

PAPER – 5 : TAXATION

Question No.1 is compulsory.

Attempt any **five** questions from the remaining **six** questions.

Working notes should form part of the answer.

Wherever necessary suitable assumptions may be made by the candidates

Question 1

- (a) Mr. Praveen engaged in retail trade, reports a turnover of ₹ 58,50,000 for the financial year 2010-11. His income from the said business as per books of account is computed at ₹ 2,90,000. Retail trade is the only source of income for Mr. Praveen.
- (i) Is Mr. Praveen eligible to opt for presumptive determination of his income chargeable to tax for the assessment year 2011-12?
- (ii) If so, determine his income from retail trade as per the applicable presumptive provision.
- (iii) In case Mr. Praveen does not opt for presumptive taxation of income from retail trade, what are his obligations under the Income-tax Act, 1961?
- (iv) What is the due date for filing his return of income under both the options?
- (b) Rahul holding 28% of equity shares in a company took a loan of ₹ 5,00,000 from the same company. On the date of granting the loan, the company had accumulated profit of ₹ 4,00,000. The company is engaged in some manufacturing activity.
- (i) Is the amount of loan taxable as deemed dividend in the hands of Rahul, if the company is a company in which the public are substantially interested?
- (ii) What would be your answer, if the lending company is a private limited company (i.e.) a company in which the public are not substantially interested?
- (c) Mr. Chandru transferred a vacant site on 28.10.2010 for ₹ 100 lakhs. The site was acquired for ₹ 9,99,300 on 30.6.2000. He deposited ₹ 50 lakhs in eligible bonds issued by Rural Electrification Corporation Ltd. (REC) on 20.3.2011.

Again, he deposited ₹ 20 lakhs in eligible bonds issued by National Highways Authority of India (NHAI) on 16.4.2011.

Compute the chargeable capital gain in the hands of Chandru for the A.Y. 2011-12.

Financial year	Cost Inflation Index
2000-01	406
2010-11	711

The Suggested Answers for Paper 5: Taxation are based on the provisions of law as amended by the Finance Act, 2010 and applicable for A.Y. 2011-12 (in the case of Income-tax), which is the assessment year relevant for May, 2011 examination.

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- (d) ABC & Co. furnishes the following information for the half-year ended 31.03.2011:
- (i) Amount received for services provided to UNICEF, (an international organization) ₹ 2,00,000.
 - (ii) Advance money received from customers ₹ 4,00,600 in respect of which services were not rendered till 31.03.2011.
 - (iii) Services billed during the half-year excluding item (i) and (ii) above, was ₹ 15,00,000 plus service tax and cess @ 10.3%.
It consists of the following:
 - (a) One customer 'X' to whom a bill of ₹ 2,20,600 plus service tax and cess @ 10.3% raised, did not pay service tax and cess.
 - (b) Customer 'Y' to whom a bill was raised for ₹ 1,00,000 plus service tax and cess has not paid the amount till 31.03.2011.
 - (c) The balance amounts billed during the year were realized fully.
- Compute the value of taxable service on which service tax is payable. (4 × 5 = 20 Marks)

Answer

- (a) (i) Yes. Since his total turnover for the F.Y.2010-11 is below ₹ 60 lakhs, he is eligible to opt for presumptive taxation scheme under section 44AD in respect of his retail trade business.
- (ii) His income from retail trade, applying the presumptive tax provisions under section 44AD, would be ₹ 4,68,000, being 8% of ₹ 58,50,000.
- (iii) In case he does not opt for the presumptive taxation scheme under section 44AD, and claims that his income is ₹ 2,90,000 (which is lower than the presumptive business income of ₹ 4,68,000), he has to maintain books of account as required under section 44AA(2) and also get them audited and furnish a report of such audit under section 44AB, since his total income exceeds the basic exemption limit of ₹ 1,60,000.
- (iv) In case he opts for the presumptive taxation scheme under section 44AD, the due date would be 31st July, 2011.
- In case he does not opt for the presumptive taxation scheme and claims that his income is ₹ 2,90,000 as per books of account, then he has to get his books of account audited under section 44AB, in which case the due date for filing of return would be 30th September, 2011.
- (b) Any payment by a company, other than a company in which the public are substantially interested, of any sum by way of advance or loan to an equity shareholder, being a person who is the beneficial owner of shares holding not less than 10% of the voting

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power, is deemed as dividend under section 2(22)(e), to the extent the company possesses accumulated profits.

- (i) The provisions of section 2(22)(e), however, will not apply where the loan is given by a company in which public are substantially interested. In such a case, the loan would not be taxable as deemed dividend in the hands of Rahul.
- (ii) However, if the loan is taken from a private company (i.e. a company in which the public are not substantially interested), which is a manufacturing company and not a company where lending of money is a substantial part of the business of the company, then, the provisions of section 2(22)(e) would be attracted, since Rahul holds more than 10% of the equity shares in the company.

The amount chargeable as deemed dividend cannot, however, exceed the accumulated profits held by the company on the date of giving the loan. Therefore, the amount taxable as deemed dividend in the hands of Rahul would be limited to the accumulated profit i.e., ₹ 4,00,000 and not the amount of loan which is ₹ 5,00,000.

(c) Computation of chargeable capital gain of Mr. Chandru for the A.Y.2011-12

Particulars	₹	₹
Sale consideration		1,00,00,000
Less: Indexed cost of acquisition		
$9,99,300 \times \frac{711}{406} =$		<u>17,50,006</u>
		82,49,994
Less: Deduction under section 54EC		
20.03.2011 RECL bonds	50,00,000	
16.04.2011 NHAI bonds	<u>20,00,000</u>	<u>70,00,000</u>
Long term capital gain		<u>12,49,994</u>

Note:

- (1) Since the site was held for more than 36 months prior to the date of transfer, it is a long-term capital asset and the capital gain arising upon its transfer is long-term capital gain.
- (2) In order to claim exemption under section 54EC, Mr. Chandru has to invest in specified bonds of RECL or NHAI within a period of 6 months from the date of transfer of the asset.
- (3) However, investments made in such bonds by an assessee during any financial year cannot exceed ₹ 50 lakhs.

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In this case, Mr. Chandru has invested ₹ 50 lakhs in RECL bonds in the F.Y.2010-11 and ₹ 20 lakhs in NHA bonds in the F.Y.2011-12, both within six months from the date of transfer. He has, therefore, fulfilled both the conditions and hence, he is eligible to claim exemption of ₹ 70 lakhs under section 54EC.

(d) Computation of value of taxable service of M/s. ABC & Co, for the half year ended 31.3.2011

		₹
(i)	Amount received for services provided to UNICEF (an international organization) is not liable to service tax	Nil
(ii)	Advance money received from customers but the services not rendered till 31.03.2011 is liable to service tax. The receipt is deemed to be inclusive of service tax and cess; hence value of taxable services is $= 4,00,600 \times \frac{100}{110.30}$	3,63,191
(iii)	Service rendered and billed during the half-year ended 31.3.2011 excluding item (i) and (ii) above ₹ 15,00,000 plus service tax and cess @ 10.3% consisted of the following:	
	(a) One customer 'X' to whom a bill of ₹ 2,20,600 plus service tax and cess was raised, did not pay the service tax and cess. Hence, the amount realized from him is to be deemed as inclusive of service tax. $2,20,600 \times \frac{100}{110.30}$	2,00,000
	(b) Customer 'Y' to whom a bill was raised for ₹ 1,00,000 plus service tax and cess. Bill has not been realized and therefore, is not liable to service tax	Nil
	(c) The balance amount billed i.e. ₹ 11,79,400 (₹ 15,00,000 – ₹ 2,20,600 – ₹ 1,00,000) since realized by the service provider, it is liable to service tax	<u>11,79,400</u>
	Value of taxable service on which service tax is payable	<u>17,42,591</u>

Question 2

- (a) Mr. Rajiv, aged 50 years, a resident individual and practicing Chartered Accountant, furnishes you the receipts and payments account for the financial year 2010-11.

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Receipts and Payments Account

Receipts	₹	Payments	₹
Opening balance (1.4.2010)		Staff salary, bonus and stipend to articled clerks	1,50,000
Cash on hand and at Bank	12,000	Other administrative expenses	48,000
Fee from professional services	9,38,000	Office rent	30,000
		Housing loan repaid to SBI (includes interest of ₹ 88,000)	1,88,000
Rent	50,000	Life insurance premium	24,000
		Motor car (acquired in Jan. 2011)	4,25,000
Motor car loan from Canara Bank (@ 9% per annum)	2,50,000	Medical insurance premium (for self and wife)	18,000
		Books bought (annual publications)	20,000
		Computer acquired on 1.11.2010 (for professional use)	30,000
		Domestic drawings	2,72,000
		Public provident fund subscription	20,000
		Motor car maintenance	10,000
		Closing balance (31.3.2011)	
		Cash on hand and at Bank	15,000
	<u>12,50,000</u>		<u>12,50,000</u>

Following further information is given to you:

- (1) He occupies 50% of the building for own residence and let out the balance for residential use at a monthly rent of ₹ 5,000. The building was constructed during the year 1997-98.
- (2) Motor car was put to use both for official and personal purpose. One-fifth of the motor car use is for personal purpose. No car loan interest was paid during the year.
- (3) The written down value of assets as on 1-4-2010 are given below:

Furniture & Fittings	= ₹ 60,000
Plant & Machinery	= ₹ 80,000

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(Air-conditioners, Photocopiers, etc.)

Computers = ₹ 50,000

Note: Mr. Rajiv follows regularly the cash system of accounting.

Compute the total income of Mr. Rajiv for the assessment year 2011-12. (12 Marks)

- (b) *Ahmed & Co. of Srinagar rendered taxable services both within and outside the State of Jammu & Kashmir. It received ₹ 26,12,000 for the services rendered inside the State of Jammu & Kashmir and ₹ 18,00,000 for the services rendered outside the State of Jammu & Kashmir.*

Compute its taxable service value and service tax liability.

In case, Ahmed & Co. was situated in Mumbai, what would be value of its taxable service and service tax liability? (4 Marks)

Answer

- (a) **Computation of total income of Mr. Rajiv for the assessment year 2011-12**

Particulars	₹	₹	₹
Income from house property			
Self-occupied			
Annual value	Nil		
Less: Deduction under section 24(b)			
Interest on housing loan			
50% of ₹ 88,000 = 44,000 but limited to	<u>30,000</u>		
Loss from self occupied property		(30,000)	
Let out property			
Annual value (Rent receivable has been taken as the annual value in the absence of other information)	60,000		
Less: Deductions under section 24			
(a) 30% of Net Annual Value 18,000			
(b) Interest on housing loan (50% of ₹ 88,000)	<u>44,000</u>		
	<u>62,000</u>	<u>(2,000)</u>	
Loss from house property			(32,000)

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Profits and gains of business or profession			
Fees from professional services		9,38,000	
Less: Expenses allowable as deduction			
Staff salary, bonus and stipend	1,50,000		
Other administrative expenses	48,000		
Office rent	30,000		
Motor car maintenance (10,000 x 4/5)	8,000		
Car loan interest – not allowable (since the same has not been paid and the assessee follows cash system of accounting)	<u>Nil</u>		
		<u>2,36,000</u>	
		7,02,000	
Less: Depreciation			
Motor car ₹ 4,25,000 x 7.5% x 4/5	25,500		
Books being annual publications @ 100%	20,000		
Furniture and fittings @ 10% of ₹ 60,000	6,000		
Plant and machinery @ 15% of ₹ 80,000	12,000		
Computer @ 60% of ₹ 50,000	30,000		
Computer (New) ₹ 30,000 @ 60% x ½ thereon	<u>9,000</u>		
		<u>1,02,500</u>	
Gross Total income			<u>5,99,500</u>
Less: Deduction under Chapter VI-A			5,67,500
Deduction under section 80C			
Housing loan principal repayment	1,00,000		
PPF subscription	20,000		
Life insurance premium	<u>24,000</u>		
Total ₹ 1,44,000 but limited to		1,00,000	
Deduction under section 80D			
Medical insurance premium paid ₹ 18,000 but limited to		<u>15,000</u>	
			<u>1,15,000</u>
Total income			4,52,500

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(b) Exigibility to service tax for services rendered in Jammu & Kashmir and other places:-

The services rendered inside the State of Jammu and Kashmir are not liable to service tax and hence, ₹ 26,12,000 is not chargeable to service tax.

The services rendered outside the State of Jammu and Kashmir are liable to service tax. Hence, receipts of ₹ 18,00,000 is liable to service tax.

The service tax liability would be $\text{₹ } 18,00,000 \times \frac{10.30}{110.30} = \text{₹ } 1,68,087.$

In case Ahmed & Co. was in Mumbai, the services rendered in the State of Jammu and Kashmir would not be liable to service tax levy and the services rendered at any place other than Jammu and Kashmir would be liable to service tax.

In effect, the value of taxable service and service tax liability would be the same. There won't be any change in value of taxable service and service tax liability.

Question 3

(a) *Shri Bala employed in ABC Co. Ltd. as Finance Manager gives you the list of perquisites provided by the company to him for the entire financial year 2010-11:*

- (i) *Medical facility given to his family in a hospital maintained by the company. The estimated value of benefit because of such facility is ₹ 40,000.*
- (ii) *Domestic servant was provided at the residence of Bala. Salary of domestic servant is ₹ 1,500 per month. The servant was engaged by him and the salary is reimbursed by the company (employer).*

In case the company has employed the domestic servant, what is the value of perquisite?

- (iii) *Free education was provided to his two children Arthy and Ashok in a school maintained and owned by the company. The cost of such education for Arthy is computed at ₹ 900 per month and for Ashok at ₹ 1,200 per month. No amount was recovered by the company for such education facility from Bala.*
- (iv) *The employer has provided movable assets such as television, refrigerator and air-conditioner at the residence of Bala. The actual cost of such assets provided to the employee is ₹ 1,10,000.*
- (v) *A gift voucher worth ₹ 10,000 was given on the occasion of his marriage anniversary. It is given by the company to all employees above certain grade.*

State the taxability or otherwise of the above said perquisites and compute the total value of taxable perquisites. (8 Marks)

(b) *State whether filing of income-tax return is mandatory for the assessment year 2011-12*

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in respect of the following cases:

- (i) Research association eligible for exemption under section 10(21) having total income of ₹2,10,000
- (ii) Registered trade union eligible for exemption under section 10(24) having following incomes:

Income from house property (computed)	₹60,000
Income from other sources (computed)	₹40,000
- (iii) A charitable trust registered under section 12AA, having total income of ₹1,90,000.
- (iv) A Limited Liability Partnership (LLP) with business loss of ₹1,30,000.

(4 Marks)

(c) State with reasons whether the following are liable for service tax :

- (i) Services rendered to Reserve Bank of India.
- (ii) Services rendered by a sub-contractor.
- (iii) Services provided to developer of special economic zone.
- (iv) Services rendered to associated enterprise.

(4 Marks)

Answer

(a) Taxability of perquisites provided by ABC Co. Ltd. to Shri Bala

- (i) Medical facility to employees' family in a hospital maintained by the employer is not a taxable perquisite. Regardless of the estimated value of benefit arising from such facility to the employee, it is exempt from tax. Therefore, the value of perquisite is Nil.
- (ii) Domestic servant was employed by the employee and the salary of such domestic servant was paid/reimbursed by the employer. It is taxable as perquisite for all categories of employees.

Taxable perquisite value = ₹ 1,500 × 12 = ₹ 18,000.

If the company had employed the domestic servant and the facility of such servant is given to the employee, then the perquisite is taxable only in the case of specified employees. The value of the taxable perquisite in such a case also would be ₹ 18,000.

- (iii) Where the educational institution is owned by the employer, the value of perquisite in respect of free education facility shall be determined with reference to the reasonable cost of such education in a similar institution in or near the locality.

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However, there would be no perquisite if the cost of such education per child does not exceed ₹ 1,000 per month.

Therefore, there would be no perquisite in respect of cost of free education provided to his child Arthy, since the cost does not exceed ₹ 1,000 per month.

However, the cost of free education provided to his child Ashok would be taxable, since the cost exceeds ₹ 1,000 per month. The taxable perquisite value would be ₹ 14,400 (₹ 1,200 × 12).

Note – An alternate view possible is that only the sum in excess of ₹ 1,000 per month is taxable. In such a case, the value of perquisite would be ₹ 2,400.

- (iv) Where the employer has provided movable assets to the employee or any member of his household, 10% per annum of the actual cost of such asset owned or the amount of hire charges incurred by the employer shall be the value of perquisite. However, this will not apply to laptops and computers. In this case, the movable assets are television, refrigerator and air conditioner and actual cost of such assets is ₹ 1,10,000.

The perquisite value would be 10% of the actual cost i.e., ₹ 11,000, being 10% of ₹ 1,10,000.

- (v) The value of any gift or voucher or token in lieu of gift received by the employee or by member of his household not exceeding ₹ 5,000 in aggregate during the previous year is exempt. In this case, the amount was received on the occasion of marriage anniversary and the sum exceeds the limit of ₹ 5,000.

Therefore, the entire amount of ₹ 10,000 is liable to tax as perquisite.

Note - An alternate view possible is that only the sum in excess of ₹ 5,000 is taxable in view of the language of Circular No.15/2001 dated 12.12.2001 that such gifts upto ₹ 5,000 in the aggregate per annum would be exempt, beyond which it would be taxed as a perquisite. As per this view, the value of perquisite would be ₹ 5,000.

Total value of taxable perquisite = ₹ 53,400 [i.e. ₹ 18,000 + 14,400 + 11,000 + 10,000].

Note - In case the alternate views are taken for items (iii) & (v), the total value of taxable perquisite would be ₹ 36,400 [i.e., ₹ 18,000 + 2,400 + 11,000 + 5,000].

- (b) (i) As per section 139(4C), a research association referred to in section 10(21) must file its return of income within the due date under section 139(1) if its total income, without giving effect to the provisions of section 10, exceeds the maximum amount which is not chargeable to income-tax.

Since the total income of the research association exceeds the basic exemption limit of ₹ 1,60,000, it has to file its return of income for the A.Y.2011-12.

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- (ii) As per section 139(4C), a registered trade union referred to in section 10(24) must file its return of income if the total income exceeds the basic exemption limit without giving effect to the provisions of section 10.
Since the total income of the trade union is less than the basic exemption limit of ₹ 1,60,000, it need not file its return of income for the A.Y. 2011-12.
 - (iii) As per section 139(4A), a charitable trust registered under section 12AA must file its return of income, if its total income computed as per the provisions of the Income-tax Act, 1961, without giving effect to the provisions of sections 11 and 12, exceeds the maximum amount which is not chargeable to income-tax. Since the total income of the charitable trust exceeds ₹ 1,60,000, it has to file its return of income for the A.Y. 2011-12.
 - (iv) As per third proviso to section 139(1), every company or firm shall furnish on or before the due date the return in respect of its income or loss in every previous year. Since LLP is included in the definition of firm under the Income-tax Act, 1961, it has to file its return mandatorily, even though it has incurred a loss.
- (c)
- (i) Services rendered to Reserve Bank of India are not liable to service tax by virtue of *Notification No. 22/2006 dated 31.05.2006*.
 - (ii) Services rendered by sub-contractor are liable to service tax. A sub-contractor is essentially a taxable service provider. The fact that services provided by such sub-contractors are used by the main service provider for completion of his work does not in any way alter the fact of provision of taxable service by the sub-contractor.
 - (iii) Services provided to developer of SEZ are not liable to service tax in view of the specific exemption granted vide *Notification No.9/2009 dated 03.03.2009*.
 - (iv) Services rendered to associated enterprise are liable to service tax. No special treatment from exigibility to service tax or exemption has been provided for services rendered to an associated enterprise.

Question 4

- (a) Decide the following transactions in the context of Income-tax Act, 1961 :
- (i) Mr. B transferred 500 shares of Reliance Industries Ltd. to M/s. B Co. (P) Ltd. on 10.10.2010 for ₹ 3,00,000 when the market price was ₹ 5,00,000. The indexed cost of acquisition of shares for Mr. B was computed at ₹ 4,45,000. The transfer was not subjected to securities transaction tax.

Determine the income chargeable to tax in the hands of Mr.B and M/s. B Co (P) Ltd. because of the above said transaction.
 - (ii) Ms. Chhaya transferred a vacant site to Ms. Dayama for ₹ 4,25,000. The stamp valuation authority fixed the value of vacant site for stamp duty purpose at 6,00,000. The total income of Chhaya and Dayama before considering the transfer of vacant

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site are ₹ 50,000 and ₹ 2,05,000, respectively. The indexed cost of acquisition for Ms. Chhaya in respect of vacant site is ₹ 4,00,000 (computed).

Determine the total income of both Ms. Chhaya and Ms. Dayama taking into account the above said transaction.

- (iii) Mr. Chezian is employed in a company with taxable salary income of ₹ 5,00,000. He received a cash gift of ₹ 1,00,000 from Atma Charitable Trust (registered under section 12AA) in December 2010 for meeting his medical expenses.

Is the cash gift so received from the trust chargeable to tax in the hands of Mr. Chezian? (6 Marks)

- (b) Balamurugan furnishes the following information for the year ended 31-03-2011:

	₹
Income from business	(1,35,000)
Income from house property	(15,000)
Lottery winning (Gross)	3,00,000
Speculation business income	1,00,000
Income by way of salary	60,000
Long term capital gain	70,000

Compute his total income, tax liability and advance tax obligations. (6 Marks)

- (c) A manufacturer sold goods to distributor for ₹ 20,000. The distributor sold the goods to the wholesaler for ₹ 24,000. The wholesaler sold the goods to the retailer for ₹ 30,000. The retailer sold the goods to the final consumer for ₹ 40,000. The VAT rate is 12.5% which is charged separately.

Compute VAT liability under Invoice method. State, why this method is preferable. (4 Marks)

Answer

- (a) (i) Transfer of shares without consideration or for inadequate consideration would attract the provisions of section 56(2)(vii), if the recipient is a firm or a company. The purpose of this provision is to prevent the practice of transferring unlisted shares at prices much below the fair market value.

The provisions of section 56(2)(vii) would, however, not be attracted in the case of, *inter alia*, transfer of shares of a company in which public are substantially interested. In this case, the shares of Reliance Industries Ltd. are transferred. Since Reliance Industries Ltd. is a company in which public are substantially interested, the provisions of section 56(2)(vii) would not be attracted in the hands of M/s. B Co. (P) Ltd.

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The indexed cost of acquisition (₹ 4,45,000) less the actual sale consideration (₹ 3,00,000) would result in a long term capital loss of ₹ 1,45,000 in the hands of Mr.B, which is eligible for set off against any other long term capital gain.

- (ii) Transfer of immovable property for inadequate consideration will not have any tax implication in the hands of transferee under section 56(2)(vii). Therefore, in the hands of transferee, i.e., Ms. Dayama, the provisions of section 56(2)(vii) would not be attracted. However, for the transferor, Ms. Chhaya, the value adopted for stamp duty purpose will be taken as the deemed sale consideration under section 50C for computation of capital gains.

Particulars	Chhaya (Transferor) ₹	Dayama (Transferee) ₹
Capital gains		
Deemed sale consideration under section 50C	6,00,000	
Less: Indexed cost of acquisition	<u>4,00,000</u>	
	2,00,000	
Other income (computed)	<u>50,000</u>	<u>2,05,000</u>
Total income	2,50,000	2,05,000

- (iii) The provisions of section 56(2)(vii) would not apply to any sum of money or any property received from any trust or institution registered under section 12AA. Therefore, the cash gift of ₹ 1 lakh received from Atma Charitable Trust, being a trust registered under section 12AA, for meeting medical expenses would not be chargeable to tax under section 56(2)(vii) in the hands of Mr. Chezian.

(b) Computation of total income of Balamurugan for the year ended 31.03.2011

Particulars	₹	₹
Salaries	60,000	
Less: Loss from house property	<u>(15,000)</u>	
Net Salary (after set off of loss from house property)		45,000
Profits and gains of business or profession		
Speculation business income	1,00,000	
Less: Business loss set-off	<u>(1,35,000)</u>	
Net business loss to be set-off against long-term capital gain	(35,000)	
Capital Gains		
Long term capital gain	70,000	

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Less: Business loss set-off	<u>(35,000)</u>	
Long term capital gain after set off of business loss		35,000
Income from other sources		
Lottery winnings (Gross)		<u>3,00,000</u>
Total Income		<u>3,80,000</u>

Computation of tax liability

Particulars	₹
On total income of ₹ 80,000 (excluding lottery winning)	Nil
On lottery winnings of ₹ 3,00,000 @ 30%	90,000
Add: Education Cess @ 2% and Secondary and higher education cess@1%	<u>2,700</u>
Total tax liability	<u>92,700</u>

The assessee need not pay advance tax since the total income (excluding lottery income) liable to tax is below the basic exemption limit. Further, in respect of lottery income, tax would have been deducted at source @ 30% under section 194B. Since the remaining tax liability of ₹ 2,700 (₹ 92,700 – ₹ 90,000) is less than ₹ 10,000, advance tax liability is not attracted.

Note

- (1) The basic exemption limit of ₹ 1,60,000 has to be first exhausted against salary income of ₹ 45,000. The unexhausted basic exemption limit of ₹ 1,15,000 can be adjusted against long-term capital gains of ₹ 35,000 as per section 112, but not against lottery winnings which are taxable at a flat rate of 30% under section 115BB.
- (2) The first proviso to section 234C(1) provides that since it is not possible for the assessee to estimate his income from lotteries, the entire amount of tax payable (after considering TDS) on such income should be paid in the remaining instalments of advance tax which are due. Where no such instalment is due, the entire tax should be paid by 31st March, 2011. The first proviso to section 234C(1) would be attracted in case of non-deduction or short-deduction of tax at source under section 194B.

(c) Computation of VAT liability under invoice method

Particulars	VAT liability ₹	Less VAT credit ₹	Tax to Government ₹
Manufacturer sells the goods to distributor. ₹ 20,000 x 12.5%	2,500	--	2,500

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Distributor sells the goods to wholesaler. ₹ 24,000 x 12.5%	3,000	2,500	500
Wholesaler sells the goods to a retailer. ₹ 30,000 x 12.5%	3,750	3,000	750
Retailer sold the goods to consumer. ₹ 40,000 x 12.5%	5,000	3,750	1,250
Total	14,250	9,250	5,000

This method is preferable as the tax is charged at each stage of sales on the entire sales value and the tax paid at the earlier stage is allowed as set off. In India, the VAT law as introduced in several States and under the Central Excise Law, this method is followed.

Question 5

(a) Mr. Chaturvedi having gross total income of ₹ 6,35,000 for the financial year 2010-11 furnishes you the following information:

- (i) Deposited ₹ 50,000 in tax saver deposit in the name of major son in a nationalized bank.
- (ii) Paid ₹ 25,000 towards premium on life insurance policy of his married daughter.
- (iii) Purchased approved long-term infrastructure bonds for ₹ 25,000 in January 2011.
- (iv) Contributed ₹ 10,000 to Prime Minister's National Relief Fund.
- (v) Donated ₹ 20,000 to a Government recognized institution for scientific research.

Note : Assume that the gross total income of Mr. Chaturvedi does not include any income under the head 'Profits and gains of business or profession'.

Compute the total income of Mr. Chaturvedi for the assessment year 2011-12. (7 Marks)

(b) List any 5 instances where the tax deductible at source in terms of section 194A will not apply. (5 Marks)

(c) When does e-payment and e-filing of service tax return become mandatory? Explain.

(4 Marks)

Answer

(a) **Computation of total income of Mr. Chaturvedi for the A.Y.2011-12**

Particulars	₹	₹
Gross total income		6,35,000
Less: Deductions under Chapter VI-A		
(i) Deposit of ₹ 50,000 in tax saver deposit in the name of major son in a nationalized bank – Fixed deposit in the name of son	-	

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does not qualify for deduction under section 80C		
(ii) Premium on life insurance policy of his married daughter - Eligible for deduction under section 80C	25,000	
(iii) Long term infrastructure bonds ₹ 25,000 eligible for deduction under section 80CCF, subject to a maximum of ₹ 20,000	20,000	
(iv) Contribution of ₹ 10,000 to PM's National Relief Fund. eligible for 100% deduction under section 80G	10,000	
(v) Payment of ₹ 20,000 to a Government recognized institution for scientific research - Eligible for deduction under section 80GGA	<u>20,000</u>	
Total Income		<u>75,000</u> <u>5,60,000</u>

- (b) The provisions of section 194A will not apply where the interest credited or paid does not exceed ₹ 10,000 where the payer is a banking company or a cooperative society engaged in the business of banking or where the interest is on any deposit with post office under any scheme framed by the Central Government and notified by it. In respect of other cases, TDS provisions under section 194A would not apply where the interest credited or paid or likely to be credited or paid during the financial year does not exceed ₹ 5,000.

The provisions of section 194A will not apply in the following cases where the -

- (1) interest is credited or paid by a firm to a partner of the firm;
- (2) interest is credited or paid to any banking company or any financial corporation established by or under a Central, State or Provincial Act or Life Insurance Corporation of India or Unit Trust of India or any company or co-operative society carrying on the business of insurance or such other institution, association or body or class of institutions, associations or bodies notified by the Central Government;
- (3) interest credited or paid by a co-operative society to a member thereof or to any other co-operative society;
- (4) interest credited or paid in respect of deposits under any scheme framed by the Central Government and notified by it in this behalf;
- (5) interest credited or paid in respect of deposits with primary agricultural credit society or a primary credit society or a co-operative land mortgage bank or a co-operative land development bank;
- (6) interest income credited or paid by the Central Government under any provision of the Income-tax Act, the Estate Duty Act, the Wealth-tax Act etc.;

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- (7) income credited or paid by way of interest on the compensation amount awarded by the Motor Accidents Claims Tribunal where the amount of such income or, as the case may be, the aggregate of the amounts of such income credited or paid during the financial year does not exceed ₹ 50,000;
- (8) income paid or payable by an infrastructure capital company or infrastructure capital fund or public sector company or scheduled bank in relation to a zero coupon bond issued on or after 1.6.2005.

Note – Any five of the above mentioned may be given in the answer.

- (c) *Notification no. 1/2010- ST dated 19.02.2010* has amended rule 6(2) of the Service Tax Rules, 1994 w.e.f. 1st April, 2010. As per the amended rule, e-payment and e-filing are mandatory in the following cases:

E-payment of service tax

An assessee shall deposit the service tax electronically through internet banking if he has paid the total service tax of ₹ 10 lakhs or more (including the amount of service tax paid by utilization of CENVAT credit) in the preceding financial year.

E-filing of service tax return

Electronic filing of service tax return is mandatory for the assessee who has paid service tax of ₹ 10 lakhs or more (including the amount of service tax paid by utilization of CENVAT credit) in the preceding financial year.

Question 6

- (a) *X Co. (P) Ltd., converted into a Limited Liability Partnership (LLP) by name All Trade LLP, with effect from 01.04.2010.*

The following details are given to you:

<i>Asst. year 2003-04 : Business loss brought forward</i>	<i>₹ 2,00,000</i>
<i>Asst. year 2010-11 : Business loss brought forward</i>	<i>₹ 5,00,000</i>
<i>(These are related to erstwhile X Co. (P) Ltd.)</i>	
<i>Total income of All Trade LLP, for the financial year 2010-11 (Before set off of brought forward business losses of erstwhile company i.e. X Co. (P) Ltd.)</i>	<i>₹ 6,00,000</i>

Assume that all the conditions prescribed in section 47(xiiib) were satisfied by X Co. (P) Ltd. at the time of conversion in to LLP.

- (i) *Explain whether All Trade LLP can set off and carry forward the business loss of its predecessor i.e. X Co. (P) Ltd.?*
- (ii) *State whether any change in partners of All Trade LLP at later date would have any tax consequence.* (4 Marks)

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- (b) Ramamurthy had 4 heavy goods vehicles as on 1.4.2010. He acquired 7 heavy goods vehicles on 27.6.2010. He sold 2 heavy goods vehicles on 31.5.2010.

He has brought forward business loss of ₹ 50,000 relating to assessment year 2007-08 of a discontinued business. Assuming that he opts for presumptive taxation of income as per section 44AE, compute his total income chargeable to tax for the assessment year 2011-12. (4 Marks)

- (c) Win Limited commenced the business of operating a three star hotel in Tirupati on 1-4-2010.

It furnishes you the following information:

- (i) Cost of land (acquired in June 2008) ₹ 60 lakhs

- (ii) Cost of construction of hotel building

Financial year 2008-09 ₹ 30 lakhs

Financial year 2009-10 ₹ 150 lakhs

- (iii) Plant and Machineries (all new) acquired during financial year 2009-10 ₹ 30 lakhs

[All the above expenditures were capitalized in the books of the company]

Net profit before depreciation for the financial year 2010-11 ₹ 80 lakhs

Determine the amount eligible for deduction under section 35AD of the Income-tax Act, 1961, for the assessment year 2011-12. (4 Marks)

- (d) How excess payment of service tax would be adjusted against service tax liability of subsequent periods? State the applicable conditions. (4 Marks)

Answer

- (a) (i) Sub-section (6A), inserted by the Finance Act, 2010 in section 72A, provides that where a private company is succeeded by a LLP fulfilling the conditions laid down in the proviso to section 47(xiiib), then, notwithstanding anything contained in any other provision of the Income-tax Act, 1961, the accumulated loss and unabsorbed depreciation of the predecessor company shall be deemed to be the loss or allowance for depreciation of the successor LLP for the purpose of the previous year in which the business reorganisation was effected and other provisions of the Act relating to set-off and carry forward of losses and depreciation allowance shall apply accordingly.

Therefore, All Trade LLP can carry forward and set-off the business loss of ₹ 7 lakh of erstwhile X Co (P) Ltd. against its business income for the F.Y.2010-11. The unabsorbed business loss will be carried forward to the next year.

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- (ii) Section 47(xiiib) requires that the shareholders of the company become partners of the LLP in the same proportion as their shareholding in the company. Further, the erstwhile shareholders of the company should continue to be entitled to receive at least 50% of the profits of the LLP for a period of 5 years from the date of conversion. If the entity fails to fulfil this condition, the benefit of set-off of business loss availed by the LLP would be deemed to be the profits and gains of the LLP chargeable to tax in the previous year in which the LLP fails to fulfil the condition.

(b) Computation of total income of Mr. Ramamurthy for A.Y.2011-12

Particulars	₹
Presumptive business income under section 44AE	
4 heavy goods vehicles for 2 months (4 x ₹ 5,000 x 2)	40,000
Balance 2 heavy goods vehicles for 10 months (2 x ₹ 5,000 x 10)	1,00,000
7 heavy goods vehicles for 10 months (7 x ₹ 5,000 x 10)	<u>3,50,000</u>
Business Income	4,90,000
Less: Brought forward business loss of discontinued business	<u>50,000</u>
Total Income	<u>4,40,000</u>

Note: The assessee is eligible for computing the income from goods carriages applying the presumptive provisions of section 44AE, since he did not own more than 10 goods carriages at any time during the previous year.

- (c) Under section 35AD, 100% of the capital expenditure incurred during the previous year, wholly and exclusively for the specified business, which includes the business of building and operating a hotel of two-star or above category anywhere in India which commences its operations on or after 1.4.2010, would be allowed as deduction from the business income. However, expenditure incurred on acquisition of any land, goodwill or financial instrument would not be eligible for deduction.

Further, the expenditure incurred, wholly and exclusively, for the purpose of specified business prior to commencement of operation would be allowed as deduction during the previous year in which the assessee commences operation of his specified business. A condition has been inserted that such amount incurred prior to commencement should be capitalized in the books of account of the assessee on the date of commencement of its operations.

Accordingly, the deduction under section 35AD for the A.Y.2011-12 in the case of Win Ltd. would be calculated as follows, assuming that the expenditures were capitalised in the books of the company on 1.4.2010, being the date of commencement of operations-

Particulars	₹ (in lakhs)
Cost of land (not eligible for deduction under section 35AD)	Nil

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Cost of construction of hotel building (₹ 30 lakhs + ₹ 150 lakhs)	180
Cost of plant and machinery	<u>30</u>
Deduction under section 35AD	<u>210</u>

Note - For A.Y.2011-12, the loss from specified business of operating a three star hotel would be ₹ 130 lakhs (i.e. ₹ 210 lakhs – ₹ 80 lakhs). As per section 73A, any loss computed in respect of the specified business referred to in section 35AD shall be set off only against profits and gains, if any, of any other specified business. The unabsorbed loss, if any, will be carried forward for set off against profits and gains of any specified business in the following assessment year.

- (d) Where an assessee has paid to the credit of Central Government any amount in excess of the amount required to be paid towards service tax liability for a month or quarter as the case may be, the assessee may adjust such excess amount paid by him against his service tax liability for the succeeding month or quarter, as the case may be. However, such an adjustment is subject to the following conditions:
- (i) Self-adjustment of excess credit would not be allowed in case of reasons involving interpretation of law, taxability, classification, valuation or applicability of any exemption notification.
 - (ii) Excess amount paid and proposed to be adjusted should not exceed ₹ 1,00,000 for the relevant month or quarter. However, in case of assessee's opting for centralized registration excess amount can be adjusted without any monetary limit provided the excess amount paid is on account of delayed receipt of details of payments from branch offices.
 - (iii) Adjustment can be made only in the succeeding month or quarter.
 - (iv) The details of self-adjustment should be intimated to the Superintendent of Central Excise within a period of 15 days from the date of such adjustment.

Question 7

- (a) Answer any **three** sub-parts out of **four** sub-parts of the question.
- (i) What are the conditions to be satisfied for the allowability of expenditure under section 37 of the Income-tax Act, 1961?
 - (ii) Answer the following with reference to the provisions of the Income-tax Act, 1961 :
 - (a) Bad debt claim disallowed in an earlier assessment year, recovered subsequently. Is the sum recovered, chargeable to tax?
 - (b) Return of income of a company was signed by the Company Secretary. Is the return a valid return?
 - (c) Tax deducted at source on salary paid to employees not remitted till the 'due date'

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for filing the return prescribed in section 139. Is the expenditure to be disallowed under section 40(a)(ia)?

- (d) X Co. Ltd. paid ₹ 120 lakhs as compensation as per approved Voluntary Retirement Scheme (VRS) during the financial year 2010-11.

How much is deductible under section 35DDA for the assessment year 2011-12?

- (iii) Ashwin doing manufacture and wholesale trade furnishes you the following information :

Total turnover for the financial year

	₹
2009-10	45,00,000
2010-11	55,00,000

State whether tax deduction at source provisions are attracted for the below said expenses incurred during the financial year 2010-11:

	₹
Interest paid to UCO Bank	41,000
Contract payment to Raj (2 contracts of ₹ 12,000 each)	24,000
Shop rent paid (one payee)	1,90,000
Commission paid to Balu	7,000

- (iv) Y Co. Ltd. furnishes you the following information for the year ended 31.3.2011:

	₹
Total turnover of Unit A located in Special Economic Zone	100 lakhs
Profit of the business of Unit A	30 lakhs
Export turnover of Unit A	50 lakhs
Total turnover of Unit B located in Domestic Tariff Area (DTA)	200 lakhs
Profit of the business of Unit B	20 lakhs

Compute deduction under section 10AA for the A. Y. 2011-12.

(3×4 = 12 Marks)

- (b) Briefly state the contents of VAT invoice (any 8 items)

(4 Marks)

Answer

- (a) (i) The following conditions are to be fulfilled for the allowability of expenditure under section 37 -

- (1) The expenditure should not be of the nature described in section 30 to 36;
- (2) It should not be in the nature of personal expenditure of the assessee;

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- (3) It should have been incurred by the assessee during the previous year.
 - (4) The expenditure should have been laid out or expended wholly or exclusively for the purposes of the business or profession.
 - (5) It should not be in the nature of a capital expenditure.
 - (6) It should not have been incurred for any propose which is an offence or which is prohibited by law.
- (ii) (a) Recovery of a bad debt claim disallowed in the earlier year cannot be brought to tax under section 41(4). Section 41(4) can be invoked only in a case where bad debts or part thereof has been allowed as deduction earlier under section 36(1)(vii).
- (b) Where the return of income of a company was signed by a company secretary although it is supposed to be signed by a Managing Director or a Director (in the absence of a Managing Director), it is a defective return, which can be rectified and not an invalid return.

Note:

- (1) *There is an alternate view that the return of income of a company, which is not signed and verified by the Managing Director or Director, is not a defective return but an invalid return and thus, void-ab-initio.*
 - (2) *In case of a company not resident in India, the return of income may be signed and verified by any person who holds a valid power of attorney. Since the question does not specify the residential status of a company, it is possible to answer that the return is valid if the company is non-resident and the Company Secretary holds a valid power of attorney.*
- (c) The salary expenditure is allowable while computing the income of the employer even though TDS has not been deposited within the due date under section 139(1). The disallowance under section 40(a)(ia) will not apply for non-deduction of tax at source from income chargeable under the head "Salaries".
- (d) It is deductible in 5 equal annual instalments commencing from the previous year of payment. ₹ 24 lakhs, being 1/5th of ₹ 120 lakhs, is deductible under section 35DDA for the A.Y.2011-12.
- (iii) As the turnover of Ashwin for F.Y.2009-10, i.e. ₹ 45 lakh, has exceeded the monetary limit of ₹ 40 lakh prescribed under section 44AB, he has to comply with the tax deduction provisions during the financial year 2010-11, subject to however the exemptions provided for under the relevant sections for applicability of TDS provisions.

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Interest paid to UCO Bank

TDS under section 194A is not attracted in respect of interest paid to a banking company.

Contract payment of ₹ 24,000 to Raj for 2 contracts of ₹ 12,000 each

TDS provisions under section 194C would not be attracted if the amount paid to a contractor does not exceed ₹ 30,000 in a single payment or ₹ 75,000 in the aggregate during the financial year. Therefore, TDS provisions under section 194C are not attracted in this case.

Shop Rent paid to one payee – Tax has to be deducted under section 194-I as the rental payment exceeds ₹ 1,80,000.

Commission paid to Balu – Tax has to be deducted under section 194-H as the commission exceeds ₹ 5,000.

Note

- (1) *The monetary limit of turnover for tax audit under section 44AB has been increased from ₹ 40 lakh to ₹ 60 lakh w.e.f. A.Y.2011-12. However, for determining the applicability of TDS provisions under section 194A for F.Y.2010-11, the turnover and monetary limit under section 44AB for F.Y.2009-10 are relevant.*
 - (2) *The Finance Act, 2010 has increased the threshold limits for applicability of TDS provisions w.e.f. 1st July, 2010. It is presumed that the payments specified in the question were made on or after 1st July, 2010, and accordingly, the reasoning has been given on the basis of the provisions as amended by the Finance Act, 2010 w.e.f. 1.7.2010.*
- (iv) 100% of the profit derived from export of articles or things or services is eligible for deduction under section 10AA, assuming that F.Y.2010-11 falls within the first five year period commencing from the year of manufacture or production of articles or things or provision of services by the Unit in SEZ. As per section 10AA(7), the profit derived from export of articles or things or services shall be the amount which bears to the profits of the business of the undertaking, being the Unit, the same proportion as the export turnover in respect of articles or things or services bears to the total turnover of the business carried on by the undertaking.

Deduction under section 10AA

$$\begin{aligned} &= \text{Profit of the business of Unit A} \times \frac{\text{Export Turnover of Unit A}}{\text{Total Turnover of Unit A}} \\ &= ₹ 30 \text{ lakhs} \times \frac{50}{100} \\ &= ₹ 15 \text{ lakhs} \end{aligned}$$

(b) Contents of VAT invoice:

The tax invoice should contain the following:

- (i) the words 'tax invoice' in a prominent place;
- (ii) name and address of the selling dealer;
- (iii) registration number of the selling dealer;
- (iv) name and address of the purchasing dealer;
- (v) registration number of the purchasing dealer;
- (vi) pre-printed or self generated serial number;
- (vii) date of issue;
- (viii) description, quantity and value of goods sold.
- (ix) rate and amount of tax charged in respect of taxable goods;
- (x) signature of the selling dealer or his regular employee duly authorised by him for such purpose.