

## 2. The Essentials of the Indian Tax System

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### **The Essentials of the Indian Tax System:**

Taxation in India can be complex, given its various forms and numerous regulations. Here's a detailed guide covering the essentials of the Indian tax system:

### **2.1 Types of Taxes in India:**

#### **2.1.1 Direct Taxes:**

- Income Tax: Levied on individual and corporate earnings.
- Corporate Tax: Specific tax on corporate profits.

#### **2.1.2 Indirect Taxes:**

- Goods and Services Tax (GST): A comprehensive tax on the manufacture, sale, and consumption of goods and services.
- Customs Duty: Taxes on goods imported into India.
- Excise Duty: Levied on the manufacture of goods within India (mostly subsumed under GST).

### **2.2 Income Tax:**

- For Individuals
- Tax Slabs: Different rates for different income brackets, updated annually.
- Exemptions: Income up to a certain limit is exempt from tax.
- For Corporations
- Tax Rates: Vary based on whether the company is domestic or foreign.

### **2.3 GST (Goods and Services Tax):**

Components: Central GST (CGST), State GST (SGST), and Integrated GST (IGST) for inter-state transactions.

Rates: Multiple rates (0%, 5%, 12%, 18%, 28%) depending on the category of goods or services.

## **2.4 Tax Filing and Deadlines:**

Individuals: Generally, July 31st for individuals (could be extended).

Corporations: September 30th for companies requiring audit; October 31st for others.

Forms: ITR forms (ITR-1 to ITR-7) for different types of taxpayers.

### **2.4.1 ITR 1 Income Tax Return:**

Who is ITR 1 for?

ITR 1 is the most commonly used Income Tax Return (ITR) form for taxpayers in India. This form is for a person who:

Annual income is less than ₹50 lakh. Income comes from the following sources:

- Salary: You can use ITR 1 if your income is only from salary.
- Business: You can use ITR 1 if you are running an independent business.
- House-Property: You can use ITR 1 if you have rented property.
- Other sources: You can use ITR 1 if you are getting income from other sources like interest, dividend, etc.
- Agriculture: You can use ITR 1 if your income is from agriculture (if your annual income is more than ₹5 lakh).

#### **A. Some eligibility criteria for using ITR 1:**

- You must be a resident of India.
- You must have a valid PAN number.
- You must have Aadhaar number.
- You must submit all documents related to your income and expenses.
- Benefits of filing ITR 1
- Tax savings: You can avail deductions and exemptions to save tax on your income.
- Getting Loan: ITR is required for getting loan from Bank and other financial institutions.
- Government Schemes: ITR is required to apply for various government schemes.
- Purchase of Insurance: ITR is required for purchase of insurance.
- Foreign Travel: ITR is required for foreign travel.

#### **B. Documents Required for Filing ITR 1:**

- PAN Number:
- Aadhaar Number:
- Form 16 (if your income is from salary):
- Documents related to house-property (if you have rental income):
- Bank Account Statement:

- Interest Certificates:
- Dividend Certificates:
- Proof of agricultural income (if your income is from agriculture):
- Proof of other income:

#### **2.4.2 ITR 2 Income Tax Return:**

ITR 2 is an Income Tax Return (ITR) form used for filing taxes in India. A bit more complicated than ITR 1, this form is for the following individuals and entities:

**Individuals:** Whose annual income exceeds ₹50 lakh and/or whose income is derived from the following sources:

- Salary (if multiple salaries or other income)
- House-property (if one or more properties)
- Foreign Assets/Income
- Capital gains/gains (sale of stock, sale of property etc.)
- Other sources (interest, dividend etc.)
- Hindu Undivided Family (HUF)

##### **A. Not eligible to use ITR 2:**

Whose income is from salary and pension only (use ITR 1) Whose income is less than ₹5 lakh from agriculture and other sources only (use ITR 1) Individuals with professional and business income and HUF (use ITR 3)

##### **B. Benefits of filing ITR 2:**

- It is possible to include various incomes
- Avail tax deductions and exemptions
- Easy to get loan
- May be required for foreign travel
- May be required to apply for government schemes

##### **C. Documents Required for Filing ITR 2:**

- PAN number
- Aadhaar number
- Salary slips and Form 16 (if your income is from salary)
- Documents related to house-property
- Bank Account Statement
- Investment Statement (Stock Statement, Mutual Fund Statement etc.)
- Proof of foreign income (if applicable)
- In case of HUF, particulars of HUF

### **2.4.3 ITR 3 Income Tax Return:**

ITR 3 is an Income Tax Return (ITR) form used for filing taxes in India.

This form is specifically for individuals with professional and business income and Hindu Undivided Family (HUF) .

#### **A. Eligible to use ITR 3:**

- Individual taxpayers with business and/or professional income (eg, doctors, lawyers, chartered accountants)
- Hindu Undivided Family (HUF) whose income is commercial and/or professional in nature

#### **B. Ineligible to use ITR 3:**

- Whose income comes only from salary and pension (use ITR 1)
- Whose income is less than ₹5 lakh from agriculture and other sources only (Use ITR 1)
- Small and Medium Businessmen (SMBP) and Self Employed (Use ITR 4)
- Companies and Incorporated Co-operative Societies (Use ITR 6)
- Charitable Trusts, Political Parties, Certain Educational Institutions (Use ITR 7)

#### **C. Benefits of filing ITR 3:**

Avail useful tax deductions and exemptions to show professional and business income.

May be necessary for convenient foreign travel for obtaining loans May be necessary for applying for government schemes.

#### **D. Documents Required for Filing ITR 3:**

- PAN number
- Aadhaar number
- Bank Account Statement
- All documentation of business and/or professional expenses
- Bill of sale and purchase (if applicable)
- Stock Statement (if applicable)
- Salary statement of employees (if applicable)
- In case of HUF, particulars of HUF

### **2.4.4 ITR 4 Income Tax Return:**

ITR 4 is an Income Tax Return (ITR) form used for filing taxes in India. This form is specifically meant for Small and Medium Business (SMBP) and self-employed taxpayers who fall under the Presumptive Tax Scheme.

#### **A. Who is eligible to use ITR 4?**

- Individual taxpayers whose professional and business income falls under the Presumptive Tax Scheme (Section 44AD, 44ADA, or 44AE)
- Hindu Undivided Family (HUF) which comes under the Presumptive Tax Scheme

#### **B. Keep it on target:**

- Your annual business turnover must be less than ₹2 crore.
- There are some disqualification criteria for using ITR 4. You cannot use ITR 4 if any of the following applies to you:
  - and resident non-ordinarily resident (RNOR) or non-resident Indian (NRI)
  - Annual income above ₹50 lakh
  - Agricultural income above ₹5,000
  - Director of the company
  - Rental income from multiple properties
  - Specific sources of income such as winning the lottery or owning a race horse
  - Investment in an unlisted share during the previous year
  - Deferred tax on ESOP (Employee Stock Option Plan) received by an eligible startup
  - Taxpayers not covered under Presumptive Tax Scheme

#### **C. Benefits of filing ITR 4:**

- Convenient and relatively straightforward form (than ITR 3)
- Avail Presumptive Tax Scheme (in some cases)
- Easy to get loan
- May be required for foreign travel
- May be required to apply for government schemes

#### **D. Documents Required for Filing ITR 4:**

- PAN Number
- Aadhaar Number
- Bank Account Statement
- Sale and Purchase Bill (if applicable)
- Bank Statements In case of HUF,
- Details of HUF

#### **2.4.5 ITR 5 Income Tax Return:**

ITR 5 is an Income Tax Return (ITR) form used for filing taxes in India.

This form is specifically for firm and business (unincorporated) taxpayers who have business income.

**A. Who is eligible to use ITR 5?**

- Firms (non-incorporated) that have business income
- Individual businesses (unincorporated) that have business income
- Association of Persons (AOP)
- Body of Individuals (BOI)
- Artificial Juridical Persons (AJP) (Unincorporated)

**B. Remember:** The ITR 5 form is relatively complicated and it is better to take the help of a tax advisor.

**Who is not eligible to use ITR 5?**

Companies and Incorporated Co-operative Societies (Use ITR 6). Individual Taxpayers ( Use ITR 1 , ITR 2 , ITR 3 , ITR 4 )

**C. Benefits of filing ITR 5**

- Useful for firms and individuals with commercial income
- Avail tax deductions and exemptions
- Easy to get loan
- May be required for foreign travel
- May be required to apply for government schemes

**D. Documents Required for Filing ITR 5**

- PAN Number
- Aadhaar Number
- Bank Account Statement
- All Documents of Business Expenses
- Sale and Purchase Bill Stock Statement (if applicable)
- Details of Partners (in case of Firm and AOP)

**2.4.6 ITR 6 Income Tax Return:**

ITR 6 is an Income Tax Return (ITR) form used for filing taxes in India. This form is specifically for companies and incorporated cooperative societies that need to file their annual income tax.

**A. Who is eligible to use ITR 6:**

- Companies: Public or Private, Indian or Foreign
- Incorporated Co-operative Societies: Incorporated under the Co-operative Act

**B. Who is not eligible to use ITR 6?**

- Individual Taxpayers) (Use ITR 1 , ITR 2 , ITR 3 , ITR 4 ) Firms and
- Unincorporated Businesses (Use ITR 5)
- Charitable Trusts, Political Parties, Certain Educational Institutions (Use ITR 7)

**C. Benefits of filing ITR 6:**

- Required for companies to pay taxes
- Avail tax deductions and exemptions
- May be required to participate in government schemes
- Convenient to get bank loan

**D. Documents Required for Filing ITR 6:**

- Company Registration
- Number (CIN)
- Bank Account
- Statement Audit
- Report (if applicable)
- Tax Deduction Certificate (TDS)
- Tax Statement (TCS) Continuous
- Tax Account Number (TAN)
- Salary Statement (if applicable)

**2.4.7 ITR 7 Income Tax Return:**

ITR 7 is an Income Tax Return (ITR) form used for filing taxes in India. This form is specifically for certain types of organizations that need to file their annual income tax.

**A. Who is eligible to use ITR 7?** Charitable Trust: A trust established for charitable and/or religious purposes

- Political Party: A political party registered with the Election Commission of India
- Specialized Educational Institutions: Universities (Established under the Universities Act, 1956) Other Educational Institutions having special status (eg, IITs, IIMs)

**B. Who is not eligible to use ITR 7?**

- Individual Taxpayers (Use ITR 1 , ITR 2 , ITR 3 , ITR 4 )
- Companies and Incorporated Co-operative Societies (Use ITR 6)
- Firms and unincorporated businesses (use ITR 5)

**C. Benefits of filing ITR 7:** Avail tax deductions and exemptions (if applicable) required for paying taxes for certain organizations may be required to participate in government schemes.

#### D. Documents Required for Filing ITR 7:

- Registration Certificate (Trust/ Vidyapeeth/ Government side)
- Bank Account Statement
- Audit Report (if applicable)
- Tax Deduction Certificate (TDS)
- Tax Return (TCS)
- Continuous Tax Account Number (TAN)
- Donation/subscription receipts (if applicable)

ITR Forms	Eligible Taxpayers	Description
ITR 1	Individual taxpayers	Annual income less than ₹50 lakh and having easy source of income (salary, person, house rent, etc).
ITR2	Individual taxpayer and Hindu Undivided Family (HUF)	Annual income exceeding ₹50 lakh or having various source of income (salary, rent, capital gains, etc).
ITR3	Individual taxpayers and HUFs	Having professional and/or business income.
ITR4	Small and Medium Business(SMBP) and Self Employed	Assessing tax under section 44AD, 44AE and 44ADA.
ITR5	Individuals and Firms(Not Incorporated)	Those with business and professional income (not incorporated firms).
ITR6	Companies and Incorporated Co-operative Societies	Companies and Incorporated Co-operative Societies.
ITR7	Charitable Trusts, Political Parties Educational Institutions	Charitable trusts, political parties, specialized educational institutions

#### 2.5 GST Filing: Monthly or Quarterly Returns Depending on Turnover:

##### A. Deductions and Exemptions:

- Section 80C: Deductions for investments in PPF, EPF, life insurance, etc.
- Section 80D: Deductions for medical insurance premiums.
- HRA: House Rent Allowance exemption.
- Standard Deduction: Fixed deduction for salaried employees.

##### B. Tax Brackets (as of AY 2023-24):

- Up to ₹2.5 lakh: Nil
- ₹2.5 lakh to ₹5 lakh: 5%
- ₹5 lakh to ₹10 lakh: 20%



- Above ₹10 lakh: 30%
- New Tax Regime: Lower rates with no exemptions, optional for taxpayers.

**C. Record-Keeping:** Documents: Maintain income statements, investment proofs, receipts, and tax returns. Duration: Retain records for at least 8 years.

#### **D. Tax Planning:**

- Investments: Utilize deductions under Section 80C, 80D, and other applicable sections.
- Retirement Plans: Contributions to provident funds and pension schemes.
- Tax Saving Instruments: Fixed deposits, National Savings Certificate (NSC), etc.

#### **E. Common Tax Forms:**

- Form 16: TDS certificate issued by employers.
- Form 26AS: Annual tax statement.
- ITR Forms: Different forms for individuals (ITR-1 for salaried, ITR-4 for presumptive income, etc.).

#### **F. Penalties and Audits:**

- Penalties: For late filing, incorrect information, and non-compliance.
- Scrutiny and Audits: Random selection or specific triggers for tax audits.

#### **G. International Taxation:**

- Double Taxation Avoidance Agreements (DTAA): Treaties with various countries to avoid double taxation.
- Foreign Income Disclosure: Mandatory for residents with foreign income/assets.

#### **H. Seeking Help:**

- Tax Professionals: Chartered Accountants (CAs) and tax consultants.
- Online Platforms: Websites and software like ClearTax, myITreturn, etc., for e-filing.

### **2.6 Summary:**

Understanding and complying with tax regulations in India involves staying informed about various tax types, filing requirements, deductions, and penalties. Proper planning and utilizing available resources can ensure compliance and optimize tax liability.

### **2.7 References:**

1. Income Tax Department Website: The official website of the Income Tax Department of India ([www.incometaxindia.gov.in](http://www.incometaxindia.gov.in)) provides a wealth of information on income tax

laws, rules, forms, and notifications. It's the primary source for understanding and managing your income tax obligations.

2. **Income Tax Act, 1961:** This is the main legislation governing income tax in India. It lays down the provisions related to various aspects of taxation, including income tax rates, exemptions, deductions, and assessments. The Act is periodically amended to incorporate changes in tax laws.
3. **CBDT Circulars and Notifications:** The Central Board of Direct Taxes (CBDT) issues circulars, notifications, and other clarifications from time to time to provide guidance on the interpretation and implementation of tax laws. These documents can help taxpayers understand their rights and obligations more clearly.
4. **Form ITR:** The Income Tax Return (ITR) forms are used by taxpayers to file their income tax returns. There are different ITR forms for different types of taxpayers and income sources. Understanding the requirements of each form and correctly filling them out is essential for compliance with tax laws.
5. **Taxation Websites of State Governments:** In addition to central taxes like income tax, some taxes are levied by state governments, such as state income tax, value-added tax (VAT), and goods and services tax (GST). Each state has its own taxation department website where you can find information specific to that state's tax laws and procedures.
6. **Tax Professionals and Consultants:** Just like in other countries, consulting with a tax professional or chartered accountant can be immensely helpful in navigating the complexities of Indian tax laws. They can provide personalized advice, help with tax planning, and assist with compliance and filing requirements.