

Taxation of a 'Goan' Governed under Portuguese Civil Code - Steps towards Removal of Difficulty

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Brief background

Goa was liberated from Portuguese regime after 450 years of Portuguese rule on December 19, 1961 and became part of India; 14 years after the rest of India got its independence. However, Goa continued to enjoy a distinct identity over the rest of India by virtue of it following the Portuguese Civil Code. The Portuguese Civil Code is still prevalent in the state of Goa in relation to marriage, inheritance, property and other personal matters and is applicable to only Goans. Goan refers to every person who or either of whose parents or any of whose grandparents was born before December 20th, 1961 in Goa.

From 19th December 1961 onwards the people of Goa by virtue of being Indian Citizen 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 in Finance Act 1994 effective from 1st April, 1994, the Income Tax Act had not specifically recognised the community of the property which is especially applicable to Goan governed under the Portuguese Civil Code for the purpose of assessment of Income Tax and therefore there were a number of litigations on the said issue.

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.

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] [\[TS-5504-HC-1974\(BOMBAY\)-O\]](#)). 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] [\[TS-5444-HC-1983\(BOMBAY\)-O\]](#)). 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] [\[TS-5315-HC-1993\(BOMBAY\)-O\]](#)).

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 (Communiaio 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.

Hardships faced by Goan assessee

This provision being unique to Goa and the said union territories and since the income tax forms and procedures are common for entire India, the special reporting requirements of the assessee covered under Section 5A was not taken into consideration. Till the times return filing was manual and returns were processed manually by the local jurisdictional officers, the process of assessment, processing and refunds did not cause any issues. Even in the case of processing errors, the rectification process was simple since one could approach the jurisdictional officer in Goa, who being familiar with the implications of provision 5A, would provide a speedy resolution and bring the case to conclusion.

The issues started when the income tax returns were required to be filed electronically and were processed centrally at the Central Processing Centre (CPC) with the processing being done using higher technology solutions and minimal manual intervention. Since the logic of Section 5A was not taken into account, the processing resulted in wrongly determining returns as defective and incorrect demands on account of non-apportionment of TDS due to matching with Form 26AS. After representations by the Goa Branch of ICAI, the Income Tax Department took this matter into consideration and implemented the declaration of being covered under Section 5A in Part A - Gen and Schedule 5A wherein the assessee is required to declare details of spouse and income shared in the income tax return from the Assessment Year 2013-14.

Issue addressed in current budget

The current budget proposal identifies and seeks to address another hardship faced by Goan assesseees. The due dates for persons covered under tax audit is 31st October as against 31st July in case of other persons. In case of an assessee covered under Section 5A, if the spouse is a partner in a firm covered under tax audit, the due date for filing is 31st October but benefit of the extended due date is not available to the assessee. The practical issue is that the income of the assessee not covered under tax audit cannot be determined till that of the spouse is determined after completion of tax audit of the firm in which the spouse is a partner. To address this issue the current budget proposes to amend Section 139 of the Income tax Act as follows:

"Amendment of section 139.

32. In section 139 of the Income-tax Act,-- (a) in sub-section (1), in Explanation 2,--

(i) in clause (a), in sub-clause (iii), after the words "any other law for the time being in force", the words, figure and letter "or the spouse of such partner if the provisions of section 5A applies to such spouse" shall be inserted;"

As stated in the Budget Memorandum:

"Since the total income of a partner can be determined after the books of accounts of such firm have been finalised, the due dates of partners are already aligned with the due date of the firm. Thus, the due date for filing of original return of income of such partner is 31st October of the assessment year. However, this relaxation is not there for spouse of such partner to whom section 5A of the Act applies. Therefore, it is proposed that the due date for the filing of original return of income be extended to 31st October of the assessment year in case of spouse of a partner of a firm whose accounts are required to be audited under this Act or under any other law for the time being in force, if the provisions of section 5A applies to them."

From the Asst. Year 2018-19, the Income tax Act implemented Section 234F for late fees for delayed filing of returns. This late fee is computed at the time of filing the income tax returns by the utilities or

softwares by considering the due date based on whether the person is covered under Section 44AB or whether the person is a partner in a firm which is covered under Section 44AB. As of now, there is provision in the ITR form for an assessee to declare being partner in a firm covered under tax audit, but there is no provision to declare that the spouse is a partner in a firm covered under tax audit. Unless such provision is made in the form, it is probable that the return may be considered as belated and late fees may be levied thereon.

Other hardships and possible solutions

Despite these improvements, the assessee continued to face hardship on account of non-apportionment of TDS in line with apportionment of income since the TDS matching logic is PAN based. After representations were made by Chartered Accountants, the Income Tax Department made modifications to Schedule TDS to capture details of TDS of spouse and apportionment thereof. The effectiveness of processing of returns after this modification will be clear after processing of returns of AY 2020-21.

The other major issue affecting the Goan assessee subsequent to introduction of e-filing and automated central processing is that there is no provision in the form to declare income of each individual, add the income of spouse and then reduce half thereof to arrive at income as per requirements of Section 5A. For the lack of a better alternative, assessee would directly declare half income but would receive notice for adjustment under Section 143(1)(a) for mismatch between income and deduction as compared to Form 26AS. Certain assessee in order to avoid mismatch of the income with Form 26AS would show the total income of both assessee and then show half amount as deduction. These assessee received enquiries for claiming high deductions since the only possible field in which this amount could be reduced was "any other deduction". This issue remains unresolved.

Suggested options based on practice followed:

Option 1: The earning spouse enters the total balance sheet and profit and loss account in ITR 3. The Schedule BP provides for a separate deduction on account of Section 5A wherein the system computes 50% of the income from BP after adjustments. Similar option to be provided under other heads of income. The earning spouse claims 50% of TDS available in Form 26AS against the PAN.

In case of the non-earning spouse, a separate line item be shown in Schedule BP as half share of income of spouse under Section 5A. 50% credit of TDS is shared to the non-earning spouse. The return of the non-earning spouse should be processed as a non-accounts case and should not be marked as defective on account of no P&L and Balance Sheet entered. No tax audit report be made applicable to the non-earning spouse.

Option 2: Husband and wife covered under Section 5A enter 50% of all Balance Sheet items and 50% of Profit and Loss Account items in ITR 3. The earning spouse claims only 50% of the TDS credit available in Form 26AS against the PAN. The non-earning spouse claims 50% of the TDS credit available in Form 26AS against the PAN of the earning spouse.

Conclusion

The current budget proposal to extend the due date for spouse of an individual covered under Section 5A being a partner in a firm covered under tax audit is a welcome move and it is encouraging to see that the Income Tax Department is proactively addressing the hardships faced by Goan assessee at the time of processing of income tax returns. Given the other changes in the income tax forms and schema for AY 2020-21 and changes expected in the forthcoming assessment years, it appears that the accuracy of processing and speed of refunds will be seamlessly implemented.