

SOLUTION TO PCC TAX PAPER HELD ON 12/5/2010

Question 1. Answer the following with reasons having regard to the Provisions of the Income tax Act, 1961 for the AY 2010-2011 **(2 marks each)**

- (i) State the scope of total income in the case of an individual, whose residential status is 'non-resident' with reference to Section 5(2) of the Act.
- (ii) Mr. X a citizen of India received salary from the Government of India for the services rendered outside India. Is the salary income chargeable to tax ?
- (iii) Mr. Anil earned Rs. 5,00,000 from sale of Coffee grown and cured (processed) by him. He claims the entire income as agricultural income, hence exempt from tax. Is he correct?
- (iv) What is the time limit for filing application seeking registration in the case of Charitable Trusts/Institutions under Section 12AA of the Act ?
- (v) In what status and tax rate Limited Liability Partnership (LLP) is taxed under the Act?

Solution:

(i) Non resident: As per section 5(2) The following income from whatever source derived will be included in total income of the Non Resident in India:

(a) Income, which is received or deemed to be received in India by or on behalf of Individual and HUF.

(b) Income, which accrues or arises or is deemed to accrue or arise to him in India.

In other words, only Indian incomes are taxable for non residents and foreign incomes are not taxable for non residents.

(ii) Salary outside India: As per section 9(1)(iii) if an employee of the government has rendered the services outside India then his salary will be deemed to accrue or arise in India and therefore taxable in India. However this is relevant only for the salary, provident fund and interest on the provident fund. This is not relevant for allowances and perquisites since they are exempt from tax under section 10(7).

(iii) Income from sale of coffee grown and cured in India: Rule 7B(1): Income from sale of coffee grown, cured by seller in India shall be bifurcated into business income and agriculture income. For this purposes 25% of the income from sale of coffee is considered as business income and 75% of the income from sale of coffee is considered as agriculture income. Hence Claim of Mr. Anil that his entire income is agriculture income is incorrect.

(iv) Registration of the trust: Section 12AA: Trust should submit an application for registration in the Form 10A to the commissioner of Income Tax before the expiry of 1 year from the date of creation of trust.

SCHEDULE OF NEW BATCHES FOR NOV 2010 EXAMS

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HUDSON LINE	28/5/2010	M/W/F	7-11 AM	Rs. 9,000

- (v) **LLP Status and rate of tax: section 2(23):** The Limited Liability Partnership Act, 2008 (LLP ACT) has enabled carrying on business or profession through a new type of entity i.e Limited Liability Partnership (LLP). The Income-tax Act did not have any special provision for taxation of LLP. Section 2(23) which defines the terms 'firm', 'partner' and 'partnership' has been amended, and an LLP defined under the LLP Act has been put on par with a partnership firm under the Indian Partnership Act, 1932 (General Partnership) for the purposes of income-tax. Consequently, provisions relating to interest and remuneration to partners will apply to an LLP. **The tax rate faced by LLP shall be same as that of Partnership firm i.e. 30% plus education cess.**

Question 2: Mr. Raman (aged 70 years), Karta of a Hindu Undivided Family (HUF) furnishes the following information for the PY 2009-2010: **(20 marks)**

- Income from the business of Poultry farming Rs. 4,00,000.
- Income by way of winning from Horse race Rs. 30,000 (Horse race won on 28/2/2010)
- Net profit from the business of dealing in Equity shares Rs. 88,500. (Computed after deducting Securities Transaction Tax (STT) of Rs. 11,500).
- Brought forward business loss relating to discontinued automobile business Rs. 38,500 (relates to AY 2007-2008).
- Payment of Life Insurance Premium (on self) Rs. 22,500.
- Contribution to Pension Fund of LIC Rs. 17,500.
- Contribution made in the name of a member of HUF in Public Provident Fund Account Rs. 20,000.
- Interest income from Company deposits Rs. 15,100.
- Housing Loan principal repaid Rs. 30,000.
- Interest on Housing loan Rs. 36,000 (actually paid Rs. 25,000).
- The HUF gave the right to receive furniture rent of Rs. 26,000 per annum by Mrs. Raman without transferring the ownership rights in her favour.
- The HUF owns a residential property which has three identical residential units. Unit 1 and Unit 2 are self occupied by the members of the HUF for residential purpose. Municipal tax paid @ Rs. 5,000 per annum for each residential unit. Unit 3 is let out for a rent of Rs. 8,000 per month. The tenant paid the Municipal tax in respect of Unit 3 as per agreement. The Assessee realised Rs. 1,20,000 on 16.4.2009 as per court order towards arrear rent for the period from 1/1/2007 to 31/12/2008.

Compute the Total Income and tax payable for the AY 2010-2011.

Solution: **Computation of taxable income for the AY 2010-2011**

Income from salary	NIL
Income from house property	1,15,200
Income from business and profession	4,50,000
Income from capital gains	NIL
Income from other sources	71,100
Gross total income	6,36,300

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Less: Deduction u/s 80C		
a) Life insurance premium	22,500	
b) Contribution to pension fund	17,500	
c) PPF	20,000	
d) Housing loan repaid	30,000	90,000
Taxable income		5,46,300

Computation of Tax liability for the AY 2010-2011

Horse races	30% of Rs. 30,000	9,000
Balance income	516300 @ slab 1	58,890
Total		67,890
Add: primary education cess @ 2%		1,357.8
Add: secondary and higher education cess @ 1%		678.9
Total income tax liability rounded off u/s 288B		69,930

Calculation of House property Income

Particulars	Unit 1 – SO	Unit 2 –DLO	Unit 3- LO
Gross annual value	Nil	Nil	96,000
Municipal taxes	NIL	Nil	Nil
Net annual value	Nil	Nil	96,000
Statutory deduction u/s 24(a) 30% of NAV	Nil	Nil	28,800
Interest on borrowed capital u/s 24(b)	12,000	12,000	12,000
Income	(12,000)	(12,000)	55,200

Calculation of Income under the head of House Property

Unit 1	(12,000)
Unit 2	(12,000)
Unit 3	55,200
Arrear of rent received	1,20,000
Less: deduction u/s 25B 30%	36,000
Net income under the head of House property	1,15,200

NOTES:

- 1) Municipal taxes for self occupied houses are not allowed to be reduced from GAV.
- 2) If municipal taxes are paid by tenant, then no deduction is allowed from GAV.
- 3) In the question we have been given 3 identical units, these should be taken as 3 different house properties. Unit 1 and unit 2 are self occupied and if more than 1 unit of house property is self occupied then any 1 unit shall be taken as self occupied and other will be regarded as deemed to be let out.

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- 4) Interest u/s 24(b) is allowed to be reduced on the accrual basis, therefore full interest of Rs. 36,000 has been considered.

Calculation of income from business and profession

Income from poultry farming	4,00,000
Income from share trading	88,500
Less: Brought forward loss	(38,500)
Income under the head of PGBP	4,50,000

NOTE: If a person has business of dealing in shares then STT paid by him is allowed as his business expenses.

Calculation of income from other sources

Income from horse races	30,000
Interest from company deposits	15,100
Rent of furniture, clubbed under section 60	26,000
Income under the head of other sources	71,100

Question 3 (a) Mr. John commenced a proprietary business in the year 2000. His capital as on 1/4/2008 was Rs. 6,00,000. On 10/4/2008 his wife gifted Rs. 2,00,000 which he invested in the business on the same date. Mr. John earned profit from his proprietary business as given below:

PY 2008-2009 = Profit Rs. 3,00,000

PY 2009-2010 = Profit Rs. 4,40,000

Compute the Income from business chargeable to tax in the hands of Mr. John for the AY 2010-2011. During the PY 2009-2010, he sold a vacant site which resulted in chargeable long-term capital gain of Rs. 5,00,000. The vacant site was sold on 20/12/2009. Compute the total income and tax liability of Mr. John and the installments of advance tax payable for the PY 2009-10. **8 marks**

Question 3 (b) Mr. Prakash has the following Assets which are eligible for depreciation at 15% on Written Down Value (WDV) basis :

1/4/2006	WDV of plant 'X' and Plant Y	Rs. 2,00,000
10/12/2009	Acquired a new plant 'Z' for	Rs. 2,00,000
22/1/2010	Sold Plant Y for	Rs. 4,00,000
	Expenditure incurred in connection with transfer	Rs. 10,000

Compute depreciation claim/chargeable capital gain if any, for the AY 2010-2011. **7 marks**

Solution:

Q3 (a) Calculation of the business income of Mr. John for the AY 2010-2011

The following amount of business profits is taxable for Mrs. John and balance is taxable for Mr. John

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Taxable Income earned X Amount invested out of asset transferred on the first day of PY
Total investment of transferee on the first day of the PY

Taxable income for the PY 2009-2010 = 4,40,000
 Amount invested out of the asset transferred by Mrs. John = 2,00,000
 Total investment of Mr. John as on 1/4/2009
 (6,00,000 + 2,00,000 + 3,00,000) = 11,00,000
 So business profits taxable for Mrs. John shall be = $4,40,000 \times 2,00,000 / 11,00,000 = 80,000$
 Business profits taxable for Mr. John shall be $4,40,000 - 80,000 = 3,60,000$

Calculation of total income and tax liability of Mr. John for the PY 2009-2010

Business income	3,60,000
Capital gains (LTCG)	5,00,000
Total / taxable income	8,60,000
Tax on LTCG @ 20%	1,00,000
Tax on normal income	26,000
Total tax	1,26,000
Add: primary education cess @ 2%	2,520
Add: secondary and higher education cess	1,260
Total tax liability	1,29,780

Calculations of installments of advance tax u/s 211

Due dates	Installment	
15/9/2009	30% of 26,780	8,034
15/12/2009	60% of 26,780 Less 1 st installment	8,034
15/3/2010	100% of 1,29,780 Less 1 st and 2 nd installment	1,13,712
Total amount		1,29,780

Q3 (b)

Calculation of WDV of the block as on 1/4/2009

Opening value of the block as on 1/4/2006	2,00,000
Less: Depreciation @ 15%	30,000
VALUE OF THE BLOCK AS ON 1/4/2007	1,70,000
Less: Depreciation @ 15%	25,500
Opening value of the block as on 1/4/2008	1,44,500
Less: Depreciation @ 15%	21,675
Opening value of the block as on 1/4/2009	1,22,825

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Calculation of depreciation under the block of assets method

Opening value of the block		1,22,825
Add: Value of asset purchased and put to use		2,00,000
Less: Money received on the sale of the asset	Restricted to the value of the block	3,22,825
Closing value of the block		NIL
Depreciation		NIL

Calculation of capital gains u/s 50

Sale consideration	4,00,000
Less: Selling expenses	10,000
Net sale consideration	3,90,000
Less: Value of the block	3,22,825
STCG	67,175

Question 4 (a) State with reasons, whether tax deduction at source provisions is applicable to the following transactions and if so, the rate of tax deduction:

1. Insurance Company paid Rs. 45,000 as Insurance Commission to its agent Mr. Hari.
2. X & Co. (Firm) engaged in wholesale business assigned a contract for construction of its godown building to Mr. Ravi, a contractor. It paid Rs. 25,00,000 to Mr. Ravi as contract payment.
3. AB Ltd. allowed a discount of Rs. 50,000 to XY & Co. (a firm) on prompt payment of its dues towards supply of automobile parts.
4. Y & Co. engaged in real estate business conducted a lucky draw and gave Maruti car to a prize winner.

Note: Assume that all the facts given above relate to Financial Year 2009-10.

8 marks

Question 4 (b) Mr. Banerjee furnishes you the following details for the year ended 31/3/2010:

Income (loss) from house property	Rs.
House-1	36,000
House-2-Self occupied	(20,000)
House-3	60,000
Profits and gains from Business or Profession	
Textile Business	2,00,000
Automobile Business	(3,00,000)
Speculation Business	2,00,000
Capital Gains	
Long-term capital gain from sale of shares (STT paid)	1,50,000
Long-term capital gain from sale of vacant site	2,00,000
Short-term capital loss from sale of building	1,00,000

(Note: Assume that the figures given above are computed and arrived at after considering eligible deductions).

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Other sources :

Gift from a Friend (non-relative) on 5.6.2009	60,000
Gift from Maternal Uncle on 25.2.2010	1,00,000
Gift from Grandfather's Younger Brother on 10.2.2010	1,00,000

Compute the total income of Mr. Banerjee for the AY 2010-2011.

6 marks

Solution:

Q4 (a) (1) TDS on insurance commission : TDS provisions are applicable u/s 194D

Insurance company paying commission to Mr. Hari will have to do TDS @10% of Rs. 45,000 at the time of credit or payment whichever is early. No TDS would have been done by the company if the commission would have been Rs. 5000 or less.

Q4 (a) (2) TDS on Contract payment: TDS provisions are applicable u/s 194C

If we assume that contract was assigned and payment was made to Mr. Ravi before 1/10/2009 then the firm is liable to do TDS @ 2% of the amount of Rs. 25,00,000

If we assume that contract was assigned and payment was made to Mr. Ravi on or after 1/10/2009 then the firm is liable to do TDS @ 1% of the amount of Rs. 25,00,000.

Q4 (a) (3) TDS on prompt payment: No TDS is applicable on the discount given on the prompt payment by the firm.

Q4 (a) (4) TDS on winnings: TDS provisions are applicable u/s 194B

Y & Co. giving the winnings from the lucky draw is liable to do TDS. Since winnings are in kind, Y & Co. has to make sure that the winner deposits the amount of tax at 30% on the market value of the car and only then car should be released.

Q4) (b) Calculation of the total income of Mr. Banerjee for the AY 2010-2011

House Property Income	House 1	36,000	
	House 2	(20,000)	
	House 3	60,000	76,000
Business Income	Textile business	2,00,000	
	Speculation business	2,00,000	
	Automobile business	(3,00,000)	1,00,000
Capital gains	LTCG from shares, STT is paid	Exempt u/s 10(38)	
	LTCG from the sale of vacant site	2,00,000	
	STCL from sale of building	(1,00,000)	1,00,000
Other sources	Gift from friend - non relative	60,000	
	Gift from relative	Exempt u/s 56	
	Gift from brother of grandfather – non relative	1,00,000	1,60,000
Total income / taxable income			4,36,000

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Question 5. Answer the following with reference to Income-tax Act, 1961: **4 marks each**

- (a) Briefly explain the term 'Manufacture' defined in Section 2 (29BA).
- (b) In whose hands the income from an asset is chargeable to tax in the case of transfer which is not revocable during the life time of the beneficiary/transferee?
- (c) List the conditions for deduction under Section 80-ID for hotels located in specified district having "World Heritage Site".
- (d) State the provisions for self assessment prescribed under Section 140A of the Act.

Q 5 (a) Section 2(29BA): Definition of manufacture:

'Manufacture' with all its grammatical variations, shall mean a change in a non-living physical object or article or thing:

- (a) resulting in transformation of the object or article or thing into a new and distinct object or article or thing having a different name, character and use; or
- (b) bringing into existence of a new object or article or thing with a different chemical composition or integral structure

Q 5(b) Clubbing of Income: section 61 and section 63

Revocable transfer has been defined in section 63. Income from asset transferred under revocable transfer shall be taxable in the hands of transferor. However revocable transfer does not include any other transfer which is not revocable during the lifetime of the transferee.

As per section 61, in case of revocable transfer income from the asset transfer is taxable for the transferor but if transfer is not revocable during the life time of the transferee then income from the asset shall be taxable in the hands of the transferee and not the transferor.

Q 5(c) World Heritage Sites: section 80-ID

- 1) Deduction is allowed if assessee has business of hotel located in the specified area, if such hotel is constructed and starts functioning at any time on or after 1/4/2007 but on or before 31/3/2010.
- 2) Specified district having a World Heritage Site means the districts of Agra, Jalgaon, Aurangabad, Kancheepuram, Puri, Bharatpur, Chhatarpur, Thanjavur, Bellary, South Parganas, Chamoli, Raisen Gava, Bhopal, Panchmahal, Kamrup, Goalpara, Nagaon, North Goa, South Goa, Darjeeling & Nilgiri.
- 3) Deduction shall be 100% of profits and gains derived from such business. Period of deduction shall be equal to 5 consecutive assessment years beginning from the assessment year in which the hotel starts functioning.
- 4) The deduction shall be available only if —
 - (a) eligible business is not formed by splitting up, or reconstruction, of an already existing business
 - (b) the eligible business is not formed by the transfer to a new business of a building previously used as a hotel.
 - (c) the eligible business is not formed by the transfer to a new business of machinery or plant previously used for any purpose
 - (d) the assessee furnishes along with the return of income, the report of an audit in such form and

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containing such particulars as may be prescribed, and duly signed and verified by an accountant certifying that the deduction has been correctly claimed.

Q 5(d) Self assessment: Section 140A:

An assessee is required to furnish his return of income and before filling his return he has to find out if any tax or interest is payable by him. The tax and interest so determined has to be paid by him before submitting return of income. This is called self assessment and tax is called self assessment tax.

In other words If any tax is payable on the basis of ROI then an assessee shall work out his taxable income and compute his tax liability and interest thereon (if any). Such amount of tax after adjusting advance tax paid by him or TDS done has to be deposited before filing return of income. This concept is known as self-assessment.

This is a voluntary payment of income tax by the assessee. If such payment is not made then assessee shall be known as assessee in default. If assessee does not pay self-assessment tax then he shall be liable to pay simple interest of 1% pm or part of the month under section 220(2) and a penalty which is to be determined by assessing officer. However amount of penalty shall not exceed 100% of the tax payable: Section 221(1).

Question 6.: Answer the following:

2 marks each

- (a) Is Service tax payable on free-service?
- (b) State the due dates for payment of Service tax in the case of an individual rendering taxable service.
- (c) A Company located in the State of Jammu & Kashmir rendered service in Delhi. Is the service provided by the Company liable for Service tax?
- (d) Do you agree with the statement that 'Tax cannot be evaded under VAT system'?
- (e) Mr. Raj rendered taxable service in February, 2010. The amount was however realised on 18/4/2010. What is the due date for payment of Service tax?

Solution:

Q6 (a) Free services:

As per the circular no 62/11/2003 issued by CBEC, If the services are provided free of cost, there shall be no service tax payable even if services are taxable. Thus no service tax is payable when the value of the services is zero. However this principal applies only when there is really a free service and not when something is recovered under some means either in monetary or non monetary.

Q6(b) Due dates for the payment of service tax:

If the service provider is an individual the service tax shall be paid to the Central Government by the

- 1) 5th of the month immediately following the quarter in which the payments are received. (6th day in the case of e-payment.)
- 2) If the payment is received during the month of March, then it due date shall be 31st day of March of the calendar year (even in case of e-payment)

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Q6(c) Services provided outside the state of Jammu and Kashmir:

There shall be no service tax on the services provided in the state of Jammu and Kashmir. However if service provider is in the state of Jammu and Kashmir and provides services to anyone outside the state of Jammu and Kashmir then service tax shall be imposed on such services rendered. Therefore services provided in Delhi by the company located in Jammu and Kashmir will be subject to service tax.

Q6 (d) Tax Evasion under VAT:

Under VAT, credit of input tax paid is allowed against the liability of tax on the final product sold. If proper records are not kept in respect of various inputs, it is not possible to claim credit. Since input tax is allowed to be set off from the ultimate tax burden thus it leads to avoidance of multiple taxation. It totally eliminates cascading effect and also discourages tax evasion since suppression of purchases will lead to loss of revenue to the dealer.

Q6 (e) Service tax at realization of payment:

Service tax is payable at the time of realization of the amount for services rendered and not at the time when billing was done. Thus charge of service tax is on the event of providing services but payment of service tax to the Government is deferred till the receipt of the value of taxable services. Therefore in this case liability to pay service tax arises when payment is received in the month of April. Since it is a case of an individual, due date for the payment shall be 5/7/2010 for the quarter ending June 2010

Question 7: X & Co. received the following amounts:

Date of receipt	Nature of receipt	Amount	Timing of providing Service
20/4/2009	For service	1,00,000	Services were rendered in July, 2009
30/6/2009	Advance for service	5,00,000	Services were rendered in July and August, 2009
05/08/2009	For service	50,000	Services were rendered in March, 2009
10/09/2009	Advance for service	3,50,000	A sum of Rs.50,000 was refunded in April, 2010 after termination of agreement. For the balance amount, service was provided in September, 2009.

Compute:

- (i) The amount of taxable service for the first two quarters of the PY 2009-2010.
(ii) The amount of Service tax payable.

6 Marks

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Solution:

Calculation for the amount of taxable value of services and service tax liability

Quarter	Value of taxable services on receipt basis	Service tax @ 10%	Education cess @ 2% + 1%	Service tax liability	Due date for the payment
April to June 2009	6,00,000	60,000	1,800	61,800	5/7/2009
July to Sep 2009	4,00,000	40,000	1,200	41,200	5/9/2009

NOTES:

- 1) Service tax is calculated even on the advance amount received.
- 2) Rs. 50,000 has been refunded in April 2010, therefore the service tax on such amount will be adjusted or refunded in the financial year 2010-2011.
- 3) We assume that X & Co. is not a small service provider and therefore exemption of Rs. 10 Lakhs has not been provided.
- 4) We assume that above mentioned amounts are not inclusive of service tax. But if we assume that above mentioned amounts are inclusive of service tax then calculations will be as under.

Calculation for the amount of taxable value of services and service tax liability, if amounts are inclusive of service tax

Quarter	Value of taxable services on receipt basis	Service tax @ 10%	Education cess @ 2% + 1%	Service tax liability	Due date for the payment
April to June 2009	5,43,971	54,397.1	1,631.92	56,029	5/7/2009
July to Sep 2009	3,62,647	36,264.7	1,087.9	37,352.6	5/9/2009

Question 8 : Answer the following:

- (a) Compute the VAT liability of Mr.P.Kapoor for the month of October, 2009, using the 'Invoice method' of Computation of VAT.

Purchases from the local market (Includes VAT @ 4%)	Rs.65,000
Storage cost incurred	Rs. 750
Transportation Cost	Rs. 1,750
Goods sold at a margin of 5% on the cost of such goods	
VAT rate on sales 12.5%	

- (b) State briefly about Provisional payment of Service tax.
 (c) What are three variants of VAT? Which of these methods is most widely used and why?

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Solution:**Q8 (a)****Calculation of VAT liability of by Mr. Kapoor**

Purchase price (Ex-VAT)	65,000 /104 X 100	62,500
Storage cost		750
Transportation cost		1,750
Total cost		65,000
Profit margin	5% of cost	3,250
Actual sale price		68,250

Output VAT

$$68250 \times 12.5\% = 8,531.25$$

Input VAT

$$65000 / 104 \times 4 = 2,500$$

VAT Liability is the difference between input VAT and output VAT

$$8531.25 - 2500 = 6031 \text{ (rounded off)}$$

Q8 (b) Provisional payment of service tax:

In case service provider is unable to correctly estimate the actual amount of service tax liability at the time of payment, for any month or quarter then he may make a written request to assistant or deputy commissioner of central excise for making the payment on the of the service tax on the provisional basis. For the purposes of provisional assessment, at the time of filling the return, the service provider is required to file a statement in form ST-3A giving details of the difference between the service tax deposited and service tax liable to be paid. The assistant or deputy commissioner of central excise, on the basis of ST-3A may complete the assessment after calling for necessary documents if needed.

Q8 (c) Variants of VAT

VAT could be levied under the following three variants:

- a) Gross product variant.
- b) Income variant.
- c) Consumption variant.

GROSS PRODUCT VARIANT: FEATURE

This variant allows deductions of VAT paid on all purchases of raw materials and components but no deduction is allowed for VAT paid on capital inputs. That is, taxes on capital goods such as plant and machinery are not deductible from the output tax in the year of purchase or in the subsequent years.

INCOME VARIANT: FEATURE

This Variant of VAT allows deductions of VAT paid on all purchases raw materials and components as well as deduction of VAT on capital goods at the rate of depreciation on capital goods.

SCHEDULE OF NEW BATCHES FOR NOV 2010 EXAMS

VENUE	DATE OF START	DAYS	TIMINGS	FEES
LAXMI NAGAR	25/5/2010	T/T/S	7-11 AM	Rs. 4,500
ROHINI	28/5/2010	M/W/F	6-9 PM	Rs. 9,000
HUDSON LINE	28/5/2010	M/W/F	7-11 AM	Rs. 9,000

CONSUMPTION VARIANT: FEATURE

Consumption variant of VAT allows deduction of VAT paid on all business purchases including capital inputs. It does not distinguish between capital goods and raw material.

Among the three variants consumption variant is most widely used in the different parts of the world but **we follow Income variant in India.**

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