Relevant Extract of Preface of Direct Tax Module issued by the ICAI

Direct tax laws and Indirect tax laws are important elements of the core competence areas of the Chartered Accountants. A thorough knowledge of direct tax laws and indirect tax laws is, therefore, necessary for the students of the CA Final course. In the new Final course, "Direct Tax Laws" constitutes Paper–7. Students are expected to acquire advanced knowledge of the provisions of direct tax laws after undergoing this course and apply such knowledge to various situations in actual practice.

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The taxation laws in our country undergo many amendments. In order to help the students to update their knowledge relating to the statutory developments in the field of direct and indirect tax laws, the Board of Studies brings out, every year, a "Supplementary Study Paper" containing all the amendments in direct and indirect taxes. This is an essential read for all our students. Another important publication, "Select cases in Direct and Indirect Taxes – An essential reading for the final course", is meant for updating the knowledge regarding judicial decisions.

A word of advice to the students – please make it a habit of referring to the bare acts as often as possible. This will not only facilitate the process of understanding the law and the sequence of sections in these Acts, but will also equip them with the professional expertise that is expected.

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Disclaimer

The Author has made each and every effort to avoid errors or omission in this suggested solution of Direct Tax Paper New Syllabus Examination of November, 2010 taken by the Institute of Chartered Accountants of India. As well as the author has placed suitable notes for taking a particular view in terms of various Judicial Authorities and provisions of Income Tax Act, 1961 and the Wealth Tax Act, 1957. It may happen that another view under certain circumstances possible, however, for that matter, the author cannot be held responsible for taking any view in this suggested solution. In spite of this, errors may creep in. Any mistake, error or discrepancy noted may be brought to the notice of author which shall be taken care of in future. It is also notified that the author will not be responsible for any damage or loss of action to anyone, of any kind, in any manner, there from.

Suggested Answers of Direct Tax (New Syllabus) Examination taken by the Institute of Chartered Accountants of India in November, 2010.

Answers to questions are to be given only in English except in the case of candidates who have opted for Hindi Medium. If a candidate has not opted for Hindi medium, his answers in Hindi will not be valued. Question No. 1 is compulsory. Attempt any five questions from the remaining six questions.

Question 1.

(a) You are the auditor of Sigma Limited under Section 44AB of the Income-tax Act, 1961. You have observed that during the previous year ended 31st March, 2010 the company has charged to Profit & Loss Account a sum of 20 lakhs, being loss due to fluctuation in foreign exchange rates arising on settlement of dues to a foreign company from whom one machine was imported in the previous year ended 31" March, 2009. The company's accounting policy of charging such exchange loss to Profit & Loss Account is in consonance with the Accounting Standard 11 notified by the Companies (Accounting Standards) Rules. State the particulars to be provided in respect of the exchange loss in the Form 3CD (Statement of Particulars) forming part of the tax audit report.

(b) Hari has acquired a residential house property in Delhi on 1st April, 2000 for Z 10,00,000 and decided to sell the same on 3 May, 2003 to Ms. Pari and an advance of Z 25,000 was taken from her. The balance money was not paid by Ms. Pari and Hari has forfeited the entire advance sum. On 3 June, 2009, he has sold this house to Mr. Suri for Z 35,00,000. In the meantime on 4th April, 2009, he had purchased a residential house in Delhi for ' 8,00,000, where he was staying with his family on rent for the last 5 years and paid the full amount as per the purchase agreement. However, Hari does not possess any legal title till 31st March, 2010, as such transfer was not registered with the registration authority. Hari has purchased another old house in Chennai on. 14'h October, 2009, from Mr. X, an Indian resident by paying Z 5,00,000 and purchase was registered with the appropriate authority. Determine the taxable capital gain arising from above transactions in the hands of Hari for Assessment Year 2010-11. Cost inflation Index : 2000-01 : 406; 2003-04 : 463; 2009-10 : 632.

(c) Chirag owns two residential flats, one in Mumbai and another in Chennai. Both the flats are meant to be used for residential purposes by Chirag and his family. The particulars of the flats are as follows :

(i) The flat at Mumbai was purchased by him in January, 1980 for Rs 10 lakhs. The flat was occupied by his friend, Suvalaxmi without rent for three months from 1s` April, 2009 to 30th June, 2009. The value of the flat as per Schedule III to the Wealth Tax Act on 31st March, 2010 is Rs 30 lakhs. Its value on the same basis as on 315' March, 1980 was Z 12 lakhs.

(ii) The flat at Chennai was purchased in March, 2007 for Z 6 lakhs.The values of the flat as per Schedule III to the Wealth Tax Act on 2007 and 31st March, 2010 are Z 3 lakhs and Z 5 lakhs respectively.

You are required to fix value of each flat for the purpose of computation of net wealth of Chirag for Assessment Year 2010-11.

(d) Mrs. E, wife of Mr. F is a partner in a firm. Her capital contribution to the firm as on 01-04-2009 was Rs. 5 lakhs, out of which Rs 3 lakhs was contributed out of her own sources and Rs. 2 lakhs was contributed out of gift from her husband. As further capital was needed by the firm, she further invested Z 2 lakhs on 01-05-2009 out of the funds gifted by her husband. The firm paid interest on capital of Rs. 80,000 and share of profit of Rs. 60,000 for the financial year 2009-10. Advise Mr. F as to the applicability of the provision of Section 64(1)(iv) and the manner thereof in respect of the above referred transactions.

(5+5+5+5=20 Marks)

Answer 1.

(a) As per section 43A of the Income Tax Act, 1961, where an assessee has acquired any asset in any previous year from a country outside India for the purpose of business and in consequence of a change in the rate of exchange during any previous year after the acquisition of such asset, there is an increase in the liability in Indian currency at the time of making payment then the amount by which the liability is so increased shall be added to the actual cost of asset.

Hence in a given case, loss arising due to fluctuation in foreign currency on settlement of dues to a foreign company from whom one machine was imported shall be treated as capital expenditure and therefore it shall be added to the actual cost of asset and the same is not allowable expenditure u/s 37 of the Act.

Therefore, in the form 3CD, following particulars shall be provided:

(1) In clause no. 14 (d) (ii) particulars in respect of charge in rate of exchange of currency.

(2) In clause no. 17 (a) particular of amount being loss on account of fluctuation in foreign currency deleted to P & L Account.

(b) **Computation of Taxable Capital Gain in the hands of Mr. Hari for A.Y.2010-11 :**

Particulars	Rs.
Sale Consideration	35,00,000/-
Less : Indexed Cost of Acquisition	(15,17,734/-)
= (10,00,000-25,000) X 632/406	
[Refer Note 1]	
Capital Gain	19,82,266/-
Less : Exemption u/s 54	
In respect of House acquired in Delhi on 04/04/2009	(8,00,000/-)
[Refer Note 2]	
In respect of House acquired in Chennai on 14/10/2009	(5,00,000/-)
	(13,00,000/-
Taxable Capital Gain	6,82,266/-

Suggested Answers is prepared by CA Ankit Talsania and dedicated to Arihant Institute Pvt. Ltd.

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Notes :

1. As per Section 51 of the Act, where any capital asset was on any previous occasion the subject of negotiations for its transfer, any advance or other money received and retained by the assessee in respect of such negotiations shall be deducted from the cost for which the asset was acquired or the written down value or the fair market value, as the case may be, in computing the cost of acquisition.

   Therefore, in a given case, forfeited amount of Rs.25,000/- is reduced from the cost of acquisition of Rs.10,00,000/- before indexing.

2. Exemption u/s 54 of the Act is available in respect of Delhi House also, as all the prescribed conditions u/s 54 is complied with. The said section does not provide that holding of legal title is necessary. If the taxpayer pays fill consideration or substantial portion of it, in terms of purchase agreement, within the prescribed period, the exemption u/s 54 is available.

(c) Computation of Net Wealth in the hands of Chirag for A.Y.2010-11:

Particulars	Rs.
Assets as per S.2(ea) of Wealth Tax Act :	
1. Flat at Mumbai as per Schedule - III	30,00,000/-
2. Flat at Chennai as per Schedule - III	5,00,000/-
Total	35,00,000/-
Less : Exemption u/s 5	
1. Flat at Mumbai as per S.5(vi)	(30,00,000/-)
Net Wealth	5,00,000/-

Notes :

1. As per Explanation 4 to Section 2(ea)(i), if the residential property is let out for a minimum period of 300 days in a previous year then it is not treated as an "asset". However, in a given case Flat in Mumbai is let out for a period less than 300 days and therefore the same shall be treated as an "asset" u/s 2(ea)(i) of Wealth Tax Act.

2. Assessee can claim exemption in respect of one house property as per Section 5(vi) and therefore Chirag can claim exemption u/s 5(vi) for Flat at Mumbai as it is having higher amount of Valuation as per Schedule – III as at valuation date.

(d) **Advise to Mr. F in respect of applicability of provisions of S.64(1)(iv) of the Act :**

As per Section 64(1)(iv) read with Explanation 2A to S.64(1), where the assets (in a given case, cash) transferred directly or indirectly by an individual to his spouse, are invested in the nature of capital contribution as partner in a firm, that part of interest receivable by the spouse from the firm in any previous year, which bears the same proportion to the interest receivable by the spouse from the firm as the value of investment as on the first day of the previous year bears to the total investment by way of capital contribution as a partner in the firm as on the said day, shall be included in the total income of the individual in that previous year.

In short, interest is required to be apportioned to the amount gifted by Mr. E as on the first day of relevant previous year which bears to the total amount of contribution of Mrs. E as on the first day of relevant previous year.

Therefore, the receivable interest is required to be proportioned between Mr. F and Mrs. E as under in view of provisions of S.64(1)(iv) of the Act :

Particulars	In the hands of Mrs. E Rs.	In the hands of Mr. F Rs.
Interest on capital		
Rs.80,000/- X 3/5*	48,000/-*	--
Rs.80,000/- X 2/5#	--	32,000/-#

It is further pointed out that only interest income is required to be clubbed in the hands of Mr. F and not profit received from the firm which is exempt u/s 1010(2A) of the Act.

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Question 2.

(a) ABC Limited was amalgamated with XYZ Limited on 01-04-2009. All the conditions of Section 2(1B) were satisfied.

ABC Limited has the following carried forward losses as assessed till the Assessment Year 2009-10 :

(i) Speculative Loss, Rs 4 lakhs

(ii) Unabsorbed Depreciation Rs 18 lakhs

(iii) Unabsorbed expenditure of capital nature on scientific research Rs 2 lakhs

(iv) Business Loss Rs 120 lakhs

XYZ Limited has computed a profit of Rs 140 lakhs for the financial year 2009-10 before setting off the eligible losses of ABC Limited but after providing depreciation at 15% per annum on Rs 150 lakhs, being the consideration at which plant and machinery were transferred to XYZ Limited. The written down value as per income-tax record of ABC Limited as on 31 March, 2009 was Rs 100 lakhs.

The above profit of XYZ Limited includes speculative profit of Rs 10 lakhs. Compute the total income of XYZ Limited for Assessment Year 2010-11 and indicate the losses/other allowances to be carried forward by it.

(b) R Limited transferred a building worth Rs. 25 lakhs to the Chief Executive Officer, Mr. Mohan Lal, a resident individual on his retirement under an agreement for not carrying on any activity related to its business for a period of five years. In course of assessment under Section 143(3), the Assessing Officer found that no tax had been deducted at source by R Limited and on that ground he disallowed the expenditure by invoking the provision of Section 40(a)(ia). Examine the correctness of the action of the Assessing Officer.

(10+6=16 Marks)

Answer 2.

(a) Computation of Total Income of XYZ Limited for A.Y. 2010-11:

Particulars		Rs. in laks
Profit before Setting off the losses of ABC Ltd.		140.00
Add : Depreciation on P&M transferred from XYZ Ltd. as per Explanation 2 to Section 43(6) – (See Note 1)		7.50
Less : Unabsorbed Depreciation	18.00	
Unabsorbed expenditure of capital nature on scientific Research.	2.00	(20.00)
Taxable Income under the head "Profits and Gains of Business or Profession"		127.50
Less : Business Loss u/s 72		(120.00)
Speculative Loss u/s 73		(4.00)
Total Income (Speculative Income)		3.50

Neither Business loss nor speculative loss shall be carried forward.

Notes :

1. As per Explanation 2 to Section 43 (6), where in any previous year, any block of assets is transferred in a scheme of amalgamation by the amalgamating company to the amalgamated company, then actual cost of block of assets in the case of amalgamated company, shall be written down value of block of assets as in the case of amalgamating company for the immediately preceding previous year. In the present case block of assets of P & M is transferred from ABC Limited to XYX Limited. The W.D.V. as per Income -Tax record of ABC Limited as on 31st March, 2009 was Rs.100 lakhs; however, XYZ Limited has claimed depreciation on Rs.150 lakhs. Therefore, in view of Explanation 2 to Section 43(6) depreciation on Rs.100 lakhs only is available to XYZ limited and not on Rs.150 lakhs.

2. Unabsorbed depreciation includes unabsorbed capital expenditure on scientific research and therefore that is also required to be reduced.

3. As per section 73 speculation loss can be set off against speculative income only. However, as per section 72 business loss can be set off against business profit. Therefore, out of Rs.127.50 lakhs which is consisting of Normal Business Profit of Rs.117.50 lakhs and Speculative Income of Rs.10.00 lakhs, first of all carried forward business losses of Rs.120.00 lakhs shall be set off against Normal Business Profit of Rs.117.50 lakhs and Speculative Income of Rs.2.50 lakhs (out of 10.00 lakhs). Thenafter carried forward speculative losses of Rs.4.00 lakhs shall be set off against balance amount of speculative income of Rs.7.50 lakhs, however, it can be set off only to the extent of Rs.4.00 lakhs. Therefore, total income of Rs.3.50 lakhs is nothing but only speculative income and accordingly neither Business loss nor speculative loss shall be carried forward to the subsequent year.

(b) As per Section 28(va), any sum whether received or receivable in cash or kind under an agreement for not carrying out any in relation any activity in relation to any business shall be treated as income chargeable to income tax under the head "Profit and gains from business or profession".

In the present case R Ltd. has transferred a building worth Rs. 25 lakhs i.e. in kind to Mr. Mohan Lal, the CEO under an agreement for not carrying out any activity related to its business for a period of 5 years. This income will be treated as income chargeable to tax under the head "Profit and gains from business or profession".

R Ltd. is not obliged to deduct tax at source under any provisions of chapter XVII-B of the Act.

Provisions of S.40(a)(ia) of the Act can be invoked when there is a violation of provisions of Chapter – XVII-B of the Act, i.e either to non-deduction of tax at source or non-deposition of tax deducted at source within time limit specified in Section 200(1) of the Act. However, in the present case, there is no obligation on the part of R. Ltd. to deduct tax at source under any provisions of Chapter XVII-B of the Act and therefore there is no violation of TDS provisions in respect of non-deduction or non-deposition of tax at source and accordingly the action of the Assessing officer in invoking provisions of section 40(a) (ia) is incorrect.

Question 3.

(a) A resident woman individual sold a house property on 16-01-2010. On the said transaction she earned a long-term capital gain of Rs 1,01,50,000. She invested a sum of Rs. 50,00,000 in capital gains bonds specified in Section 54 EC on 05-03-2010. She further invested a sum of Rs. 50,00,000 in the same bonds on 05-05-2010. Her other income for the financial year 2009-1.0 was Rs. 46,000.

Compute the tax payable by her for the Assessment year 2010-11.

(b) ILT Limited is engaged in manufacturing pipes and tubes. The Profit & Loss 10 Account of the company for the year ended 31st March, 2010 shows a net profit of Rs. 405 lakhs. The following information and particulars are furnished to you. You are required to compute total income of the company for Assessment Year 2010-11 indicating reasons for treatment of each item.

(i) A group Free Air 'Ticket was provided by a supplier for reaching a certain volume of purchase during the financial year 2009-10. The same is encashed by the company for Rs. 10 lakhs on April 2010.

(ii) A regular supplier of raw materials agreed for settlement of Z 8 lakhs instead of Z 10 lakhs for poor quality of material supplied during the previous year which was not given effect in the running account of the supplier.

(iii) Andhra Bank sanctioned and disbursed a term loan in the financial year 2006-07 for a sum of T 50 lakhs. Interest of Rs 8 lakhs was in arrears. The bank has converted the arrear interest into a new loan repayable in ten equal instalments. During the year the company has paid two instalments and the amount so paid has been reduced from Funded Interest in the Balance Sheet.

(iv) The company remitted Rs. 5 lakhs as interest to a company incorporated in USA on a loan taken two years ago. Tax deducted under Section 195 from such interest has been deposited by the company on 15th June, 2010.

(v) Liquidated damage of Rs 3 lakhs received from KS Limited for delay in supply of plant and machinery has been shown under the head "Other income" in Profit & Loss Account.

(vi) Sandeep, a sales executive stationed at HO at Delhi, was on official tour in Bangalore from 31st May, 2009 to 18th June, 2009 and 28th September, 2009 to 15th October, 2009 for the business development. The Company has paid Sandeep's salary, in cash, from its local office at Bangalore for the month of May 2009 (payable on 1St June) and September 2009 (payable on Ist October), amounting to Rs. 25,000 and Rs 27,000 respectively (net of TDS and other deduction), as Sandeep has no bank account at Bangalore.

(vii) The company has taken up initiative to restructure its debt and paid Rs 20,000 to a financial company, M/s ABC Ltd., towards pre-payment premium. As per the scheme, Rs 50,000 loan was waived against its loan and B Limited directly credited to its reserve account, considering loan waiver amount as capital receipt.

(viii) The company has contributed Rs 50,000 to an electoral trust and the same stands included under the head "General Expenses".

(6+10=16 marks)

Answer 3

(a) Computation of Tax payable of a resident woman for the A.Y.2010-11:

Particulars	Amount in Rs.
Long term Capital gain	1,01,50,000/-
Less : Investment made in Specific Assets on 05/03/2010.	50,00,000/-
Investment made in Specific Assets on 05/05/2010.	50,00,000/-
Total Capital Gain	1,50,000/-
Other Income	46,000/-
Total Income	1,96,000/-
Income Tax	600/-
Education Cess and Secondary and Higher Education Cess	18/-
Tax Payable	**618/-**

Note :

Provisions of Section 54EC(1) provides that investment should be made within six months from the end of the month in which transfer took place. Further proviso to section 54EC(1) provides that Investment made by an assessee in specified assets should not exceed Rs. 50 lakhs in any financial year.

In the present case, assessee has made investment in capital gain bonds specified in Section 54EC of the Act on 05/03/2010 and 05/05/2010 for Rs.50 lakhs each. The assessee has complied all the conditions specified in S.54EC of the Act i.e investments in specified capital gain bonds have been made within six months from the end of the month in which transfer took place and in any previous year amount of investment does not exceed Rs.50 lakhs. Therefore, deduction u/s 54EC amounting to Rs.1 Crore is available to the assessee in present case.

(b) Computation of Total Income for ITI Limited for A.Y. 2010-11:

Particulars		Rs. (In lakhs)	Rs. (In lakhs)
Net Profit as per P&L A/c.			405.00
Add :			
(i) Group free Air Tickets provided by a supplier for reading a certain volume of purchases	(See Note - 1)	10.00	
(ii) Remission or cessation of Trading liability u/s 41(1)		2.00	
(iii)No Adjustment is required	(See Note - 3)	-	
(iv) Addition u/s 40(a)(i) on account of Non-Deposition of TDS within time limit specified u/s 200(1)	(See Note – 4)	5.00	
(v) Liquidated Damages	(See Note – 5)	(3.00)	
(vi) No Addition u/s 40A(3) As per Rule 6DD(i)	(See Note – 6)	-	
(vii) No Adjustment is required.	(See Note – 7)	-	

		14.00	14.00
Gross Total & Income			419.00
Less : Deduction under chapter – VI-A			
(Viii) Section 80 GGB – Deduction			0.50
	Total Income		419.50

Notes :

(i) Receipt of free Air Tickets on account of reaching a certain volume of purchase is a incentive in kind to achieve particular target and the same is taxable on accrual basis as per mercantile system of accounting irrespective of the fact whether the same is encashed or not or even in the same financial year or in subsequent financial year.

(ii) Supplier has agreed to settle at Rs. 8 lakhs instead of Rs. 10 lakhs for supply of raw material which is nothing but remission or cessation of trading liability for which the assessee has claimed expenditure in the form of 'Purchase'. Therefore in view of provisions of Section 41(1), remitted or ceased liability is required to be taxed in the hands of asseesee.

(iii) Expenditure of Rs. 8 lakhs of interest in arrear would have been claimed in A.Y. 2006-07 which is now converted into loan. Therefore, now on account of repayment of such amount no effect is required to be given in profit & Loss Account.

(iv) As per section 40(a)(i) of the Income Tax Act, 1961, if the tax is deducted at source and not deposited within the time limit specified in section 200 (1) of the Act, then the said expenditure is not allowable to the assesse. In the present case, the assessed has deducted tax at source u/s 195 but deposited the same after the time-limit specified u/s 200 (1) of the Act, hence interest expenditure is not allowed u/s 40 (a)(i) of the Act.

(v) Liquidated damages of Rs. 3 lakhs received by assessed were directly and intimately linked with the procurement of a Capital Asset viz. Plant & Machinery. This is not in ordinary course of business and therefore, the same is required to be treated as "Capital Receipt" and not "Revenue Receipt". Hence, the same is excluded from total income. This situation is squarely covered by the Supreme Court decision in the case of ***Saurashtra Cement Ltd.*** ***reported in 325 ITR 422.***

(vi) As per rule 6DD(i) read with section 40 A(3) of the Act, expenditure will not be disallowed even if the payment in cash in excess of Rs.20,000/- in a single day has been made. "Payment made by an assesses by way of salary to his employee after deducting tax from salary in accordance with the provisions of section 192 and when such employee.

(a) is temporally posted for a continuous period of 15 days. Or more in a place other than his normal place of duty or on a ship; and

(b) Does not maintain any account in any bank at such place or ship.

In the present case, Sandeep is temporarily posted for a continuous period of 15 days or more in a place other than his normal place of stay and he was not having bank account at that place i.e. Bangalore and also the salary in cash has been made after deduction of tax at source u/s 192 of the Act.

In view of above noted provisions, no addition is required to be made u/s 40 A (3) of the Act.

(vii)Rs. 20,000/- is a pre payment of premium on account of restructuring of debt which is not a revenue expenditure, hence no expenditure can be claimed. It is also presumed that it is not debited to P&L Account and therefore no adjustment is made in computation of Total Income.

So for as waiver of loan amounting to Rs. 50,000/- is concerned, the same cannot be added u/s 41(1) of the Act, as it is not a trading liability and the assesses has given correct treatment.

(viii) Contribution made to Electoral trust is allowable deduction u/s 80GGB of the Act, hence the same is reduced from gross total income.

Question 4.

(a) Dishant received a notice under Section 148 from the Assessing Officer for Assessment Year 2004-05 on the ground that depreciation on certain assets was allowed in excess. The Assessing Officer recorded the reason for reopening. The original assessment was completed under Section 143(3). In course of reassessment proceeding the Assessing Officer also disallowed certain sum under Section 14A in respect of expenses purported to be in relation to dividend from companies and tax-free interest. However, the Assessing Officer did not record the reason for applying the provision of Section 147 in respect of the issue of disallowance under Section 14A and passed the order disallowing the excess depreciation and also certain sum under Section 14A. Is there any infirmity in the order passed by the Assessing Officer?

(b) (i) Who shall sign and verify the return of income of a limited liability partnership?

(ii) XYZ LLP is liquidated. What is the liability of partners of XYZ LLP in respect of its tax dues ?

(iii) PQR LLP has a profit of Z 500 I lths after charging interest on capital for P amounting to T 10 lakhs calculated at 15% p.a. as per the agreement, but before considering remuneration to partners. What is the maximum admissible amount of remuneration to partners assuming all the partners are working partners and remuneration is authorized by the LLP instrument ?

(c) Who can be an e-return Intermediary, as notified by CBDT ?

(d) ITP Limited is engaged in growing and manufacturing tea in India. It commenced its operation from 1s` April, 2008. It acquired plant and machinery, factory building and furniture at cost of T 40 lakhs, T 25 lakhs and T 10 lakhs respectively in the previous year 2008-09. All the assets were put to use for more than 180 days during 2008-09. Compute the written down value of each block of assets as on 1" April, 2009.

(3+6+4+3=16 Marks)

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Answer 4.

(a) As per sub-section (2) to section 148, before issuing notice u/s 148, reason to reopen the assessment is required to be recorded.

Once the assessment is reopened the Assessing officer can add such income for which the assessment was reopened and also any other income chargeable to tax which has escaped assessment and which comes to his notice subsequently in the course of assessment proceedings u/s 147 of the Act.

However, several judicial authorities had pronounced that reassessment proceedings shall be restricted to only such issues which have been specifically recorded by the AO before issuing the notice for re-opening the assessment.

To overcome this situation, an Explanation 3 to section 147 is now inserted by the Finance Act (No.2) Act, 2009 with retrospective effect from 1st April, 1989 to provide that the A.O. can assess or re-assess income in respect of any issue which has escaped assessment even if the same comes to his notice subsequently in the course of reassessment proceedings and the same was not recorded by him earlier at the time of issuing the which for re-opening the assessment.

Therefore, in the present case there is no infirmly in the order passes by A.O.

(b)

(i) Designated partner or when such designated partner for unavoidable reason is unable then any other partner of LLP shall sign and verity the Return of Income of LLP.

(ii) In the event of liquidation of XYZ LLP, all the partners of XYZ LLP are jointly and severally liable along with LLP for the amount of the tax.

(iii) Computation of Remuneration payable to partners of PQR LLP.

Particulars	Rs. in lakhs
Profit	500
Add : Interest not admissible as per Section 40(b)	2
Book Profit	**502**

Working of remuneration to Partners of LLP.

(i) In First 3 lakhs	Rs.2.70 laks(Rs.1.50 lakhs or 90% of Rs.3.00 lakhs which ever is higher)	
(ii) On the balance amount of Profit	Rs. 294 lakhs i.e 60% of Rs.490 lakhs	
Total Remuneration		Rs.296.70 lakhs

(c) As per CBDT Notification, following persons are qualified to become an e-return Intermediary.

(1) Public Sector Undertaking as defined u/s 2 (36A) of the Act or any other company in which public are substantially interested within meaning of section 2(18) of the Act or any subsidiary of these companies or

(2) A company incorporated in India, including a bank, having a net worth of Rs. 1 crore or

(3) A firm of Chartered Accountants or Company Secretaries or Advocates, if it has been allocated PAN.

(4) A Chartered Accountants or Company Secretaries or Advocates or Tax Return Preparers, if PAN is allotted

(5) Drawing or Disbursing officer of a Government Department.

(d) Computation of the written down value of following block of Assets as on 1st April, 2009.

Particulars	Plant & Machinery Rs. in lakhs	Factory Building Rs. in lakhs	Furniture Rs. in lakhs
W.D.V. as on 01/04/2008	--	--	--
Additions – for more than 180 days	40	25	10
Cl. W.D.V. for depreciation	40	25	10
Depreciation Rate	15%	10%	10%
Depreciation –			
Attributable to Business Income i.e 40%	2.40	1.00	0.40
Attributable to Agr. Income i.e 60%	3.60	1.50	0.60
W.D.V. as on 31/03/09	37.60	24.00	9.60
W.D.V. as on 01/04/09	**37.60**	**24.00**	**9.60**

Note :

As per the supreme court decision in the case of *CIT vs. Doom Dooma India Ltd. reported in 310 ITR 392*, depreciation attributable to business income can only be deducted from the WDV of block of Assets in the case of Assesses who derives part income from agriculture activity and part income from taxable business income.

However, this decision of the Apex Court is nullified by *inserting provisions of Explanation 7 to Section 43(6) of the Act by the Finance Act (No.2), 2009 with affect from 01/04/2010.*

As this amendment is prospective in nature the same is not applicable in the given case and therefore the law laid down by the Apex Court in Doom Dooma is applied under the given circumstances.

Question 5. Attempt any four questions out of the following:

(a) CG Ltd. is engaged in the business of conversion of jumbo rolls of films into saleable packets/rolls of standard size. Is the company entitled to claim deduction under Section 80-IB ?

(b) SK Enterprises, an exporter of soft toys, filed its return of income disclosing a total income of T 8.50 lakhs after claiming deduction under Section 10 B of the Income-tax Act for Rs. 4 lakhs. The return was processed under Section 143(1) and income as per return of income was accepted. Later on it was noticed by the Assessing Officer that the assessee had offered interest income on fixed deposit under the head "profits and gains of business or profession", but it was required to be assessed under the head "income from other sources". The Assessing Officer initiated rectification proceeding by issue of notice under Section 154 and after hearing the assessee passed order under Section 154 including the interest income under the head "income from other sources" and adjusting the claim of the assessee under Section 10 B. Examine the correctness of the action of the Assessing Officer.

(c) A charitable institution registered under Section 12A of the Income-tax Act, 1961 filled in Form No. 10 for seeking permission to accumulate unapplied income under Section 11(2) of the Act for the objects of the institution and submitted it to the Assessing Officer along with the resolution for accumulation. The Assessing Officer found that the objects for which accumulation was sought were not particularised in as much as they covered the entire range of objects of the institution. Can the Assessing Officer deny the benefit of accumulation in such case?

(d) The residential premises of Mr. X, an income tax practitioner was searched under Section 132. During the search certain incriminating documents were seized. From the documents seized it was revealed that he had been claiming and receiving income tax refunds by filing bogus TDS certificates with returns of income prepared by him even in the names of nonexisting persons. Discuss whether the refund collected illegally by Mr. X by producing bogus TDS certificates constitute income chargeable to tax.

(e) People Housing Ltd. is engaged in the business of constructing residential and commercial properties. One of the building properties was included in the closing stock in the Balance Sheet. The said building was let out for a monthly rent as suitable buyers could not be found. All other buildings had been sold by the company. State with reasons whether the income by way of rent from the unsold property is assessable as income from business or income from house property.

(4+4+4+4+4=20 Marks)

Answer 5

(a) As per the Supreme Court's decision in the care of India Cine Agencies VS. CIY [308 ITR 98 (SC)], conversion of Jumbo rolls of films into saleable packets / rolls of standard size is manufacturing activity.

Deduction u/s 80IB is available to the Industrial Undertaking who is engaged in the business of manufacturing or production of article or thing.

Under the given circumstances, business of CG Ltd. is that of manufacturing as per India Cine Agencies (Supra) and therefore the company is entitled to deduction u/s 80 IB of the Act.

(b) As per section 10 B of the Act, deduction is available to such profits and gains as are derived by a 100% EOU from the export of articles or things or computer software.

Strictly speaking with the provisions of section 10B of the Act, interest from fixed deposits is not profits and gains derived from the export of articles or things and therefore deduction u/s 10B on interest income can't be availed.

However, ratio can be drawn from the Rajasthan High Court decision in the care of CIT vs. Hycron Radio Ltd. reported in 308 ITR 251, wherein it has been held that language of Section 10B provides for exemption with respect to any profits and gains derived by assessee and same is not confined to any 'Profits' and gains of business and profession as provided in section 14 (D) and therefore interest income would fall within expression 'profits and gains' and assessee would be entitled to exemption u/s 10B in respect of such interest income. Therefore, following the decision of Rajasthan High Court as noted above, deduction u/s 10B is available on interest income.

In the present case, the return was processed u/s 143(1) of the Act and the assessing officer initiated proceedings u/s 154 of the Act and passed the order u/s 154 of the Act rectifying the said so called mistake. Provisions of S.154 of the Act can be invoked only when there is a mistake apparent from the record. The issue as to whether interest on Fixed Deposit is eligible for deduction u/s 10B of the Act is debatable and there can be more than one possible views and therefore though interest may not be eligible for deduction u/s 10B of the Act it is not a mistake apparent from record. Hence, the action of assessing officer to initiate proceedings and pass the order u/s 154 of the Act to treat such interest income as income from other sources is incorrect.

(c) The given case is squarely covered by the Delhi High Court decision in the case of CIT vs. Hotel & Restaurant Association reported in 261 ITR 190 and another in the case of Bharat Krishak Samaj us DIT reported in 306 ITR 153.

In the case of Hotel & Restaurant (Supra), it has been held that it is not necessary for a charitable trust to particularize each and every object for which accumulation is sought. It is enough if the assesses seeks accumulation for the object of trust.

As well as in the case of Bharat Krishak Samaj (Supra), it has been held that the claim of accumulation of unapplied income cannot be denied even if the objects for which accumulations are sought are not particularized in as much as they cover entire range of objects of trust.

Therefore in a given case, the Assessing officer cannot deny the benefit of accumulation in view of above quoted decisions.

(d) The given case is squarely covered by the Madras High Court decision in the case of CIT vs. K. Thangamahi, reported in 309 ITR 15, wherein it has been held that income might have been earned illegally or by resorting to unlawful means, but illegality tainted with earning has no hearing on its taxability and such earned income would be still liable for assessment and therefore income earned by assesses from income tax refunds collected by him illegally by producing bogus TDS certificates would be assessed under the Act.

Hence, in a given case, Mr. X is liable to tax on the refund collected illegally by producing bogus TDS Certificates.

(e) The main business of People Housing Ltd. is construction of residential and commercial properties. In a given case, People Housing Ltd. has sold all other buildings constructed by it, however, one building could not be sold out as suitable buyers were not found out, which was included in closing stock in the Balance Sheet, and therefore it was let out for a monthly rent. This renting out of property is incidental and subservient to the main business of People Housing Ltd. and therefore such rent income can not be treated as Income from House Property but is required to be treated as Profit and Gains from Business or Profession.

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Question 6.

(a) Fearless General Finance & Investment Limited, a residuary non-banking company, is accepting public deposit, issued deposit certificate and repaid back after some period of time along with interest, under different schemes run by it. Following transactions were noted from their books of account:

(i) Mr. A, an individual, has deposited Rs 15,000 on 1st May, 2006 for 48 months in cheque and another Rs 15,000 on 30th June, 2009 in cash to purchase a new certificate of 48 months tenure.

(ii) Mr. A has applied for premature withdrawal against both the certificates and the company has paid him Rs 16,500, by a bearer cheque, against principal and interest on 23rd March, 2010, due against his first certificate (purchased in 2006) and Rs 15,500 in cash on 25th March, 2010, against the second certificate. Discuss the violation of income tax provision if any and consequential penalty for each transaction. Will it make any difference if the certificates were held jointly with Mrs. A, wife of Mr. A, while repaying back in cash or bearer cheque?

(b) The net profit of ABP Ltd. as per Profit & Loss Account for the previous year 2009-10 is 100 lakhs after debiting/crediting the following items:

(i) Provision for income-tax : Rs 15 lakhs

(ii). Provision for deferred tax: Rs 8 lakhs

(iii) Proposed Dividend: Rs 20 lakhs

(iv) Depreciation debited to Profit & Loss Account is Rs 12 lakhs. This includes depreciation on revaluation of asset to the tune of Rs. 2 lakhs.

(v) Profit from unit established in Special Economic Zone: Rs 30 lakhs

(vi) Provision for permanent diminution in value of investments: Rs 2 lakhs

Brought forward losses and unabsorbed depreciation as per books of the company are as follows:

Previous year	Brought forward Loss (: in lakhs)	Unabsorbed Depreciation (in lakhs)
2006-07	2	5
2007-08	—	3
2008-09	10	2

Compute book profit of the company under Section 115 JB for Assessment Year 2010-11.

(7+9=16 Marks)

Answer 6.

(a) (i) As per provisions of Section 269SS of the Act, no person shall take or accept from any other person any loan or deposit otherwise than by account payee cheque or account payee bank draft if

(1) the amount of such loan or deposit or the aggregate amount of such loan and deposit ; or

(2) on the date of taking or accepting such loan or deposit, any loan or deposit taken or accepted earlier by such person from the depositor is remaining unpaid (whether repayment has fallen due or not), the amount or the aggregate amount remaining unpaid ; or

(3) the amount or the aggregate amount referred to in (1) together with the amount or the aggregate amount referred to in clause (2)

is 20,000/- or more.

And if the amount is accepted otherwise than account payee cheque or account payee bank draft, then the person shall be liable to penalty u/s 271D of the Act for an amount of deposit so taken or accepted.

In the given case, Fearless General Finance & Investment Limited has already accepted deposit of Rs.15,000/- on 01/05/2006 in cheque and during the year under consideration on 30/06/2009, it has accepted an amount of Rs.15,000/- in cash, which has resulted into in excess of aggregate amount of Rs.20,000/- as (iii) mentioned above. Therefore provisions of Section 269SS will be invoked and such company will be required to pay penalty of Rs.15,000/- as per provisions of S.271D of the Act.

(ii) As per provisions of S.269T of the Act, company shall not repay any loan or deposit made with it otherwise than by an account payee cheque or account payee bank draft drawn in the name of the person who has made the loan or deposit if—

(*a*) the amount of the loan or deposit together with the interest, if any, payable thereon, or

(*b*) the aggregate amount of the loans or deposits held by such person with the branch of the banking company or co-operative bank or, as the case may be, the other company or co-operative society or the firm, or other person either in his own name or jointly with any other person on the date of such repayment together with the interest, if any, payable on such loans or deposits,

is Rs.20,000/- or more

In a given case, such company has made payment otherwise than account payee cheque or account payee bank drawn in excess of Rs.20,000/- during the year under consideration and therefore provisions of S.269T will be invoked and as per provisions of S.271F of the Act, such company will be required to pay penalty equal to the amount of repayment i.e 22,000/-

Provisions of S.269T and consequential penalty provisions of S.271F of the Act will be applicable even if the certificates were held jointly with Mrs. A, wife of Mr. A, while repaying bank in cash or bearer cheque as per provided in provisions of S.269T of the Act.

(b) Computation of Book Profit of ABP Ltd. 4/5 115YB for A.Y. 2010-11:

Particulars	Rs. in lakhs	Rs.in lakhs
Net Profit as per Profit & Loss Account.		100
Positive Adjustments:		
(i) Provision for Income Tax	15	
(ii) Proposed Dividend	20	
(iii) Depreciation debited to P&L Account	12	
(iv) Provision for Deferred Tax	8	
(v) Pro. of Permanent Diminution in value of investment	2	57
Negative Adjustments		
(i) Depreciation debited to P&L Account excluding depreciation on revaluation of assets	(2)	
(ii) Profit from unit established in SEZ	(30)	
(iii) Amount of loss brought forward or unabsorbed depreciation whichever is less as per books of accounts.	(10)	(42)
Book Profit		115

Note :

	Loss Brought Forward Loss	Unabsorbed Depreciation
	Rs. In lakhs	Rs. In lakhs
2006-07	2	5
2007-08	-	3
2008-09	10	2
Total loos as per Books of Accounts	12	10

Lower amount is 10 lakhs in respect of unabsorbed depreciation which shall be deducted from net profit to determine book profit.

It is also pointed out that total business loss and unabsorbed depreciation as per books of accounts is required to be taken into consideration and not losses / unabsorbed depreciation per year is required to be taken into consideration for negative adjustment to Book profit. Therefore, total unabsorbed depreciation of Rs.10 lakhs which is less than total business losses of Rs.12 lakhs is taken into consideration for negative adjustment to determine book profit.

Question 7.

(a) Ranjit has taken an interest-free loan of Rs. 10 lakhs from his company. The amount is utilized by him for purchasing a house on 30-06-2008. The house is self-occupied. As per the scheme of the company, loan would be recovered in 40 equal monthly instalments recoverable immediately after the completion 18th month from the date of purchase. The SBI lending rate of similar loan on 1-4-2009 was 9.75%. Calculate the perquisite value of such loan in the hands of Ranjit for the assessment year 2010-11. Is it possible to get deduction of perquisite value of interest under Section 24(b) ? Does it make any difference, if the house is given on rent?

(b) Mr. Ram, a resident individual following cash basis of accounting has the following assets as on 31-03-2010. Compute his net wealth for the assessment year 2010-2011:

	Particulars	Valuation as on 31-03-2010(in Lakhs)
(i)	Self-occupied residential house	60
(ii)	Owning of a guest house situated 26 kms from the municipality	30
(iii)	Property used for his business	50
(iv)	One residential complex consisting of 10 dwelling units. He intended to sell 5 units which are kept vacant for want of prospective buyers for the whole year. 2 units are vacant from 05-01-2010. 3 units are let out fully for the whole year.	500

(c) What are the nature and value of transactions to be reported in Annual Information Return by the following entities?

(i) A banking company;

(ii) Registrar or Sub-registrar appointed under the Registration Act.

What is the time limit for filing such return?

(d) Can the Transfer Pricing Officer accept use of multiple-year data for determination of Arm's Length Price in an international transaction?

(5+5+3+3=16 Marks)

Answer 7

(a) Calculation of perquisite value of loan in the hands of Ranjit for A.Y.2010-11:

Month	Maximum monthly outstanding amount on last day of Month Rs.	Interest Rs.
April-09	10,00,000	10,00,000 x 9.75% x $^1/_{12}$ = 8,125.00
May-09	10,00,000	10,00,000 x 9.75% x $^1/_{12}$ = 8,125.00
June-09	10,00,000	10,00,000 x 9.75% x $^1/_{12}$ = 8,125.00
July-09	10,00,000	10,00,000 x 9.75% x $^1/_{12}$ = 8,125.00
Aug-09	10,00,000	10,00,000 x 9.75% x $^1/_{12}$ = 8,125.00
Sept-09	10,00,000	10,00,000 x 9.75% x $^1/_{12}$ = 8,125.00
Oct-09	10,00,000	10,00,000 x 9.75% x $^1/_{12}$ = 8,125.00
Nov-09	10,00,000	10,00,000 x 9.75% x $^1/_{12}$ = 8,125.00
Dec-09	10,00,000	10,00,000 x 9.75% x $^1/_{12}$ = 8,125.00
Jan-10	9,75,000	9,75,000 x 9.75% x $^1/_{12}$ = 7921.88
Feb-10	9,50,000	9,50,000 x 9.75% x $^1/_{12}$ = 7718.75
Mar-10	9,25,000	9,25,000 x 9.75% x $^1/_{12}$ = 7515.63
Value of Perquisites		96,281.26

Deduction u/s 24 (b) of the Act is only available if the interest is payable on borrowed loan. Under the given case, Ranjit has taken an interest free loan and therefore deduction u/s 24(b) of the Act can't be availed on the perquisite value of interest free loan.

(b) Computation of Net wealth of Mr. Ram for A.Y. 2010-11:

Particulars	Valuation as on 31/03/2010 Rs. in lakhs
Assets as per Section 2(ea) of Wealth Tax Act:	
(i) Self occupied residential house	60
(ii) Owning a guest house situated 26 kms from the municipality	30
(iii) Property used for his business as per Exception Three to S.2(ea)(i)	Nil
(iv) One Residential Complex consisting of 10 dwelling units	
- 5 units vacant	250
- 2 units vacant from 05/10/2010	100
- 3 units let out	Nil
(See Note)	
Total	440
Less : Exempted Assets as per Section 5	
(i) Residential Complex consisting of 10 dwelling units treated as a single house and exemption is claimed u/s 5(vi) (See Note)	(350)
Net Wealth	90

Notes :

1. Residential Complex Consisting of 10 dwelling units is an asset as per Sec. 2 (ea) (i) of the Act. However, 3 units are let out for more than 300 days and therefore they cannot be treated as assets as per exception four to sec. 2 (ea) (i) of the Wealth Tax Act.

2. As per section 5 (vi), Assessee can claim one house as exempted assets. In a given case a residential complex consisting of 10 devilling units can be considered as a single

house for the purpose of exemption u/s 5(vi) of the Act and therefore the same is reduced from total wealth to determine net wealth.

This view is supported by the Allahabad High Court decision in the case of Shiv Narain Chaudhari vs. CWT 108 ITR 104 (All.), wherein it has been held that a house may consist of more than one self-contained dwelling unit and that if there is a unity of structure, the mere fact that such self-contained dwelling units are occupied by different persons, will not make that house into several houses.

(c) The nature and valve of transactions to be reported in Annual Information Return by following entities are as under:

1. Banking Company	Cash Deposits aggregating to Rs. 10 lakhs or more in a year in any saving bank account of a person.
2. Registrar of Sub-Registrar appointed under the Registration Act.	Purchase or sale of immovable property valued at Rs. 30 lakhs or more.

The Return of AIR should be furnished on or before 31st August, immediately following the financial year in which the transaction is registered or recorded.

(d) As per rule 10B(4), the data to be used in analysing the comparability of an uncontrolled transaction with an international transaction shall be the data relating to the financial year in which the international transaction has been entered into.

Therefore, in a given case the TPO cannot accept use of multiple year data for determining ALP in an International transaction.

However, proviso to rule 10 B (4) also provides that data for 2 years prior to such financial year may also be considered if such data reveals facts which could have an influence on the determination of ALP in an international transactions.