

Income Tax on Agricultural Income: Exemption Limit, Tax Calculation, Examples

Agriculture is said to be the primary occupation in India. It is usually the only source of income for the large rural population in India. The country as a whole is entirely dependent on agriculture for its basic food requirements. The government has numerous schemes, policies and other measures to promote growth in this sector – one of them being an exemption from income tax.

Agricultural income is specifically defined under the Income Tax Act, and there are certain conditions that must be met for the income to qualify for exemption. Let us take a look at the provisions of the law in this regard.

Meaning of Agricultural Income

The Income-tax Act has its own **definition of agricultural income** which constitutes the following 3 main activities:

I. Rent or revenue earned from agricultural land situated in India:

Rent or revenue earned from land located in India and used for agricultural purposes. However, the amount received on the sale of land is not covered under the definition of agricultural income.

II. Income from agricultural land in the following ways:

1. **Agriculture:** The meaning of agriculture though not covered in the Act, has been laid down by the Supreme Court in the case *CIT v. Raja Benoy Kumar Sahas Roy* where agriculture has been explained to consist of two types of operations – **basic operations** and **subsequent operations**.

- The **basic operations** would include cultivation of the land and consequently tilling of the land, sowing of seeds, planting and all such operations that require human skill and effort directly on the land itself.
- The **subsequent operations** would include operations that are carried out for growth and preservation of the produce like weeding, digging soil around the crops grown etc and also those operations which would make the product fit for use in the market like tending, pruning, cutting, harvesting, etc. Income derived from saplings or seedlings grown in a nursery would also be considered to be agricultural income whether or not the basic operations were carried out on land.

2. **Through the performance of a process by the cultivator or the receiver of rent (in-kind) that results in the agricultural produce being fit to be taken to the market:** Such processes involve manual or mechanical operations that are ordinarily employed to make the agricultural produce fit for the market and the original character of such produce is retained.
3. **Through the sale of such agricultural produce:** Where the produce does not undergo ordinary processes employed to become marketable, the income arising on sale would generally be partly agricultural (exempt) income and part of it will be non-agricultural (taxable) income.

The Income Tax has prescribed rules to make this bifurcation regarding agricultural and non-agricultural produce for products like tea, coffee, rubber, etc

Operation	Agricultural Income	Non-Agricultural Income
Growing and Manufacturing Tea	60%	40%
Manufacturing Rubber	65%	35%
Growing and curing Coffee	75%	25%
Coffee grown, cured, roasted, and grounded with or without mixing chicory or other flavouring ingredients	60%	40%

III. Income derived from farm building required for agricultural operations:

The conditions for classifying income derived from farm building as agricultural income are as follows:

- The building should be on or in the surrounding area of the agricultural land. Also, the rent receiver or cultivator of the land, by reason of his connection with the land, requires the building as a house to stay or as a storehouse or uses it for these kinds of situations
- Either of the two conditions should be satisfied:
 - The land is assessed by either land revenue or a local rate assessed and collected by government officers; OR
 - If the above condition is not satisfied, the land should not be located within the following region:

Aerial distance from municipality*	Population as per last preceding census.
Within 2 kms	10,000 to 1,00,000
Within 6 kms	1,00,000 to 10,00,000
Within 8 kms	> Rs. 10,00,000

*Municipality includes municipal corporation, notified area committee, town area committee, town committee and cantonment board.

Note: Even where the local population is < 10,000, the land should also not be situated within the jurisdiction of the local municipality or cantonment board.

In cases where the activities have only some distant relation to land like dairy farming, breeding, rearing of livestock, poultry farming, etc. they do not form a part of agriculture income.

Indirect connection with land :

We have seen above that agricultural income is exempt, whether it is received by the tiller or the landlord. However, non-agricultural income does not become agricultural merely on account of its indirect connection with the land. The following examples will illustrate the above point.

Example: A rural society has its principal business of selling butter which was made from the cream sold to them by farmers. The making of butter was a factory process separated from the farm.

The butter resulting from the factory operations separated from the farm was not an agricultural product and the society was, therefore, not entitled to exemption under section 10(1) in respect of such income.

Example: X was the managing agent of a company. He was entitled to a commission at the rate of 10% p.a. on the annual net profits of the company. A part of the company's income was agricultural income. X claimed that since his remuneration was calculated with reference to the income of the company, part of which was agricultural income, such part of the commission as was proportionate to the agricultural income was exempt from income tax.

Since X received remuneration under a contract for personal service calculated on the amount of profits earned by the company; such remuneration does not constitute agricultural income.

Example: In regard to forest trees of spontaneous growth, which grow on the soil without any human skill and labour, there is no cultivation of the soil at all. Even though operations in the nature of forestry operations performed by the assessee may have the effect of nursing and fostering the growth of such forest trees, it cannot constitute agricultural operations.

Income from the sale of such forest trees of spontaneous growth does not, therefore, constitute agricultural income.

Examples of Agricultural Income

The following are some the examples of agricultural income:

- Income from the sale of seeds.
- Income from the sale of replanted trees.

- Interest on capital received by a partner from a firm engaged in agricultural operations.
- Income from growing flowers and creepers.
- Rent received for agricultural land.
- Profits received by a partner from a firm involved in agrarian produce or activities.
- Income from growing of bamboo.

Examples of Non-Agricultural Income

Below are some examples of non-agricultural income:

- Income from poultry farming.
- Income from agricultural land held as stock-in-trade
- Any dividend paid from an organization's agriculture income.
- Income from dairy farming.
- Income from bee hiving.
- Income from fisheries.
- Income from cutting and selling timber trees.
- Income from butter and cheese making.
- Receipts from TV serial shooting in the farmhouse.

Taxation of Agricultural Income

As discussed above, agricultural income is exempt from income tax.

However, the Income-tax Act has laid down a method to **indirectly tax such income**. This method or concept may be called the **partial integration of agricultural income with non-agricultural income**. It aims at taxing the non-agricultural income at higher rates of tax.

Applicability:

This method is applicable to individuals, HUFs, AOPs, BOIs, and artificial juridical persons, when the following conditions are met:

- Net agricultural income is greater than Rs. 5,000 during the year; and
- Non-agricultural income is above the basic exemption limit:
 - Greater than Rs 2.5 lakh for individuals below 60 years of age and all other applicable persons (old regime)
 - Greater than Rs 3 lakh for individuals between 60 – 80 years of age (old regime)
 - Greater than Rs 5 lakh for individuals above 80 years of age (old regime)
 - Greater than Rs 3 lakh irrespective of the age of the person (new regime)

In simple terms, the non-agricultural income should be greater than the maximum amount not chargeable to tax (as per the slab rates).

Thus companies, firms/LLP, co-operative societies, and local authorities are excluded from using this method.

Calculation of Agricultural Income

(1) Calculate Tax on:
(Non-agricultural income + net agricultural income)

(2) Calculate Tax on:
(Net Agricultural income + Maximum exemption limit as per slab rates)

(3) Calculate final tax (1) - (2) as above and:
(-) Rebate, if available
(+) Surcharge, as applicable
(+) Education and Secondary and higher education cess

Example:

Income from other sources is Rs.7,00,000 and Net agriculture income Rs.2,00,000. The calculation of agriculture relief and net tax payable under the old tax regime is as follows

1. Total taxes on Rs.9,00,000 (Non-agricultural income + net agricultural income) = Rs.92,500 (before education cess @ 4%)
2. Total taxes on Rs.4,50,000 (Basic exemption limit + net agricultural income) = Rs.10,000 (before education cess @ 4%)
3. Net tax payable shall be Rs.82,500 (Rs.92,500 - Rs.10,000) + education cess @ 4%

Tax liability on agricultural income over and above the basic exemption limit shall be allowed as a relief. The higher the proportion of agriculture income in your total income higher the agriculture tax relief one can enjoy.

Which ITR to File for Agricultural Income?

Agricultural income is to be shown under the column of Agriculture Income in [ITR-1](#). But ITR-1 applies only when the agricultural income is up to Rs 5,000. In case it exceeds the limit of Rs.5,000, [ITR-2](#) form must be filed.

Tax Benefit Under Section 54B

Section [54B](#) provides relief of capital gains to taxpayers who sell their agricultural land and acquire another agricultural land from the sale proceeds. The conditions for claiming the benefit u/s 54B are:

- The taxpayer should be an individual or HUF.
- The asset transferred should be agricultural land, whether a long-term or short-term capital asset.
- The agricultural land should be used for agricultural purposes for at least two years immediately preceding the date of transfer of land.
- The taxpayer should acquire/purchase another agricultural land within two years from the transfer date.

The exemption amount under section 54B is the lower of the following:

- Amount of capital gains arising on transfer of agricultural land.
- Investment in a new agricultural land or the amount deposited in the Capital Gains Deposit Account Scheme.

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