*[ This question paper contains 6 printed pages. The model answers follow. ]*

**Your Roll No.** . . . . . . . . . . . . . . . .

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|---|---|
| Name of the Paper | PERSONAL TAX PLANNING AND TAX MANAGEMENT |
| Name of the Course | B.Com. (H) UGCF |
| Type of the Paper | DSE |
| Semester | VII |
| Governing law | Income-tax Act, 2025, as amended by the Finance Act, 2026, read with the Income-tax Rules, 2026 |
| Tax Year | 2026-27 (1 April 2026 to 31 March 2027) |

**Duration : 3 Hours** **Maximum Marks : 90**

## Instructions for Candidates

1. Write your Roll No. on the top immediately on receipt of this question paper.
2. Attempt all the questions. All questions carry equal marks.
3. All parts of a question are to be attempted together.
4. The use of a simple calculator is allowed.
5. Answers may be written in English or Hindi, but the same medium should be used consistently throughout the paper.

## Question 1

**(a)** Explain the scope of tax planning by reference to the period over which it operates, distinguishing short-range from long-range planning with an example of each. Set out the principal areas of personal tax planning open to a resident individual, and state three limits beyond which planning must not go. **(9)**

**(b)** Shri Ashok, a citizen of India, had lived and worked in Dubai for twelve years. He returned to India permanently on 1 July 2026 and remained here for the rest of the year. Determine his residential status for Tax Year 2026-27, and state whether the following are chargeable in his hands — (i) rent of ₹6,00,000 from a flat at Dubai, received and retained there; (ii) profit of ₹4,00,000 from a business at Sharjah controlled wholly from Delhi; and (iii) ₹8,00,000 of past savings remitted from Dubai to his Indian bank account in August 2026. **(9)**

**O R**

**(a)** Explain tax planning through exempted income. Deal with the architecture of section 11 read with Schedule II, distinguish an exemption from a deduction and from a rebate, and set out four exempt receipts a resident salaried individual should plan for, stating in each case whether it survives the default regime. **(9)**

**(b)** Shri Rakesh has two minor children. Aarav, aged 12, earned ₹60,000 as interest on a fixed deposit made in his name out of a gift from his grandfather. Ira, aged 15, suffers from a disability of the nature specified in section 154; she earned ₹40,000 by selling her paintings at an exhibition and ₹25,000 as interest on a bank deposit. The total income of Shri Rakesh is greater than that of his wife. Determine the amount to be clubbed under section 99(1)(c) under each regime, with reasons. **(9)**

## Question 2

Shri Manish, aged 38, resident, is employed at Mumbai. His emoluments and outgoings for Tax Year 2026-27 are as follows.

| Particulars | Amount (₹) |
|---|---|
| Basic salary | 80,000 a month |
| Dearness allowance (the whole forming part of retirement benefits) | 20,000 a month |
| House rent allowance (rent actually paid at Mumbai ₹45,000 a month) | 40,000 a month |
| Children education allowance (two children) | 8,000 a month |
| Transport allowance (he is not a disabled employee) | 3,000 a month |
| Leave travel concession (₹90,000 spent on air fare, one journey, December 2026) | 1,00,000 |
| Employer's contribution to the notified pension scheme (14% of basic and dearness allowance) | 1,68,000 |
| Professional tax paid by him | 2,500 |
| His own contribution to the recognised provident fund | 1,20,000 |
| Health insurance premium — ₹25,000 self and family, ₹10,000 father aged 70 | 35,000 |
| Housing loan on his self-occupied house — principal repaid | 80,000 |
| Housing loan on his self-occupied house — interest paid | 2,60,000 |

**(a)** Compute his total income and tax liability under the default regime and under the optional regime, and advise him which to adopt. **(9)**

**(b)** State the three classes into which allowances fall, with two examples of each, and explain why a reimbursement against bills is a better instrument than an allowance for an employee who will be taxed under section 202(1). **(9)**

**O R**

**(a)** Shri Vikram has been offered a package costing his employer ₹18,00,000 a year. The employer is willing to pay the whole of it as basic salary, or to structure it as the employee wishes. Shri Vikram will pay rent of ₹25,000 a month at Pune, has two school-going children, will contribute ₹1,50,000 to the public provident fund and will pay ₹25,000 as health insurance premium. Design a structure that minimises his tax under the optional regime, compute the tax under the wholly-basic package and under your structure, and state the saving. **(9)**

**(b)** Distinguish an allowance, a perquisite and a reimbursement. State which of the three the default regime leaves untouched, and why that fact governs the design of every pay package from 1 April 2026. **(9)**

## Question 3

**(a)** Modern Traders, a firm, owns a single block of plant and machinery carrying depreciation at 15 per cent, the written down value of which on 1 April 2026 was ₹20,00,000. On 20 November 2026 it purchased and put to use new machinery costing ₹10,00,000. In February 2027 it sold an item out of the block for ₹3,00,000. Its profit for the year, before depreciation and after debiting ₹90,000 paid in cash on a single day to a single supplier against a single bill, is ₹14,00,000. Compute the depreciation allowable and the profits and gains of the business, giving reasons for each adjustment. **(9)**

**(b)** Smt. Uma, aged 63, resident, the widow of a Government servant, received during Tax Year 2026-27 — family pension ₹4,80,000; winnings from a television game show ₹2,00,000 gross, from which ₹60,000 was deducted at source; dividend ₹80,000 from an Indian company, for realising which she paid ₹5,000 to a collection agent; interest on a savings bank account ₹18,000; and interest on bank fixed deposits ₹62,000. She has no other income and is taxed under the default regime. Compute her income under the head "Income from other sources", her tax liability and the balance payable or refundable. **(9)**

**O R**

**(a)** Shri Pranav, aged 50, resident, sold on 15 October 2026 a plot of land purchased in May 2011 for ₹10,00,000, the indexed cost of which is ₹22,00,000, for ₹40,00,000. In December 2026 he sold, for ₹9,50,000, listed equity shares bought in August 2025 for ₹6,00,000, securities transaction tax having been paid on both legs. His income from other sources is ₹4,50,000. He makes no reinvestment and is taxed under the default regime. Compute his total income and tax liability, showing the working of the option in section 197(3). **(9)**

**(b)** Shri and Smt. Bakshi own a house at Jaipur in equal and definite shares, let out at ₹40,000 a month. Its municipal value is ₹4,20,000, its fair rent ₹5,00,000 and its standard rent ₹4,80,000. Municipal taxes of ₹48,000 were paid during the year, ₹30,000 by the owners and ₹18,000 by the tenant. The tenant paid no rent for February and March 2027 and the conditions for treating it as unrealised rent are satisfied. During the year the owners also recovered ₹60,000 of unrealised rent of an earlier year in respect of another house since sold. Interest on the housing loan for the Jaipur house was ₹3,60,000. Compute the income of each co-owner under the head "Income from house property". **(9)**

## Question 4

**(a)** Explain the three points at which the law touches an investment, and use them to compare the public provident fund, the equity linked savings scheme and a five-year bank fixed deposit. State the lock-in of each, the deduction available, the treatment of the accretion and the charge on withdrawal, and identify which of the three a taxpayer in the default regime should still hold, and why. **(9)**

**(b)** Shri Harish, aged 66, resident, has ₹1,50,000 to place for five years. He may put it either in a five-year bank fixed deposit bearing interest at 7.5 per cent a year, paid annually, or in the public provident fund bearing 7.1 per cent. His total income before this investment is ₹9,00,000 and he has no other interest income. Compute the post-tax return of each in the first year under the optional regime and under the default regime, and advise him. **(9)**

**O R**

**(a)** Discuss the Hindu undivided family as a vehicle of investment. State what income belongs to the family and what does not, the exemptions and deductions the family may and may not claim, the bar imposed by the clubbing provisions, and three cautions a planner must observe. **(9)**

**(b)** Shri Nitin, aged 44, resident, drew a gross salary of ₹16,00,000 for Tax Year 2026-27. He contributed ₹1,50,000 to the public provident fund and ₹60,000 of his own to the notified pension scheme, paid ₹1,10,000 as interest on a loan taken for his daughter's higher education (the seventh year of the loan) and ₹30,000 as health insurance premium, being ₹20,000 for himself and ₹10,000 for his mother aged 72. Compute his total income and tax liability under both regimes and advise him. **(9)**

## Question 5

**5.** Write a short note on any THREE of the following: **(6 × 3 = 18)**

- **(i)** Best judgment assessment under section 271
- **(ii)** Tax collection at source
- **(iii)** Revision under section 377 and revision under section 378
- **(iv)** The permanent account number, and the tax credit statement in Form 168
- **(v)** Appeal to the Commissioner (Appeals)

E N D O F T H E Q U E S T I O N P A P E R

MODEL ANSWERS

# Personal Tax Planning and Tax Management

Mock Paper II · DSE 7.9 · B.Com. (Hons.) and B.Com. (Prog.), Semester VII · Tax Year 2026-27

| Particulars | Details |
|---|---|
| Question paper | M O C K – II |
| Governing law | Income-tax Act, 2025 (Act No. 30 of 2025), as amended by the Finance Act, 2026 |
| Rules | Income-tax Rules, 2026 |
| Tax Year | 2026-27 (1 April 2026 to 31 March 2027) |
| Maximum marks | 90 — Questions 1 to 4 in two parts of 9 marks each with an internal choice; Question 5, a short note on any three of five items at 6 marks each |
| Compiled by | Advocate Dr. S. B. Rathore |

### How to use these answers

Work the paper first, with a pen and a clock, in three hours. Only then open this booklet. An answer you have read is not an answer you can write.

Every alternative is answered here, so that the booklet may be used whichever half of each question you attempted. In the examination you must attempt one only.

The computations are set out in the statutory order — head by head, then gross total income, then Chapter VIII, then tax. Marks are given for that order even where a figure goes wrong, and are lost where the order is abandoned even though the figures are right.

Every figure is followed by its authority in square brackets. Reproduce the section number: it is the single cheapest mark in this paper.

The note at the end of each answer records the errors that recur in scripts. Read them; they are worth more than the answers.

ANSWER

# Question 1 — Unit 1 : Basic Concepts

## 1 (a) The scope of tax planning by reference to the period

*Nine marks. Short-range and long-range with an example each — three; the areas of personal tax planning — four; the limits — two.*

Tax planning may be classified by the period over which it operates. The distinction is not academic: it decides whether a measure can be taken after the year has begun, and whether it can be reversed.

| | Short-range planning | Long-range planning |
|---|---|---|
| Meaning | Planning undertaken within a tax year, generally towards its close, to reduce the tax of that year alone | Planning laid down at the beginning and carried through several years, without an immediate benefit in the first of them |
| Example | Selling a listed share on 2 April instead of 30 March, so that the gain falls into the next tax year and a fresh ₹1,25,000 threshold under section 198 becomes available; or investing ₹1,50,000 in the public provident fund in the last week of March | Buying a house in the joint names of husband and wife, each of whom has independent income, so that the interest, the annual value and the eventual capital gain are split for as long as the house is held |
| Reversibility | Usually reversible, and often repeated year by year | Rarely reversible. The option under section 202(4), once withdrawn by a business assessee, cannot be exercised again while the business subsists |
| Risk | Low. The law of the year is known | Higher. The law may change; a long-range plan must be tested against the possibility that the relief on which it rests is withdrawn |

### The areas of personal tax planning

| Area | The instruments | Where it is dealt with |
|---|---|---|
| The regime | Section 202 — the choice between the default and the optional regime | Unit 1 and every later Unit |
| Residential status | Sections 5 and 6 — the count of days, the relaxations, the not-ordinarily-resident category | Unit 1 |
| Exempted income | Section 11 with Schedule II, and Schedule III for the salary head | Unit 1 |
| Permissible deductions | Chapter VIII — sections 123 to 154 | Units 1 and 3 |
| Clubbing | Sections 96 to 100 and section 25(a) — planning around them, not through them | Unit 1 |
| The five heads | Salary structure, self-occupied or let out, depreciation and presumptive taxation, the period of holding and the section 82 to 86 exemptions, the character of a receipt under section 92 | Unit 2 |
| Investments | The avenue, the pattern of taxation and the post-tax yield | Unit 3 |
| Tax management | Advance tax, deduction at source, the return, the assessment | Unit 4 |

### Three limits beyond which planning must not go

**One.** The limit of legality. The means must be lawful and the disclosure complete. The moment a receipt is suppressed or an expense invented, the exercise ceases to be planning and becomes evasion.

**Two.** The limit of legislative purpose. Sections 178 to 184 permit an arrangement whose main purpose is a tax benefit to be declared impermissible if it lacks commercial substance or abuses the Act. A benefit Parliament did not intend to confer is not safe merely because the words of the section can be made to cover it.

**Three.** The limit of commercial sense. A plan that saves ₹50,000 of tax and locks ₹5,00,000 for fifteen years at a poor rate has cost more than it saved. Tax is one cost among several, and the planner who forgets it is the largest of them makes the commonest professional mistake.

## 1 (b) Residential status of Shri Ashok

*Nine marks. The count and the status — three; the not-ordinarily-resident test — two; the three receipts — four.*

### Step 1 — the count of days

| Period | Days |
|---|---|
| July, August, October, December 2026 and January, March 2027 (31 days each) | 186 |
| September and November 2026 (30 days each) | 60 |
| February 2027 | 28 |
| **Total stay in India, 1 July 2026 to 31 March 2027** | **274** |

The stay of 274 days exceeds 182 days, so the first basic condition in section 6(2) is satisfied and Shri Ashok is RESIDENT for Tax Year 2026-27. No relaxation under section 6(3) is in issue: he did not leave India during the year, and he is not a visiting non-resident.

### Step 2 — ordinarily resident or not? [section 6(13)]

A resident is “not ordinarily resident” if, among other tests, he has been a non-resident in nine out of the ten tax years preceding the tax year, or has been in India for 729 days or less in the seven preceding years. Shri Ashok lived and worked in Dubai for twelve years, so he was a non-resident in each of the ten preceding years — far more than the nine the test requires.

**Conclusion**

Shri Ashok is RESIDENT BUT NOT ORDINARILY RESIDENT for Tax Year 2026-27.

The status matters because it is the only status in which foreign income is partly taxed and partly not, and the line is drawn by the source, not by the receipt.

### Step 3 — the three receipts [section 5]

| Receipt | Analysis | Chargeable? |
|---|---|---|
| (i) Rent ₹6,00,000 from a flat at Dubai, received and retained there | Accrues outside India and is received outside India, from a source that is neither a business controlled from India nor a profession set up in India | NO |
| (ii) Profit ₹4,00,000 from a business at Sharjah controlled wholly from Delhi | Accrues outside India, but from a BUSINESS CONTROLLED FROM INDIA. This is the single exception that distinguishes a not-ordinarily-resident from a non-resident | YES |
| (iii) ₹8,00,000 of past savings remitted from Dubai in August 2026 | A remittance is not income. It is the movement of a sum that was income of an earlier year, and it is chargeable in no year on that account | NO |

**Examiner's note — where marks are lost**

Treating him as non-resident because he was abroad for twelve years. The count is made for the tax year in question, and he was here 274 days of it.

Taxing the Dubai rent. A not-ordinarily-resident is not taxed on foreign income except from a business controlled from India or a profession set up in India.

Taxing the remittance. Remittance of past savings is the classic examination trap; the sum was income of another year and is not income of this one.

Omitting the second limb of section 6(13). The status is decided in two steps — resident or not, then ordinarily or not — and both carry marks.

## 1 (a) OR Tax planning through exempted income

*Nine marks. The architecture of section 11 — two; exemption, deduction and rebate distinguished — three; four exempt receipts with the regime position — four.*

Section 11 provides that in computing the total income of a person, any income falling within Schedule II shall not be included. The exemption operates at the very threshold of the computation: the receipt never becomes part of total income at all, and no question of a deduction from it arises. For the salary head, Schedule III performs the same office in respect of allowances and perquisites.

| | Exemption | Deduction | Rebate |
|---|---|---|---|
| Where it operates | On the receipt, before total income is arrived at | On the income, after gross total income is arrived at | On the tax, after it has been computed |
| Authority | Section 11 with Schedule II; Schedule III for salary | Chapter VIII — sections 123 to 154; and sections 19 and 22 within the heads | Section 156 |
| Can it create a loss? | The question does not arise; the receipt never enters | No — section 122(2) bars a Chapter VIII deduction from exceeding gross total income | No; the rebate cannot exceed the tax |
| Example | Agricultural income | Public provident fund contribution — section 123 | ₹60,000 in the default regime where total income does not exceed ₹12,00,000 |

### Four exempt receipts a resident salaried individual should plan for

| Receipt | Authority | Survives the default regime? |
|---|---|---|
| Agricultural income | Section 2(5) with Schedule II, Table Sl. No. 1 | YES — but it is drawn back for rate purposes by partial integration where it exceeds ₹5,000 and the non-agricultural income exceeds ₹4,00,000 |
| Share of profit from a firm in which he is a partner | Schedule III, Sl. No. 1 | YES — the exemption is unaffected by section 202(2) |
| House rent allowance, and the leave travel concession | Schedule III, Sl. Nos. 11 and 8, with Rules 279 and 277 | NO — both are withdrawn by section 202(2)(a). Together they are usually the largest exemption in a salary package, and their withdrawal is the chief reason the two regimes diverge |
| Interest on, and the maturity of, the public provident fund | Schedule II | YES — only the deduction on contribution under section 123 is lost; the accretion and the maturity remain exempt |

The planning lesson is that the value of an exemption is not the same in the two regimes, and that the exemptions which survive — agricultural income, the share of profit, the provident fund accretion, gratuity and commuted pension under section 19 — are precisely the ones a planner should build upon from 1 April 2026.

## 1 (b) OR The minor children of Shri Rakesh

*Nine marks. The rule, the three exclusions and the parent — three; Aarav — three; Ira — three.*

Section 99(1)(c) includes the income of a minor child in the total income of the parent whose total income, before including that income, is the greater. Here that is Shri Rakesh. Three categories are excluded from the clubbing —

- income accruing on account of work done by the child;
- income from activities in which his skill, talent, specialised knowledge or experience is applied; and
- the income of a minor child suffering from a disability of the nature specified in section 154.

| Child and income | Analysis | Optional (₹) | Default (₹) |
|---|---|---|---|
| Aarav, 12 — interest ₹60,000 on a fixed deposit made out of his grandfather's gift | None of the three exclusions applies. The whole is clubbed with Shri Rakesh, less the exemption of ₹1,500 per child in Schedule III, Sl. No. 17 — which, being in Schedule III, does not survive section 202(2)(a) | 58,500 | 60,000 |
| Ira, 15 — ₹40,000 from selling her own paintings | Income from the application of her own skill and talent. Excluded on that ground alone, in either regime | NIL | NIL |
| Ira, 15 — ₹25,000 of bank interest | Not income from her skill; but she suffers from a disability of the nature specified in section 154, and the THIRD exclusion takes the whole of her income out of the clubbing | NIL | NIL |

| Child and income | Analysis | Optional (₹) | Default (₹) |
|---|---|---|---|
| **AMOUNT CLUBBED WITH SHRI RAKESH** | | **58,500** | **60,000** |

Ira's ₹65,000 is assessed in her own hands. A minor is an assessee in his own right wherever the clubbing provision does not reach; the return is furnished by the guardian on the child's behalf.

**Examiner's note — where marks are lost**

Clubbing Ira's interest. The disability exclusion is not confined to income from her own effort — it takes out the whole of the minor's income.

Giving the ₹1,500 exemption in the default regime. It sits in Schedule III and goes with the rest of Schedule III.

Giving ₹1,500 for each of the two children when only one child's income is clubbed. The exemption attaches to the income included, not to the number of children.

Clubbing with the mother. The section says the parent with the greater total income, and the question tells you which that is.

ANSWER

# Question 2 — Unit 2 : Income from Salaries

## 2 (a) Shri Manish — the two regimes compared

*Nine marks. The allowance workings — three; the two computations — four; the advice — two.*

### Working note 1 — house rent allowance [Schedule III, Sl. No. 11, with Rule 279]

Salary for this purpose is basic salary plus that part of the dearness allowance which forms part of retirement benefits — here the whole of it. Salary = (₹80,000 + ₹20,000) × 12 = ₹12,00,000. Rent paid = ₹45,000 × 12 = ₹5,40,000. Mumbai is one of the eight cities, so the third limb is 50 per cent.

| Limb | Amount (₹) |
|---|---|
| (a) Allowance received (₹40,000 × 12) | 4,80,000 |
| (b) Rent paid less 10% of salary (5,40,000 – 1,20,000) | 4,20,000 |
| (c) 50% of salary (Mumbai) | 6,00,000 |
| Exempt — the least of the three | 4,20,000 |
| **Taxable house rent allowance** | **60,000** |

### Working note 2 — the other allowances

- Children education allowance ₹96,000 received (₹8,000 × 12). Exempt ₹3,000 per month per child for two children = ₹72,000 [Rule 280(2), Sl. No. 7]. Taxable ₹24,000 in the optional regime; the whole ₹96,000 in the default regime.
- Transport allowance ₹36,000. The exemption in Rule 280(2), Sl. No. 10 is confined to a DISABLED employee. Shri Manish is not one, so the whole is taxable in both regimes.
- Leave travel concession ₹1,00,000, of which ₹90,000 was spent on air fare for one journey. Exempt to the extent spent, so ₹10,000 is taxable in the optional regime; the whole ₹1,00,000 in the default regime.
- Employer's pension contribution ₹1,68,000 is included in gross salary. The deduction is 10 per cent of salary — ₹1,20,000 — in the optional regime [section 124(1)], the employer not being Government; and 14 per cent — ₹1,68,000, the whole — in the default regime [section 124(2)].
- Professional tax ₹2,500 is deductible under section 19(1), Table Sl. No. 1 in the optional regime only.
- The self-occupied house: annual value nil; interest ₹2,60,000 restricted to ₹2,00,000 by section 22(2)(a), giving a loss of ₹2,00,000, which section 109(1)(b) permits to be set off in full against other heads — in the optional regime only. In the default regime section 202(2)(a)(v) allows nothing at all.

### Computation of total income and tax

| Particulars | Optional (₹) | Default (₹) |
|---|---|---|
| Basic salary (₹80,000 × 12) | 9,60,000 | 9,60,000 |
| Dearness allowance (₹20,000 × 12) | 2,40,000 | 2,40,000 |
| House rent allowance — taxable | 60,000 | 4,80,000 |
| Children education allowance — taxable | 24,000 | 96,000 |
| Transport allowance | 36,000 | 36,000 |
| Leave travel concession — taxable | 10,000 | 1,00,000 |
| Employer's contribution to the notified pension scheme | 1,68,000 | 1,68,000 |
| GROSS SALARY | 14,98,000 | 20,80,000 |
| Less: s. 19(1) Sl. No. 1 — professional tax | 2,500 | Nil |
| Less: s. 19(1) Sl. No. 2 — standard deduction | 50,000 | 75,000 |
| INCOME FROM SALARIES | 14,45,500 | 20,05,000 |
| Income from house property — self-occupied | (2,00,000) | Nil |
| GROSS TOTAL INCOME | 12,45,500 | 20,05,000 |

| Particulars | Optional (₹) | Default (₹) |
|---|---|---|
| Less: s. 123 — provident fund ₹1,20,000 + housing loan principal ₹80,000, capped | 1,50,000 | Nil |
| Less: s. 124(1) / 124(2) — employer's contribution | 1,20,000 | 1,68,000 |
| Less: s. 126 — health insurance (25,000 + 10,000) | 35,000 | Nil |
| TOTAL INCOME | 9,40,500 | 18,37,000 |
| Tax before cess | 1,00,600 | 1,67,400 |
| Add: cess at 4% | 4,024 | 6,696 |
| **TAX PAYABLE (rounded, s. 516)** | **1,04,620** | **1,74,100** |

- Tax, optional: ₹12,500 on the slab to ₹5,00,000 + 20% of ₹4,40,500 (₹88,100) = ₹1,00,600.
- Tax, default: 5% of ₹4,00,000 + 10% of ₹4,00,000 + 15% of ₹4,00,000 + 20% of ₹2,37,000 = ₹20,000 + ₹40,000 + ₹60,000 + ₹47,400 = ₹1,67,400.

**Advice**

Shri Manish should EXERCISE THE OPTION under section 202(4) and be taxed under the optional regime. His tax is then ₹1,04,620 against ₹1,74,100 — a saving of ₹69,480.

The reason is the size of what he loses in the default regime: house rent allowance ₹4,20,000, the interest on his self-occupied house ₹2,00,000, section 123 ₹1,50,000, section 126 ₹35,000, the children education allowance ₹72,000 and the leave travel concession ₹90,000 — some ₹9,67,000 of relief, against which the wider slabs, the extra ₹25,000 of standard deduction and the extra ₹48,000 of pension deduction are no answer.

Compare this with Smt. Anjali in Mock Paper I, where the default regime won. The lesson is that neither regime is better in the abstract. The test is arithmetical, and it must be worked every year.

## 2 (b) The three classes of allowance

| Class | Treatment | Examples |
|---|---|---|
| Fully taxable | The whole amount enters gross salary | Dearness allowance; city compensatory allowance; overtime allowance; servant allowance; non-practising allowance |
| Partly exempt | Exempt up to a limit, or up to the amount actually spent; the balance is taxable | House rent allowance [Sch. III, Sl. No. 11, Rule 279]; children education and hostel expenditure allowances [Rule 280(2)] |
| Fully exempt | Not included in gross salary at all | Allowances paid by the Government to a citizen of India for services rendered outside India; the allowances of a High Court or Supreme Court Judge |

Why a reimbursement is the better instrument in the default regime. An allowance is a fixed monetary payment made whether or not the employee spends it; it is chargeable in full unless Schedule III exempts it, and section 202(2)(a) withdraws almost the whole of Schedule III. A reimbursement, by contrast, is the repayment of expenditure the employee has actually incurred for the employer's purposes and on the employer's behalf. It is not a gain to him at all, and so is outside the charge — in either regime. Section 202(2) has nothing to withdraw, because no exemption was ever needed.

*The practical rule: from 1 April 2026, wherever a package can pay for a thing instead of paying an allowance towards it — the telephone bill, the fuel bill, the subscription, the books — it should. The cost to the employer is identical and the employee keeps the whole of it.*

## 2 (a) OR Shri Vikram — designing the package

*Nine marks. The structure proposed — three; the two computations — four; the saving and the reasoning — two.*

### The wholly-basic package

| Particulars | Amount (₹) |
|---|---|
| Gross salary — the whole ₹18,00,000 paid as basic salary | 18,00,000 |
| Less: standard deduction | 50,000 |

| Particulars | Amount (₹) |
|---|---|
| | |
| GROSS TOTAL INCOME | 17,50,000 |
| Less: s. 123 — public provident fund | 1,50,000 |
| Less: s. 126 — health insurance | 25,000 |
| TOTAL INCOME | 15,75,000 |
| Tax — ₹12,500 + 20% of ₹5,00,000 + 30% of ₹5,75,000 | 2,85,000 |
| Add: cess at 4% | 11,400 |
| **TAX PAYABLE** | **2,96,400** |

### The structure proposed

The design rests on three principles — pay for a thing rather than pay an allowance towards it; keep the basic salary high enough to carry the house rent allowance and the pension contribution, which are both percentages of it; and use every allowance that is exempt to the extent spent.

| Component | Amount (₹) | Why |
|---|---|---|
| Basic salary | 9,00,000 | Half the package — enough to carry a 50% house rent allowance and a 10% pension contribution |
| House rent allowance | 4,50,000 | 50% of basic; Pune is one of the eight cities |
| Children education allowance (two children) | 72,000 | ₹3,000 per month per child — exempt in full |
| Leave travel concession | 60,000 | Exempt to the extent spent on fare, one journey in the block 2026-2029 |
| Telephone and internet reimbursed against bills | 48,000 | A reimbursement, not an allowance — outside the charge altogether |
| Employer's contribution to the notified pension scheme | 90,000 | 10% of basic salary — the ceiling in section 124(1) |
| Special allowance — the balance | 1,80,000 | Fully taxable; keep it as small as possible |
| **COST TO THE EMPLOYER** | **18,00,000** | **Identical to the wholly-basic package** |

### The computation on the structure proposed

House rent allowance exempt — the least of ₹4,50,000 received; ₹3,00,000 rent less ₹90,000 (10% of ₹9,00,000) = ₹2,10,000; and 50% of ₹9,00,000 = ₹4,50,000. Exempt ₹2,10,000; taxable ₹2,40,000.

| Particulars | Amount (₹) |
|---|---|
| Basic salary | 9,00,000 |
| House rent allowance — taxable | 2,40,000 |
| Children education allowance — wholly exempt | Nil |
| Leave travel concession — wholly exempt | Nil |
| Telephone and internet reimbursement — not chargeable | Nil |
| Employer's contribution to the notified pension scheme | 90,000 |
| Special allowance | 1,80,000 |
| GROSS SALARY | 14,10,000 |
| Less: standard deduction | 50,000 |
| GROSS TOTAL INCOME | 13,60,000 |

| Particulars | Amount (₹) |
|---|---|
| Less: s. 124(1) — 10% of ₹9,00,000 | 90,000 |
| Less: s. 123 — public provident fund | 1,50,000 |
| Less: s. 126 — health insurance | 25,000 |
| TOTAL INCOME | 10,95,000 |
| Tax — ₹12,500 + 20% of ₹5,00,000 + 30% of ₹95,000 | 1,41,000 |
| Add: cess at 4% | 5,640 |
| **TAX PAYABLE** | **1,46,640** |

**The saving**

₹2,96,400 − ₹1,46,640 = ₹1,49,760, at no extra cost whatever to the employer.

Every rupee of it comes from the composition of the package, not from its size. That is the whole of salary planning, and it is why an employer who allows an employee to structure his own package gives him something worth having.

Note that this design works only in the OPTIONAL regime. Shri Vikram must exercise the option under section 202(4). In the default regime ₹3,42,000 of the exemptions would vanish and only the reimbursement and the pension contribution would survive.

## 2 (b) OR Allowance, perquisite and reimbursement

| | Allowance | Perquisite | Reimbursement |
|---|---|---|---|
| What it is | A fixed sum of money paid periodically, whether or not the employee spends it | A benefit or amenity provided in kind, or a facility placed at the employee's disposal | Repayment of expenditure actually incurred by the employee for the employer's purposes, against evidence |
| Charged under | Section 16, as part of salary | Section 17, valued under the Rules | Not charged at all — it is a recoupment, not a gain |
| Relief available | Only if Schedule III exempts it | Only if the Rules value it at nil — free education up to ₹3,000 per month per child, meals up to ₹200 per meal, the employer's own hospital | None is needed |
| Position under the default regime | Schedule III is withdrawn, so the allowance is taxable in full | UNTOUCHED. Section 202(2)(a) does not withdraw the perquisite valuation rules | UNTOUCHED. There was never an exemption to withdraw |

The default regime therefore leaves two of the three instruments intact, and that single fact governs the design of every pay package from 1 April 2026. The allowance, which was the mainstay of Indian salary planning for forty years, is now the weakest component in the package; the facility and the reimbursement are the strongest. An employer who converts ₹3,00,000 of allowances into ₹3,00,000 of facilities and reimbursements has given an employee in the 30 per cent bracket about ₹93,600 a year and has spent nothing.

ANSWER

# Question 3 — Unit 2 : Business, Other Sources and Capital Gains

## 3 (a) Modern Traders — depreciation and business income

*Nine marks. The block and the half-year rule — four; the cash disallowance — three; the final computation — two.*

### Working note 1 — the block of assets [section 33]

Depreciation is allowed on the written down value of the BLOCK, not asset by asset. Section 33 allows half the normal rate where an asset is acquired and put to use in the tax year for less than 180 days. The machinery was put to use on 20 November 2026; from that date to 31 March 2027 is 132 days, which is less than 180. The half-year rule therefore applies to the addition, and to the addition only.

| Particulars | Amount (₹) |
|---|---|
| Written down value of the block on 1 April 2026 | 20,00,000 |
| Less: moneys payable on the item sold in February 2027 | 3,00,000 |
| Balance carrying the full rate | 17,00,000 |
| Depreciation at 15% | 2,55,000 |
| Add: new machinery put to use on 20 November 2026 — ₹10,00,000 at half of 15%, that is 7.5% | 75,000 |
| TOTAL DEPRECIATION ALLOWABLE | 3,30,000 |
| **Written down value carried forward (20,00,000 + 10,00,000 – 3,00,000 – 3,30,000)** | **23,70,000** |

No capital gain arises on the sale. Where an item is sold out of a block that survives the sale, and the moneys payable do not exceed the written down value plus the additions, the proceeds are simply deducted from the block; the profit or loss is absorbed in the depreciation of this and later years.

### Working note 2 — the cash payment [section 36]

A payment made otherwise than by an account payee cheque, an account payee bank draft or a prescribed electronic mode, exceeding ₹10,000 to a single person in a single day, is disallowed in full by section 36 — the counterpart of section 40A(3) of the 1961 Act. The payment of ₹90,000 was made in cash, on one day, to one supplier, against one bill. None of the prescribed exceptions is shown to apply. The whole ₹90,000 is disallowed and added back to the profit, and the fact that the expenditure was genuine and was incurred for the business is no answer.

### Computation of profits and gains of business or profession

| Particulars | Amount (₹) |
|---|---|
| Profit as computed, before depreciation and after debiting the cash payment | 14,00,000 |
| Add: cash payment disallowed [section 36] | 90,000 |
| Profit before depreciation | 14,90,000 |
| Less: depreciation under section 33 | 3,30,000 |
| **PROFITS AND GAINS OF BUSINESS OR PROFESSION** | **11,60,000** |

#### Examiner's note — where marks are lost

Applying the half rate to the whole block. It applies only to the asset acquired and put to use for less than 180 days.

Counting from the date of purchase instead of the date the asset was PUT TO USE. Section 33 speaks of use, and the examiner gives the two dates precisely to test it.

Computing a short-term capital gain on the sale. The block survives; there is none.

Disallowing only the excess of ₹90,000 over ₹10,000. The whole payment goes.

Deducting the depreciation before adding back the disallowance. The order does not change the answer here, but it does where a loss results, and marks are given for the order.

## 3 (b) Smt. Uma — income from other sources

*Nine marks. The family pension deduction — two; the five receipts — three; the tax with the rebate point — four.*

| Particulars | Working | Amount (₹) |
|---|---|---|
| Family pension | Received ₹4,80,000; deduction under section 93(1)(d) is the LOWER of one-third (₹1,60,000) and ₹25,000 — the figure being ₹25,000 in the default regime and ₹15,000 in the optional one | 4,55,000 |
| Winnings from a game show | Gross ₹2,00,000. Section 94(4) forbids any deduction whatever — not the entry fee, not an expense | 2,00,000 |
| Dividend | ₹80,000 less ₹5,000 paid to a collection agent, allowed by section 93(1)(a) | 75,000 |
| Savings bank interest | The deduction under section 153 is a Chapter VIII deduction and does not survive the default regime, so nothing is allowed even though she is a senior citizen | 18,000 |
| Fixed deposit interest | Chargeable in full, for the same reason | 62,000 |
| **INCOME FROM OTHER SOURCES, and TOTAL INCOME** | | **8,10,000** |

### Computation of tax

| Particulars | Amount (₹) |
|---|---|
| Tax on the winnings — 30% of ₹2,00,000 [section 194] | 60,000 |
| Tax on the balance ₹6,10,000 at the default slabs — 5% of (6,10,000 – 4,00,000) | 10,500 |
| Tax before rebate | 70,500 |
| Less: rebate under section 156(2) — see note | 10,500 |
| Tax after rebate | 60,000 |
| Add: cess at 4% | 2,400 |
| TAX AND CESS | 62,400 |
| Less: tax deducted at source on the winnings | 60,000 |
| **BALANCE PAYABLE** | **2,400** |

**The rebate point — this is where the question is won or lost**

Her total income of ₹8,10,000 does not exceed ₹12,00,000, and she is a resident individual taxed under the default regime, so section 156(2) would give her a rebate of up to ₹60,000.

But section 156(3) provides that no rebate shall be allowed against the tax on income charged at the special rates. The tax of ₹60,000 on the winnings is therefore beyond the reach of the rebate.

The rebate is available only against the ₹10,500 of slab tax, and is limited to that figure. A candidate who allows ₹60,000 of rebate arrives at a refund; a candidate who allows none arrives at ₹62,400 payable. Both are wrong, and the second is the commoner.

## 3 (a) OR Shri Pranav — capital gains and the option in section 197(3)

*Nine marks. The land and the two computations under section 197(3) — four; the shares under section 198 — three; the aggregate tax — two.*

## Working note 1 — the land

The plot was purchased in May 2011 and sold in October 2026, so it was held for far more than 24 months and the gain is long-term. Because it is land, it was acquired before 23 July 2024, and Shri Pranav is a resident individual, section 197(3) gives him the benefit of the LOWER of two computations. The choice is between rates and bases, and it must be worked both ways.

| | Without indexation | With indexation |
|---|---|---|
| Full value of consideration | 40,00,000 | 40,00,000 |
| Less: cost of acquisition | 10,00,000 | 22,00,000 (indexed) |
| Long-term capital gain | 30,00,000 | 18,00,000 |
| Rate | 12.5% | 20% |
| **TAX** | **3,75,000** | **3,60,000** |

The lower figure is ₹3,60,000, so the WITH-INDEXATION computation prevails and the tax on the land is ₹3,60,000. Note the shape of the test: indexation wins whenever the indexed cost is high enough relative to the consideration, and the break-even is reached where the indexed cost exceeds about 37.5 per cent of the consideration above the original cost. Here the indexed cost is more than twice the original cost, and indexation wins comfortably.

## Working note 2 — the listed shares

Bought August 2025, sold December 2026 — held for about sixteen months, which is more than twelve, so the gain is long-term. Securities transaction tax was paid on both legs, so section 198 applies: 12.5 per cent on the amount exceeding ₹1,25,000.

| Particulars | Amount (₹) |
|---|---|
| Sale consideration | 9,50,000 |
| Less: cost of acquisition | 6,00,000 |
| Long-term capital gain | 3,50,000 |
| Less: the threshold in section 198 | 1,25,000 |
| Chargeable at 12.5% | 2,25,000 |
| **Tax** | **28,125** |

## Computation of total income and tax

| Particulars | Amount (₹) |
|---|---|
| Income from other sources | 4,50,000 |
| Long-term capital gain on the land (taken without indexation for the purpose of total income; section 197(3) operates on the tax, not on the income) | 30,00,000 |
| Long-term capital gain on the shares | 3,50,000 |
| TOTAL INCOME | 38,00,000 |
| Tax on other income at the default slabs — 5% of (4,50,000 – 4,00,000) | 2,500 |
| Tax on the land — section 197 read with section 197(3) | 3,60,000 |
| Tax on the shares — section 198 | 28,125 |
| Tax before cess | 3,90,625 |
| Add: cess at 4% | 15,625 |
| **TAX PAYABLE (rounded, s. 516)** | **4,06,250** |

- No surcharge arises: the total income of ₹38,00,000 does not exceed ₹50,00,000.
- No rebate: section 156(2) is confined to a total income of ₹12,00,000, and section 156(3) would in any event bar it against the special-rate tax.
- No basic-exemption shelter is available under sections 197(2) or 198(3): the other income of ₹4,50,000 already exceeds the basic exemption of ₹4,00,000 in the default regime. Had his other income been, say, ₹3,00,000, the unused ₹1,00,000 could have been set against the special-rate gains — a point worth two marks in any year it is asked.

**Examiner's note — where marks are lost**

Working only one of the two computations under section 197(3). The section is an option; the marks are in the comparison.

Applying section 197(3) to the shares. It is confined to land or building, and to a resident individual or Hindu undivided family.

Giving the ₹1,25,000 threshold to the land. It belongs to section 198 alone.

Taxing the whole ₹3,50,000 of share gain at 12.5%.

Charging the special-rate gains at slab rates because the assessee is in the default regime. The special rates apply under both regimes.

## 3 (b) OR The Bakshis — a co-owned house

*Nine marks. The gross annual value with unrealised rent — three; the deductions — two; the arrears — two; the co-ownership — two.*

| Particulars | Amount (₹) |
|---|---|
| Municipal value | 4,20,000 |
| Fair rent | 5,00,000 |
| Higher of the two | 5,00,000 |
| Standard rent — the cap | 4,80,000 |
| Expected rent | 4,80,000 |
| Actual rent receivable (₹40,000 × 12) | 4,80,000 |
| Less: unrealised rent for February and March 2027 | 80,000 |
| Actual rent received or receivable | 4,00,000 |
| GROSS ANNUAL VALUE — the higher of the expected rent and the actual rent | 4,80,000 |
| Less: municipal taxes paid by the OWNERS (₹18,000 paid by the tenant is not deductible) | 30,000 |
| NET ANNUAL VALUE | 4,50,000 |
| Less: 30% of net annual value [section 22(1)(a)] | 1,35,000 |
| Less: interest on borrowed capital — no ceiling for a let-out house | 3,60,000 |
| Loss from the Jaipur house | (45,000) |
| Add: unrealised rent of an earlier year recovered [section 23] | 60,000 |
| Less: 30% thereof | 18,000 |
| INCOME FROM HOUSE PROPERTY | (3,000) |
| **SHARE OF EACH CO-OWNER — one-half [section 24]** | **(1,500)** |

- The arrears are chargeable in the year of receipt whether or not the assessee still owns the property, and a deduction of 30 per cent is allowed against them. That the other house has been sold is therefore irrelevant.
- Section 24 applies because the shares of the co-owners are definite and ascertainable. The property is not assessed as an association of persons; each co-owner is assessed on his own share, and each carries his own loss.

- Each co-owner may set off his ₹1,500 against another head to the extent of ₹2,00,000 under section 109(1)(b) — in the optional regime. In the default regime the set-off is not available at all, and the loss is carried forward under section 110.

ANSWER

# Question 4 — Unit 3 : Tax Planning through Investments

## 4 (a) The three points, and three avenues compared

*Nine marks. The three points — two; the comparison — five; the default-regime survivor — two.*

The law touches an investment at three points and at no others — when the money goes in, while it grows, and when it comes out. Every question on this Unit is a question about one of the three, and the four patterns (E-E-E, E-E-T, T-E-E, T-T-E) are simply the sixteen possible combinations reduced to the four that occur in practice.

| | Public provident fund | Equity linked savings scheme | Five-year bank deposit |
|---|---|---|---|
| Point 1 — going in | Section 123, within the aggregate ₹1,50,000 | Section 123, within the aggregate ₹1,50,000 | Section 123, within the aggregate ₹1,50,000 |
| Point 2 — while it grows | Interest exempt — 7.1% for the second quarter of 2026-27 | No annual charge; the fund is not taxed | Interest TAXABLE every year, whether drawn or not |
| Point 3 — coming out | Wholly exempt | Section 198 — 12.5% on the long-term gain above ₹1,25,000 | The principal returns untaxed |
| Lock-in | Fifteen years, extendable in blocks of five | Three years, counted unit by unit | Five years |
| Pattern | E – E – E | E – E – T | E – T – E |
| Chief merit | Certainty and complete exemption | The shortest lock-in in section 123, and an equity return | Simplicity, and the section 153 shelter for a senior citizen |

Which of the three should a taxpayer in the DEFAULT regime still hold? The public provident fund. In the default regime the first point disappears for all three alike — section 123 is withdrawn, and so is section 153. What is left is the second and the third point, and there the provident fund alone is exempt at both. The equity linked scheme keeps its equity return but pays 12.5 per cent on exit, and the deposit is now taxed annually at the full marginal rate with no shelter at all. The provident fund therefore survives the change of regime better than either — not as a tax deduction, which it no longer is, but as a tax-free compounding vehicle, which it still is.

## 4 (b) Shri Harish — deposit or provident fund?

*Nine marks. The optional regime — three; the default regime — three; the advice — three.*

### In the optional regime

| Particulars | Bank deposit | Provident fund |
|---|---|---|
| Interest in the first year | 7.5% of ₹1,50,000 = ₹11,250 | 7.1% of ₹1,50,000 = ₹10,650 |
| Is it taxed? | Chargeable, but section 153 shelters up to ₹50,000 of interest on ANY account for a resident senior citizen. He has no other interest income, so the whole ₹11,250 is sheltered | Exempt outright |
| Tax borne | NIL | NIL |
| **POST-TAX RETURN** | **7.50%** | **7.10%** |

In the optional regime the deposit wins, because section 153 makes its interest effectively exempt while the deposit remains liquid after five years rather than fifteen. Both also earn the section 123 deduction of ₹1,50,000, which is common to them and therefore drops out of the comparison.

### In the default regime

Neither section 123 nor section 153 survives. His total income of ₹9,00,000 falls in the 10 per cent band of the default slabs, so his marginal rate with cess is 10.4 per cent.

| Particulars | Bank deposit | Provident fund |
|---|---|---|
| Interest in the first year | 11,250 | 10,650 |

| Particulars | Bank deposit | Provident fund |
|---|---|---|
| Less: tax at 10.4% | 1,170 | Nil |
| Interest retained | 10,080 | 10,650 |
| **POST-TAX RETURN** | **6.72%** | **7.10%** |

**Advice**

The answer turns entirely on the regime, which is why the regime must be settled first.

IN THE OPTIONAL REGIME — the five-year deposit, at a post-tax 7.50 per cent against 7.10 per cent, and with a lock-in of five years instead of fifteen.

IN THE DEFAULT REGIME — the public provident fund, at 7.10 per cent against 6.72 per cent. The deposit loses 78 basis points to tax that the fund does not pay.

A caution to add for the client: if his interest income should later exceed ₹50,000 the section 153 shelter is exhausted and the deposit loses its advantage even in the optional regime. The comparison must be made on his whole interest income, not on this deposit alone.

## 4 (a) OR The Hindu undivided family as a vehicle of investment

*Nine marks. What income belongs to the family — three; what it gets and does not get — two; the clubbing bar — two; the cautions — two.*

### What income belongs to the family, and what does not

| Belongs to the family | Belongs to the member personally |
|---|---|
| Income from ancestral property, and from property received on a partition | Salary, professional fees and anything else earned by a member's own labour or skill |
| Income from property thrown into the common stock — subject to section 99(3) | Income from a member's self-acquired property that has not been thrown in |
| Income from the investment of family funds — deposits, shares, house property | Remuneration paid to the karta for managing the family business, if reasonable and paid under a valid agreement |
| Income of a business carried on with family funds | A gift received by a member in his individual capacity |

### What the family gets, and what it does not

| The family DOES get | The family does NOT get |
|---|---|
| Its own basic exemption and its own slabs — a second set of the whole rate structure | The rebate under section 156, which is confined to a resident INDIVIDUAL |
| Sections 123 and 126, and section 153 up to ₹10,000 on a savings account | The higher exemption limit of a senior citizen, and the ₹50,000 limit under section 153 — a family has no age |
| The two nil-annual-value houses under section 21(7), independently of its members | Section 124(3) — the additional ₹50,000 for a contribution to the notified pension scheme, which only an individual may claim |
| Its own ₹1,25,000 threshold under section 198, and its own ceilings under sections 82 to 86 | The deductions under sections 127 and 154 for disability, which are personal to an individual |

### The clubbing bar

Section 99(3) provides that where an individual, being a member of the family, converts his self-acquired property into family property, or throws it into the common stock, otherwise than for adequate consideration, the income from that property continues to be included in HIS total income. Section 99(4) continues the clubbing after a partition in respect of the share allotted to the spouse. Between them the two sub-sections destroy the simplest scheme of all — creating a family by transferring one's own assets to it — and leave the family useful only where it has, or can lawfully acquire, funds of its own.

### Three cautions for the planner

**One.** The family must have a genuine nucleus. A Hindu undivided family with no ancestral property, no gift from a stranger and no partition behind it will be looked at closely, and the income assessed in the karta's hands.

**Two.** Keep the family separate in fact and not merely in form — its own permanent account number, its own bank account, its own books, and no mixing of the karta's personal receipts with the family's.

**Three.** A sole surviving coparcener cannot be assessed as a family; and once a partition is recorded under the Act it cannot be undone. A family is easy to create and difficult to unwind, which makes it long-range planning in the strictest sense.

## 4 (b) OR Shri Nitin

*Nine marks. The four deductions — four; the two computations and the advice — five.*

| Particulars | Optional (₹) | Default (₹) |
|---|---|---|
| Gross salary | 16,00,000 | 16,00,000 |
| Less: standard deduction [s. 19(1), Sl. No. 2] | 50,000 | 75,000 |
| GROSS TOTAL INCOME | 15,50,000 | 15,25,000 |
| Less: s. 123 — public provident fund | 1,50,000 | Nil |
| Less: s. 124(3) and (4) — his own pension contribution, ceiling ₹50,000 | 50,000 | Nil |
| Less: s. 129 — interest on the education loan, no monetary ceiling | 1,10,000 | Nil |
| Less: s. 126 — health insurance (20,000 + 10,000) | 30,000 | Nil |
| TOTAL INCOME | 12,10,000 | 15,25,000 |
| Tax before cess | 1,75,500 | 1,08,750 |
| Add: cess at 4% | 7,020 | 4,350 |
| **TAX PAYABLE (rounded)** | **1,82,520** | **1,13,100** |

- Section 124(3) and (4) allows ₹50,000 OVER AND ABOVE the ₹1,50,000 of section 123. He contributed ₹60,000; the ceiling is ₹50,000, and the extra ₹10,000 earns nothing. He should have contributed exactly ₹50,000 and placed the balance elsewhere.
- Section 129 carries no monetary ceiling, but it runs for the initial tax year and seven tax years more, or until the interest is paid in full, whichever is earlier. This is the seventh year, so the deduction is available; in the ninth it will not be.
- Health insurance: ₹20,000 for himself is within the ₹25,000 limit, and ₹10,000 for his mother aged 72 is within the ₹50,000 limit for a senior citizen.
- Tax, optional: ₹12,500 + 20% of ₹5,00,000 + 30% of ₹2,10,000 (₹63,000) = ₹1,75,500. Tax, default: ₹20,000 + ₹40,000 + 15% of ₹3,25,000 (₹48,750) = ₹1,08,750.

**Advice**

Shri Nitin should remain in the DEFAULT regime. His tax is ₹1,13,100 against ₹1,82,520 — a saving of ₹69,420.

₹3,40,000 of hard-won deductions are worth less to him than the wider slabs and the extra ₹25,000 of standard deduction. He should nevertheless keep paying the education loan and the insurance premium; what he should stop doing is treating them as a tax plan.

The one change worth making: ask his employer to contribute to the notified pension scheme up to 14 per cent of his salary under section 124(2). That is the only deduction of any size the default regime still allows, and at his marginal rate of 15 per cent every ₹1,00,000 so contributed is worth ₹15,600 to him.

ANSWER

# Question 5 — Unit 4 : Short Notes

*Three of the five are to be attempted, at six marks each. All five are answered here. A six-mark note wants a definition, the governing section, the figures or the dates, and one planning or practical point — in that order, and in about a page.*

## (i) Best judgment assessment under section 271

- WHAT IT IS. An assessment in which the Assessing Officer determines the total income to the best of his judgment, on the material before him and after such enquiry as he considers necessary, because the assessee has not put him in a position to determine it on the evidence.
- WHEN IT IS MADE. Where the assessee fails to furnish the return; or fails to comply with a notice or a direction requiring him to produce accounts or documents; or where the Assessing Officer is not satisfied with the correctness or completeness of the accounts, or where the method of accounting has not been regularly followed.
- THE SAFEGUARD. A show-cause notice is MANDATORY. The assessment is ex parte in the sense that it is made without the assessee's cooperation, but it is not made without his being heard, and an order made without the notice is bad.
- IT MUST NOT BE ARBITRARY. "Best judgment" means an honest and fair estimate on some material — past results, comparable cases, the gross profit rate of the trade, the assets and expenditure disclosed. It is a judgment, not a punishment, and a wild estimate with nothing behind it will be set aside in appeal.
- TIME LIMIT. Eighteen months from the end of the tax year, extended from twelve by the Finance Act, 2026.
- REMEDY. Appeal to the Commissioner (Appeals) within thirty days. The assessee may also ask the Assessing Officer to reopen the assessment where he shows sufficient cause for the default.
- THE PRACTICAL POINT. The cheapest answer to a best judgment assessment is to avoid one. Filing a return, however late, and complying with a notice, however imperfectly, moves the assessment from section 271 to section 270 and puts the burden of proof back where it belongs.

## (ii) Tax collection at source

Collection at source is the mirror image of deduction at source. Where deduction is made by the person who PAYS, collection is made by the person who RECEIVES — the seller of specified goods or the grantor of a specified right — who collects a percentage of the consideration from the buyer, over and above the price, and pays it to the credit of the Central Government against the buyer's permanent account number.

| | Deduction at source [ss. 392, 393] | Collection at source [s. 394] |
|---|---|---|
| Who acts | The payer | The seller or grantor |
| Where the tax comes from | Withheld out of a sum payable to the recipient | Collected in addition to the price, from the buyer |
| Whose credit | The payee's | The buyer's |
| Cash flow | The recipient gets less | The buyer pays more |

### Why the Act uses it

- To reach trades in which income is hard to trace — liquor, timber, forest produce, scrap and mining leases, where the buyer's purchases are a better index of his turnover than his own books.
- To create an audit trail. The collection is reported against the buyer's number and appears in his Form 168, so the Department learns of purchases he may not have disclosed.
- To capture high-value transactions — the sale of a motor vehicle above the prescribed value, and remittances abroad under the Liberalised Remittance Scheme, are the two that catch ordinary individuals.

**The examinable rule — and the contrast with deduction**

Where the buyer fails to furnish his permanent account number, tax is collected at the HIGHER of twice the rate in the Table and five per cent.

On DEDUCTION the floor is the higher of the prescribed rate and 20 per cent; on COLLECTION it is twice the rate or 5 per cent. The two are examined together and are constantly confused. The reason for the difference is that collection rates are low — 1 or 2 per cent — so a flat 20 per cent floor would be punitive out of all proportion.

On a motor vehicle costing ₹15,00,000: 1 per cent is ₹15,000; twice the rate is ₹30,000; the 5 per cent floor is ₹75,000. A buyer who does not give his number pays ₹75,000 — ₹60,000 of his own money locked up for a year for nothing.

The management point: tax collected at source is not a cost. It is a payment of the buyer's own tax, it appears in Form 168, it is set off against his liability exactly as tax deducted is, and it is deducted in computing advance tax under section 405. Capitalising it in the cost of the asset and claiming depreciation on it is wrong twice over — it overstates the cost and forgoes the credit.

## (iii) Revision under section 377 and revision under section 378

Both are revisions by the Commissioner, and there the resemblance ends. One is a supervisory power exercised against the assessee; the other is a discretionary relief granted to him.

| | Section 377 — prejudicial to the revenue | Section 378 — in favour of the assessee |
|---|---|---|
| Who invokes it | The Principal Commissioner or Commissioner, of his own motion. The assessee cannot ask for it | The assessee by application, or the Commissioner of his own motion |
| The ground | The order of the Assessing Officer is ERRONEOUS in so far as it is PREJUDICIAL TO THE INTERESTS OF THE REVENUE. BOTH limbs must be satisfied — an order that is merely erroneous, or merely unfavourable to the revenue, is not enough | Any order, which the Commissioner may revise in any manner NOT PREJUDICIAL to the assessee |
| Limitation | Two years from the end of the financial year in which the order sought to be revised was passed | One year from the order, or from the application |
| Opportunity | The assessee must be heard before the order is passed | The assessee has himself applied, and no order to his prejudice may be made |
| Remedy against it | Appeal to the Appellate Tribunal | NO appeal lies. The only remedy is a writ petition |

The practical point on section 377 is the double requirement. An order that takes a view the Commissioner dislikes is not "erroneous" if it is one of two views reasonably open on the material; and an order that is erroneous but costs the revenue nothing cannot be revised. Most successful challenges to a section 377 order are made on one or other of those two limbs, and it is worth saying so in an answer.

## (iv) The permanent account number, and the tax credit statement in Form 168

### The permanent account number [section 262 with Rule 159]

| Point | Position |
|---|---|
| Who must obtain one | Every person whose total income exceeds the maximum amount not chargeable to tax; every person carrying on a business or profession whose turnover exceeds the prescribed figure; every person required to furnish a return; and every person entering a transaction specified in Rule 159 |
| Where it must be quoted | In every return, in every correspondence with the Department, in every challan, and in the transactions specified in Rule 159 — the purchase or sale of immovable property above the prescribed value, of a motor vehicle, the opening of a bank or demat account, a large cash deposit, and the rest |
| Where a person has none | He furnishes a declaration in Form 97 (the old Form 60), and the person receiving it reports it in Form 98 (the old Form 61) |
| Aadhaar | The number must be linked to the Aadhaar number. Failure attracts a fee under section 430, and an unlinked number becomes INOPERATIVE |
| Penalty | Section 467 — for failure to obtain, to quote, or to quote correctly |

**Why an inoperative number is the most expensive mistake in this Part**

An assessee whose number has become inoperative is treated, for deduction and collection, as a person who has furnished no number at all. Five consequences follow automatically — tax is deducted at 20 per cent; tax is collected at twice the rate or 5 per cent; any declaration in Form 121 is invalid; no certificate can be granted under section 395; and refunds are withheld, with no interest for the period of inoperability.

Every one of the five is reversed by a single act of linking. It is the highest return on five minutes' work anywhere in the Act.

### The tax credit statement — Form 168

Form 168 replaces the old Form 26AS. It is the assessee's account with the Department — a consolidated statement, drawn from the deductors' and collectors' own quarterly statements and from the challans, of everything paid on his behalf or by him.

| What Form 168 shows | Drawn from |
|---|---|
| Tax deducted at source, deductor by deductor, quarter by quarter | The deductors' quarterly statements |
| Tax collected at source | The collectors' quarterly statement |
| Advance tax and self-assessment tax paid by the assessee | The challans |
| Refunds issued during the year | The Department's own records |
| Demands outstanding | The Department's own records |

The management point: reconcile Form 168 before filing, not after. A credit that does not appear in Form 168 will not be allowed in the processing under section 270(1), however good the certificate in the assessee's hands; and the cure — persuading the deductor to revise his quarterly statement — takes months. Nearly every demand raised on a salaried assessee at the summary stage is a Form 168 mismatch and nothing else.

## (v) Appeal to the Commissioner (Appeals)

- WHERE IT SITS. It is the FIRST rung of the ladder — Commissioner (Appeals), then the Appellate Tribunal, then the High Court, then the Supreme Court. It is the only level at which the assessee alone ordinarily appeals.
- PERIOD. Thirty days from the service of the order or of the notice of demand. The Commissioner (Appeals) may admit an appeal after thirty days if satisfied that there was sufficient cause for the delay.
- FORM AND FEE. Filed electronically in the prescribed form, with the grounds of appeal and a statement of facts, on payment of the prescribed fee, which varies with the assessed income.
- CONDITION PRECEDENT. Where the assessee has filed a return, the tax on the RETURNED income must have been paid; where he has not filed one, he must have paid an amount equal to the advance tax payable. An appeal filed without this is not maintainable, and the point is frequently missed.
- POWERS — THE WIDEST OF ANY APPELLATE AUTHORITY. He may confirm, reduce, ENHANCE or annul the assessment. The power of enhancement is peculiar to this level — the Appellate Tribunal has none — and it may be exercised only after giving the assessee a reasonable opportunity of showing cause.
- ADDITIONAL EVIDENCE. Admitted only in the circumstances the Rules prescribe, and after giving the Assessing Officer an opportunity to examine it.
- THE PRACTICAL POINT. Because he may enhance, a first appeal is not a one-way bet. An assessee who appeals against a small addition and thereby draws attention to a larger one he had got away with may leave the appeal worse off than he entered it. The grounds should be drawn narrowly.

| Rung | Appeal lies to | Period | Note |
|---|---|---|---|
| First | Commissioner (Appeals) | 30 days | May enhance; may condone delay |
| Second | Appellate Tribunal | 60 days; cross-objections 30 days | FINAL on a question of fact; cannot enhance |
| Third | High Court | 120 days | Only on a substantial question of law |
| Fourth | Supreme Court | On a certificate, or by special leave | — |

SUMMARY

# The answers at a glance

| Q. | Part | The figure or the conclusion | Marks |
|---|---|---|---|
| 1 | (b) | Stay 274 days; non-resident in 9 of 10 preceding years; RESIDENT BUT NOT ORDINARILY RESIDENT. Dubai rent not chargeable; Sharjah profit chargeable; remittance not income | 9 |
| 1 | (b) OR | Clubbed with Shri Rakesh — ₹58,500 optional, ₹60,000 default. Nothing of Ira's income is clubbed | 9 |
| 2 | (a) | Total income ₹9,40,500 optional / ₹18,37,000 default; tax ₹1,04,620 against ₹1,74,100 — exercise the option; saving ₹69,480 | 9 |
| 2 | (a) OR | Wholly basic ₹2,96,400; structured ₹1,46,640; saving ₹1,49,760 | 9 |
| 3 | (a) | Depreciation ₹3,30,000; cash payment ₹90,000 added back; business income ₹11,60,000 | 9 |
| 3 | (b) | Income from other sources ₹8,10,000; tax and cess ₹62,400; balance payable ₹2,400 after ₹60,000 of tax deducted at source | 9 |
| 3 | (a) OR | Land — with indexation ₹3,60,000 is lower; shares ₹28,125; total income ₹38,00,000; tax ₹4,06,250 | 9 |
| 3 | (b) OR | House property loss ₹3,000; ₹1,500 for each co-owner | 9 |
| 4 | (b) | Optional — the deposit at 7.50% against 7.10%. Default — the provident fund at 7.10% against 6.72% | 9 |
| 4 | (b) OR | Total income ₹12,10,000 optional / ₹15,25,000 default; tax ₹1,82,520 against ₹1,13,100 — stay in the default regime | 9 |
| 5 | (ii) | Collection at source — no permanent account number: twice the rate or 5%, whichever is higher (contrast 20% on deduction) | 6 |
| 5 | (iii) | Section 377 — two years, appeal to the Tribunal. Section 378 — one year, writ only | 6 |

**The two papers side by side**

In Mock Paper I the salaried assessee was better off in the DEFAULT regime; in this paper she and he are better off in the OPTIONAL one. Nothing has changed in the law between the two papers — only the facts.

That is the single lesson the pair of papers is designed to teach. There is no rule of thumb about the regimes, no threshold of salary above or below which one of them wins. There is only the arithmetic, and it must be done twice, every year, for every client.

FOR THE TEACHER

# Coverage of this paper

*Not part of the question paper. The allocation follows the pattern of the University question papers of December 2025 for this course — five questions of 18 marks each, Questions 1 to 4 in two parts of 9 marks with an internal choice, and Question 5 a short note on any three of five items at 6 marks each.*

| Q. | Unit | What the question covers | Marks |
|---|---|---|---|
| 1 | Unit 1 | Basic concepts of tax planning; residential status; clubbing; the choice of regime under section 202 | 9 + 9 |
| 2 | Unit 2 | Tax planning — income from salaries | 9 + 9 |
| 3 | Unit 2 | House property, business or profession, capital gains, other sources | 9 + 9 |
| 4 | Unit 3 | Tax planning through investments | 9 + 9 |
| 5 | Unit 4 | Short notes — Part A collection and recovery, Part B assessment, returns, appeals and revision | 6 × 3 |
| | | **Total** | **90** |