Qn. 1 Mr. Dinesh Karthik, a resident individual aged 45, furnishes the following information pertaining to the year ended 31.3.2010 : [16 marks]

(i) He is a partner in Badrinath & Co. He has received the following amounts from the firm :

Interest on capital at 15%	Rs. 3,00,000
Salary as working partner (at 1% of firm's sales)	Rs. 90,000

(ii) He is engaged in a business in which he manufactures wheat flour from wheat. The Profit and Loss account pertaining to this business (summarised form) is as under :

To	Rs.	By	Rs.
Salaries	1,20,000	Gross profit	12,50,000
Bonus	48,000	Interest on Bank FD	
		(Net of TDS 5,000)	45,000
Car expenses	50,000	Agricultural income	60,000
Machinery repairs	2,34,000	Pension from LIC Jeevandhara	24,000
Advance tax	70,000		
Depreciation			
Car	3,00,000		
Machinery	1,25,000		
Net profit	4,32,000		------------
	13,79,000		13,79,000

Opening WDV of assets are as under :

	Rs.
Car	3,00,000
Machinery	6,50,000
(Used during the year for 170 days)	
Additions to machinery	
New purchased on 23.9.2009	2,00,000
New purchased on 12.11.2009	3,00,000
Old purchased on 12.4.2009	1,25,000
(All assets added during the year were put to use immediately after purchase)	

Of the total bonus amount, Rs. 15,000 was paid on 11.10.2009.

One-fifth of the car expenses are towards estimated personal use of the assessee.

(iii) In March, 2008, he had sold a house at Chennai. Arrears of rent relating to this house amounting to Rs. 75,000 was received in February, 2010.

(iv) Details of his Savings and Investments are as under :

	Rs.
Life Insurance premium for policy in the name of his major son employed in LMN Ltd. at a salary of Rs. 6 lacs p.a. Sum assured Rs. 2,00,000	50,000
Contribution to Pension Fund of National Housing Bank (This was met partially from out of premature withdrawal of deposit in Post Office Time Deposit made on 12.3.2006 Principal component Rs. 55,000 and Interest Rs. 5,000)	70,000
Medical Insurance premium for his father aged 70, who is not dependent on him	22,000

You are required to compute the total income of Mr. Dinesh Karthik for the assessment year 2010-11 and the tax payable by him. Also indicate whether interest, if any, under sections 234A and 234B are payable, assuming that the return was filed on 28th September, 2010.

Computation of interest, if any, is NOT required.

Ans. 1 **Computation of Gross Total Income for the Assessment Year 2010-11**

Income from Salary		Nil
Income from House Property		
Arrear of rent received	75,000	
Less : Deduction u/s 24 @ 30%	22,500	52500

<u>Income from PGBP</u>

Income from Wheat flour business **(WN. 1)**		536250	
Salary to working partner **(WN. 2)**		90000	
Interest on capital $\left(\frac{300000}{15\%} \times 12\%\right)$ **(WN. 2)**		240000	866250

<u>Income from other sources</u>

Interest on Bank FD gross		50000	
Pension from LIC Jeevan Dhara		24000	
<u>Premature withdrawal from Post Office</u>			
Principal	55000		
Interest	5000	60000	134000
Gross Total Income			1052750

Less : <u>Deduction under chapter VIA</u>

Deduction u/s 80 C	LIC Premium (200000 x 20%)	40000		
Deduction u/s 80 CCC	Pension fund	70000		
		110000		
	BUT SUBJECT TO MAXIMUM LIMIT OF		100000	
<u>Deduction u/s 80 D</u>				
Medical Insurance premium Rs. 22000 but subject to maximum of			20000	120000
Total Income				932750

<u>Calculation of Tax Liability of Mr. Dinesh Kartik for A. Y. 2010 – 11</u> : -

<u>With Agricultural Income</u> : -

(a) For first Rs. 160000	NIL	
(b) For next Rs. 140000 @ 10%	14000	
(c) For next Rs. 200000 @ 20%	40000	
(d) For balance Rs. 492750 @ 30%	147825	

Tax		201825

Less : - Tax on (Basic exemption + Agricultural Income)

(a) For first Rs. 160000	NIL	
(b) For balance Rs. 60000 @ 10%	6000	
	----------	6000
Gross Tax liability =		195825
Add : Education cess @ 3 % =		5875
		201700
Less : Advance tax paid =		70000
TDS =		5000

Net Tax liability		126700

Interest u/s 234A: The due date of filing of ROI for Mr. Kartik is 31st july 2010. Since he has filed his ROI on 28th Sep. 2010 therefore interest u/s 234A shall be charged @1% per month for the period of delay.

Interest u/s 234B : Since Mr. Kartik has not paid 90% of his advance tax on or before 31st march 2010 therefore interest u/s 234B shall be charged.

Working Note : -

(1) Profit as per P/L A/c		432000
Add : Advance Tax	70000	
Depreciation for separate consideration	425000	
1/5 th of Car Expenses for personal use u/s 38(2)	10000	
Bonus not paid u/s 43B	15000	520000

Less : Receipts not taxable under PGBP head/ exempt from tax				
Interest on Bank F. D		45000		
Agriculture Income exempt u/s 10		60000		
Pension from LIC Jeevan Dhara exempt u/s 10		24000		129000
Less : Allowable Expenses				
Depreciation u/s 32 on Car (300000 x 20%)		60000		
Less : 1/5th Disallowed u/s 38(2) for personal use		12000	48000	
Depreciation u/s 32 on block of Machine				
Opening WDV		650000		
Add : Cost of asset acquired during the year		625000		
		1225000		
Less : Moneys payable in respect of machine sold		NIL		
WDV of the block for the previous year 2009-2010		1225000		
Depreciation				
On opening WDV (650000 x 15%)	97500			
On addition for full year (200000 x 15%)	30000			
On addition for full year (125000 x 15%)	18750			
On addition for ½ year (300000 x 7.5%)	22500			
Additional depreciation on new machine acquired during the p.y.				
For full year (200000 x 20%)	40000			
For ½ year (300000 x 20% x 1/2)	30000		238750	286750
				536250

Note 2 : As per Sec 28(viii), any interest, salary, bonus, commission or remuneration due to or received by a partner of a firm from such firm. Where any such interest, salary etc has been disallowed u/s 40(b) in the case of the firm, the same shall not be taxed in the case of the partner.

Qn. 2 (a) Mr. Tenzingh is engaged in composite business of growing and curing (further processing) Coffee in Coorg, Karnataka. The whole of coffee grown in his plantation is cured. Relevant information pertaining to the year ended 31.3.2010 are given below : [6 marks]

	(Rs.)
WDV of Car as on 1.4.2009	3,00,000
WDV of machinery as on 31.3.2009 (15% rate)	15,00,000
Expenses incurred for growing coffee	3,10,000
Expenditure for curing Coffee	3,00,000
Sale value of cured Coffee	22,00,000

Besides being used for agricultural operations, the car is also used for personal use; disallowance for personal use may be taken at 20%. The expenses incurred for car running and maintenance are Rs. 50,000. The machines were used in coffee curing business operations.

Compute the income arising from the above activities for the assessment year 2010-11. Show the WDV of the assets as on 31.3.2010.

Ans. 2 (a) Income from Tenzingh
(for the assessment year 2010-2011)

			Rs.
Sales			22,00,000
Less : Expenses -			
Incurred in growing coffee		310000	
Expend for curing coffee		300000	
Depreciation on block of machinery (1500000 x 15%)		225000	
Depreciation on block of Car 300000 x 15%	= 45,000		
Less : Disallowed u/s 38(2) for personal use @20%	= 9,000	36000	
Running & Maintenance Exp of Car	50000		

Less : Disallowed u/s 38(2) for personal use @20% =	10000	40000	9,11,000
Composite Income			12,89,000

Business Income = 25% x 12,89,000
= 3,22,250/-

Agricultural Income = 75% x 12,89,000
= 9,66,750 /-

	Opening WDV	Depreciation for the A/Y 2010-2011	Closing WDV
Block of Machinery	Rs. 15,00,000	Rs. 2,25,000	Rs. 12,75,000
Block of Car	Rs. 3,00,000	Rs. 36,000	Rs. 2,64,000

Note : **RULE 7B: INCOME FROM THE MANUFACTURE OF COFFEE**

(1) Income derived from the sale of coffee grown and cured by the seller in India shall be computed as if it were income derived from business, and 25% of such income shall be deemed to be income liable to tax.

(2) Income derived from the sale of coffee grown, cured, roasted and grounded by the seller in India, with or without mixing chicory or other flavoring ingredients, shall be computed as if it were income derived from business, and 40% of such income shall be deemed to be income liable to tax.

Qn. 2 (b) Mr. Raj Kumar sold a house to his friend Mr. Dhuruv on 1st November, 2009 6 *^ for a consideration of Rs. 25,00,000. The Sub-Registrar refused to register the document for the said value, as according to him, stamp duty had to be paid on Rs. 45,00,000, which was the Government guideline value. Mr. Raj Kumar preferred an appeal to the Revenue Divisional Officer, who fixed the value of the house as Rs. 32,00,000 (Rs. 22,00,000 for land balance for building portion). The differential stamp duty was paid, accepting the said value determined. Assuming that the fair market value is Rs. 32,00,000, what are the tax implications in the hands of Mr. Raj Kumar and Mr. Dhuruv for the assessment year 2010-11 ? Mr. Raj Kumar had purchased the land on 1st June, 2006 for Rs. 5,19,000 and completed the construction of house on 1st October, 2007 for Rs. 14,00,000.

Cost inflation indices may be taken as 519 for the financial year 2006-07, 582 -for the financial year 2007-08 and 632 for the financial year 2009-10. **[6 marks]**

Ans. 2 (b) **Computation of Taxable income of Mr. Raj Kumar**

For Land

Period of holding : 1.6.2006 to 31.10.2009 i.e. more than 36 months therefore Land is a Long term Capital Asset.

Sales consideration	2200000
Less : Indexed cost of acquisition $519000 \times \frac{632}{519}$	632000

Long term capital gain	1568000

For Building

Period of holding : 1.10.2007 to 31.10.2009 i.e. less than 36 months therefore Building is a Short term Capital Asset.

Sales consideration	1000000
Less : Cost of Acquisition	1400000

Short term capital loss =	(4,00,000)

Note : u/s 70 Short Term Capital can be set off from long term capital gain. Therefore total capital gain taxable will be Rs. 11,68,000. It is assumed that the other income of Mr. Raj kumar is more than minimum amount not chargeable to tax i.e. Rs. 1,60,000.

Net tax liability of Mr. Raj kumar for the Assessment Year 2010-2011: -

Long term capital gain on land @20% u/s 112	
Tax liability (Rs. 11,68,000 x 20%)	= Rs. 233600
Add : Education Cess @3%	= Rs. 7008
Total	Rs. 240608
	Or Rs. 240610

Net tax liability of Mr. Dhuruv for the Assessment Year 2010-2011: - There will be no tax liability in hands of Mr. Dhuruv.

Qn. 3. From the following particulars of Income furnished by Mr. Anirudh pertaining to the year ended 31.3.2010, compute the total income for the assessment year 2010-11, if he is : [10 marks]

(i) Resident and ordinary resident;
(ii) Resident but not ordinarily resident;
(iii) Non-resident :

Particulars	Amount (Rs.)
(a) Profit on sale of shares in Indian Company received in Germany	15,000
(b) Dividend from a Japanese Company received in Japan	10,000
(c) Rent from property in London deposited in a bank in London, later on remitted to India through approved banking channels	75,000
(d) Dividend from RP Ltd., an Indian Company	6,000
(e) Agricultural income from lands in Gujarat	25,000

Ans. 3

Particulars	**Resident & Ordinarily Resident (Rs.)**	**Resident but not ordinarily resident (Rs.)**	**Non-Resident (Rs.)**
Profit on sale of shares of Indian company received in Germany **(Note 1)**	15000	15000	15000
Dividend from a Japanese company received in Japan	10000	--	--
Rent for house property in London deposited in Bank of London	75000	--	--
Dividend from Indian Company Exempt u/s 10(34)	Exempt	Exempt	Exempt
Agricultural Income from lands in Gujarat exempt u/s 10(i)	Exempt	Exempt	Exempt
Total Income	**100000**	**15000**	**15000**

Note 1: Profit on sale of shares of Indian Company is exempt u/s 10(38) provided the it is long term capital gain and securities transaction tax is paid on that gain.

Qn. 4. Answer the following questions with regard to the Provisions of the Income tax Act, 1961 : [3x4=12 marks]

(a) State the concessions granted to transport operators from 1st October, 2009 onwards in the context of cash payments under section 40A(3) and deduction of tax at source under section 194-C.

(b) What are the conditions to be fulfilled by a Charitable Trust under section 12A for applicability of exemption provisions contained in sections 11 and 12?

(c) What are the particulars required to be furnished with the return of income, as per section 139(6) ?

Ans. 4 (a) Concessions granted to Transport operators from 1.10.2009:

(1) Section 40(A)(3) : Where the assessee incurs any expenditure in respect of which a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or account payee bank draft, exceeds Rs. 20,000, no deduction shall be allowed in respect of such expenditure.

Section 40(A)(3A) : Where an allowance has been made in the assessment for any year in respect of any liability incurred by the assessee for any expenditure and subsequently during any previous year (hereinafter referred to as subsequent year) the assessee makes payment in respect thereof, otherwise than by an account payee cheque drawn on a bank or account payee bank draft, the payment so made shall be deemed to be the profits and gains of business or profession and accordingly chargeable to income-tax as income of the subsequent year if the payment or aggregate of payments made to a person in a day, exceeds Rs. 20,000:

However, in both the above two cases, where payment is made on or after 1-10-2009 for plying, hiring or leasing goods carriages, the payment shall have to be made by account payee cheque or account payee draft if the amount of payment exceeds Rs. 35,000 instead of Rs. 20,000 applicable in all other cases.

(2) Provisions for payments and tax deducted at source to transporters: From 1.10.2009 the Act has exempted payments to transport operators from the purview of TDS. However, this would only apply in cases where the operator furnishes his Permanent Account Number(PAN) to the deductor. Deductor who make payments to transporters without deducting TDS (as they have quoted PAN) will be required to intimate these PAN details to the Income Tax Department in the prescribed format.

(3) W.E.F. 1.10.2009 If the contractor is an individual or HUF, TDS shall be made only at the rate of 1% and not at the rate of 2%.

Ans. 4 (b) A trust is required to apply for registration in Form 10A with the Commissioner of Income tax. It is to be noted that exemption will be available from the assessment year relevant to the financial year in which such application is made.

<u>Procedure for Registration [Sec. 12AA]</u>
The Commissioner, on receipt of an application for registration of a trust or institution shall –
- call for such documents or information from the trust or institution as he thinks necessary in order to satisfy himself about the genuineness of activities of the trust or institution; and
- make such inquiries as he may deem necessary in this behalf.

Where he is –
- satisfied about the objects of the trust or institution and the genuineness of its activities, he shall pass an order in writing registering the trust or institution. A copy of such order shall be sent to the applicant.
- Not so satisfied, he shall pass an order in writing refusing to register the trust or institution. A refusal-order shall not be passed unless the applicant has been given a reasonable opportunity of being heard.

<u>Time limit for registration</u>
Every order granting or refusing registration shall be passed before the expiry of 6 months from the end of the month in which the application was received.

Ans. 4 (c) Particulars required to be furnished with the Return of Income [Section 139(6)] : The prescribed form of the returns referred to in Sec 139(1) & Sec 139(3), and in Section 142(1)(i) shall, in such cases as may be prescribed, require the assessee to furnish :

a. the particulars of income exempt from tax,
b. assets of the prescribed nature,
c. value and belonging to him,
d. his bank account and credit card held by him,
e. expenditure exceeding the prescribed limits incurred by him under prescribed heads and
f. such other outgoings as may be prescribed.

Qn 5. Provide brief answer to the following questions on Service tax : [4 x 2 = 8 marks]

(a) Is Service tax payable in respect of services provided in the Indian territorial waters ?
(b) Is Service tax leviable on fee collected by Public authorities while performing statutory functions under the provisions of law ?
(c) Can an assessee file a revised Service tax return ?
(d) Explain the term "Commercial training or Coaching centre."

Ans. 5 (a) Chapter V of the Finance Act, 1994 (i.e. the service tax law), extends to the whole of “India” except the state of Jammu and Kashmir. Since 'India' includes territorial waters of India, the services provided in the territorial waters of India (i.e. up to 12 nautical miles from the land mass of India) are also liable to service tax.

Ans. 5 (b) Clarification on service tax on service provided while performing statutory duty by any authority under law [Circular No.96/2007 ST dated 23-08-2007]

Sovereign/public authorities perform functions assigned to them under the law in force, known as "statutory functions". Authorities providing such functions, required to be performed as per law, may collect specific amount or fee and the amount so collected is deposited into government account. The fee or amount collected as per the provisions of the relevant statute for performing such functions is in the nature of a compulsory levy. Such activities are purely in public interest and are undertaken as mandatory and statutory functions. These are not to be treated as services provided for a consideration. Therefore, such activities assigned to and performed by a sovereign / public authority under the provisions of any law, do not constitute taxable services. Any amount / fee collected in such cases are not to be treated as consideration for the purpose of levy of service tax.

However, if a sovereign / public authority provides a service, which is not in the nature of statutory activity and the same is undertaken for a consideration (not a statutory fee), then in such cases, service tax would be leviable as long as the activity undertaken falls within the scope of a taxable service as defined.

Ans. 5 (c) Revised Return : An assessee may submit a revised return, in Form ST-3, in triplicate, to correct a mistake or omission, within 90 days from date of submission of original return.

Ans. 5 (d)

- Commercial training or coaching centre:
  - means any institute or establishment providing commercial training or coaching for imparting skill or knowledge or lessons on any subject or field other than the sports, with or without issuance of a certificate and includes coaching or tutorial classes
  - but does not include -
    a. pre-school coaching and training centre or
    b. any institute or establishment which issues any certificate or diploma or degree or any educational qualification recognised by law for the time being in force.

Qn 6. (a) Virat Kohli & Co., a partnership firm, is providing taxable legal consultancy services, for the second consecutive assessment year. The firm furnishes the following information relating to the services rendered, bills raised, amounts received relating to this service, for the year ended 31.3.2010 : [8 marks]

	Rs.
(i) Free services rendered to poor people (Value of the services computed on comparative basis)	40,000
(ii) Advances received from clients for which no taxable service has been rendered so far	5,00,000
(iii) Services billed to clients Gross amount (Service tax has been charged separately in all the bills; the firm follows mercantile system of accounting)	12,00,000
(iv) The firm has received the following amounts during the year :	
Relating to taxable services rendered in March, 2009 (excluding service tax at applicable rates and TDS under section 194-J of the IT Act, 1961 to the tune of Rs. 45,320)	5,44,680
Relating to taxable services rendered in current year 2009 (excluding Service tax at applicable rates and TDS under section 194-J of the IT Act, 1961 to the tune of Rs. 1,20,000)	9,80,000
(*includes Rs. 50,000 for appearance fee before Labour Court received from another firm)	
Service tax has been separately received for applicable items in (iv) above.	

You are required to compute the value of taxable services for the year ended 31.3.2010 and the Service tax payable, briefly explaining the treatment of each item above.

(b) Answer the following questions on Service tax : [9 marks]

(i) What is the scope of taxable service in respect of membership of Clubs or Associations ? State the exception to the same.

(ii) Does a service provider have an option to pay Service tax at a rate different from the general rate applicable on gross value of taxable services, in the case of purchase and sale of foreign currency ?

(iii) What is the late fee payable for delay in furnishing the Service tax return ? Can the same be waived ?

Ans. 6 (a) **Computation of value of taxable service and Service tax payable for the year ended 31.03.2010 in the hands of Virat Kohli & Co.**

Particulars	**Amount**
Free services to poor people (Note A)	Nil
Advance received from clients (Note B)	500000
Receipt for taxable services rendered in march 2009 (544680+45320) (Note c)	590000
Taxable services rendered in current year 2009 (980000+120000-50,000) (Note C)	10,50,000

Value of Taxable Services	21,40,000
Service Tax Payable $\left(21{,}40{,}000 \times \frac{10.30}{110.30}\right)$	1,99,837

Note A- No service tax is payable for services rendered free of cost hence the free service rendered to the poor people shall not be taxable.

Note B- Since service tax is payable on receipt basis, the advance received for the services not rendered shall be liable to tax when the advance is received for the same.

Note C- Payment received for the services given in past shall be taxed in the year of receipt since service tax is payable on receipt basis. The appearance fee by a lawyer for appearing in the court of law is exempt from service tax and hence Rs. 50,000 received for appearance fee before Labour Court shall not be liable to tax. TDS deducted is a part of receipt therefore will be added back.

Ans. 6 (b) (i) Inclusions in scope :

⇨ Charges recovered by clubs or associations for membership and providing various services.
⇨ Companies or societies are also liable to pay service tax.
⇨ Amounts paid by members for provisions of services to the guests of a member, amount paid for get-togethers and functions charged over and above the subscription amount.
⇨ Any additional fees and Life membership fees must be treated in same way as subscription.

Exemption to resident welfare association if member's contribution doesn't exceed Rs. 3,000 p.m. per member: The taxable service provided or to be provided, by a resident welfare association to its members is fully exempt from service tax, if -

(a) the sole criterion for its membership is the residential status of a person in a residential complex or locality, and

(b) total consideration received from an individual member by the said association for providing the said services does not exceed Rs. 3,000 per month.

Note: Resident welfare association is eligible to avail of exemption even if it is registered as a cooperative society with the Registrar of Co-operative Societies.

Ans. 6 (b) (ii) The person liable to pay service tax in relation to purchase or sale of foreign currency, including money changing, provided by a foreign exchange broker, including an authorised dealer in foreign exchange or an authorized money changer shall have the option to pay an amount calculated @ 0.25% of the gross amount of currency exchanged towards discharge of his service tax liability instead of paying service tax @ 10.30%.
However, such option shall not be available in cases where consideration for the service provided or to be provided is shown separately in the invoice, bill or challan issued by the service provider.

Ans. 6 (b) (iii) Penalty for delayed filing of return may be charged as per following schedule (subject to maximum of Rs.2000) :

Delay	Penalty
Up to 15 days	Rs. 500
16 to 30 days	Rs. 1000
31 days onward	Rs.1000 plus Rs.100 per day from 31 day onwards (subject to max of Rs.2000)

Where the amount of service tax payable is nil, the Central Excise Officer may, on being satisfied that there is sufficient reason for not filing the return, reduce or waive the aforesaid penalty.

Qn. 7. Answer the following questions on VAT : [4 x 2 = 8]

(a) What are the items aggregated in the Addition method to calculate the VAT payable ? When is this method mainly used ?

(b) Is any threshold exemption limit fixed for dealers to obtain VAT registration, as per the White Paper ? If yes, why is the same provided ?

(c) Is the VAT chain continued when a purchasing dealer opts for VAT composition scheme ? What is the loss to the seller and buyer opting for the composition scheme, and the subsequent buyers ?

(d) Can it be said that VAT brings about certainty to a great extent in the matter of interpretational issues ? If so, how ?

Ans. 7 (a) Under addition method of calculation of VAT the aggregate of all factor payments such as rent/depreciation of building, hire charges/depreciation of machinery, interest on capital, wages and salaries, etc and profit are aggregated.

This method is mainly used when the relevant details and Invoices of sales and purchases made by the dealer are not available and assessment of VAT liability is not possible through Invoice method.

Ans. 7 (b) In order to provide relief to small dealers, the White Paper provided that registration for VAT shall not be compulsory for dealers having annual turnover below a threshold limit (viz. Rs. 5 lakhs).
However, subsequently, the Empowered committee of State Finance Ministers allowed the States to increase the threshold exemption limit upto Rs. 10 lakhs. While the exemption limit upto Rs. 5 lakhs is applicable in all States, the increased exemption limit of upto Rs. 10 lakhs has been adopted only by a few states, as per their discretion.
The small dealers/business-man or big dealers form two separate classes, which cannot be treated alike under the law. The revenue earned from the two differs but not the cost of administration. Hence, in order to avoid increased cost of administration without much increase in revenue, and also with a view to provide relief to small dealers, the special schemes like threshold exemption are necessary. Thus, while the big dealers are not spared, the small dealers are freed from hassles of procedural compliance.

Ans. 7 (c) If the composition scheme is availed by a dealer then such dealer cannot avail input tax credit in respect of input tax paid. Hence the dealer will be loosing the input tax credit on purchases made by him. He will not be able to pass on the benefit of input tax credit, which will add to the cost of the goods.

The purchaser shall not get any tax credit for the purchases made by him from the dealer operating under the composition scheme. Therefore, as soon as a dealer opts for the composition scheme, the VAT chain will be broken, and the benefit of tax paid earlier will not be passed on to the subsequent buyers.

Ans. 7 (d) VAT system is based simply on transactions. Thus there is no need to go through complicated definitions like sales, sales price, turnover of purchases and turnover of sales. The tax is also broad-based and applicable to all sales in business leaving little room for different interpretations. Thus, this system brings certainty in the matter of interpretational issues to a great extent.

Qn. 8 (a) Mr. X, a dealer in Mumbai dealing in consumer goods, submits the following information pertaining to the Month of March, 2010 : [8 marks]

(i) Exempt goods 'A' purchased for Rs. 2,00,000 and sold for Rs. 2,50,000.

(ii) Goods 'B' purchased for Rs. 2,25,000 (including VAT) and sold at a margin of 10% profit on purchases (VAT rate 12.5%) ;

(iii) Goods 'C' purchased for Rs. 1,00,000 (excluding VAT) and sold for Rs. 1,50,000 (VAT rate 4%) ;

(iv) His unutilized balance in VAT input credit on 1.3.2010 was Rs. 1,500.

Compute the turnover, Input VAT, Output VAT and Net VAT payable by Mr. X,

(b) Answer the following questions on VAT : [3 x 3 = 9]

(i) What are the merits of VAT in the context of tax evasion, neutrality and transparency ?

(ii) State the importance of VAT invoice/tax invoice in administering VAT.
(iii) Discuss the tax consequences of Stock transfer under the VAT scheme.

Ans. 8 (a) **Computation of Turnover, Input VAT, Output VAT**

Particulars	Purchase	Input VAT	Sales	Output VAT
(i) Exempt goods 'A'	200000	Nil	250000	Nil
(ii) Goods B	200000	25000	220000	27500
(iii) Goods C	100000	4000	150000	6000
	500000	29000	620000	33500

Computation of Net VAT payable

Opening balance in INPUT VAT Credit	1500
(+) Current INPUT VAT Credit	29000
Total INPUT VAT (a)	30500
OUTPUT VAT (b)	33500
Net VAT Payable (b – a)	3000

Ans. 8 (b) (i) Tax evasion will be reduced - The adoption of VAT helps in reducing evasion of tax. There is self-assessment and, therefore, better tax compliance being less chances of tax evasion. It has the merit of 'self-policing' in that it induces businesses to demand invoice from their suppliers to enable them to obtain credit for the tax paid on their purchases against their total tax liability. Under a system where the tax is levied only at one stage, primarily at the first point of sale, as has been the predominant practice under state sales taxes, shifting the value added to subsequent stages can reduce tax liability. VAT serves to counter this by bringing the value added at all stages under the tax. As against the system of administration of sales tax, VAT requires that all the dealers must issue tax invoices. The subsequent dealer would maintain these invoices in order to benefit from tax deduction. This would enable the tax authority to cross check the declared transactions between taxpayers, consequently reducing the propensity to evade tax. In fact, the requirement of maintaining the vouchers (invoices) works as self-policing, the evasion of tax.

VAT has a novel feature of tax transparency. That is, the total burden of tax on a particular commodity is clearly seen from the transactions. Hence, the economic analysis of the tax structure is convenient. Also, in international trade, this enhances tax neutrality. Under the sales tax system it is difficult to estimate the exact amount of refund for export. In most cases, the statistical evidence suggests that the tax on inputs and raw materials or on capital goods is under-compensated.

The greatest virtue of VAT lies in its neutrality that is, non-interference with the choices or decisions of economic agents in the matter of location of business, as well as business organization. Under VAT, the tax liability does not depend on the number of times a product is traded before reaching the final consumer or how much of the value is added at what stage in the production-distribution process. There is, thus, no incentive for companies to integrate vertically or for shunning specialization unlike under a regime of turnover tax or a sales tax that makes no allowance for taxes paid at earlier stages. Under VAT, the allocation of resources is left to be decided by the free play of market forces and competition and not driven by tax considerations.

Ans. 8 (b) (ii) VAT invoice is important because it -

- determines the input tax credit;
- helps in preventing cascading effect of taxes;
- helps in implementing VAT i.e. multi-point taxation on the value addition;
- promotes assurance of invoices;
- assists in performing audit and investigation activities effectively;
- checks evasion of tax.

Ans. 8 (b) (iii) If any stock is purchased within the state and VAT credit is availed of the input tax paid and the same is transferred out of state as stock transfer/consignment transfers/branch transfer, input tax paid in excess of 4% will be eligible for tax credit and the balance if any shall be reversed and no credit shall be available for the same.