

SECTION 5A of Income Tax Act 1961 With Reference to Goan Salaried Tax Payers

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Abstract: Under the Income Tax Act 1961 income is taxable in the hands of the person who earns it, however an exception to this rule is section 5A, which is applicable only to Goans. Section 5A was inserted by the Finance Act, 1994 and covers apportionment of income between spouses governed by the Portuguese Civil Code as applicable to the State of Goa.

Keywords: Section 5A, Salary income, Communion of property (Portuguese civil code), Goan Spouses, Clubbing of income, Apportionment of income.

INTRODUCTION:

Under the provisions of the Income Tax Act 1961, income is taxable in the hands of the person who earns it irrespective of the nature of the income. The exception to this rule is provided by section 5A applicable only to Goans.

Income Tax Act 1961 contains specific section 5A which was inserted by Finance Act, 1994 effective retrospectively from 1st April, 1963. This section governs the apportionment of income between spouses governed by Portuguese civil code as applicable in the State of Goa and reads as under:

5A (1) “Where the husband and wife are governed by the system of Community of Property (known under the Portuguese Civil Code of 1860 as “COMMUNIAO DOS BENS”) in force in the State of Goa and in the Union territories of Dadra and Nagar Haveli and Daman and Diu, the income of the husband and of the wife under any head of income shall not be assessed as that of such Community of Property (whether treated as an association of persons or a body of individuals), but such income of the husband and of the wife under each head of income (other than under the head “Salaries”) shall be apportioned equally between the husband and the wife and the income so apportioned shall be included separately in the total income of the husband and of the wife respectively, and the remaining provisions of this Act shall apply accordingly”. (Section 5A(1), Income Tax Act, 1961)

5A (2) “Where the husband or, as the case may be, the wife governed by the aforesaid system of Community of Property has any income under the head “Salaries”, such income shall be included in the total income of the spouse who has actually earned it”. (Section 5A (2), Income Tax Act, 1961)

The implications of this section on an individual, governed under the Portuguese Civil Code of 1860 as

applicable in Goa, is that income from any source earned by either spouse, not being salary, is to be clubbed together, summed up and equally divided in the hands of each spouse. The said income could be in the nature of professional income, business income, income from capital gains from sale of property or financial instruments, rental income from house property, income from interest on bank deposits, interest on bank savings accounts, dividend income or any income from financial instruments. However, salary income will not be apportioned equally between both the spouses and will be taxed in the hands of the spouse who earns it.

BACKGROUND AND EVOLUTION:

Goa was liberated from Portuguese regime on December 19, 1961. From this date, onwards the people of Goa are liable to be taxed under the provisions of Income Tax Act, 1961 because it is deemed that the said Act is extended to the territory which is newly annexed to the Union of India. Till Section 5A was specifically introduced, the Income Tax Act had not recognised the community of the property which is especially applicable to goan citizen for the purpose of assessment of Income Tax.

The concept of Community of Property was first tested in a court of law in 1974 when the Bombay High Court held that a house property which yielded income became the property of the communion of the husband and wife and they were not liable to be assessed as a ‘Body of Individuals’ (BOI) but they were entitled to be assessed in their individual and separate capacity under the Income Tax Act. (CIT V Purushotam Gangadhar Bhende [1977] 106 ITR 932).

BOI is a separate taxable entity under the Income Tax Act. Under this status the entire income instead of being

equally divided between both the spouse was clubbed together and taxed as a separate entity/person.

Upholding the same view, the Bombay High Court in 1983 held that Income from business run by the communion of the husband and wife married as per the custom of Goa should be assessed separately in equal share to each of them and not in the hands of the Body of individual of the communion. (Addl. CIT V. Valentino F. Pinto [1984] 150 ITR 408).

The above two decisions in respect of income from house property and income from business reinforced and recognised the system prevailing in the State of Goa in the Community of Property between the spouses.

However, subsequently Bombay High Court in 1994 took a different stand with respect to income from salary. It was held that income from salary should be assessed and taxed on such individual who draws the salary and as such the share of income on the basis of the principal of Community of Property need not be adhered to. The Court also held that the income from business, share of income from partnership firm and interest earned on bank accounts has to be assessed in the hands of the Body of Individual consisting of husband and wife and not separately in the hands of each spouse. (CIT V. Modu Timblo (individual) [1994] 206 ITR 647).

In conclusion, the Court in the said case stated that the communion of husband and wife married under the custom of Goa and governed by the Portuguese Civil Code constitutes a Body of Individual for the purpose of the Income Tax Act and it will have to be decided in respect of each head of income whether the income has accrued or arisen to the Body of Individual as such or to its members individually.

In view of the above decision, for a taxpayer domiciled in Goa and who opted for the Portuguese Civil Code it became impossible for him to apply the principal of community of the property in the matter of income tax assessment and became disentitled to claim the benefit of sharing the income between both the spouses and thus of the assessment individually. They all became liable for assessment as Body of Individual which created harshness and resentment amongst the people of Goa since applying the concept of Body of Individual resulted in higher tax outgrow and as such even small businesses had to pay tax. On behalf of Goan assesses this issue was taken up by a core group of Chartered Accountants from Goa before the Finance Ministry. The Finance Minister after grasping the uniqueness of the problem acted to obviate this difficulty by introducing Section 5A in the Income Tax Act in Finance Act, 1994 which came into force on 1st April, 1994. Retrospectivity was given to this section from 1st April, 1963.

The Finance Minister while presenting the Annual Finance budget for 1994-95 made the following statement in his speech which throws more light on the issue. It states as under:

“The system of Community of Property (communiao Dos Bens) is peculiar to the people living in Goa, Daman, Diu Dadra & Nagar Haveli. Recently, certain judicial decision has

been handed down according to which business income of a Goanese family becomes taxable entirely in the hands of a single entity. The decisions affect the time honoured method of dividing such income equally and assessing such income separately in the hands of the husband and wife. This I understand has given rise to unnecessary tensions and anxiety amongst Goan couples. To set at rest all controversies in this area, I proposed to make suitable amendments in Income Tax act to ensure that expecting for salaries to any other income arising to the citizens governed by the system of Community of Property in Goa, will be divided equally and assessed separately in the hands of the husband and wife”. (Finance Budget, 1994-95 Sec (1994)206 ITR(St.)5,30).

Thus, 5A reduced the rigours of the judgement in case of Modu Timblo.

CRITICAL ANALYSIS:

Section 5A as it stands today provides that the income of the husband and wife governed under the Portuguese Civil Code in force in the state of Goa shall be divided equally between the husband and wife and the apportioned income will be included separately in the total income of the respective spouse. This shall apply to all heads of income u/s 14 of the Income Tax Act I.e. Income from House property, Profits & gains of Business and Profession, Capital gains, Income from other Sources except from Income from salary. Income from salary would be taxable in the hands of the spouse who actually earned it. Example of calculation of income applying Section 5A and without it is attached.

Some Goan salaried taxpayers aggrieved by the fact that income from salary under the provisions of Section 5A was taxable in the hands of the person who actually earned it and therefore since they could not apportion the salary equally between both the spouses as was provided for the other heads of income filed a writ petition in the Bombay High Court challenging the Constitutional validity of Section 5A on the grounds that it was discriminatory to salaried goan assesses.

It was argued that the sole purpose of bringing about the amendment to the Act by introducing this new section, was to recognise the principal of Community of Property and as such the benefit of sharing of income individually between the husband and wife should have been extended even to salary. This distinction was not based on any substantial differentiation vis-à-vis other income and hence was hostile to salaried person.

The principal ground of the writ was that this stand was violative of Article 14 of the Constitution of India since the provisions of Section 5A discriminated against salaried assesses and was consequently unjust and unequitable. It was further argued that Section 14 of the Income Tax Act provides for the computation of income under five heads of income viz Salary, House property, Capital gains, Profession/business and Other sources. Each head of income has to be treated separately for the purpose of computation of income to give specific deduction or computation provided for the respective heads. But this does not change the character of each head of income

since all heads are income. If a person is having income from all five heads of income, even though those five heads for the purpose of assessment or computation are treated differently, it does not lose its essential character of income or in other words all the head of income meant the separate nature of income. These heads imply only source of income. The Supreme Court emphasised that Income Tax Act puts tax on income, profits & gains irrespective from the source from which they are derived. That the several heads into which income is divided under the Income Tax Act does not make different kinds of taxes. The tax is always one; but it may arise from different sources to which the different rules of computation have to be applied. (CIT v/s Karanpura Development Co. Ltd. v/s CIT, (SC) 1962).

Hence the contention in the writ was that though Section 14 denotes separate heads of sources of income, in reality and in law all this is income and one head of income cannot be discriminated or taken away or excluded for a different treatment from another head. Therefore, if once Parliament recognises the principal of Community of Property, salary alone cannot be excluded for computing the income of husband and wife.

It was pointed out by relying on another Supreme Court verdict that there are no circumstances or justification for Parliament to exclude Salary when the existing condition in the State of Goa was recognised and that recognition is reflected in enacting Section 5A and thus exclusion of salary under any parameters laid down by the said Supreme Court decision was not justified. (Ram Krishna Dalmia V. Justice S.R. Tendolkar (SC)).

On the other hand, the Government contended that for the calculation of income under the separate heads have been treated separately by the Income Tax Act itself. There was nothing wrong in excluding salaried person for the purpose of assesment in the manner provided under Section 5A. And even in the case of salaried Goans it was only salary that could not be apportioned. Their balance income whether from house property, other sources, capital gains or professional/business income was to be divided equally between both spouses.

The Income Tax department has justified this stand by stating before the Bombay High Court where the writ was being heard at para 12 of their written submissions as under:

“12. With reference to para .39 of the petition and the grounds set out in para. 41, it is denied that Section 5A of the Income - Tax Act is a colourable piece of legislation and/or that it is arbitrary and discriminatory and/or in any manner whatsoever violative of any fundamental right or Article 300A of the Constitution. The Section was introduced after considering the decisions of the High Court of Bombay and due to the administrative problems arising out of creation of body of individuals. The said section was introduced stating the income would be computed first and then divided between husband and wife so as to overcome the administrative problems, not legal problems. All the decisions of the Bombay High Court having been accepted and the income under the head ‘House property’ (being divided after the decision in the matter of Purushottam

G. Bhende [1977] 106 ITR 932 (Bom)), income from capital gains and other sources are also being assessed separately as decided by the Bombay High Court in the case of Modu Timblo [1994] 206 ITR 647. With reference to business or professional income, the Court decided that the income arose in the hands of the ‘body of individuals’ which created administrative problems like re-opening settled procedures, adjustment of taxes paid in individual status etc. In order to avoid these procedural problems, the benefit of sharing of income is extended to the business/professional income as well. Hence, introduction of Section 5A cannot be considered as arbitrary and in no way discriminatory against any class of persons. All submissions made by the petitioners in the said paras and the grounds therein which are contrary to and inconsistent with what is stated by me herein and in the rest of the affidavit in reply are denied as though specifically set out herein and traversed.”

The Honourable High Court distinguished the arguments put forward in support of division of salary income between spouses by stating that here they were dealing with a fiscal statute and that the reasons stated for assailing the exclusion of salaried persons from the operation of 5A was not based on any legal ground.

It justified 5A for Goans because of the historical background, social conditions and also because for centuries together the people of the State of Goa had been separated from the main stream of the Nation during the Portuguese rule. The Court held that it is a well settled principal that the statute cannot be challenged on the ground that certain persons have been given a special treatment and because the petitioners were not extended that benefit, the statute is bad. That cannot be a ground of challenge much less under Article 14 of the Constitution of India. It is quite natural that the legislature could not embrace all classes of people for the purpose of assessment of tax. The Court referred to a judgement of the Supreme Court wherein it has been held that legislation enacted for the achievement of a particular object or purpose need not be all embracing. It is for the legislature to determine the categories it would embrace within the scope of legislation and merely because certain categories which would stand on the same footing as those which are covered by the legislation are left out would not render laws which has been enacted in any manner discriminatory and violative of the fundamental right guaranteed by Article 14 of the Constitution. (Sakhawant Ali V. State of Orissa (SC)).

The Court held that the argument of the salaried assesses that they should also be included in the category for giving benefit of sharing the salary income between the spouses is a matter of policy. And that the policy may not always fit in the square of logic. As such Parliament is justified in grouping the salaried persons as separate and distinct in that context.

The argument of the petitioners was that once Section 14 of the Income Tax Act operated and classified the income assessed in the manner provided in the Act, then it is the total

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income from all the sources that is to be shared between husband and wife taking into account principle of Community of Property. According to the petitioners what really is meant by Section 5A is charging of income which stand is erroneous. The computation of income is done under Section 14 of the Act. But Section 5A too has prescribed another method of computation of income as regards the spouses of Goan Origin who follows the rule of Community of Property. Therefore, Section 5A has also laid down a computation by which calculation for each head of income is to be done separately. The income so arrived at under each head of income, except salary, is to be divided equally between both husband and wife. Salary earned by the concerned spouse will be added under the Head Salary to income of the said person without any division.

Therefore, the Bombay High Court in the said case of the Goan Salaried Petitioners held that it is a well settled principal that a fiscal statute cannot be challenged on the ground that certain persons have been given a special treatment and because the petitioners are not extended the benefit, the statute should be banned. This cannot be a ground of challenge much less under article 14 of the Constitution of India. (Goa

Salary Taxpayers V. Union of India and Ors [2001, 249 ITR 195 Bom]).

As such the Court concluded that Section 5A is constitutionally valid and rejected the challenge of the petitioners against it.

CONCLUSION:

In conclusion, Section 5A is a unique Goan specific section incorporated in the Income Tax Act for Goans governed under Portuguese Civil Code and majority of Goans have been benefitting by way of lower taxes thanks to Section 5A.

EXAMPLE OF SECTION 5A

Mr Fernandes is having net income from business of Rs, 7,50,000 and Mrs Fernandes is drawing salary of Rs 9,00,000 p.a. Interest on Fixed deposit in hands of Mr Fernandes is Rs 2,80,000 and Mrs Fernandes is Rs 2,20,000. Interest on savings account received by Mr & Mrs. Fernandes is Rs 12,000 & Rs. 8,000 respectively.

Therefore, the computation of total income considering the provisions of Section 5A will be as follows.

STATEMENT OF TOTAL INCOME AS ON 31/03/XXXX

PARTICULARS	TOTAL	MR AMOUNT	MRS AMOUNT
INCOME FROM SALARY			
SALARY	9,00,000	0	9,00,000
INCOME FROM BUSINESS			
Net profit on Business	7,50,000	3,75,000	3,75,000
INCOME FROM OTHER SOURCES			
Interest on Fixed Deposits	5,00,000	2,50,000	2,50,000
Interest on Saving Account	20,000	10,000	10,000
GROSS TOTAL INCOME	21,70,000	6,35,000	15,35,000
LESS DEDUCTION U/S CHAPTER VIA			
80C			
PPF	3,00,000	1,50,000	1,50,000
80TTA (INTEREST ON SAVING ACCOUNT)	20,000	10,000	10,000
NET TAXABLE INCOME	18,50,000	4,75,000	13,75,000

Without considering provisions of Section 5A

STATEMENT OF TOTAL INCOME AS ON 31/03/XXXX

PARTICULARS	TOTAL	MR AMOUNT	MRS AMOUNT
INCOME FROM SALARY			
SALARY	9,00,000	0	9,00,000
INCOME FROM BUSINESS			
Net profit on Business	7,50,000	7,50,000	0
INCOME FROM OTHER SOURCES			
Interest on Fixed Deposits	5,00,000	2,80,000	2,20,000
Interest on Saving Account	20,000	12,000	8,000
GROSS TOTAL INCOME	21,70,000	10,42,000	11,28,000
LESS DEDUCTION U/S CHAPTER VIA			
80C			
PPF	3,00,000	1,50,000	1,50,000
80TTA (INTEREST ON SAVING ACCOUNT)	20,000	10,000	8,000
NET TAXABLE INCOME	18,50,000	8,82,000	9,70,000

REFERENCES:

1. CIT v/s Purushotam Gangadhar Bhende (Bombay High Court, 1977) ITR Volume 106; pp:932
2. CIT v/s Valentino Pinto (Bombay high Court, 1984) ITR, Volume 150, pp:408
3. CIT v/s Modu Timblo (Bombay High Court,1994) ITR, Volume 206, pp:647
4. Finance Budget 1994-95, ITR, Volume 206, pp:530
5. CIT v/s Karanpura Development Co. Ltd (Supreme Court,1962) ITR, Volume 44, pp:362
6. Ram Krishna Dalmia v/s S.R. Tendulkar (Supreme Court)
7. Sakhawant Ali v/s State of Orissa (Supreme Court)
8. Goa salary Tax payer’s v/s Union of India and others (Supreme Court, 2001) ITR, Volume 249, pp:195
9. Section 5A (1) and (2) of the Income Tax Act, 1961.