,000	
	Interest paid on loan taken from bank for payment of advance income-tax not allowed as deduction since the same is not for the purpose of business or profession	60,000	
	Provision for loss of subsidiary not allowed as deduction	85,000	**48,35,000**
Profit and gains from business			**83,60,890**

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Note: The expenditure incurred on advertisement in the souvenir published by a political party is disallowed as per section 34(2)(c) while computing income under the head "Profit and Gains of Business or Profession" but the same would be allowed as deduction under section 136 from the gross total income of the company.

3.7 AMOUNTS NOT DEDUCTIBLE IN CERTAIN CIRCUMSTANCES [SECTION 35]

Section 35 provides for disallowance of certain expenses as follows:

Amounts are not deductible in the case of all assessees

(i) Taxes on income [Section 35(a)]

Section 35(a) provides for disallowance of following amounts:-

(a) tax paid on income,

(b) tax paid by employer referred to in Schedule III (Table: Sl. No. 10) i.e., tax on non-monetary perquisites of employees, paid by the employer or

(c) tax paid in any other country for which relief is eligible under section 159 or 160 (Double Taxation Relief)

Any surcharge or cess on such tax are treated as includible in tax and accordingly they are also not allowed as deduction.



Tax paid on non-monetary perquisites on behalf of employees - *In case of an employee, deriving income in the nature of perquisites (other than monetary payments), the amount of tax on such income paid by his employer is exempt from tax in the hands of that employee.*

Section 35(a)(ii) provides that, such payment of tax is not allowed as deduction from the income of the employer. Thus, the payment of tax on non-monetary perquisites by an employer on behalf of employee will be exempt from tax in the hands of employee but will not be allowable as deduction in the hands of the employer.

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(ii) Sum payable to a resident where there is a default of deduction of tax at source [Section 35(b)(i)]

Section 35(b)(i) provides that **30% of any sum payable to a resident**, on which tax is deductible at source under Chapter XIX-B, shall be disallowed if–

(i) such tax has not been deducted during the tax year; or

(ii) such tax, after deduction during the tax year, has not been paid upto the due date specified in section 263(1).

Where in respect of such sum, tax is deducted in any subsequent year or is deducted during the tax year but paid after the due date specified in section 263(1), 30% of such sum shall be allowed as deduction in computing the income of the tax year in which such tax has been paid.

Where the assessee is required to and fails to deduct the whole or any part of tax on any such sum but is not deemed as assessee in default under section 398(2) by reason that such payee –

(i) has furnished his return of income under section 263;

(ii) has taken into account such sum for computing income in that return of income; and

(iii) has paid the tax due on the income declared by him in such return of income, and the payer furnishes a certificate to this effect from an accountant in such form as may be prescribed,

it would be deemed that the assessee has deducted and paid the tax on such sum on the date on which return of income has been furnished by the payee.



Since the date of furnishing the return of income by the payee is taken to be the date on which the payer has deducted tax at source and paid the same, 30% of such expenditure/payment in respect of which the payer has failed to deduct tax at source shall be disallowed under section 35(b)(i) in the year in which the said expenditure is incurred. However, 30% of such expenditure will be allowed as deduction in the subsequent year in which the return of income is furnished by the payee, since tax is deemed to have been deducted and paid by the payer in that year.

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Tax on royalty paid to Mr. A, a resident, has been deducted during the tax year 2026-27, the same has to be paid by 31st August/ 31ts October 2027, as the case may be. Otherwise, 30% of royalty paid would be disallowed in computing the income for T.Y. 2026-27. If in respect of such royalty, tax deducted during the T.Y.2026-27 has been paid after 31st August/ 31st October, 2027, 30% of such royalty disallowed in T.Y. 2026-27, would be allowed as deduction in the year of payment, i.e. T.Y. 2027-28.

ILLUSTRATION 12

Delta Ltd. credited the following amounts to the account of resident payees in the month of March, 2027 without deduction of tax at source. What would be the consequence of non-deduction of tax at source by Delta Ltd. on these amounts during the tax year 2026-27, assuming that the resident payees in all the cases mentioned below have not paid the tax, if any, which was required to be deducted by Delta Ltd.?

	Particulars	***Amount (₹)***
(1)	*Salary to its employees (credited and paid in March, 2027)*	*14,00,000*
(2)	*Directors' remuneration (credited in March, 2027 and paid in April, 2027)*	*28,000*

Would your answer change if Delta Ltd. has deducted tax on directors' remuneration in April, 2027 at the time of payment and remitted the same in July, 2027?

SOLUTION

Non-deduction of tax at source on any sum payable to a resident on which tax is deductible at source as per the provisions of Chapter XIX-B would attract disallowance under section 35(b)(i).

Therefore, non-deduction of tax at source on any sum paid by way of salary on which tax is deductible under section 392 or any sum credited or paid by way of directors' remuneration on which tax is deductible under section 393(1) [Table: Sl.No.6(iii)(c)], would attract disallowance@30% under section 35(b)(i). Whereas in case of salary, tax has to be deducted at the time of payment, in case of directors' remuneration, tax has to be deducted at the time of credit of such sum to the account of the payee or at the time of payment, whichever is earlier.

Therefore, in both cases, i.e., salary and directors' remuneration, tax is deductible

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in the T.Y.2026-27, since salary was paid in that year and directors' remuneration was credited in that year. Therefore, the amount to be disallowed under section 35(b)(i) while computing business income for T.Y.2026-27 is as follows –

	Particulars	Amount paid in ₹	Disallowance u/s 35(b)(i)@ 30% (₹)
(1)	Salary [tax is deductible under section 392]	14,00,000	4,20,000
(2)	Directors' remuneration [tax is deductible under section 393(1) [Table: S.No.6(iii)(c)], without any threshold limit]	28,000	8,400
Disallowance under section 35(b)(i)			**4,28,400**

If the tax is deducted on directors' remuneration in the next year i.e., T.Y.2027-28 at the time of payment and remitted to the Government, the amount of ₹ 8,400 would be allowed as deduction while computing the business income of T.Y. 2027-28.



Disallowance of any sum paid to a resident at any time during the tax year without deduction of tax under section 35(b)(i) [Circular No.10/2013 dated 16.12.2013]

There have been conflicting interpretations by judicial authorities regarding the applicability of provisions of section 35(b)(i)

with regard to the amount not deductible in computing the income chargeable under the head 'Profits and gains of business or profession'. Some court rulings have held that the provisions of disallowance under section 35(b)(i) apply only to the amount which remained payable at the end of the relevant financial year and would not be invoked to disallow the amount which had actually been paid during the tax year without deduction of tax at source.

Departmental View: The CBDT's view is that the provisions of section 35(b)(i) would cover not only the amounts which are payable as on 31st March of a tax year but also amounts which are payable at any time during the year. The statutory provisions are amply clear and in the context of section 35(b)(i) the term "payable" would include "amounts which are paid during the tax year".

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ILLUSTRATION 13

During the tax year 2026-27, the following payments/expenditure were made/incurred by Mr. Yuvan Raja, a resident individual (whose turnover during the year ended 31.3.2026 was ₹ 99 lakhs):

(i) Interest of ₹ 45,000 was paid to Rehman & Co., a resident partnership firm, without deduction of tax at source;

(ii) ₹ 15,00,000 was paid as salary to a resident individual without deduction of tax at source;

(iii) Commission of ₹ 26,000 was paid to Mr. Vidyasagar, a resident, on 2.7.2026 without deduction of tax at source.

Briefly discuss whether any disallowance arises under the provisions of section 35(b)(i) of the Income-tax Act, 2025 assuming that the payees in all the cases mentioned above, have not paid the tax, if any, which was required to be deducted by Mr. Raja?

SOLUTION

Disallowance under section 35(b)(i) of the Income-tax Act, 2025 is attracted where the assessee fails to deduct tax at source as is required under the Act, or having deducted tax at source, fails to remit the same to the credit of the Central Government within the stipulated time limit.

(i) The obligation to deduct tax at source from interest paid to a resident arises under section 393(1) (Table: S.No. 5(iii)) in the case of an individual, whose total turnover exceeds ₹ 1 crore during the tax year immediately preceding the tax year, i.e., T.Y.2025-26. Thus, in present case, since the turnover of the assessee is less than ₹ 100 lakhs in T.Y. 2025-26, he is not liable to deduct tax at source. Hence, disallowance under section 35(b)(i) is not attracted in this case.

(ii) Under section 35(b)(i), disallowance of 30% of the sum payable would be attracted in respect of all sums on which tax is deductible under Chapter XIX-B. Section 392, which requires deduction of tax at source from salary paid, is covered under Chapter XIX-B. The obligation to deduct tax at source under section 392 arises, in the hands all assessee-employer even if the turnover does not exceed ₹ 1 crore during the tax year immediately preceding the tax year.

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Therefore, in the present case, the disallowance under section 35(b)(i) is attracted for failure to deduct tax at source under section 392 from salary payment. However, only 30% of the amount of salary paid without deduction of tax at source would be disallowed i.e. ₹ 4,50,000 (₹ 15 lakhs × 30%).

(iii) The obligation to deduct tax at source under section 393(1) [Table: S.No. 1(ii)] from commission paid in excess of ₹ 20,000 to a resident arises in the case of an individual, whose total turnover exceeds ₹ 1 crore during the tax year immediately preceding the tax year, i.e., T.Y.2025-26. Thus, in present case, since the turnover of the assessee is less than ₹ 1 crore in T.Y. 2025-26, he is not liable to deduct tax at source under section 393(1) [Table: S.No. 1(ii)]. Mr. Raja is not required to deduct tax at source u/s 393(1) [Table: S.No. 6(ii)(c)] also since the aggregate of such commission to Mr. Vidyasagar does not exceed ₹ 50 lakhs during the T.Y. 2026-27. Therefore, disallowance under section 35(b)(i) is not attracted in this case.

(iii) Sum payable to a non-resident where there is a default of deduction of tax at source [Section 35(b)(ii)]

Section 35(b)(ii) provides for 100% disallowance of any interest, royalty, fees for technical services or other sum chargeable under this Act, which is payable,-

(a) outside India or

(b) in India to a non-resident, not being a company or to a foreign company,

on which tax is deductible at source under Chapter XIX-B and such tax has not been deducted during the tax year or, after deduction during the tax year, has not been paid upto the due date specified in section 263(1).

It is also provided that where in respect of any such sum, tax is deducted in any subsequent year, or is deducted during the tax year but paid after the due date specified in section 263(1), such sum shall be allowed as a deduction in computing the income of the tax year in which such tax has been paid.

Where the assessee is required to and fails to deduct the whole or any part of tax on any such sum but is not deemed as assessee in default under section 398(2) by reason that such payee –

(i) has furnished his return of income under section 263;

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(ii) has taken into account such sum for computing income in that return of income; and

(iii) has paid the tax due on the income declared by him in such return of income, and the payer furnishes a certificate to this effect from an accountant in such form as may be prescribed,

it would be deemed that the assessee has deducted and paid the tax on such sum on the date on which return of income has been furnished by the payee.



Since the date of furnishing the return of income by the payee is taken to be the date on which the payer has deducted tax at source and paid the same, such expenditure/payment in respect of which the payer has failed to deduct tax at source shall be disallowed under section 35(b)(ii) in the year in which the said expenditure is incurred. However, such expenditure will be allowed as deduction in the subsequent year in which the return of income is furnished by the payee, since tax is deemed to have been deducted and paid by the payer in that year.



CIT v. Maruti Suzuki India Limited (2018) 407 ITR 165 (Del)

Issue: Can payments made by an assessee to a non-resident agent who does not have any income assessable in India be disallowed under section 35(b)(ii) for non-deduction of tax at source on the ground that no application was made by the assessee under section 395(2) for making deduction of tax at source at Nil rate?

Analysis & Decision: The non-resident agent who operated outside India did not have any income arising in India. Accordingly, **the commission earned by a non- resident agent who was in the business of selling Indian goods abroad, did not accrue or arise in India, and hence, no tax was deductible on such commission payment to a non-resident agent.**

Since the assessee has made payment to a non-resident agent and such income is not chargeable to tax in India, section 35(b)(ii) could not be invoked to disallow deduction of such payment for non-deduction of tax at source while computing the business income of the assessee.

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(iv) Contribution to a provident fund or the fund established for the benefit of employees [Section 35(b)(iii)]

Section 35(b)(iii) provides for disallowance of any contribution to a provident fund or the fund established for the benefit of employees of the assessee, unless the assessee has made effective arrangements to make sure that tax shall be deducted at source from any payments made from the fund which are chargeable to tax under the head 'Salaries'.

(v) Salaries payable outside India or to non-resident where there is a default of deduction of tax at source [Section 35(c)]

Section 35(c) provides for disallowance of any sum which is chargeable under the head 'Salaries' if it is payable outside India or to a non-resident on which tax is deductible at source under Chapter XIX-B and if such tax has not been deducted or after deduction has not been paid.

(vi) Amounts are not deductible in case of State Government Undertaking

As per section 35(d), any amount

(i) paid by way of royalty, licence fee, service fee, privilege fee, service charge, etc., which is levied exclusively on, or

(ii) any amount appropriated, directly or indirectly, from

a State Government undertaking by the State Government would not be allowed as deduction.

A State Government undertaking includes –

(a) a corporation established by or under any Act under State Act

(b) a company in which more than 50% of the paid up equity share capital is held by the State Government

(c) a company in which more than 50% of the paid up equity share capital is held singly or jointly by (a) or (b);

(d) a company or corporation in which the State Government has the right to appoint the majority of directors or to control the management or policy decisions, directly or indirectly, including by virtue of its shareholding or

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management rights or shareholders agreements or voting agreements or in any other manner

(e) an authority, a board or an institution or a body established or constituted by or under any State Act or owned or controlled by the State Government.

(vii) Amounts are not deductible in case of any firm assessable as such or a limited liability partnership (LLP)

(1) Remuneration to non-working partner - Any expenditure in the nature of salary, bonus, commission or remuneration, by whatever name called, to any partner who is not a working partner would not be allowed as deduction. (In the following discussion, the term 'remuneration' is applied to denote payments in the nature of salary, bonus, commission);

(2) Remuneration to a working partner and interest to any partner not authorized by deed or authorized by deed but relates to an earlier period - Any expenditure on the remuneration to a working partner and interest to any partner would not be allowed as deduction if it is –

- not authorised by the partnership deed applicable for the period for which such remuneration or interest is paid or
- authorised by and is as per the terms of partnership deed but relates to the period prior to the date of such partnership deed, or which was not authorised by the earlier partnership deed



If a firm incorporates the clause relating to payment of remuneration to the working partners, by executing an appropriate deed, say, on July 1, 2026 but effective from April 1, 2026, the firm will get deduction for the remuneration paid to its working partners from July 1, 2026 onwards, but not for the period from April 1 to June 30. It will not be possible to give retrospective effect to oral agreements entered into vis-a-vis such remuneration prior to putting the same in a written partnership deed.

(3) Remuneration to a working partner in excess of prescribed limits - Any remuneration paid to a working partner, authorised by a partnership deed and falling after the date of the deed in excess of the following limits:

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Book Profits	Quantum of deduction
On the first ₹ 6 lakh of book profit or in case of a loss	₹ 3,00,000 or 90% of book profit, whichever is higher
On the balance of the book profit	60% of book profit

Meaning of certain terms

Term	Meaning
Book Profit	The net profit as shown in the profit and loss account for the relevant tax year computed as per the provisions for computing income from profits and gains. The above amount should be increased by the aggregate remuneration to all the partners of the firm if such amount has been deducted while computing the net profit.
Working partner	An individual who is actively engaged in conducting the affairs of the business or profession of the firm of which he is a partner.

ILLUSTRATION 14

A firm assessed as such has paid ₹ 8,50,000 as remuneration to its partners for the T.Y.2026-27, as authorized by its partnership deed, and it has a book profit of ₹ 10 lakhs as computed under section 35(e). What is the remuneration allowable as deduction?

SOLUTION

The allowable remuneration calculated as per the limits specified in section 35(e)(iii) would be –

Particulars	₹
On first ₹ 6 lakh of book profit [₹ 6,00,000 × 90%]	5,40,000
On balance ₹ 4 lakh of book profit [₹ 4,00,000 × 60%]	2,40,000
	7,80,000

The excess amount of ₹ 70,000 (i.e., ₹ 8,50,000 – ₹ 7,80,000) would be disallowed as per section 35(e)(iii).

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(4) Interest to any partner as authorized by the deed in excess of 12% p.a. - Any interest to any partner as authorized by the partnership deed exceeding 12% simple interest p.a. would be disallowed.

(5) (i) Where an individual is a partner in a firm in a representative capacity:

(a) interest paid by the firm to such individual otherwise than as partner in a representative capacity shall not be taken into account for the purposes of disallowance under this clause.

(b) interest paid by the firm to such individual as partner in a representative capacity and interest paid by the firm to the person so represented shall be taken into account for the purposes of disallowance under this clause.

(ii) Where an individual is a partner in a firm otherwise than in a representative capacity, interest paid to him by the firm to such individual shall not be taken into account for the purposes of disallowance under this clause if he receives the same on behalf of or for the benefit of any other person.



Mr. A is a partner in ABC & Co. on behalf of Shah HUF. Interest to its partners @15% is authorised by ABC & Co. ABC & Co. pays ₹ 7 lakhs as interest to Mr. A out of which ₹ 4 lakhs on the funds advanced by Mr. A in his individual capacity and ₹ 3 lakhs on the funds advanced by him in his representative capacity on behalf of Shah HUF. The interest of ₹ 4 lakhs paid to Mr. A in his individual capacity is allowed as deduction subject to section 36(2) and shall not be taken into account for purpose of section 35(e). Whereas the interest paid to Mr. A in his representative capacity would be allowed to the extent of ₹ 40 lakhs i.e., ₹ 3 lakhs/15% x 12%.

ILLUSTRATION 15

Rao & Jain, a partnership firm consisting of two partners, reports a net profit of ₹ 17,00,000 before deduction of the following items:

(1) Salary of ₹ 40,000 each per month payable to two working partners of the firm (as authorized by the deed of partnership).

(2) Depreciation on plant and machinery under section 33 (computed) ₹ 1,50,000.

(3) Interest on capital at 15% per annum (as per the deed of partnership). The amount of capital eligible for interest is ₹ 5,00,000.

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Compute:

(i) Book-profit of the firm under section 35(e) of the Income-tax Act, 2025.

(ii) Allowable working partner salary for the tax year 2026-27 as per section 35(e).

SOLUTION

(i) As per 35(e)(v), "book profit" shall mean the net profit as per the profit and loss account for the relevant tax year computed as per Chapter IV-D as increased by the aggregate amount of the remuneration to all the partners of the firm if the such amount has been already deducted while computing the net profit.

In the present case, the net profit given is before deduction of depreciation on plant and machinery, interest on capital of partners and salary to the working partners. Therefore, the book profit shall be as follows:

Computation of Book Profit of the firm under section 35(e)

Particulars	₹	₹
Net Profit (before deduction of depreciation, salary and interest)		17,00,000
Less: Depreciation under section 33	1,50,000	
Interest @ 12% p.a. [being the maximum allowable as per section 35(e)] (₹ 5,00,000 × 12%)	60,000	2,10,000
Book Profit		**14,90,000**

(ii) Salary actually paid to working partners = ₹ 40,000 × 2 × 12 = ₹ 9,60,000.

As per the provisions of section 35(e)(iii), the salary paid to the working partners is allowed subject to the following limits –

On the first ₹ 6,00,000 of book profit or in case of a loss	₹ 3,00,000 or 90% of book profit, whichever is more
On the balance of the book profit	60% of the balance book profit

Therefore, the maximum allowable working partners' salary for the T.Y. 2026-27 in this case would be:

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Particulars	₹
On the first ₹ 6,00,000 of book profit [(₹ 3,00,000 or 90% of ₹ 6,00,000) whichever is more]	5,40,000
On the balance of book profit [60% of (₹ 14,90,000 - ₹ 6,00,000)]	5,34,000
Maximum allowable partners' salary	**10,74,000**

Hence, allowable working partners' salary for the T.Y. 2026-27 as per the provisions of section 35(e)(iii) is ₹ 9,60,000.

(viii) Amounts are not deductible in case of an association of persons or body of individuals

As per section 35(f), the expenditure incurred by an AOP or a BOI in the nature of interest, salary, bonus, commission or remuneration, by whatever name called, made to a member of such association or body shall not be allowed as a deduction in computing the income of the association or body.

It has been further provided that

- where interest has been paid by an AOP or BOI to its member and such member has also paid interest to the AOP/BOI, then only such excess interest, if any, paid by the association or body shall not be allowed as deduction under this clause.
- Where an individual is a member in an AOP/BOI in a representative capacity:
  - (a) the disallowance under this clause shall not be applicable in respect of interest paid to or received from such individual otherwise than his capacity as representative capacity.
  - (b) the disallowance under this clause shall be applicable in respect of interest paid to or received from an individual in his representative capacity.
  - (c) the disallowance under this clause shall not be applicable in respect of interest paid to a member, otherwise than as representative member, on behalf or for the benefit of any other person.

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3.8 EXPENSES OR PAYMENTS NOT DEDUCTIBLE IN CERTAIN CIRCUMSTANCES [SECTION 36]

Section 36 provides the circumstances in which expenses or payments are not deductible. The provisions of this section shall apply even if they conflict with any other provision of the Act relating to computation of income under the head "Profits and gains of business or profession".

(i) Payments to relatives and associates

Section 36(2) provides that if the assessee incurs any expenditure for which payment has been or is to be made to any specified person *[See column (2) of Table below)* which in the opinion of the Assessing Officer is excessive or unreasonable having regard to the:

(a) fair market value of the goods, service of facilities; or

(b) legitimate needs of the business or profession carried on by the assessee; or

(c) benefit derived by or accruing to the assessee therefrom,

so much of the expenditure as considered excessive or unreasonable by the Assessing Officer shall not be allowed as deduction.

"Specified Person" for different categories of assessees has been defined in section 36(3) as follows:

Assessee	Specified Person
(1)	**(2)**
Individual	1. Any relative of the individual assessee 2. Any person who carries on a business or profession, if • the individual has a substantial interest in the business of that person **or** • any relative of the individual has a substantial interest in the business of that person
Company, Firm, HUF or AOP	1. Any director, partner of the firm or member of the family or association or any relative of such director, partner or member or

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<table>
<tr><td></td><td>2. In case of a company assessee, any individual who has substantial interest in the business or profession of the company or any relative of such individual or
3. Any person who carries on a business or profession, in which the Company/ Firm/ HUF/ AOP or director of the company, partner of the firm or member of the family or association or any relative of such director, partner or member has substantial interest in the business of that person.</td></tr>
<tr><td>All assessees</td><td>The following are specified persons:
<table>
<tr><th>Person who has substantial interest in the assessee's business</th><th>Other related persons of such person, who has a substantial interest in the assessee's business</th></tr>
<tr><td>Company/ AOP/ Firm/ HUF</td><td>♦ Any director of such company, partner of such firm or the member of such family or association <u>or</u>
♦ Any relative of such director, partner or member <u>or</u>
♦ Any other company carrying on business or profession in which the first mentioned company has a substantial interest</td></tr>
<tr><td>A director, partner or member</td><td>♦ Company/ Firm/ AOP/ HUF of which he is a director, partner or member <u>or</u>
♦ Any other director/ partner/ member of such Company/ Firm/ AOP/ HUF <u>or</u>
♦ Any relative of such director, partner <u>or</u> member</td></tr>
</table></td></tr>
</table>

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Relative in relation to an Individual means the spouse, brother or sister or any lineal ascendant (maternal as well as paternal) or descendant of that individual [Section 2(94)].

Substantial interest in a business or profession

A person shall be deemed to have a substantial interest in a business or profession if -

- in a case where the business or profession is carried on by a company, such person is, at any time during the tax year, the beneficial owner of equity shares carrying not less than 20% of the voting power and
- in any other case, such person is, at any time during the tax year, beneficially entitled to not less than 20% of the profits of such business or profession.



CIT v. Great City Manufacturing Co. (2013) 351 ITR 156 (All)

Issue: Can remuneration paid to working partners as per the partnership deed be considered as unreasonable and excessive for attracting disallowance under section 36(2), even though the same is within the statutory limit prescribed under section 35(e)(iii)?

Analysis & Decision: Section 35(e)(iii) prescribes the limit of remuneration to working partners, and deduction is allowable up to such limit while computing the business income. If the remuneration paid is within the ceiling limit provided under the section, then, recourse to provisions of section 36(2) cannot be taken.

The Assessing Officer is only required to ensure that the remuneration is paid to the working partners mentioned in the partnership deed, the terms and conditions of the partnership deed provide for payment of remuneration to the working partners and the remuneration is within the limits prescribed under section 35(e)(iii). If these conditions are complied with, then, the Assessing Officer cannot disallow any part of the remuneration on the ground that it is excessive by invoking the provisions of section 36(2).

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(ii) Payments exceeding ₹ 10,000 made otherwise than through specified banking or online mode

According to section 36(4), where in respect of any expenditure incurred by the assessee, any payment or aggregate of payments made in a day to a person exceeds ₹ 10,000 and is not made through specified banking or online mode, then the expenditure by way of such payments shall not be allowed as a deduction.

Meaning of "Specified Banking or Online Mode" [Section 66(32)]

Specified Banking or Online Mode mean a transaction by

- an account payee cheque or
- an account payee bank draft or
- use of electronic clearing system through a bank account or
- through such other electronic mode, as may be prescribed.

As per Rule 48 of the Income-tax Rules, 2026, "other electronic modes of payment" are the following:

- Credit Card;
- Debit Card;
- Net Banking;
- IMPS (Immediate Payment Service);
- UPI (Unified Payment Interface);
- RTGS (Real Time Gross Settlement);
- NEFT (National Electronic Funds Transfer);
- BHIM (Bharat Interface for Money) Aadhaar Pay, and
- Tier-III: Full KYC Central Bank Digital Currency wallets, P-CBDC, Wholesale/Cross-border CBDC.

The provision applies to all categories of expenditure involving payments for goods or services which are deductible in computing the taxable income.



If, in respect of an expenditure of ₹ 32,000 incurred by X Ltd., 4 cash payments of ₹ 8,000 are made on a particular day to one Mr. Y – one in the morning at 10 a.m., one at 12 noon, one at 3 p.m. and one at 6 p.m.,

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the entire expenditure of ₹ 32,000 would be disallowed under section 36(4), since the aggregate of cash payments made in a day to Mr. Y exceeds ₹ 10,000.

Payments in excess of ₹ 10,000 made otherwise than through specified banking or online mode deemed to be the income of the subsequent year, if expenditure has been allowed as deduction in any tax year on due basis [Section 36(5)]

In case of an assessee following mercantile system of accounting,

- if an expenditure has been allowed as deduction in any tax year on due basis and
- payment in respect of such expenditure is made during a subsequent year and
- payment or aggregate of payments made in a day to a person exceeds ₹10,000 and
- payment is not made through specified banking or online mode,

then, such payment shall be deemed to be the income under the head "Profits and gains of business or profession" in such subsequent tax year.

Increase in limit of cash payment, where payment made to transport operator



The limit would be ₹ 35,000 in case of payment made to transport operators for plying, hiring or leasing goods carriages, otherwise than through prescribed modes. Therefore, payment or aggregate of payments up to ₹ 35,000 in a day can be made to a transport operator **otherwise than** through specified banking or online mode. In all other cases, the limit would continue to be ₹ 10,000 [Section 36(6)].

Bar on Plea Regarding Mode of Payment

No person is allowed to raise, in any suit or other proceeding, a plea based on the ground that the payment was not made or tendered in cash or in any other manner. This is irrespective of anything contained in any other law for the time being in force or in any contract [Section 36(8)].

Cases where disallowances would not be attracted

(i) Loan transactions: It does not apply to loan transactions because advancing of loans or repayments of the principal amount of loan does not constitute

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an expenditure deductible in computing the taxable income. However, interest payments of amounts exceeding ₹ 10,000 at a time are required to be made through specified banking or online mode as interest is a deductible expenditure.

(ii) **Payment made by commission agents:** This does not apply to payment made by commission agents for goods received by them for sale on commission or consignment basis because such a payment is not an expenditure deductible in computing the taxable income of the commission agent.

For the same reason, this requirement does not apply to advance payment made by the commission agent to the party concerned against supply of goods.

However, where commission agent purchases goods on his own account but not on commission basis, the requirement will apply. The provisions regarding payments through specified banking or online mode apply equally to payments made for goods purchased on credit.

Exceptions to section 36(4) and 36(5)

As per rule 26, no disallowance under section 36(4) shall be made and no payment shall be deemed to be the profits and gains of business or profession under section 36(5) where a payment or aggregate of payments made to a person in a day, otherwise through specified banking or online mode or through other electronic mode prescribed in Rule 48, exceeds ₹10,000 in the cases and circumstances specified hereunder, namely:

(a) where the payment is made to

- (i) the Reserve Bank of India or any banking company;
- (ii) the State Bank of India or any subsidiary bank;
- (iii) any co-operative bank or land mortgage bank;
- (iv) any primary agricultural credit society or any primary credit society;
- (v) the Life Insurance Corporation of India;

(b) where the payment is made to the Government and, under the rules framed by it, such payment is required to be made in legal tender;

(c) where the payment is made by

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(i) any letter of credit arrangements through a bank;

(ii) a mail or telegraphic transfer through a bank;

(iii) a book adjustment from any account in a bank to any other account in that or any other bank;

(iv) a bill of exchange made payable only to a bank;

(d) where the payment is made by way of adjustment against the amount of any liability incurred by the payee for any goods supplied or services rendered by the assessee to such payee;

(e) where the payment is made for the purchase of -

(i) agricultural or forest produce; or

(ii) the produce of animal husbandry (including livestock, meat, hides and skins) or dairy or poultry farming; or

(iii) fish or fish products; or

(iv) the products of horticulture or apiculture,

to the cultivator, grower or producer of such articles, produce or products;

(f) where the payment is made for the purchase of the products manufactured or processed without the aid of power in a cottage industry, to the producer of such products;

(g) where the payment is made in a village or town, which on the date of such payment is not served by any bank, to any person who ordinarily resides, or is carrying on any business, profession or vocation, in any such village or town;

(h) where any payment is made to an employee of the assessee or the heir of any such employee, on or in connection with the retirement, retrenchment, resignation, discharge or death of such employee, on account of gratuity, retrenchment compensation or similar terminal benefit and the aggregate of such sums payable to the employee or his heir does not exceed ₹ 50,000;

(i) where the payment is made by an assessee by way of salary to his employee after deducting the income-tax from salary in accordance with the provisions of section 192 of the Act, and when such employee -

(i) is temporarily posted for a continuous period of fifteen days or more in a place other than his normal place of duty or on a ship; and

(ii) does not maintain any account in any bank at such place or ship;

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(j) where the payment is made by any person to his agent who is required to make payment in cash for goods or services on behalf of such person;

(k) where the payment is made by an authorised dealer or a money changer against purchase of foreign currency or travelers cheques in the normal course of his business.

(iii) Marked to market loss or other expected loss

Section 36(9) provides that no deduction or allowance in respect of marked to market loss or other expected loss shall be allowed except as allowable under section 32(h). Section 32(h) provides that marked to market loss or other expected loss as computed as per the ICDS notified under section 276(2), would be allowed as deduction. ICDS I provides that marked to market losses would not be allowed unless the same is in accordance with any other ICDS. Therefore, only marked to market losses specifically permitted under any other ICDS would be allowable as deduction under section 32. Other marked to market losses would not be allowed as deduction as per section 36(9).

3.9 CERTAIN DEDUCTIONS ALLOWED ON ACTUAL PAYMENT BASIS ONLY [SECTION 37]

- The following sums payable, which are otherwise allowable as a deduction under the Act, are allowed as deduction only in that tax year in which such sum is actually paid i.e., on actual payment basis.
- This provision is applicable irrespective of:
  - (a) any provision to the contrary in the Act; or
  - (b) method of accounting regularly followed; or
  - (c) the tax year in which liability was incurred.
- The sums covered by the provisions of this section are as follows [Sec. 37(2)]:
  - (a) **Tax, duty, cess, surcharge or fee,** by whatever name called, levied under any law in force, or
  - (b) **Contribution of the employer to a provident fund or superannuation fund or gratuity fund** or any other fund for the welfare of employees, or

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(c) Amount payable by employer **in lieu of any leave at the credit of the employee,** or

(d) **Bonus or Commission** for services rendered payable to employees, or

(e) **Interest on loans or advances or borrowings** from **specified financial entities** as per the terms and conditions of the agreement governing such loans or advances or borrowings, or

(f) Amount payable **to the Indian Railways for use of Railway assets,** or

(g) amount payable by the assessee to a micro or small enterprise beyond the time limit specified in section 15 of the Micro, Small and Medium Enterprises Development Act, 2006 (MSMED Act). (A brief discussion about section 15 of MSMED Act has been given in subsequent part of this chapter.)

- **If the amounts referred to above in clauses (a) to (f)**, are paid **after the end of tax year** in which the liability was incurred **but on or before the due date of filing return of income under section 263(1)** for such tax year, the deduction towards such sum is allowed in such tax year [Section 37(3)].

- **Meaning of "sum payable" for the purposes of section 37(2)(a)**

  Sum payable means a sum for which the assessee has incurred liability in the tax year even though such sum might not have been payable within that year under the relevant law.



Shasun Chemicals & Drugs Ltd v. CIT (2016) 388 ITR 1 (SC)

Issue: In a case where payment of bonus due to employees is paid to a trust and such amount is subsequently paid to the employees before the stipulated due date, would the same be allowable while computing business income?

Analysis & Decision: The embargo contained in section 37(2)(d) and 32(a) does not come in the way of the assessee's claim, since the bonus was ultimately paid to the employees before the due date as per the statutory requirement. Therefore, the payment in respect of bonus is allowable as deduction.

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- **Conversion of interest into a loan or borrowing or debenture or any other instrument**

If interest on loans or advances or borrowings referred to in clause (e) above is converted into a loan or advance or debenture or any other instrument by which the liability to pay is deferred to a future date, the interest so converted shall not be deemed to have been actually paid and hence, would not be allowed as deduction. The provision reiterates the rationale that conversion of interest into a loan or advance or debenture or any other instrument by which the liability to pay is deferred to a future date does not amount to actual payment.



Circular No.7/2006 dated 17.7.2006

The manner in which the converted interest will be allowed as deduction has been clarified in Circular No.7/2006 dated 17.7.2006. The unpaid interest, whenever actually paid to the bank or financial institution, will be in the nature of revenue expenditure deserving deduction in the computation of income. Therefore, irrespective of the nomenclature, the deduction will be allowed in the tax year in which the converted interest is actually paid.

Meaning of specified financial entities

(a) A public financial institution or

(b) State Financial Corporation or

(c) State Industrial Investment Corporation or

(d) such class of non-banking financial companies as may be notified by the Central Government or

(e) a scheduled bank or

(f) a co-operative bank (other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank).

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Frontier Information Tech Ltd. v DCIT (ITA 239/2008, Judgment, Telangana High Court)

Issue: Whether conversion of interest due on loan into equity of the company amounts to actual payment of the interest and is to be allowed as deduction as per section 37 of the Income-tax Act, 2025?

Facts of the Case: The assessee-company, a developer of software, had converted the interest due of ₹ 75.75 lakhs to Andhra Pradesh Industrial Development Corporation Limited, being a State industrial investment corporation and interest of ₹ 39.94 lakhs to Andhra Pradesh State Financial Corporation into equity shares. The Assessing Officer held that actual payment of the amount was sine qua non for allowing deduction under section 37. It was further held that conversion of outstanding interest liability into loan i.e., funding interest or into equity did not amount to actual payment. Accordingly, the amount was disallowed under section 37 on the ground that the same was not actually paid.

Analysis and Decision: The High Court held that as the liability of the assessee to pay interest ceased to exist on issue of shares, the same would tantamount to actual payment within the meaning of section 37. The assessee, therefore, is entitled to claim the benefit of deduction under section 37.

ILLUSTRATION 16

Hari, an individual, carried on the business of purchase and sale of agricultural commodities like paddy, wheat, etc. He borrowed loans from Andhra Pradesh State Financial Corporation (APSFC) and Indian Bank and has not paid interest as detailed hereunder:

		₹
(i)	*Andhra Pradesh State Financial Corporation (T.Y. 2025-26 & 2026-27)*	*15,00,000*
(ii)	*Indian Bank (T.Y. 2026-27)*	*30,00,000*
		45,00,000

Both APSFC and Indian Bank, while restructuring the loan facilities of Hari during the year 2026-27, converted the above interest payable by Hari to them as a loan

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repayable in 60 equal installments. During the year ended 31.3.2027, Hari paid 5 installments to APSFC and 3 installments to Indian Bank.

Hari claimed the entire interest of ₹ 45,00,000 as an expenditure while computing the income from business of purchase and sale of agricultural commodities. Examine whether his claim is valid and if not, what is the amount of interest, if any, allowable.

SOLUTION

According to section 37, any interest payable on the term loans to specified financial entities (which includes, *inter alia*, State Financial Corporation and Scheduled bank) shall be allowed only in the year of payment of such interest irrespective of the method of accounting followed by the assessee.

Where there is default in the payment of interest by the assessee, such unpaid interest may be converted into loan. Such conversion of unpaid interest into loan shall not be construed as payment of interest for the purpose of section 37. The amount of unpaid interest so converted as loan shall be allowed as deduction only in the year in which the converted loan is actually paid.

In the given case of Hari, the unpaid interest of ₹ 15,00,000 due to APSFC and of ₹ 30,00,000 due to Indian Bank was converted into loan. Such conversion would not amount to payment of interest and would not, therefore, be eligible for deduction in the year of such conversion. Hence, claim of Hari that the entire interest of ₹ 45,00,000 is to be allowed as deduction in the year of conversion is not tenable. The deduction shall be allowed only to the extent of repayment made during the tax year. Accordingly, the amount of interest eligible for deduction for the T.Y.2026-27 shall be calculated as follows:

	Interest outstanding (₹)	**Number of Instalments**	**Amount per instalment (₹)**	**Instalments paid**	**Interest allowable (₹)**
APSFC	15 lakhs	60	25,000	5	1,25,000
Indian Bank	30 lakhs	60	50,000	3	1,50,000
Total amount eligible for deduction					**2,75,000**

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♦ **Non-applicability of section 37 in respect of employee's Contribution to welfare funds [Section 37(6)]**

As per section 2(49)(o), any sum received by an assessee, being an employer from his employee as contribution to any provident fund or superannuation fund or any fund set up under Employee's State Insurance Act, 1948 or any other fund for the welfare of employees would be considered as the income of an employer.

The deduction in respect of above sum shall be allowed to the assessee under section 29(1)(e) only if such sum is credited by the assessee to the employee's account in the relevant fund by the due date applicable in his case for filing return of income under section 263(1) in respect of that tax year.

As per section 37(1), the sums specified in section 37(2), which includes any sum payable as an employer by way of contribution to a provident fund or superannuation fund or gratuity fund or any fund for the welfare of employees, would be allowable during the tax year in which such sums are actually paid. This is subject to the provisions of section 37(3) that if these sums have been paid on or before the 'due date' applicable in his case for filing return of income under section 263(1) in respect of that tax year in which they are otherwise allowable as a deduction under this Act (original tax year), they shall be allowed as deduction in the original tax year.

The impact of above mechanism is that if the sums specified u/s 37(2) are paid after the due date of filing of return of income for the original tax year, they shall still be allowed in the year in which they have been actually paid.

Section 37(6) provides that the provisions of section 37 shall not apply to employee's contribution received by employer towards any welfare fund. It means that if this contribution is paid after the due date under section 263(1), this would never be eligible for deduction.

The above provision can be summarized in the form of table given below:

Employee's contribution related to Tax Year X

If paid	Deduction
Upto the due date of filing of return of income for Tax Year X	Allowed in the tax year X
After the due date of filing of return of income for Tax Year X	Never allowed

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Employer's contribution related to Tax Year X

If pd	Deduction
Upto the due date of filing of return of income for Tax Year X	Allowed in the tax year X
After the due date of filing of return of income for Tax Year X	Allowed in the tax year of actual payment

- If a deduction in respect of any sum payable has already been allowed in any tax year when such liability was incurred, it shall not be allowed again in any subsequent tax year when it is paid [Section 37(5)].

Payment to Micro or Small enterprise [Section 37(2)(g)]

Any sum payable by the assessee to a micro or small enterprise beyond the time-limit specified in section 15 of the Micro, Small and Medium Enterprises Development Act, 2006 would be allowed as deduction only in that tax year in which such sum is actually paid.

Section 15 of the of the Micro, Small and Medium Enterprises Development Act, 2006 mandates payment of goods or services to supplier, being a micro or small enterprises by the buyer on or before the date agreed upon between them in writing i.e., as per the written agreement, which cannot be more than 45 days from the day of acceptance or the day of deemed acceptance of any goods or services by a buyer from a supplier. If there is no such written agreement, the payment shall be made before the appointed day i.e., within 15 days.

If the sum payable by the assessee to a micro or small enterprise is paid as per written agreement (maximum within 45 days) or within 15 days in case of no agreement, the deduction can be claimed on accrual basis if mercantile method of accounting is followed by the assessee.

However, if the sum payable by the assessee to a micro or small enterprise is not paid as per written agreement or within 15 days in case of no agreement, the deduction would be allowed in the tax year in which it is actually paid.



Mr. A has purchased goods of ₹ 10,000 from A & Co., a micro enterprise on 1.3.2027. As per the written agreement between them, the payment

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has to be made by 5.4.2027. Mr. A follows mercantile method of accounting.

(i) If Mr. A paid the sum on 2.4.2027

Since Mr. A paid the sum on or before 5.4.2027, the deduction would be allowed in T.Y. 2026-27.

(ii) If Mr. A paid the sum on 20.4.2027

Since Mr. A paid the sum beyond the time limit, the deduction would not be allowed in the T.Y. 2026-27 but would be allowed in the year of actual payment i.e., in T.Y. 2027-28.



Suppose Mr. Raju has purchased goods of ₹ 10,000 from A & Co., a medium enterprise on 1.3.2027. As per the written agreement between them, the payment has to be made by 5.4.2027, however Mr. Raju paid the sum on 10.4.2027. Mr. Raju follows mercantile method of accounting.

*In such case, since disallowance under section 37(2)(g) is not applicable on sum payable to **medium enterprise**, the deduction would be allowed in T.Y. 2026-27 on due basis.*

Meaning of Micro and Small enterprise

S. No.	Meaning		
(1)	**Micro Enterprise**		
	Investment in Plant and Machinery or Equipment ≤ ₹ 2.5 crore	**AND**	Turnover ≤ ₹ 10 crore
(2)	**Small Enterprise**		
	Investment in Plant and Machinery or Equipment ≤ ₹ 25 crore	**AND**	Turnover ≤ ₹ 100 crore

3.10 CERTAIN SUMS DEEMED AS PROFITS AND GAINS OF BUSINESS OR PROFESSION [SECTION 38]

This section enumerates certain receipts which are deemed to be income under the head "profits and gains of business or profession". Such receipts would attract charge even if the business from which they arise had ceased to exist prior to the

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year in which the liability under this section arises. The particulars of such receipts are given below:

(i) Remission or cessation of trading liability [Section 38(1)(a)]

- Suppose an allowance or deduction has been made in any tax year in respect of loss, expenditure or trading liability incurred by A. Subsequently, if A has obtained, whether in cash or in any manner whatsoever, any amount in respect of such loss or expenditure of some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by A, or the value of benefit accruing to him shall be taxed as income of that tax year.
- It does not matter whether the business or profession in respect of which the allowance or deduction has been made is in existence in that year or not.
- Here cessation or remission of such trading liability includes a unilateral act of write-off of such liability in assessee's accounts.
- It is possible that after the above allowance in respect of loss, expenditure, or trading liability has been given to A, he could have been succeeded in his business by another person. In such a case, the successor will be liable to be taxed in respect of any such benefit or amount received by him during a subsequent tax year.

Successor in business [Section 38(6)(b)]

(i) Where there has been an amalgamation of a company with another company, the successor will be the amalgamated company.

(ii) In case of a demerger, the successor will be the resulting company.

(iii) Where a firm carrying on a business or profession is succeeded by another firm, the successor will be the other firm.

(iv) In any other case, where one person is succeeded by any other person in that business or profession, the other person will be the successor.

(ii) Balancing charge, sale of capital asset used for scientific researh, recovery of a bad debt subsequently and withdrawal from reserves created [Section 38(1)(b), 1(c), 1(d) and 1(e)]

The provisions of section 38(1)(b) relating to balancing charge, section 38(1)(c) relating to sale of capital assets acquired for scientific research, section 38(1)(d)

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dealing with recovery of bad debts and of section 38(1)(e) relating to withdrawal from special reserve created have been dealt with earlier under the respective items.

(iii) Brought forward losses of defunct business [Section 38(3)]

In cases where a receipt is deemed to be profit of a business under section 38 [except Balancing Charge covered u/s 38(1)(b)] relating to a business that had ceased to exist and there is an unabsorbed loss, not being a speculation loss, which arose in that business during the tax year in which it had ceased to exist and which has not been set off, it would be set off against income that is chargeable under this section even after the expiry of 8 years.

3.11 SPECIAL PROVISION FOR COMPUTATION OF COST OF ACQUISITION OF CERTAIN ASSETS [SECTION 40]

(i) Where an asset is acquired by the amalgamated company under a scheme of amalgamation or acquired by the assessee under a gift or will or an irrevocable trust or either by way of total or partial partition of HUF and such asset is sold as stock-in-trade by the amalgamated company or the assessee, then in computing the profits and gains derived from sale of such stock-in-trade, the cost of acquisition of stock-in-trade to the amalgamated company or the assessee shall be the cost of acquisition of the asset to the amalgamating company or the transferor or donor as increased by the cost, if any, of any improvement made and the expenditure incurred wholly and exclusively in connection with such transfer.

(ii) Where the capital asset of the amalgamating company or the transferor or donor is taken over by the amalgamated company or the assesseee as a capital asset and has been converted into stock-in-trade and revalued, provisions of section 67(6) will apply. In such a case, the provisions of section 40 will not apply.

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3.12 TREATMENT OF FOREIGN EXCHANGE FLUCTUATIONS

Capitalising impact of foreign exchange fluctuation [Section 42]

(a) The section deals with the situation where **at the time of making payment** during the tax year, there is a **variation in liability** of an assessee as expressed in Indian currency in relation to an asset acquired for the purpose of business or profession from a country outside India due to change in rate of exchange.

(b) The **variation in liability** shall be added or reduced from the following:

(i) the actual cost of the asset under section 39

(ii) the amount of capital expenditure incurred by a company for promoting family planning amongst its employees under section 32(i)

(iii) the amount of capital expenditure incurred on scientific research under section 45(1)(a)(i)

(iv) the cost of acquisition of a non-depreciable capital asset falling under section 72.

The amount arrived at after such addition or deduction shall be taken to be the actual cost of the asset or the amount of capital expenditure or the cost of acquisition of the capital asset, as the case may be.

(c) Liability shall exclude any part met directly or indirectly by any other person or authority and the **variation in liability** shall be

B - C

B = payment expressed in Indian currency at the time when it is made

(a) towards the whole or part of the cost of asset; or

(b) towards repayment of the whole or part of the moneys borrowed, directly or indirectly, along with interest in foreign currency, specifically for acquiring such asset;

C = liability, corresponding to the amount referred in B, in Indian currency at the time of acquisition of such asset.

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(d) Where the assessee has entered into a contract with authorised dealer[9] for providing him with a specified sum in a foreign currency on or after a stipulated future date at the rate of exchange specified in the contract to enable him to meet the whole or any part of the liability aforesaid, the amount, if any, for adjustment under this section shall be computed with reference to the rate of exchange specified therein.

Taxation of foreign exchange fluctuation [Section 43]

(i) Section 43 provides that, subject to the provisions of section 42, any gain or loss arising on account of any change in foreign exchange rates on foreign currency transactions shall be treated as income or loss, as the case may be, which shall be computed as per the notified ICDS i.e., ICDS VI: The effects of changes in foreign exchange rates.

(ii) The provisions shall be applicable to all foreign currency transactions including those relating to –

(a) monetary items and non-monetary items

(b) translation of financial statements of foreign operations

(c) forward exchange contracts and

(d) foreign currency translation reserves.

3.13 OTHER PROVISIONS

Stamp Duty Value of land and building to be taken as the full value of consideration in respect of transfer, even if the same are held by the transferor as stock-in-trade [Section 53]

(a) In case of transfer of an asset (other than a capital asset), being land or building or both, if the consideration received or accrued from such transfer is less than the stamp duty value, then such stamp duty value) shall be

[9] *as defined in section 2 of the Foreign Exchange Management Act, 1999*

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deemed to be the full value of the consideration for computing profits and gains from such transfer.

(b) If the stamp duty value does not exceed 110% of the consideration received or accruing then, the consideration received or accrued shall be deemed to be the full value of consideration.

(c) Further, if the date of an agreement fixing the value of consideration for the transfer of asset and the date of registration for transfer of such asset are different, then the stamp duty value as on date of the agreement may be taken to be the full value of consideration. for transfer instead of on the date of registration for such transfer, if the amount of consideration or part thereof has been received by specified banking or online mode on or before the date of agreement for transfer of such asset.

(c) The Assessing Officer may refer the valuation of the capital asset to a valuation officer in the following cases -

(1) Where the assessee claims that the stamp duty value exceeds the fair market value of the property as on the date of transfer and

(2) the stamp duty value has not been disputed in any appeal or revision or no reference has been made before any other authority, court or the High Court.

(e) If the value determined by the Valuation on a reference made exceeds the stamp duty value, such stamp duty value shall be taken as the full value of the consideration.

(f) **Meaning of stamp duty value:** It means the value adopted or assessed or assessable by any authority of the Central Government or State Government for the payment of stamp duty in respect of an immovable property, where the expression "assessable" shall mean the value which any authority of that Government would have adopted or assessed as if it were referred to such authority for the purposes of payment of stamp duty, irrespective of anything to the contrary contained in any other law in force.

The term "assessable" covers transfers executed through power of attorney.

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Date of transfer of land / building held as stock-in-trade	Actual consideration	Stamp duty value on the date of agreement	Stamp duty value on the date of registration	Full value of consideration	Remark
	₹ in lakhs				
Example:					
1/9/2026	100 (₹ 10 lakhs received by **A/c payee cheque** on 1/7/2026)	120 (1/7/2026)	210 (1/9/2026)	120	As part of the consideration is received by A/c payee cheque on the date of agreement, Stamp duty value (SDV) on the date of agreement to be adapted as full value of consideration, since the SDV exceeds 110% of consideration i.e., ₹ 110 lakhs.
Example:					
1/9/2026	100 (₹ 10 lakhs received **by cash** on 1/7/2026)	109 (1/7/2026)	130 (1/9/2026)	130	SDV on the date of registration to be adapted as full value of consideration and such SDV exceeds 110% of consideration

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					i.e., ₹ 110 lakhs. Since part of consideration is received by cash on the date of agreement, the SDV on the date of agreement cannot be considered vis-à-vis actual consideration.
Example:					
31/1/2027	100 (₹ 10 lakhs received by **A/c payee cheque** on 1/7/2026)	109 (1/7/2026)	130 (31/1/2027)	100	Actual sales consideration would be the full value of consideration, since SDV on the date of agreement does not exceed 110% of actual consideration. SDV on the date of agreement can be considered *vis-à-vis* actual consideration, since part of the consideration has been received by account payee

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					cheque on the date of agreement.
Example:					
31/3/2027	100 (Full amount received in cash on the date of registration)	120 (1/5/2026)	130 (31/3/2027)	130	Stamp duty value of the date of registration would be the full value of consideration since the stamp duty value exceeds 110% of consideration i.e., ₹ 110 lakhs.

Special provisions for deduction in case of business for prospecting etc. for mineral oil [Section 54]

(a) **Eligible assessee -** Section 54 enables the assessee who undertakes specified oil exploration business to claim certain deduction while computing the income under the head "Profits and gains of business or profession".

(b) **Meaning of specified oil exploration business -** Specified oil exploration business means business consisting of prospecting for or extraction or production of mineral oils where -

- the Central Government has entered into an agreement with the assessee;
- such agreement is entered for association or participation of the Central Government or any person authorised by it; and
- such agreement is laid before each House of Parliament

(c) **Allowable deduction -** The allowance permissible deduction under this section shall be –

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for the period before the beginning of commercial production	expenditure towards infructuous or abortive exploration incurred in respect of any surrendered area
for the period after the commencement of commercial production	expenditure (whether before or after such production) in respect of drilling or exploration activities or services or in respect of physical assets used in that connection
for the tax year of commencement of commercial production and such succeeding tax years as specified in the agreement	towards depletion of mineral oil in the mining area

The deductions shall be either in lieu or in addition to any allowance admissible under the Act as specified in the agreement entered and computed and made in the manner specified in the agreement.

It has been specifically provided that the other provisions of the Act are being deemed, for the purpose of this allowance, to have been modified to such extent.

(d) Taxability in case of transfer - Where the business or any interest therein as referred to in (a) above is wholly or partly transferred as per the provisions of the agreement, the profit shall be charged to tax or deduction shall be allowed in the following manner:

	Transaction	Manner of deduction
(1)	**Case 1:** Where the proceeds of the transfer is less than the expenditure incurred remaining unallowed	The expenditure remaining unallowed **as reduced by** the proceeds of transfer shall be allowed in the tax year in which the business or interest has been transferred. Amount of deduction = Expenditure remain unallowed – Sale proceeds
	Case 2: Where the proceeds of the transfer is greater than the amount	The proceeds of transfer **as reduced by** the expenditure remaining unallowed shall be the profit chargeable under the "Profits and

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	of expenditure remaining unallowed but less than total amount of expenditure	gains of business or profession" for the tax year in which such transfer takes place and no deduction shall be allowed for the expenditure incurred remaining unallowed in the tax year in which such transfer takes place or any subsequent tax year.
		Taxable as profits and gains from business and profession = Sale proceeds – Expenditure remain unallowed
		Amount of deduction = NIL
	Case 3: Where the proceeds of the transfer is greater than the amount of expenditure remaining unallowed but not covered in case 2	The total amount of expenditure incurred in connection with the business or to obtain interest therein **as reduced by** the expenditure remaining unallowed shall be the profit chargeable under the "Profits and gains of business or profession" for the tax year in which such transfer takes place and no deduction shall be allowed for the expenditure incurred remaining unallowed in the tax year in which such transfer takes place or any subsequent tax year.
		Taxable as profits and gains from business and profession = Total amount of expenditure – Expenditure remain unallowed
		Amount of deduction = NIL
(2)	**Transfer of business or interest therein in a scheme of amalgamation**	
	If the amalgamating company sells or transfers the business or interest therein to the amalgamated company,	The provisions of section 54 will continue to apply to the amalgamated company as it would have applied to the amalgamating company as if the transfer had not taken place.

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	being an Indian company under the scheme of amalgamation	The tax treatment in cases 1, 2 & 3 given in (1) above will not apply to the amalgamating company.
(3)	**Transfer of business in a scheme of demerger**	
	If the demerged company sells or transfers the business or interest therein to the resulting company, being an Indian company under the scheme of demerger	The provisions of section 54 will continue to apply to the resulting company as it would have applied to the demerged company as if the transfer had not taken place. The tax treatment in cases 1, 2 & 3 given in (1) above will not apply to the demerged company.

If the business or interest is no longer in existence in the year of transfer, the taxability would arise in the above manner if such business is in existence in the said year.

Note: Mineral oil includes petroleum and natural gas.

Special Provision in case of interest income of Public Financial Institutions [Section 56]

The interest income in relation to such categories of bad and doubtful debts, as may be prescribed, having regard to the guidelines issued by the Reserve Bank of India of a specified financial institution shall be chargeable to tax under the head "Profits and gains of business or profession" in the tax year in which such interest is

- credited to the profit and loss account or
- actually received

whichever is earlier.

Specified financial institution means -

- a public financial institution or
- a scheduled bank or
- a co-operative bank other than
  - a primary agricultural credit society or

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- a primary co-operative agricultural and rural development bank or
- a State Financial Corporation or
- a State Industrial Investment Corporation or
- notified class of non-banking financial companies

Revenue recognition for construction and service contracts [Section 57]

The profits and gains arising from a construction contract or a contract for providing services shall be determined on the basis of percentage of completion method (POCM) as per the notified ICDS i.e., ICDS III: Construction Contracts.

The profits and gains arising from a contract for providing services shall be computed on the basis of –

Method	Condition
Project completion method	If the duration of such contract is not more than 90 days
Straight line method	If the contract involves indeterminate number of acts over a specific period of time

For the purpose of percentage of completion method, project completion method or straight line method –

(i) the contract revenue shall include retention money;

(ii) the contract cost shall not be reduced by any incidental income in the nature of interest, dividends or capital gains.

3.14 MAINTENANCE OF BOOKS OF ACCOUNT [SECTION 62]

(i) Maintain the books of account and other documents [Section 62(1)]

Section 62(1) provides that the following persons are required to keep and maintain such books of accounts and other documents to enable the Assessing Officer to compute his total income under the Act:

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- any person carrying on specified profession or
- any person carrying on business or any profession, not being a specified profession mentioned above, and satisfying the specified conditions.

Meaning of books or books of account [Section 2(19)]

It includes ledgers, day-books, cash books, account-books and other books, whether kept –

(a) in written form; or

(b) in electronic or any digital form, or on cloud-based storage, or on any electromagnetic data storage device, such as floppy, disc, tape, portable data storage device, external hard drives, or memory cards; or

(c) as print-outs of data stored in electronic or digital form or on storage devices mentioned in sub-clause (b);

Meaning of specified profession [Section 62(4)]

Legal, medical, engineering, architectural, accountancy, technical consultancy, interior decoration, information technology or company secretary or any other profession as notified by the CBDT.

(ii) Conditions for any person carrying on business or profession [other than specified professions [Section 62(2)]

Any person carrying on business or any profession, not being a specified profession mentioned above, is required to keep and maintain such books of accounts and other documents to enable the Assessing Officer to compute his total income under the Act if the person satisfies any of the following conditions:

In case of Individual or HUF

(i) **In relation to existing business or profession:** Where the **income** from the existing business or profession **exceeds ₹ 2,50,000 or its total sales, turnover or gross receipts from such** business or profession **exceed ₹ 25,00,000** in **any one of three years immediately preceding** the tax year; or

(ii) **In relation to newly set up business or profession:** Where the business or profession is newly set up in the tax year, the **income** from business or profession **is likely to exceed ₹ 2,50,000** or its **total sales, turnover or gross**

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receipts from such business or profession **are likely to exceed ₹ 25,00,000** during such tax year.

In case of person (other than individual or HUF)

(i) **In relation to existing business or profession:** Where the **income** from the existing business or profession **exceeds ₹ 1,20,000** or its **total sales, turnover or gross receipts from such** business or profession **exceed ₹ 10,00,000 in any one of three years** immediately preceding the tax year; or

(ii) **In relation to newly set up business or profession:** Where the business or profession is newly set up in the tax year, the income from business or profession is **likely to exceed ₹ 1,20,000** or its **total sales, turnover or gross receipts** from such business or profession are **likely to exceed ₹ 10,00,000** during the tax year;

Showing lower income as compared to income computed on presumptive basis under section 58 or section 61[10]: Where during the tax year, the assessee referred to in section 58(2) or section 61(2) (Table: Sl. Nos. 4 and 5) has claimed that his income from business or profession is lower than the deemed profits as per section 58(2) or section 61(2).

(iii) Power of the CBDT

The CBDT may prescribe

- the books of account and other documents (including inventories, wherever necessary) to be kept and maintained
- particulars to be contained therein
- the form, manner and place at which they shall be kept and maintained; and
- the period for which such books of account and other documents are to be retained

Rules pertaining to maintenance of books of accounts & other documents:

Rule 46 of the Income-tax Rules, 2026 contains details relating to the books of account and other documents to be maintained by certain professionals under section 62(1).

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[10]*Section 61 will be discussed in Chapter 21: Non-resident taxation in Module 4 of the Study Material.*

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(iv) Books of Accounts to be maintained

As per Rule 46(1), every person required to keep and maintain books of account and other documents under section 62(1)(b) shall maintain such books of account and other documents that enable the Assessing Officer to compute his total income under the Act.

Prescribed class of persons: As per Rule 46(2), every person carrying on legal, medical, engineering, or architectural profession or the profession of accountancy or technical consultancy or interior decoration or authorised representative or film artist shall keep and maintain the books of account and other documents specified in Rule 46(4).

However, the provisions of Rule 46(2) are not applicable in the following cases:

- in relation to any tax year in the case of any person if his gross receipts in the profession do not exceed ₹ 1,50,000 in any one of the 3 years immediately preceding the tax year;
- where the profession has been newly set up in the tax year, his total gross receipts in the profession for that year **are not likely to exceed ₹ 1,50,000**.



The professionals whose gross receipts are less than the specified limits given above are also required to maintain books of account but these have not been specified in the Rule.

In other words, they are required to maintain such books of account and other documents as may enable the Assessing Officer to compute the total income in accordance with the provisions of this Act.

Prescribed books of accounts and other documents [Rule 46(4)]

The following books of account and other documents are required to be maintained.

(i) a cash book;

(ii) a journal, if accounts are maintained on mercantile basis;

(iii) a ledger;

(iv) Copies of bills and receipts issued by the person, for sums equal to or exceeding ₹ 250;

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(v) Original bills and receipts in respect of expenditure equal to or exceeding ₹ 250 incurred by the person and issued to him,

(vi) Payment vouchers prepared and signed by the person, where the expenditure incurred does not exceed ₹ 250, and the cash book maintained by the person does not contain adequate particulars in respect of such expenditure.

In case of a person carrying on medical profession, he will be required to maintain the following in addition to the list given above [Rule 46(6)]:

(i) a daily case register in Form 25

(ii) an inventory under broad heads, as on the first and last day of the tax year, of the stock of drugs, medicines and other consumable accessories used for his profession.

Place at which books to be kept and maintained

The books and documents shall be kept and maintained at the place where the person is carrying on the profession, or where the profession is carried on in more places than one, at the principal place of his profession. However, if the person keeps and maintains separate books of account in respect of each place where the profession is carried on, such books of account and other documents may be kept and maintained at the respective places at which the profession is carried on.

Books of account maintained in electronic mode

The books of account and other documents maintained in electronic mode shall remain accessible in India at all times, and the back-up of such books of account and other documents maintained in electronic mode, shall be kept in servers physically located in India, and shall be updated on a daily basis. [Rule 46(8)]

Period for which the books of account and other documents are required to be kept and maintained

The above books of account and documents shall be kept and maintained for a period of 7 tax years from the end of the relevant tax year.

ILLUSTRATION 17

Vinod is a person carrying on profession as film artist. His gross receipts from profession are as under:

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	₹
Financial year 2023-24	*1,15,000*
Financial year 2024-25	*1,80,000*
Financial year 2025-26	*2,10,000*

What is his obligation regarding maintenance of books of accounts for Tax Year 2026-27 under section 62 of Income-tax Act, 2025?

SOLUTION

Section 62(1) requires every person carrying on any profession as film artist to maintain such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of the Income-tax Act, 2025.

As per Rule 46(2) read with Rule 46(3), a person carrying on a notified profession shall be required to maintain **specified books of accounts, only if**:

(i) his gross receipts in the profession has exceeded ₹ 1,50,000 in all the three years immediately preceding the relevant tax year; or

(ii) it is a new profession which is setup in the relevant tax year, it is likely to exceed ₹ 1,50,000 in that tax year.

In the present case, Vinod is a person carrying on profession as film artist. Since his gross receipts have not exceeded ₹ 1,50,000 in tax year 2023-24, the requirement under section 62 to compulsorily maintain the prescribed books of account is not applicable to him for T.Y. 2026-27.

Mr. Vinod, however, is required to maintain such books of accounts as would enable the Assessing Officer to compute his total income.

(vi) Penalty for failure to maintain books of account [Section 441]

If a person fails to keep and maintain any such books of account and other documents as required by section 62 or the rules made thereunder, in respect of any tax year or to retain such books of account and other documents for the specified period, the Assessing Officer or the Joint Commissioner (Appeals) or the Commissioner (Appeals) may direct a penalty of ₹ 25,000 under section 441.

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3.15 TAX AUDIT [SECTION 63]

(i) Requirement of Tax Audit:

It is obligatory for the persons mentioned in column (2) of the table below, carrying on business or profession, to get his accounts of the tax year audited by an Accountant before the "specified date" by a Chartered Accountant, if the conditions mentioned in the corresponding row of column (3) are satisfied

	Persons	When tax audit is required?
(1)	**(2)**	**(3)**
1	**Every Person carrying on Business or Profession [other than that taxable on presumptive basis u/s 58(2) or section 61(2) (Table: Sl. No. 4 and 5)]**	
(a)	In case of a person carrying on business – subject to provisions of clause (b)	If his total sales, turnover or gross receipts in business > **₹ 1 crore** in the relevant tax year
(b)	If in case of such person carrying on business - (i) Aggregate of all amounts received in cash (including amount received for sales, turnover or gross receipts) during the tax year ≤ 5% of the said amount; and (ii) Aggregate of all payment made including amount incurred for expenditure in cash during the tax year ≤ 5% of the said payments	If his total sales, turnover or gross receipts in business > **₹ 10 crore** in the relevant tax year
	Note – The payment or receipt, as the case may be, by a cheque drawn on a bank or by a bank draft, which is not account payee, would be deemed to be the payment or receipt, as the case may be, in cash.	
(c)	In case of a person carrying on profession	If his gross receipts in profession > **₹ 50 lakhs** in the tax year.
***Note** – The requirement of tax audit u/s 63 does not apply to a person who declares profits and gains of business or profession for the tax year as per the presumptive basis u/s 58(2) or 61(2).*		

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2	**In case of Business or Profession taxable on presumptive basis u/s 58(2) or 61(2) (Table: Sl. No. 4 and 5)**	
	In case of an assessee covered u/s 58(2) or 61(2) (Table: Sl. No. 4 and 5)	If such assessee claims that the profits and gains from business or profession in the relevant T.Y. are lower than the deemed profits as per those sections

(ii) Audit Report

The above-mentioned persons have to furnish by the specified date, a report of such audit in the prescribed form, duly signed and verified by the accountant. For this purpose, the Board has prescribed under Rule 47, Form No. 26 containing form of audit report and particulars to be furnished therewith. The audit report furnished may be revised by the person by getting revised report of audit from a chartered accountant, duly signed and verified by such chartered accountant, if there is payment by such person after furnishing of report which necessitates recalculation of disallowance under section 35 or section 37. The said revised audit report has to be furnished before the end of the relevant financial year succeeding the tax year for which the report pertains.

(iii) Accounts audited under other statutes are considered

Where a person is required to get his accounts audited by or under any other law, it will be sufficient if such person gets the accounts audited of such business or profession under such law before the specified date and furnishes by that specified date the report of such audit along with the report of the accountant in the prescribed form.



The provision regarding compulsory audit does not imply a second or separate audit of accounts of companies whose accounts are already required to be audited under the Companies Act, 2013. The provision only requires that companies should get their accounts audited under the Companies Act, 2013 before the specified date and in addition to the report required to be given by the auditor under the Companies Act, 2013 furnish a report for tax purposes in the prescribed form.

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(iv) Specified date

The expression **"specified date"** in relation to the accounts of the tax year or years relevant to any tax year means the date one month prior to the due date for furnishing the return of income under section 263(1).

The due date for furnishing return of income in case of assessees (other than companies) who are required to get their accounts audited is 31st October of the financial year succeeding the relevant tax year. Hence, the specified date for tax audit would be 30th September of the financial year succeeding the relevant tax year.[11]

(v) Fees for failure

If any person fails to get his accounts audited for any tax year or years and furnish the audit report as required under section 63, the person shall be liable to pay following fees under section 428(c):

For a delay upto 1 month for which such failure continues	₹ 75,000
Delay beyond 1 month	₹ 1,50,000

3.16 SPECIAL PROVISION FOR COMPUTING PROFITS AND GAINS OF BUSINESS OR PROFESSION ON PRESUMPTIVE BASIS IN CASE OF CERTAIN RESIDENTS [SECTION 58]

Section 58 provides for computation of profits of certain business or profession on presumptive basis where profits are to be calculated in a pre-determined manner.

(1) Applicability of the provisions

- Provisions of this section apply if the following conditions are fulfilled:
  - (i) Assessee carries on any specified business or profession (as mentioned in column B of the Table below)

---

[11] *In case of a person whose due date for filing return of income is 30th November of the financial year succeeding the relevant tax year, the specified date for tax audit would be 31st October of the financial year succeeding the relevant tax year.*

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(ii) Assessee is an eligible assessee (as specified in column C of the Table below)

(iii) Total turnover or gross receipts of business or profession during the tax year does not exceed the limit specified in column D of the table below.

- If the above-mentioned conditions are fulfilled, the profits of the business or profession shall be computed by applying presumptive rate in the manner specified in column E of the Table below and such profits shall be deemed to be the profits and gains of such business or profession chargeable to tax under the head "Profits and gains of business or profession" [Section 58(2)].

Sl. No.	Specified business or profession	Assessee	Total turnover or gross receipts of business or profession during tax year	Manner of computation
A	B	C	D	E
1.	**Any business other than the business specified in 2.**	Eligible assessee	(a) ≤ ₹ 2 crores; or (b) ≤ ₹ 3 crores, where the amount or aggregate of amounts received, in cash, ≤ 5% of the total turnover or gross receipts.	(A) The aggregate of (i) 6% of total turnover or gross receipts which is received by specified banking or online mode during the tax year or before the due date specified in section 263(1) in respect of that tax year;

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				(ii) 8% of total turnover or gross receipts as reduced by the turnover or gross receipts covered in (i); or (B) profit claimed to have been actually earned, whichever is higher.

Meaning of eligible assessee

Eligible Assessee means a resident individual, HUF or Partnership firm (but not LLP), and who

(i) has not claimed deduction Chapter VIII Part C– "Deductions in respect of certain incomes", for the relevant tax year.

(ii) does not carry on specified profession as defined in section 62(4).

(iii) does not earn any income in the nature of commission or brokerage;

(iv) does not carry on any agency business;

Note: *The receipt of amount or aggregate of amounts by a cheque drawn on a bank or by a bank draft, which is not account payee, shall be deemed to be the receipt in cash.*

2.	**Business of plying, hiring or leasing goods carriage**	An assessee, who owns ≤ 10 goods carriages at any time		(A) The aggregate of **(i) For a heavy goods vehicle:** ₹ 1,000 per ton of gross vehicle weight or

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		during the tax year.		unladen weight, as the case may be, for each vehicle for every month or part of a month; **(ii) For a vehicle, other than heavy goods vehicle:** ₹ 7,500, for each goods carriage for every month or part of a month during which the vehicle is owned by the assessee in the tax year or (B) Profit claimed to have been actually earned, whichever is higher.
Allowability of salary and interest to partner in case of assessee is a firm - Where the assessee is a firm, the salary and interest paid to its partners shall be deducted from the income computed as per presumptive provisions subject to the conditions and limits specified in section 35(e).				
Goods carriage treated as owned by the assessee - An assessee, who is in possession of a goods carriage, whether taken on hire purchase or on instalments and for which the whole or part of the amount payable is still due, shall be deemed to be the owner of such goods carriage.				

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Meaning of heavy goods vehicle - Any goods carriage, the gross vehicle weight of which exceeds 12,000 kilograms.

In respect of a tractor or a road-roller, where the gross vehicle weight is not applicable, and unladen weight exceeds 12,000 Kilograms, the profits and gains from each goods carriage shall be at the rate of ₹ 1,000 per ton of unladen weight for every month or part of the month [Clarification dated 14.8.2019].

Provisions of section 62 and 63 not to apply and for computing monetary limit of maintenance of accounts and tax audit, gross receipt from such business not to be included - The provisions of sections 62 and 63 shall not apply in so far as they relate to the above business of plying, hiring or leasing goods carriage and in computing the monetary limits under those sections, the gross receipts or, as the case may be, the income from the said business shall be excluded.

3.	**Specified profession as referred to in section 62(4) namely legal, medical, engineering, architectural, accountancy, technical consultancy, interior decoration, information technology or company secretary or any other profession as notified by the CBDT**	Specified assessee	(a) ≤ ₹ 50 lakhs; or (b) ≤ ₹ 75 lakhs, where the amount or aggregate of amounts received, in cash, ≤ 5% of the total turnover or gross receipts.	50% of the gross receipts or profit claimed to have been actually earned, whichever is higher.

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Meaning of specified assessee: Specified assessee means an individual or a firm, other than an LLP, who is a resident in India.

Note: *The receipt of amount or aggregate of amounts by a cheque drawn on a bank or by a bank draft, which is not account payee, shall be deemed to be the receipt in cash.*

Meaning of Specified banking or online mode

Specified Banking or Online Mode mean transaction by

- an account payee cheque or
- an account payee bank draft or
- use of electronic clearing system through a bank account or
- through such other electronic mode, as may be prescribed.

As per Rule 48 of the Income-tax Rules, 2026, "other electronic modes of payment" are the following:

(a) Credit Card;

(b) Debit Card;

(c) Net Banking;

(d) IMPS (Immediate Payment Service);

(e) UPI (Unified Payment Interface);

(f) RTGS (Real Time Gross Settlement);

(g) NEFT (National Electronic Funds Transfer);

(h) BHIM (Bharat Interface for Money) Aadhaar Pay, and

(i) Tier-III: Full KYC Central Bank Digital Currency wallets, P-CBDC, Wholesale/Cross-border CBDC.

(2) Non-applicability of section 26 to 54

The provisions of sections 26 to 54, to the extent contrary to this section, shall not apply to the manner of computation of profits and gains of the specified business or profession.

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(3) Requirement of maintenance of books of account u/s 62 and audit u/s 63 [Section 58(3)]

If the assessee referred to in above table **claims that**

(a) **his profits and gains actually earned from the specified business or profession are lower** than the profits or gains computed by applying the presumptive provisions, and

(b) **whose total income exceeds the basic exemption limit for that year,** such assessee has to

(i) keep and maintain such books of account and other documents as required under section 62 and

(ii) get the accounts audited and furnish a report of such audit as required under section 63.

(4) No deduction, loss or allowance allowed [Section 58(4)]

Any loss, allowance or deduction allowable under the provisions of the Act, shall not be allowed against the income computed in the manner specified in above table.

(5) Written down value of asset [Section 58(6)]

The WDV of any asset used for the purpose of specified business or profession shall be computed as if the assessee had claimed and was actually allowed deduction in respect of depreciation thereon for each of the relevant tax years.

(6) Consequences if the eligible assessee referred to in Table: S. No. 1 who has once declared profits as per section 58(2) does not declare profits as per section 58(2) in the subsequent 5 tax years

Where an eligible assessee declares profit for any tax year as per the provisions of section 58(2) (Table: S. No. 1) and he declares profit for any of the five tax years succeeding such tax year in contravention of the provisions of section 58(1), then he shall not be eligible to claim the benefit of the provisions of this section for five tax years subsequent to the tax year in which the profit has not been declared as per the provisions of the said sub-section [Section 58(7)].

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In such a case, the assessee would have to **maintain books of account and other documents as required under section 62** and get them audited and furnish report as required under section 63, **if his total income exceeds the basic exemption limit in those years** [Section 58(8)].



Let us consider the following particulars relating to a resident individual, Mr. A, being an eligible assessee carrying on retail trade business whose total turnover do not exceed ₹ 2 crore in any of the tax years 2026-27 to 2028-29.

Particulars	***T.Y.2026-27***	***T.Y.2027-28***	***T.Y.2028-29***
Total turnover (₹)	*1,80,00,000*	*1,90,00,000*	*2,00,00,000*
Amount received through specified banking or online mode before the due date specified in section 263(1) in respect of that tax year.	*1,60,00,000*	*1,45,00,000*	*1,80,00,000*
Income offered for taxation (₹)	*11,20,000*	*12,30,000*	*10,00,000*
% of gross receipts	*6% on ₹ 1.60 crore and 8% on ₹ 20 lakhs*	*6% on ₹ 1.45 crore and 8% on ₹ 45 lakhs*	*5% on ₹ 2 crore*
Offered income as per presumptive taxation scheme u/s 58	*Yes*	*Yes*	*No*

In the above case, Mr. A, an eligible assessee, declares profits as per presumptive taxation under section 58 for T.Y.2026-27 and T.Y.2027-28 and offers income of ₹ 11.20 lakhs and ₹ 12.30 lakhs on gross receipts of ₹ 1.80 crore and ₹ 1.90 crore, respectively.

However, for T.Y.2028-29, he offers income of only ₹ 10 lakhs on turnover of ₹ 2 crores, which amounts to 5% of his gross receipts. As per section 58(3), he is required to maintain books of account under section 62 and get the same audited under section 63 for T.Y. 2028-29. Since he has offered income in contravention with the provisions of section 58(1) for T.Y. 2028-29, he will not be eligible to claim the benefit of section 58 for next five years subsequent to the tax year 2028-29 i.e., from T.Y.2029-30 to 2033-34.

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ILLUSTRATION 18

Mr. Praveen engaged in retail trade, reports a turnover of ₹ 2,98,50,000 for the tax year 2026-27. Amount received in cash during the T.Y. 2026-27 is ₹ 14,00,000 and balance through specified banking and online mode on or before 31st August 2027. His income from the said business as per books of account is ₹ 15,00,000 computed as per the provisions of Chapter IV-D "Profits and gains from business or Profession" of the Income-tax Act, 2025. Retail trade is the only source of income for Mr. Praveen. T.Y. 2025-26 was the first year for which he declared his business income in accordance with the provisions of presumptive taxation u/s 58[12].

(i) Is Mr. Praveen also eligible for presumptive determination of his income chargeable to tax for the tax year 2026-27?

(ii) If so, determine his income from retail trade as per the applicable presumptive provision.

(iii) In case Mr. Praveen wants to declare profits as per books of account from retail trade, what are his obligations under the Income-tax Act, 2025?

(iv) What is the due date for filing his return of income under both the options?

SOLUTION

(i) Yes. Since his cash receipts during the T.Y. does not exceed 5% of the total turnover (14,00,000/2,98,50,000 x 100) and his total turnover for the T.Y.2026-27 is below ₹ 3 crores, he is eligible for presumptive taxation scheme under section 58 (Table: Sl. No. 1) in respect of his retail trade business.

(ii) His income from retail trade, applying the presumptive tax provisions under section 58(Table: Sl. No. 1), would be ₹ 18,19,000 (₹ 1,12,000, being 8% of ₹ 14,00,000 + ₹ 17,07,000, being 6% of ₹ 2,84,50,000).

(iii) Mr. Praveen had declared profit for the tax year 2025-26 in accordance with the presumptive provisions and if he wants to declare profits as per books of account which is lower than the presumptive income for any of the five consecutive tax years i.e., T.Y. 2026-27 to T.Y. 2030-31, he would not be eligible to claim the benefit of presumptive taxation for five tax years subsequent to the tax year in which the profit has not been declared in accordance the

[12] *Erstwhile section 44AD of Income-tax Act, 1961*

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presumptive provisions i.e. if he declares profits lower than the presumptive income in say T.Y.2026-27, then, he would not be eligible to claim the benefit of presumptive taxation for T.Y. 2027-28 to T.Y. 2031-32.

Consequently, Mr. Praveen is required to maintain the books of accounts and get them audited under section 63, since his income exceeds the basic exemption limit.

(iv) In case he declares his profits as per presumptive income under section 58, the due date would be 31st August, 2027.

In case he declares profits as per books of account which is lower than the presumptive income, he is required to get his books of account audited, in which case the due date for filing of return of income would be 31st October, 2027.

ILLUSTRATION 19

Mr. X commenced the business of operating goods vehicles on 1.4.2026. He purchased the following vehicles during the T.Y.2026-27. Compute his income under section 58 for T.Y.2026-27.

	Gross Vehicle Weight (in kilograms)	***Number***	***Date of purchase***
(1)	*7,000*	*2*	*10.04.2026*
(2)	*6,500*	*1*	*15.03.2027*
(3)	*10,000*	*3*	*16.07.2026*
(4)	*11,000*	*1*	*02.01.2027*
(5)	*15,000*	*2*	*29.08.2026*
(6)	*15,000*	*1*	*23.02.2027*

Would your answer change if the two goods vehicles purchased in April, 2026 were put to use only in July, 2026?

SOLUTION

Since Mr. X does not own more than 10 vehicles at any time during the tax year 2026-27, he is eligible to declare profits as per the presumptive taxation scheme under section 58. ₹ 1,000 per ton of gross vehicle weight or unladen weight per month or part of the month for each heavy goods vehicle and ₹ 7,500 per month

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or part of month for each goods carriage other than heavy goods vehicle, owned by him would be deemed as his profits and gains from such goods carriage.

Heavy goods vehicle means any goods carriage, the gross vehicle weight of which exceeds 12,000 kg.

(1)	(2)	(3)	(4)
Number of Vehicles	**Date of purchase**	**No. of months for which vehicle is owned**	**No. of months × No. of vehicles [(1) × (3)]**
For Heavy goods vehicles			
2	29.08.2026	8	16
1	23.02.2027	2	2
			18
For goods vehicles other than heavy goods vehicle			
2	10.4.2026	12	24
1	15.3.2027	1	1
3	16.7.2026	9	27
1	02.1.2027	3	3
			55

The presumptive income of Mr. X under section 58 for T.Y.2026-27 would be -

₹ 6,82,500, i.e., 55 × ₹ 7,500, being for other than heavy goods vehicle + 18 x ₹ 1,000 x 15 ton being for heavy goods vehicle.

The answer would remain the same even if the two vehicles purchased in April, 2026 were put to use only in July, 2026, since the presumptive income has to be calculated per month or part of the month for which the vehicle is owned by Mr. X.

3.17 METHOD OF COMPUTING DEDUCTION IN THE CASE OF BUSINESS REORGANISATION OF CO-OPERATIVE BANKS [SECTION 64]

(1) This section provides the manner in which the deduction under following sections are to be allowed in a case where business reorganisation of a co-operative bank has taken place during the tax year:

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(i) Section 33 - Depreciation

(ii) Section 44 - Amortisation of certain preliminary expenses

(iii) Section 52(1) (Table: S. No. 1) - Expenditure incurred for the purposes of amalgamation or demerger

(iv) Section 52(1) (Table: S. No. 2) - Amount paid to an employee in connection with his voluntary retirement

(2) Quantum of deduction to predecessor co-operative bank or to successor co-operative bank or to the converted banking company: The amount of deduction allowable to the predecessor co-operative bank or to the successor co-operative bank or to the converted banking company under section under section 33 or 44 or 52(1) (Table: Sl. No. 1 or 2) has to be determined in accordance with the following formula-

(i) **For predecessor co-operative bank**

$$A \times \frac{B}{C}$$

(ii) **For successor co-operative bank or converted banking company**

$$A \times \frac{D}{C}$$

A = the amount of deduction allowable to the predecessor co-operative bank if the business reorganisation had not taken place;

B = the number of days comprised in the period beginning with the 1st day of the tax year and ending on the day immediately preceding the date of business reorganisation; and

C= the total number of days in the tax year in which the business reorganisation has taken place.

D= the number of days comprised in the period beginning with the date of business reorganisation and ending on the last day of the tax year; and



Let us take a case where the deduction allowable under section 33 to the predecessor co-operative bank is, say, ₹ 1,20,000 and the business re-organisation took place on 1.11.2026. Then, the deduction allowable to the predecessor co-operative bank under section 33 would be ₹ 70,356 i.e., ₹ 1,20,000 x 214/365. The deduction allowable to the successor co-operative bank or to the converted banking company would be ₹ 49,644 i.e., ₹ 1,20,000 x 151/365.

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(3) Manner for computing deduction: The provisions of section 44 or 52(1) (Table: Sl. No. 1 or 2) shall, in a case where an undertaking of the predecessor co-operative bank entitled to the deduction under said section is transferred before the expiry of the period specified therein to a successor co-operative bank or to a converted banking company on account of business reorganisation, apply to the successor co-operative bank or to converted banking company in the tax years subsequent to the year of business reorganisation as they would have applied to the predecessor co-operative bank, as if the business reorganisation had not taken place.

Meaning of certain terms:

Term	Meaning
Business reorganisation	The reorganisation of business involving the amalgamation or demerger of a co-operative bank or conversion of a primary co-operative bank [Section 65(d).
Conversion	Transition of a primary co-operative bank to a banking company under the scheme of the RBI as notified vide its circular no. DCBR. CO. LS. PCB. Cir. No. 5/07.01.000/2018-19, dated 27.09.2018 [Section 65(e)].
Converted banking company	A banking company formed as a result of conversion from primary co-operative bank [Section 65(f)].
Co-operative bank	"Co-operative bank" shall have the same meaning as specified in Part V of the Banking Regulation Act, 1949. [Sec. 2(31)]
Banking company	A company to which the Banking Regulation Act, 1949 applies and includes any bank or banking institution referred to in section 51 of that Act. [Sec. 66(2)]
Predecessor co-operative bank	The amalgamating co-operative bank or the demerged co-operative bank or primary co-operative bank which has been succeeded as a result of conversion [Section 65(i)].
Primary co-operative bank	The meaning assigned to it in clause (ccv) of section 56 of the Banking Regulation Act, 1949 [Section 65(j)]
Successor co-operative bank	The amalgamated co-operative bank or the resulting bank [Section 65(l)].

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Amalgamated co-operative bank	(1) a co-operative bank with which one or more amalgamating co-operative banks merge; or (2) a co-operative bank formed as a result of merger of two or more amalgamating co-operative banks [Section 65(c)].
Amalgamating co-operative bank	(1) a co-operative bank which merges with another co-operative bank; or (2) every co-operative bank merging to form a new co-operative bank [Section 65(b)].
Amalgamation	The merger of an amalgamating co-operative bank with an amalgamated co-operative bank, if – (1) all the assets and liabilities of the amalgamating co-operative bank or banks immediately before the merger (other than the assets transferred, by sale or distribution on winding up, to the amalgamated co-operative bank) become the assets and liabilities of the amalgamated co-operative bank; (2) the members holding 75% or more voting rights in the amalgamating co-operative bank become members of the amalgamated co-operative bank; and (3) the shareholders holding 75% or more in value of the shares in the amalgamating co-operative bank (other than the shares held by the amalgamated co-operative bank or its nominee or its subsidiary, immediately before the merger) become shareholders of the amalgamated co-operative bank [Section 65(a)].
Demerger	The transfer by a demerged co-operative bank of one or more of its undertakings to any resulting co-operative bank, in such manner that- (1) all the assets and liabilities of the undertaking or undertakings immediately before the transfer become the assets and liabilities of the resulting co-operative bank;

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	(2) the assets and the liabilities are transferred to the resulting co-operative bank at values (other than change in the value of assets consequent to their revaluation) appearing in its books of account immediately before the transfer; (3) the resulting co-operative bank issues, in consideration of the transfer, its membership to the members of the demerged co-operative bank on a proportionate basis; (4) the shareholders holding 75% or more in value of the shares in the demerged co-operative bank (other than shares already held by the resulting bank or its nominee or its subsidiary immediately before the transfer), become shareholders of the resulting co-operative bank, otherwise than as a result of the acquisition of the assets of the demerged co-operative bank or any undertaking thereof by the resulting co-operative bank; (5) the transfer of the undertaking is on a going concern basis; and (6) the transfer is in accordance with the conditions specified by the Central Government, by notification in the Official Gazette, having regard to the necessity to ensure that the transfer is for genuine business purposes [Section 65(g)].
Demerged co-operative bank	The co-operative bank whose undertaking is transferred, pursuant to a demerger, to a resulting bank [Section 65(h)].
Resulting co-operative bank	(1) one or more co-operative banks to which the undertaking of the demerged co-operative bank is transferred in a demerger; or (2) any co-operative bank formed as a result of demerger [Section 65(k)].

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ILLUSTRATION 20

Alpha Co-operative Bank amalgamated with Beta Co-operative Bank on 1.12.2026. The depreciation for the year ended 31.3.2027 calculated as per Income-tax Rules 2026, allowable to Alpha Co-operative Bank had the amalgamation had not taken place amounts to ₹ 2,40,000. Compute the deduction on account of depreciation allowable in the hands of Alpha Co-operative Bank and Beta Co-operative Bank for T.Y. 2026-27.

SOLUTION

The amount of deduction allowable to the amalgamating co-operative bank (i.e. Alpha Co-operative bank, in this case) under section 33 has to be determined in accordance with the following formula -

$$A \times \frac{B}{C}$$

The amount of deduction allowable to the amalgamated co-operative bank (i.e. Beta Co-operative bank, in this case) under section 33 has to be determined in accordance with the formula -

$$A \times \frac{D}{C}$$

A = the amount of deduction allowable to the predecessor co-operative bank (i.e. Alpha Co-operative bank, in this case) if the business reorganisation had not taken place. In this case, the amount of deduction is ₹ 2,40,000.

B = the number of days comprised in the period beginning with the 1st day of the tax year (i.e., 1.4.2026, in this case) and ending on the day immediately preceding the date of business reorganization (i.e., 30.11.2026, in this case); and

C = the total number of days in the tax year in which the business reorganisation has taken place (i.e., 365 days).

D = the number of days comprised in the period beginning with the date of business reorganisation (i.e. 1.12.2026, in this case) and ending on the last day of the financial year (i.e. 31.3.2027);

In this case, the deduction that would have been allowable under section 33 to Alpha co-operative bank had the business reorganization had not taken place is ₹ 2,40,000 and the business re-organisation took place on 1.12.2026. Therefore, the deduction allowable to Alpha co-operative bank under section 33 would be ₹1,60,438 i.e., ₹ 2,40,000 x 244/365. The deduction allowable to Beta co-operative bank would be ₹ 79,562 i.e., ₹ 2,40,000 x 121/365.

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3.18 COMPUTATION OF BUSINESS INCOME IN CASES WHERE INCOME IS PARTLY AGRICULTURAL AND PARTLY BUSINESS IN NATURE

Income from manufacture of rubber, coffee and tea [Rule 271]

(1) In case of incomes specified in the table below, the income shall be computed as if it were income derived from business and a percentage of such incomes shall be deemed to be the income liable to tax.

S. No.	Nature of Income	% of such income deemed to be the income liable to tax
1	Income from sale of rubber products derived from rubber plant grown by the seller **in India [Refer Note Below]**	35%
2	Income derived from the sale of coffee grown and cured by the seller **in India**	25%
3	Income derived from the sale of coffee grown, cured, roasted, and grounded by the seller in India with or without mixing chicory or other flavouring ingredients	40%
4	Income derived from the sale of tea grown and manufactured by the seller **in India**	40%
Note - *Income from sale of centrifuged latex or cenex or latex-based crepes (such as pale latex crepe) or brown crepes (such as estate brown crepe, remilled crepe, smoked blanket crepe or flat bark crepe) or technically specified block rubbers manufactured or processed from field latex or coagulum obtained from rubber plants grown by the seller in India.*		

(2) In computing such income, an allowance shall be made in respect of the cost of planting rubber plants, coffee plants and tea bushes, in replacement of plants or bushes that have died or become permanently useless in an area already planted, if such area has not previously been abandoned.

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(3) For the purpose of determining such cost, no deduction shall be made in respect of the amount of any subsidy which, under the provisions of Schedule III (Table: S. No. 21), is not includible in the total income.

Note: *The percentage of income as mentioned above is to be treated as taxable income and the balance shall be treated as agriculture income.*

ILLUSTRATION 21

Miss Vivitha, a resident and ordinarily resident in India, has derived the following income from various operations (relating to plantations and estates owned by her) during the year ended 31-3-2027:

S. No.	***Particulars***	***₹***
(i)	*Income from sale of centrifuged latex processed from rubber plants grown in Darjeeling.*	*3,00,000*
(ii)	*Income from sale of coffee grown and cured in Yercaud, Tamil Nadu.*	*1,00,000*
(iii)	*Income from sale of coffee grown, cured, roasted and grounded, in Colombo. Sale consideration was received at Chennai.*	*2,50,000*
(iv)	*Income from sale of tea grown and manufactured in Shimla.*	*4,00,000*
(v)	*Income from sapling and seedling grown in a nursery at Cochin. Basic operations were not carried out by her on land.*	*80,000*

You are required to compute the business income and agricultural income of Miss Vivitha for the tax year 2026-27.

SOLUTION

Computation of business income and agricultural income of Ms. Vivitha for the T.Y.2026-27

Sr. No.	**Source of income**	**Gross (₹)**	**Business income**		**Agricultural income**
			%	**₹**	**₹**
(i)	Sale of centrifuged latex from rubber plants grown in India.	3,00,000	35%	1,05,000	1,95,000
(ii)	Sale of coffee grown and cured in India.	1,00,000	25%	25,000	75,000

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(iii)	Sale of coffee grown, cured, roasted and grounded outside India. **(See Note 1 below)**	2,50,000	100%	2,50,000	-
(iv)	Sale of tea grown and manufactured in India	4,00,000	40%	1,60,000	2,40,000
(v)	Saplings and seedlings grown in nursery in India **(See Note 2 below)**	80,000		Nil	80,000
	Total			**5,40,000**	**5,90,000**

Notes:

1. Where income is derived from sale of coffee grown, cured, roasted and grounded by the seller in India, 40% of such income is taken as business income and the balance as agricultural income. However, in this question, these operations are done in Colombo, Sri Lanka. Hence, there is no question of such apportionment and the whole income is taxable as business income. Receipt of sale proceeds in India does not make this agricultural income. In the case of an assessee, being a resident and ordinarily resident, the income arising outside India is also chargeable to tax.
2. Section 2(5)(d) provides that the income derived from saplings or seedlings grown in a nursery would be deemed to be agricultural income whether or not the basic operations were carried out on land.

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TEST YOUR KNOWLEDGE

Questions

1. *Examine critically the following cases in the context of provisions contained in the Income-tax Act, 2025 relevant for Tax Year 2026-27. Support the answers with relevant case laws and workings.*

   (a) *Mr. Janak is proprietor of M/s. Yash Texnit which is engaged in garment manufacturing business. The entire block of Plant & Machinery chargeable to depreciation @ 15%, has 20 different machinery items as at 31-03-2027. One of the machineries used for packing has become obsolete and was discarded by Mr. Janak in July 26.*

   Assessee filed its return for T.Y. 2026-27 claiming total depreciation of ₹40 lakhs which includes ₹4 lakhs being the depreciation claimed on the machinery item discarded by Mr. Janak. The A.O. disallowed the claim of depreciation of ₹4 lakhs during the course of scrutiny assessment.

   Comment on the validity of action taken by A.O.

   (b) *X. Ltd. issued debentures in the tax year 2026-27, which were to be matured at the end of 5 years. The debenture holder was given an option of one time upfront payment of ₹60 per debenture on account of interest which was to be immediately paid by the company. As per the option exercised by the debenture holders, company paid interest upfront to them in the first year itself and the same was claimed as deduction in the return of the company. But in the accounts, the interest expenditure was shown as deferred expenditure to be written off over a period of 5 years. During the course of assessment, the Assessing Officer spread the upfront interest paid over a period of five-year term of debentures and allowed only one-fifth of the amount in the tax year 2026-27. Examine the correctness of the action of Assessing Officer.*

2. *Compute the quantum of depreciation available under section 33 of the Income-tax Act, 2025 in respect of the following items of Plant and Machinery purchased by PQR Textile Ltd., by paying through account payee cheque, which is engaged in the manufacture of textile fabrics, for the year ended 31-3-2027. Assume company does not opt for the provisions of section 200:*

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	(₹ in crores)
New machinery installed on 1-5-2026	*84*
New Windmill purchased and installed on 18-6-2026	*22*
Lorries for transporting goods to sales depots (purchased and put to use in July, 2026)	*3*
Items purchased after 30th November 2026:	
Fork-lift trucks, used inside factory	*4*
Computers installed in office premises	*1*
Computers installed in factory	*2*
New imported machinery	*12*

The new imported machinery arrived at Chennai port on 30-03-2027 and was installed on 3-4-2027. All other items were installed during the year ended 31-3-2027.

The company was newly started during the year.

Also, compute the WDV of the various blocks of assets as on 1.4.2027 after charging depreciation for T.Y. 2026-27.

3. *(A) Examine the taxability and/ or allowability of the following receipts or expenditures under the provisions of the Income-tax Act, 2025, for the tax year 2026-27:*

   (i) Secret commission was paid during the tax year 2026-27.

   (ii) P Ltd. paid dollars equivalent to ₹ 50 lakhs as sales commission for the year ended 31.03.2027, without deducting tax at source, to Mr. Rodrigues, a citizen of UK and non-resident who acted as agent for booking orders, from various customers who are outside India.

   (B) Can the following transactions be covered under section 37 for disallowance?

   (i) A bank guarantee given by a company towards disputed tax liabilities.

   (ii) Interest payable to Goods and Services Tax Department but not paid before the due date specified in section 263(1).

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4. *ILT Limited is engaged in manufacturing of pipes and tubes. The profit and loss account of the company for the year ended 31st March, 2027 shows a net profit of ₹405 lakhs. The following information and particulars are furnished to you. You are required to compute total income of the company for Tax Year 2026-27 indicating reasons for treatment of each item, assuming that the company has not opted for special provisions under section 200 or 201*

   (i) A group free air ticket was provided by a supplier for reaching a certain volume of purchase during the financial year 2026-27. The same is encashed by the company for ₹ 10 lakhs in April 2026 and credited to General Reserve Account.

   (ii) A regular supplier of raw materials agreed for settlement of ₹ 8 lakhs instead of ₹ 10 lakhs for poor quality of material supplied during the tax year which was not given effect in the running account of the supplier.

   (iii) Andhra Bank sanctioned and disbursed a term loan in the financial year 2023-24 for a sum of ₹ 50 lakhs. Interest of ₹ 8 lakhs was in arrears. The bank has converted the arrear interest into a new loan repayable in 10 equal instalments. During the year, the company has paid 2 instalments and the amount so paid has been reduced from Funded Interest in the Balance Sheet.

   (iv) The company remitted ₹ 5 lakhs as interest to a company incorporated in USA on a loan taken 2 years ago. Tax deducted under section 393(2) from such interest has been deposited by the company on 15th July, 2027. The said interest was debited to profit and loss account.

   (v) Sandeep, a sales executive stationed at HO at Delhi, was on official tour in Bangalore from 31st May, 2026 to 18th June, 2026 and 28th September, 2026 to 15th October, 2026 for the business development. The company has paid Sandeep's salary in cash, from its local office at Bangalore for the month of May, 2026 (payable on 1st June) and September 2026 (payable on 1st October), amounting to ₹45,000 and ₹47,000 respectively (net of TDS and other deduction), as Sandeep has no bank account at Bangalore. These were included in the amount of "salary" debited to Profit and Loss Account.

   (vi) The company has contributed ₹ 50,000 by account payee cheque to an electoral trust and the same stands included under the head "General Expenses".

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5. *G Ltd., a company in which public are substantially interest, is engaged in the business of growing and manufacturing tea in India. For the tax year ended 31.03.2026, its composite business profits before allowing deduction u/s 48 is ₹ 60,00,000. On 01.09.2026, it deposited a sum of ₹ 11,00,000 in the Tea Development Account. During the tax year 2024-25, G Ltd. incurred a business loss of ₹ 14,00,000 which has been carried forward. On 25.01.2027, it withdrew ₹ 10 lakhs, from deposit account which is utilized as under:*

₹ 6,00,000 for purchase on non-depreciable asset as per the scheme specified.

₹ 3,00,000 for purchase of machinery to be installed in the office premises.

₹ 1,00,000 was spent for the purpose of scheme on 5.4.2027.

(i) You are required to determine business income of G Ltd. and the tax consequences that may arise from the above transactions in the T.Y. 2026-27.

(ii) What will be the consequence if the asset which was purchased for ₹ 6,00,000 is sold for ₹ 8,00,000 in April, 2027.

6. *The trading and profit and loss account of Pingu Trading Pvt. Ltd. having business of agricultural produce, consumer items and other products for the year ended 31.03.2027 is as under:*

Trading Account

Particulars	₹	Particulars	₹
Opening Stock	3,75,000	Sales	1,55,50,000
Purchases	1,25,75,000	Closing Stock	4,50,000
Freight & Cartage	1,26,000		
Gross profit	29,24,000		
	1,60,00,000		**1,60,00,000**

Profit and Loss Account

Particulars	₹	Particulars	₹
Bonus to staff	47,500	Gross profit	29,24,000
Rent of premises	53,500	Income-tax refund	20,000
Advertisement	5,000	Warehousing charges	15,00,000

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Bad Debts	*75,000*		
Interest on loans	*1,67,500*		
Depreciation	*71,500*		
Goods and Services tax demand paid	*1,08,350*		
Miscellaneous expenses	*5,25,650*		
Net profit of the year	*33,90,000*		
	44,44,000		***44,44,000***

On scrutiny of records, the following further information and details were extracted/ gathered:

(i) There was a survey under section 253 on the business premises on 31.3.2027 in which it was revealed that the value of closing stocks of 31.3.2026 was ₹ 8,75,000 and a sale of ₹ 75,000 made on 13.3.2027 was not recorded in the books. The value of closing stocks after considering these facts and on the basis of inventory prepared by the department as on 31.3.2027 worked out at ₹ 12,50,000, which was accepted to be correct and not disputed.

(ii) Income-tax refund includes amount of ₹ 4,570 of interest allowed thereon.

(iii) Bonus to staff includes an amount of ₹ 7,500 paid in the month of December 2026, which was provided in the books on 31.03.2026.

(iv) Rent of premises includes an amount of ₹ 5,500 incurred on repairs. The assessee was under no obligation to incur such expenses as per rent agreement.

(v) Advertisement expenses include an amount of ₹ 2,500 paid for advertisement published in the souvenir issued by a political party. The payment is made by way of an account payee cheque.

(vi) Miscellaneous expenses include:

(a) amount of ₹ 15,000 paid towards penalty for non-fulfillment of delivery conditions of a contract of sale for the reasons beyond control,

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(b) *amount of ₹ 1,00,000 paid to the wife of a director, who is working as junior lawyer for taking an opinion on a disputed matter. The junior advocate of High Courts normally charges only ₹ 25,000 for the same opinion,*

(c) *amount of ₹ 1,00,000 paid to an Electoral Trust by cheque.*

(vii) *Goods and Services Tax demand paid includes an amount of ₹ 5,300 charged as penalty for delayed filing of returns and ₹ 12,750 towards interest for delay in deposit of tax.*

(viii) *The company had made an investment of ₹ 25 lakhs on the construction of a warehouse in rural area for the purpose of storage of agricultural produce. This was made available for use from 15.09.2026 and the income from this activity is credited in the Profit and Loss account under the head "Warehousing charges".*

(ix) *Depreciation under the Income-tax Act, 2025 works out at ₹ 65,000.*

(x) *Interest on loans includes an amount of ₹ 80,000 paid to Mr. X, a resident, on which tax was not deducted.*

Compute the income chargeable to tax for tax year 2026-27 of Pingu Trading Pvt. Ltd, ignoring MAT and provisions of section 200. Support your answer with working notes.

7. (a) *A Ltd. paid IDBI Bank a lump sum pre-payment premium of ₹ 1.2 lakhs on 7.4.2027 for restructuring its debts and reducing its rate of interest. It claimed the entire sum as business expenditure for the T.Y.2026-27. The Assessing Officer, however, held that the pre-payment premium should be amortised over a period of 10 years (being the tenure of the restructured loan), and thus, allowed only 10% of the pre-payment premium in the T.Y.2026-27. Discuss, with reasons, whether the contention of A Ltd. is correct or that of the Assessing Officer.*

(b) *Explain the tax treatment of emergency spares (of plant and machinery) acquired during the year which, even though kept ready for use, have not actually been used during the relevant tax year.*

8. *"Easy Call Ltd.", to provide telecom services in Mumbai, obtained a licence on 1.4.2024 for a period of 10 years ending on 31.3.2034 against a fee of ₹ 27*

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lakhs to be paid in 3 installments of ₹ 9 lakhs each by April, 2024, April, 2025 and April, 2026, respectively. The company has commenced business on 1.4.2025.

Explain, how the payment made for licence fee shall be dealt with under the Income-tax Act, 2025 and the amount, if any, deductible for T.Y. 2026-27.

9. *Alpha Ltd., a manufacturing company, has disclosed a net profit of ₹ 12.50 lakhs for the year ended 31st March, 2027. You are required to compute the taxable income (ignore the provisions of section 200) of the company for the Tax year 2026-27, after considering the following information, duly explaining the reasons for each item of adjustment:*

   (i) Advertisement expenditure debited to profit and loss account includes the sum of ₹ 60,000 paid in cash to the sister concern of a director, the market value of which is ₹ 52,000.

   (ii) Repairs of plant and machinery debited to profit and loss account includes ₹ 1.80 lakhs towards replacement of worn out parts of machineries. Such expenditure does not increase the future benefit from the asset beyond its previously assessed standard of performance.

   (iii) A sum of ₹ 6,000 on account of liability foregone by a creditor has been taken to general reserve. The original purchases was debited to the Profit & Loss Account in the T.Y.2022-23.

   (iv) Sale proceeds of import entitlements amounting to ₹ 1 lakh has been credited to Profit & Loss Account, which the company claims as capital receipt not chargeable to income-tax.

   (v) Being also engaged in the biotechnology business, the company incurred the following expenditure on in-house research and development as approved by the prescribed authority:

      (a) Research equipments purchased ₹ 1,50,000.

      (b) Remuneration paid to scientists ₹ 50,000.

   The total amount of ₹ 2,00,000 is debited to the profit and loss account.

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10. (i) *A corporation was set up by the State Government transferring all the buses owned by it for a consideration of ₹75 lakhs, which was discharged by the Corporation by issue of equity shares. The Corporation in its assessment claimed depreciation. Can the depreciation be denied in the Corporation's hands on the ground that there was no registration of the buses in favour of the Corporation?*

(ii) *Ravi succeeded to his father's business in the year 2024. In the tax year ended 31.3.2027, Ravi has written off the balance in the name of 'Y' which relates to supply made by his father, when he carried on business. Ravi desires to know whether the write off could be eligible for deduction.*

Answers

1. (a) The issue under consideration is whether disallowance of depreciation made by the Assessing Officer with regard to the discarded asset, in arriving at the written down value of the block of assets, is justified.

One of the conditions for claim of depreciation under section 33 is that the eligible asset must have been put to use for the purpose of business or profession.

The other aspect to be considered is whether merely discarding an obsolete machinery, which is physically available, will attract the expression "moneys payable" appearing in section 41(1), so as to deduct its value from the written down value of the block.

The facts in the present case are similar to facts in the case of *CIT v. Yamaha Motor India Pvt. Ltd. (2010) 328 ITR 297*, wherein the Delhi High Court observed that the expression "used for the purposes of the business" in section 33 of the Income-tax Act, 2025[13] when used with respect to discarded machinery would mean the use in the business, not only in the relevant financial year/tax year, but also in the earlier financial years.

The discarded machinery may not be actually used in the relevant tax year but depreciation can be claimed as long as it was used for the purposes of business in the earlier years provided the block continues

[13] *section 32 of Income-tax Act 1961*

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to exist in the relevant tax year. Therefore, the condition for claiming depreciation in respect of the discarded machine would be satisfied if it was used in the earlier tax years for the business.

For the purpose of section 66(13), "moneys payable" means the sale price, in case of sale, or the insurance, salvage or compensation moneys payable in respect of the asset. In this case, the machinery has not been sold as machinery or scrap or disposed off, and it continues to exist. Hence, there is no "moneys payable" in this case, which alone is deductible while computing the WDV of the block to which it belongs.

Applying the rationale of the above case, the action of the Assessing Officer in disallowing ₹ 4 lakhs, being the depreciation claim attributable to discarded machinery, on the ground that the same was not put to use in the relevant tax year, is invalid, since the said machinery was put to use in the earlier tax years.

(b) The issue under consideration is whether, in a case where debentures are issued with maturity at the end of five years, and the debenture holders are given an option of upfront payment of interest in the first year itself, can the entire upfront interest paid, be claimed as deduction by the company in the first year or should the same be deferred over a period of five years; and would the treatment of such interest as deferred revenue expenditure in the books of account have any impact on the tax treatment.

The facts of the case are similar to the facts in *Taparia Tools Ltd. v. JCIT (2015) 372 ITR 605*, wherein the above issue came up before the Supreme Court. In that case, it was observed that under section 32(b) of the Income-tax Act, 2025[14], the amount of interest paid in respect of capital borrowed for the purposes of business or profession, is allowable as deduction.

The moment the option for upfront payment was exercised by the subscriber, the liability of X Ltd. to make the payment in that year had arisen. Not only had the liability arisen in the tax year in question, it was even quantified and discharged as well in that very year.

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[14] *section 36(1)(iii) of Income-tax Act 1961*

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As per the rationale of the Supreme Court ruling in *Taparia Tools Ltd.'s* case, when the deduction of entire upfront payment of interest is allowable as per the Income-tax Act, 2025, the fact that a different treatment was given in the books of account could not be a factor which would bar the company from claiming the entire expenditure as a deduction.

Accordingly, the action of the Assessing Officer in spreading the upfront interest paid over the five-year term of debentures and restricting the deduction in the T.Y.2026-27 to one-fifth of the upfront interest paid is **not** correct. The company is eligible to claim the entire amount of interest paid upfront as deduction under section 32(b) in the T.Y.2026-27.

2. Computation of depreciation allowance under section 33 for the T.Y. 2026-27

Particulars	Normal Depreciation [u/s 33(3)(a)]	Additional Depreciation [u/s 33(8)]
	(₹ in crores)	
(A) Plant and Machinery (15% block) (Put to use for 180 days or more)		
- New machinery installed on 01.05.2026	84.00	84.00
- Lorries for transporting goods to depots	3.00	-
	87.00	84.00
Normal Depreciation @15% & additional deprecation @20%	**13.05**	**16.80**
(B) Plant and Machinery (15% block) (Put to use for less than 180 days – hence, depreciation is restricted to 7.5%, being 50% of 15%)		
- Fork-lift trucks, used inside a factory	4.00	4.00

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	Normal Depreciation @ 7.5% & additional depreciation @10%	**0.30**	**0.40**
(C)	**Plant and Machinery (40% block) (Put to use for less than 180 days, hence depreciation restricted to 20%, i.e., 50% of 40%)**		
	- Computers installed in office premises	1.00	-
	- Computers installed in factory	2.00	2.00
		3.00	**2.00**
	Normal depreciation @20% & additional depreciation@10%	**0.60**	**0.20**
(D)	**Plant and Machinery (40% block) (Put to use for 180 days or more)** ***(See Note 1)***		
	- New windmill purchased and installed on 18.06.2026	22.00	22.00
	Normal Depreciation @ 40% & additional depreciation @ 20%	**8.80**	**4.40**
Total depreciation and additional depreciation			
	- Plant and Machinery (15% block) (A +B)	13.35	17.20
	- Plant and Machinery (40% block) (C + D)	9.40	4.60
Depreciation available under section 32 = ₹ 44.55 crores			

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Computation of Written Down Value (WDV) after charging depreciation for T.Y. 2026-27

Particulars		Plant & Machinery	
		15%	40%
		(₹ in crores)	
WDV as on 01.04.2026 (The company was started during the year – as given in question)		Nil	Nil
Add: Plant and Machinery acquired during the year			
- New Machinery installed on 01.05.2026	84.00		
- Lorries for transporting goods to sales depots	3.00		
- Fork-lift trucks, used inside factory	4.00		
- New imported machinery	12.00	103.00	-
- New Windmill purchased and installed on 18.6.2026		-	22.00
- Computers installed in office premises		-	1.00
- Computers installed in factory		-	2.00
		103.00	**25.00**
Less: Asset sold during the year		Nil	Nil
WDV as on 31.3.2027 (before charging depreciation)		103.00	**25.00**
Less: Depreciation for the T.Y.2026-27			
- Normal depreciation		13.35	9.40
- Additional depreciation		17.20	4.60
WDV as on 1.4.2027 (after charging depreciation for T.Y. 2026-27)		**72.45**	**11.00**

Notes:

(1) Windmills and any specially designed devices which run on windmills would be eligible for depreciation @ 40%.

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(2) New imported machinery was not installed during the tax year 2026-27. Hence, it would not be eligible for additional depreciation for T.Y. 2026-27. It would also not be eligible for normal depreciation for T.Y 2026-27, since it was not put to use in the T.Y.2026-27 being the year of acquisition.

(3) It may be noted that investment in the following plant and machinery would not be eligible for additional depreciation under section 33(8):

(a) Lorries for transporting goods to sales depots, being vehicles/road transport vehicles; and

(b) Computers installed in office premises.

(4) As per section 2(28) of the Motor Vehicles Act, 1988, the definition of a "vehicle" excludes, *inter alia*, a vehicle of special type adopted for use only in a factory or in any enclosed premises. Therefore, fork-lift trucks used inside the factory would not fall within the definition of "vehicle". Hence, it is eligible for additional deprecation under section 33(8).

3. (A) (i) Secret commission is one of the forms of commission payment generally made by business organizations. Secret commission is a payment for obtaining business orders or contracts from parties and /or customers and paid to employees and / or officials of those parties and / or customers or companies from whom business orders are obtained by the assessee.

Section 34(2)(a) of Income-tax Act, 2025 provides that any expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law, shall not be included in any expenditure laid or expended wholly and exclusively for the purpose of business or profession and no deduction or allowance shall be made in respect of such expenditure. In view of section 34(2)(a), any expenditure incurred for a purpose which is an offence and prohibited by law cannot be allowed as expenditure. Therefore, since secret commission payment is a payment for an offence prohibited by law, the same cannot be allowed as deduction.

(ii) A foreign agent of an Indian exporter operates in his own country and no part of his income accrues or arises in India. His commission is usually remitted directly to him and is, therefore, not received by him or on his behalf in India. The commission paid

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to the non-resident agent for services rendered outside India is, thus, not chargeable to tax in India.

Since commission income for booking orders by non-resident who remains outside India is not subject to tax in India, disallowance under section 35(b)(ii) is not attracted in respect of payment of commission to such non-resident outside India even though tax has not been deducted at source. Thus, the amount of ₹ 50 lakhs remitted to Mr. Rodrigues outside India in foreign currency towards commission would not attract disallowance under section 35(b)(ii) for non-deduction of tax at source.

(B) **(i)** For claiming deduction of any expense enumerated under section 37, the requirement is that the actual payment and not deemed payment. Furnishing of bank guarantee cannot be equated with actual payment. Actual payment requires that money must flow from the assessee to the public exchequer as specified in section 37. Therefore, deduction of an expense covered under section 37 cannot be claimed by merely furnishing a bank guarantee *[CIT v. McDowell & Co Ltd (2009) 314 ITR 167 (SC)]*

(ii) Interest payable to Goods and Services Tax department is part of Goods and Services Tax.

Therefore, interest payable to Goods and Services Tax department, which is not paid before the "due date" of filing of return of income, would attract disallowance under section 37 [*Mewar Motors v. CIT (2003) 260 ITR 218 (Raj)]*

4. Computation of total income of ILT Ltd. for the T.Y.2026-27

Particulars	₹ (in lakhs)	
Profits and gains from business or profession		
Net profit as per profit and loss account		405.00
Add: **Items debited to profit and loss account, but to be disallowed and items not considered in accounts but to be taxed**		
Value of group free air ticket provided by a supplier is taxable as business income under section 26(2)(f), as the value of any benefit, whether convertible into	10	

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money or not, arising from business is taxable as business income.		
Amount waived by the supplier of raw materials is a deemed income under section 38(1)(a), as the expenditure was allowed as deduction in the last year and there is a benefit by way of remission or cessation of a trading liability. The fact that effect was not given in the running account of supplier is not relevant.	2	
Interest payable outside India to a foreign company is allowable **[See Note 1 below]**	-	
Salary paid to employee Sandeep is eligible for deduction. Disallowance under section 36(4) will not apply **[See Note 2 below]**	-	
Contribution to electoral trust is not an allowable expenditure while computing business income. Hence, the same has to be added back, since it is included in general expenses.	0.50	12.50
		417.50
***Less:* Amount of deduction allowable**		
Under section 37(1), interest on loan due to any specified financial entities is allowed as deduction, if such interest is actually paid irrespective of the method of accounting followed by the assessee. Conversion of arrear interest into a fresh loan by a bank cannot be considered as actual payment of interest. However, the amount of funded interest (i.e., converted loan) actually paid is allowable as deduction. Hence, ₹ 1,60,000, being two instalments of ₹ 80,000 each, actually paid is deductible.		1.60
Business Income		**415.90**
Gross total income		**415.90**
***Less:* Deduction under Chapter VIII-B**		
Deduction under section 136 in respect of contribution by the assessee company to an electoral trust.		0.50
Total Income		**415.40**

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Notes:

1. Since tax has been deducted on interest payable outside India to a foreign company during the tax year 2026-27 and the same has been deposited before the due date of filing return of income under section 263(1), disallowance under section 35(b)(ii) is not attracted. Since the interest has already been debited to profit and loss account, no further adjustment is required.
2. In respect of payment of salary to sales executive in cash, no disallowance under section 36(4) is to be made as the payments fall within the scope of Rule 26. Salary paid to him in cash is allowable as the executive was temporarily posted for a continuous period of more than 15 days in Bangalore which is not the place of his normal duty. Further tax was deducted from such salary under section 392 and he does not maintain any bank account in Bangalore. No disallowance under section 36(4) is attracted in respect of such salary.

5. (i) Computation of Business Income of G Ltd. and tax consequences for the T.Y. 2026-27

Particulars	₹
₹ 10,00,000 being the amount withdrawn from Tea Development Account has to be utilized in the prescribed manner, otherwise, the withdrawn amount would be chargeable to tax as business income. In the given case, the taxability of withdrawal amount based on their utilization is as follows:	
- ₹ 6,00,000, out of the amount withdrawn from the deposit account, utilised for purchase of non-depreciable asset as per the specified scheme. [As per paragraph 4 of Schedule IX, no deduction would be allowed under section 48 since amount is spent out of ₹ 11 lakh deposited in Tea Development Account, which has already been allowed as deduction in T.Y.2025-26 **(See Working Note below)**].	Not taxable

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- ₹ 3,00,000, being the amount utilized for purchase of machinery to be installed in the office premises is not a permissible utilization. Hence, the amount would be deemed as profits and gains of business of the tax year 2026-27 as per paragraph 3(3) of Schedule IX.	3,00,000
- ₹ 1,00,000 was spent for the purpose of scheme on 05.04.2027. As per paragraph 3(4) of Schedule IX, this amount would be taxable since the same is not utilized during the same tax year (i.e., T.Y. 2026-27) in which the amount is withdrawn from the deposit account.	1,00,000
When any part of withdrawal amount becomes taxable, the agricultural and non-agricultural portions of income must be segregated. Accordingly, ₹ 1,60,000, being 40% of ₹ 4,00,000 (₹ 3,00,000 + ₹ 1,00,000) would be chargeable to tax as business income and the balance ₹ 2,40,000, being 60% of ₹ 4,00,000 would be agricultural income exempt from tax.	

Working Note:

Computation of Business Income of G Ltd. for the T.Y. 2025-26

Particulars	₹
Composite business profits before allowing deduction under section 48	60,00,000
Less: Deduction under section 48(1) would be the lower of:	
- Amount deposited in Tea Development Account on or before 30.9.2026 [i.e., ₹ 11,00,000]	
- 40% of profits of such business [i.e., ₹ 24,00,000, being 40% of ₹ 60,00,000]	11,00,000
	49,00,000
Less: 60% of ₹ 49,00,000, being agricultural income **[as per Rule 271]**	29,40,000

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Business income	19,60,000
Less: Brought forward business loss of T.Y.2024-25 set-off as per section 112	14,00,000
Business income chargeable to tax	5,60,000

(ii) Consequences, if asset purchased out of deposit account is sold during the tax year 2027-28

As per paragraph 5 of Schedule IX , if the asset is acquired in accordance with the scheme and is sold before the expiry of eight years from the end of the tax year in which it was acquired, then, the cost of such asset which is relatable to the deduction allowed shall be deemed to be the profits and gains from business or profession of the tax year in which asset is sold.

Therefore, ₹ 6,00,000 would be deemed to be the business income (composite) for the T.Y.2027-28. However, since the full cost of the asset was deducted in the tax year 2026-27 (being part of ₹ 11 lakh deposited in Tea Development Account) before segregation of agricultural income and non-agricultural income, the agricultural and non-agricultural portions of income should be segregated in the year in which such amount becomes taxable on account of sale of asset before the expiry of eight years. Therefore, ₹ 3,60,000, being 60% of ₹ 6,00,000 would represent agricultural income. The balance ₹ 2,40,000 being 40% of ₹ 6,00,000 would be chargeable to tax as business income.

Moreover, the difference between the sale consideration and purchase price of the asset would be chargeable to tax as "Short term capital gains", which is computed as follows:

Sales consideration	8,00,000
Less: Cost of acquisition	6,00,000
Short term capital gain	**2,00,000**

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6. Computation of Income of Pingu Trading Pvt. Ltd. chargeable to tax for the T.Y.2026-27

Particulars		₹
Net profit as per profit and loss account		33,90,000
Less:	Income-tax refund credited in the profit and loss account, out of which interest is to be considered separately under the head "Income from other sources"	20,000
		33,70,000
Add:	**Expenses either not allowable or to be considered separately but charged in the profit & loss account**	
	- Repair expenses on rented premises where assessee is under no obligation to incur such expenses are not allowable as per section 28(1). However, if such expenses are required for carrying on the business efficiently, the same are allowable under section 34. In this case, assuming that such expenses are required for carrying on business efficiently, the same are allowable under section 34.	-
	- Advertisement in the souvenir of political party not allowable as per section 34(2)(c) **(See Note 2)**	2,500
	- Payment made to the wife of a director examined as per section 36(2) and the excess payment made to be disallowed **(See Note 4)**	75,000
	- Payment made to electoral trust by cheque **(See Note 5)**	1,00,000
	- Penalty levied by the Goods and Services tax department for delayed filing of returns not	5,300

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	allowable as being paid for infraction of law **(See Note 6)**		
	- Depreciation as per books		71,500
	- 30% of interest paid on loan paid to Mr. X, a resident, without deduction of tax at source not allowable as per section 35(b)(i).		24,000
			36,48,300
Less:	Depreciation allowable as per Income-tax Act, 2025		65,000
			35,83,300
Less:	Income from specified business (warehousing charges) credited to profit and loss account, to be considered separately **(See Note 7)**		15,00,000
Income from business (other than specified business)			**20,83,300**
Add: Difference in the value of stocks detected on survey under section 253 on 31.03.2027 chargeable as income **(See Note 8)**			3,75,000
			24,58,300
Computation of income/ loss from specified business (See Note 7)			
Income from specified business		₹ 15,00,000	
Less: Deduction under section 46 @ 100% of ₹ 25 lakhs		₹ 25,00,000	
Loss from specified business to be carried forward as per section 114		**(₹ 10,00,000)**	
Income from Other Sources			
Interest on income-tax refund			4,570
Gross Total Income			**24,62,870**
***Less:* Deduction under section 136**			

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Contribution to political party **(See Note 2)**	₹ 2,500	
Contribution to an Electoral trust **(See Note 5)**	₹ 1,00,000	1,02,500
Total Income		**23,60,370**

Notes:

(1) Bonus for the tax year 2025-26 paid after the due date for filing return for that year would have been disallowed under section 37 for the T.Y.2025-26. However, when the same has been paid in December 2026, it should be allowed as deduction in the T.Y.2026-27. Since it is already included in the figure of bonus to staff debited to profit and loss account for this year, no further adjustment is required.

(2) The amount of ₹ 2,500 paid for advertisement in the souvenir issued by a political party attracts disallowance under section 34(2)(c). However, such expenditure falls within the meaning assigned to "contribute" under section 182 of the Companies Act, 2013, and is hence, eligible for deduction under section 136. Any contribution to the political party or electoral trust made by way of cash is not allowed as deduction under section 136. Since in the present case, the payment to the political party is made by way of an account payee cheque, it is allowed as deduction under section 136.

(3) The penalty of ₹ 15,000 paid for non-fulfilment of delivery conditions of a contract for reasons beyond control is not for the breach of law but was paid for breach of contractual obligations and therefore, is an allowable expense.

(4) It has been assumed that ₹ 25,000 is the reasonable payment for the wife of Director, working as a junior lawyer, since junior advocates of High Courts normally charge only ₹ 25,000 for the same opinion and therefore, the balance ₹ 75,000 has been disallowed.

(5) Payment to an electoral trust qualifies for deduction under section 136 since the payment is made by way of a cheque. However, since the

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amount has been debited to profit and loss account, the same has to be added back for computing business income.

(6) The interest of ₹ 12,750 paid on the delayed deposit of goods and services tax is for breach of contract and hence, is allowable as deduction. However, penalty of ₹ 5,300 for delay in filing of returns is not allowable since it is for breach of law.

(7) Deduction @ 100% of the capital expenditure is available under section 46 in respect of specified business of setting up and operating a warehouse facility for storage of agricultural produce. It is presumed that ₹ 25 lakhs does not include expenditure on acquisition of any land.

The loss from specified business under section 46 (warehousing) should be segregated from the income from other businesses, since, as per section 73A(1), any loss computed in respect of any specified business referred to in section 46 shall not be set off except against profits and gains, if any, of any other specified business.

In view of the provisions of section 114, the loss of ₹ 10 lakhs from the specified business cannot be set-off against income from other businesses. Such loss has to be carried forward to be set-off against profit from specified business in the next tax year. The return should be filed on or before the due date under section 263(1) for carry forward of such losses.

(8) The business premises were surveyed and differences in the figures of opening and closing stocks and sales were found which have not been disputed and accepted by the assessee. Therefore, the trading account for the year is to be re-cast to arrive at the correct amount of the gross profit/ net profit for the purpose of return of income to be filed for the tax year ended on 31.3.2027.

Revised Trading Account

Particular	₹	Particular	₹
Opening Stock	8,75,000	Sales (₹ 1,55,50,000 + ₹ 75,000)	1,56,25,000
Purchases	1,25,75,000	Closing Stock	12,50,000

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Freight and Cartage	1,26,000		
Gross Profit	32,99,000		
	1,68,75,000		1,68,75,000

The difference of gross profit of ₹ 32,99,000 - ₹ 29,24,000 = ₹ 3,75,000 is to be added as income of the business for the year as undisclosed income[15].

7. (a) This issue came up before the Delhi High Court in *CIT v. Gujarat Guardian Ltd (2009) 177 Taxman 434*.The Court observed that the assessee company's claim for deduction has to be allowed in one lump sum keeping in view the provisions of section 37 of the Income-tax Act, 2025[16], which provide that any sum payable as interest on any loans or advances or borrowings from specified financial entities shall be allowed to the assessee in the year in which the same is paid, irrespective of the periods, in which the liability to pay such sum is incurred by the assessee according to the method of accounting regularly followed by the assessee. The High Court concurred with the Tribunal's view supporting the assessee that in terms of section 32(b) and section 2(59), respectively of the Income-tax Act, 2025[17], the deduction for pre-payment premium was allowable. Since there was no dispute that the pre-payment premium was nothing but interest and that it was paid to a specified financial entity i.e. IDBI Bank, the Court held that, in terms of section 37(2)(e) of the Income-tax Act, 2025[18], the assessee's claim for deduction has to be allowed in the year in which the payment has actually been made.

Therefore, applying the ratio of the above case, the contention of A Ltd. is correct and not that of the Assessing Officer.

Note *– Section 32(b) provides for deduction of interest paid in respect of capital borrowed for the purposes of business or profession. Section 2(59) defines interest to include, inter alia, any other charge in respect of the moneys borrowed or debt incurred. Section 37 provides for certain*

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[15] No loss (whether brought forward or otherwise) or unabsorbed depreciation can be set-off against undisclosed income.

[16] section 43B of Income-tax Act, 1961

[17] section 36(1)(iii) read with section 2(28A) of Income-tax Act, 1961

[18] section 43B(d) of Income-tax Act, 1961

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deductions to be allowed only on actual payment. From a combined reading of these three sections, it can be inferred that –

(i) pre-payment premium represents interest as per section 2(59);

(ii) such interest is deductible as business expenditure as per section 32(b);

(iii) such interest is deductible in one lump-sum on actual payment as per section 37(2)(e).

(b) As per ICDS V on Tangible Fixed Assets, machinery spares shall be charged to the revenue as and when consumed. When such spares can be used only in connection with an item of tangible fixed asset and their use is expected to be irregular, they shall be capitalised. Where the spares are capitalised as per the above requirement, the issue as to provision of depreciation arises – whether depreciation can be provided where such spares are kept ready for use or is it necessary that they are actually put to use. This issue was dealt with by the Delhi High Court in *CIT v. Insilco Ltd (2010) 320 ITR 322*. The Court observed that the expression "used for the purposes of business" appearing in section 33 of the Income-tax Act, 2025[19] also takes into account emergency spares, which, even though ready for use, yet are not consumed or used during the relevant period. This is because these spares are specific to a fixed asset, namely plant and machinery, and form an integral part of the fixed asset. These spares will, in all probability, be useless once the asset is discarded and will also have to be disposed of. In this sense, the concept of passive use which applies to standby machinery will also apply to emergency spares. Therefore, once the spares are considered as emergency spares required for plant and machinery, the assessee would be entitled to capitalize the entire cost of such spares and claim depreciation thereon.

***Note** – One of the conditions for claim of depreciation is that the asset must be "used for the purpose of business or profession". In the past, courts have held that, in certain circumstances, an asset can be said to be in use even when it is "kept ready for use". For example, depreciation can be claimed by a transport company on spare engines kept in store in case of need, though they have not actually been used by the company.*

[19] section 32 of Income-tax Act 1961

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Hence, in such cases, the term "use" embraces both active use and passive use for business purposes.

8. The payment made for acquiring the licence to operate telecom services in Mumbai shall be subject to deduction as per the scheme in section 52. As per section 52, any amount actually paid for acquiring any right to operate licence to operate telecommunication services shall be allowed as deduction in equal instalments during the number of years for which the license is in force.

If the payment is made before the commencement of business: The deduction shall be allowed beginning with the year of commencement of business.

In any other case: It will be allowed commencing from the year of payment. Deduction shall be allowed up to the year in which the license shall cease to be in force.

The amount of deduction available for T.Y. 2026-27 is worked out below:-

(1)	(2)	(3)	(4) = (3)/(2)
Tax year of payment	**Unexpired period of license**	**Instalment paid (₹)**	**Deduction in respect of each instalment (₹)**
2024-25	9 years	9,00,000	1,00,000
2025-26	9 years	9,00,000	1,00,000
2026-27	8 years	9,00,000	1,12,500
		27,00,000	**3,12,500**

The deduction under section 52 from Tax year 2026-27 shall be ₹ 3,12,500.

9. Computation of taxable income of Alpha Ltd. for the T.Y.2026-27

Particulars	₹
Net profit as per profit and loss account	12,50,000
***Add:* Items debited to profit and loss A/c but not deductible or income to be taxed**	
1. **Payment of advertisement expenditure of ₹ 60,000**	
(i) ₹ 8,000, being the excess payment to a relative disallowed under section 36(2)	8,000

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	(ii) As the payment is made in cash and since the remaining amount of ₹ 52,000 exceeds ₹ 10,000, 100% shall be disallowed under section 36(4).	52,000
2.	Under section 28, expenditure relatable to current repairs regarding plant, machinery or furniture is allowed as deduction. The test to determine whether replacement of parts of machinery amounts to repair or renewal is whether the replacement is one which is in substance replacement of defective parts or replacement of the entire machinery or substantial part of the entire machinery [*CIT v. Darbhanga Sugar Co. Ltd. [1956] 29 ITR 21 (Pat)]*. Here expenditure on repairs does not bring in any new asset into existence. Such replacement can only be considered as current repairs. Hence, no adjustment is required. Further, as per ICDS V on Tangible Fixed Assets, only an expenditure that increases the future benefits from the existing asset beyond its previously assessed standard of performance has to be added to the actual cost.	
3.	Liability foregone by creditor chargeable as business income but not credited to profit and loss account [Taxable under section 38(1)(a)]	6,000
4.	Sale proceeds of import entitlements. The sale of the rights gives rise to profits or gains taxable under section 26(2)(e). As the amount has already been credited to profit and loss account, no further adjustment is necessary.	-
5.	Expenditure on in-house research and development is entitled to a weighted deduction of 100% of the expenditure (both capital and revenue) so incurred under section 45(2)(i). As the amount has already been debited to profit and loss account, no further adjustment is necessary	-
Taxable Income		**13,16,000**

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10. (i) The decision of the Supreme Court in *Mysore Minerals Ltd v. CIT (1999) 239 ITR 775* is relevant in the context of the facts stated. The term "asset used" in section 33 must be assigned a wider meaning and anyone in possession of property in his own title, exercising dominion over the property, to the exclusion of others and having the right to use and enjoy it, must be taken to be the owner.

Registration of the buses is only a formality to perfect the title and does not bar enjoyment. The Corporation cannot, therefore, be denied depreciation on the buses. A similar decision was also taken in *CIT v. J & K Tourism Development Corporation (2001) 248 ITR 94 (J&K)*.

(ii) The deduction of bad debt is allowed if it is written off in the books of account of the assessee. In this case, Ravi has succeeded to the business carried on by his father. Under section 31(2) the amount has been written off in the books of account as irrecoverable is eligible for deduction provided the debt has been taken into account in computing the income of the business in an earlier tax year.

Therefore, Ravi is eligible for deduction in respect of the amount due in the name of Y which is written off in the books of account as bad debt, even though the debt represents the amount due for the supplies made by previous owner viz. deceased father of Ravi [*CIT v. T. Veerabhadra Rao, K. Koteswara Rao and Co (1985) 155 ITR 152 (SC)]*.

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[i] *registered under section 12 of the SEBI Act, 1992 in accordance with the provisions of the Securities Contracts (Regulation) Act, 1956 or the SEBI Act, 1992 or the Depositories Act, 1996 and the rules, regulations or bye-laws made or directions issued under those Acts*

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