

MOCK TEST PAPER – 2

PCC: GROUP – II

PAPER – 5 : TAXATION

SUGGESTED ANSWERS / HINTS

1. (a) Computation of taxable income of Mrs. Sita and Mrs. Geeta for the A.Y.2012-13

S. No.	Particulars	Mrs. Sita	Mrs. Geeta
		₹	₹
(I)	Salaries Pension received from State Government Pension received from Australian Government is not taxable in the case of a non-resident since it is earned and received outside India	Nil	10,000
		<u>Nil</u>	<u>10,000</u>
(II)	Income from house property Rent received from house property at Delhi (assumed to be the annual value in the absence of other information i.e. municipal value, fair rent and standard rent) Less: Deduction under section 24(a)@30%	60,000 <u>18,000</u> <u>42,000</u>	30,000 <u>9,000</u> <u>21,000</u>
(III)	Capital gains Long-term capital gain on sale of land at Delhi Short term capital gain on sale of shares of Indian listed companies in respect of which STT was paid	1,00,000 <u>20,000</u> <u>1,20,000</u>	50,000 <u>2,00,000</u> <u>2,50,000</u>
(A)	Gross Total Income [(I)+(II)+(III)] Less: Deductions under Chapter VIA	1,62,000	2,81,000
1.	Deduction under section 80C		
1.	LIC Premium paid	-	10,000
2.	Premium paid to Australian Life Insurance Corporation	10,000	
3.	Tax Saving Bond (assuming that they are notified infrastructure bonds)		

	eligible for deduction under section 80C)	<u>30,000</u>	<u>20,000</u>
		40,000	30,000
2.	Deduction under section 80D – Mediclaim premium paid (assuming that the same is paid by cheque)	<u>Nil</u>	<u>5,000</u>
		40,000	35,000
(B)	Total deduction under Chapter VIA is restricted to income other than capital gains taxable under sections 111A & 112	<u>40,000</u>	<u>31,000</u>
(C)	Total income (A-B)	<u>1,22,000</u>	<u>2,50,000</u>
	Tax liability of Mrs. Sita for A.Y. 2012-13		
	Tax on long-term capital gains @ 20%	20,000	
	Tax on short-term capital gains @ 15%	<u>3,000</u>	
		23,000	
	Tax liability of Mrs. Geeta for A.Y.2012-13		
	Tax on short-term capital gains @ 15% of ₹60,000 [i.e. ₹ 2,00,000 less ₹ 1,40,000, being the unexhausted basic exemption limit as per proviso to section 111A]		9,000
	Education cess @ 2% & SHEC@ 1%	<u>690</u>	<u>270</u>
	Total tax payable	<u>23,690</u>	<u>9,270</u>

Note :

- (1) Long-term capital gains is chargeable to tax @ 20% as per section 112.
- (2) Short-term capital gains on transfer of equity shares in respect of which securities transaction tax is paid is subject to tax @ 15% as per section 111A.
- (3) In case of resident individuals, if the basic exemption limit is not fully exhausted against other income, then the long-term capital gains/short-term capital gains will be reduced by the unexhausted basic exemption limit and only the balance will be taxed at 20%/10% respectively. However, this benefit is not available to non-residents. Therefore, while Mrs. Geeta can set-off unexhausted basic exemption limit against long-term capital gains and short-term capital gains taxable under section 111A, Mrs. Sita cannot do so.
- (4) Since long-term capital gains is taxable at the rate of 20% and short-term capital gains is taxable at the rate of 15%, it is more beneficial for Mrs. Geeta to first exhaust her basic exemption limit of ₹ 1,90,000 against long-term

capital gains of ₹ 50,000 and the balance limit of ₹ 1,40,000 (i.e., ₹ 1,90,000 – ₹ 50,000) against short-term capital gains.

- (b) On analyzing the information given about the period of stay of Rupesh in India, the following position emerges:

Previous year	Assessment year	Period of stay (Number of days)
2008- 2009	2009- 2010	303
2009- 2010	2010- 2011	-
2010- 2011	2011- 2012	61
2011- 2012	2012- 2013	62

Considering the number of days of stay during each of the previous years, the residential status of Rupesh is determined as follows:

- For the assessment year 2009-2010, Rupesh has stayed for not less than 182 days during the relevant previous year 2008-2009. Hence, he is a resident. Also he satisfies the two additional conditions for not ordinarily resident. Therefore, status of Rupesh for the A.Y.2009-10 is Resident but Not Ordinarily Resident.
- For the assessment year 2010-11, he has never stayed in India. Therefore, he is a non-resident, as having not fulfilled any of the two basic conditions.
- For the assessment year 2011-12, the period of stay is 60 days. According to section 6, an individual who stays for 60 days or more should also fulfill the requirement of stay of 365 days or more during the preceding 4 years. This limb of the basic condition is not satisfied and therefore, he is a non-resident.
- For the assessment year 2012-13, the period of stay does not satisfy any of 2 basic conditions. Therefore, he is a non-resident.

Note : -

The information about stay of Rupesh's wife and children in India is not relevant to determine the residential status of Rupesh. Similarly, maintenance of a residence in India is not relevant for determination of residential status.

- (c) **Computation of VAT payable for the quarter ending 31st March, 2012:-**

Particulars	₹	₹
Output tax payable = ₹ 1,00,00,000 × 4%		4,00,000
Less: Input tax credit		
On raw material purchased @ 12.5%		
(₹ 60,00,000 × 12.5%)	7,50,000	
Less: Inputs used in the manufacture of exempted goods		

sold (₹ 20,00,000 × 12.5%) [Note – 1]	<u>2,50,000</u>	<u>5,00,000</u>
Net VAT payable		(1,00,000)
CST payable on inter state sale adjusted (₹ 10,00,000 × 2%)		20,000
Balance of input tax credit carried forward to next quarter (₹ 20,000-₹ 1,00,000)		80,000

Note:

1. If the goods manufactured from raw material are exempt from tax, no input tax credit is available on such raw material.
2. Import duty paid on high seas purchases is not eligible for input tax credit.
3. Purchases of raw material within the State on which VAT has been paid @ 4% are not eligible for input tax credit because invoice for the said purchases does not show the amount of tax separately.

2. (a) Computation of Relief under section 89 for the Assessment Year 2012-13

Particulars	₹	₹
Salary Income for the year excluding the arrears		5,60,000
Add: Arrears relating to Financial Year 2005-06		<u>40,000</u>
Gross Total Income		6,00,000
Less: Deduction under chapter VI-A		
Contribution to Public Provident Fund		<u>35,000</u>
Total Income		<u>5,65,000</u>
Assessment year 2012-13		
Tax on ₹ 5,65,000		
First ₹ 1,80,000	Nil	NIL
Next ₹ 3,20,000	10%	32,000
Balance ₹ <u>65,000</u>	20%	<u>13,000</u>
<u>5,65,000</u>		45,000
Add: Education cess @ 2%		900
Secondary and higher education cess @1%		<u>450</u>
Tax on total income (including arrears) (A)		<u>46,350</u>
Total Income excluding arrears		5,25,000
Tax on ₹ 5,25,000		
First ₹ 1,80,000	Nil	NIL
Next ₹ 3,20,000	10%	32,000
Balance ₹ <u>25,000</u>	20%	<u>5,000</u>

	<u>5,25,000</u>	37,000	
Add : Education cess @ 2%		740	
Secondary and higher education cess @ 1%		<u>370</u>	
Tax on total income (excluding arrears) (B)		<u>38,110</u>	
Difference between A & B I			8,240
Assessment Year 2006-07			
Total Income assessed			1,40,000
Add: Arrears relating to Financial year 2005-06			<u>40,000</u>
Total income (including arrears)			1,80,000
Tax on ₹ 1,80,000		11,000	
Add: Education Cess @ 2%		<u>220</u>	
Tax on total income (including arrears) (C)		<u>11,220</u>	
Total Income excluding arrears			1,40,000
Tax on ₹ 1,40,000		4,000	
Add: Education Cess @ 2%		<u>80</u>	
Tax on total income (excluding arrears) (D)		<u>4,080</u>	
Difference between C & D II			7,140
Relief under section 89 (I – II)			1,100
Tax payable for A.Y. 2012-13 (₹ 46,350 – ₹ 1,100)			45,250

(b) An individual is said to be resident in India in any previous year, if he -

- has been in India during that year for a total period of 182 days or more, or
- has been in India during the four years immediately preceding that year for a total period of 365 days or more and has been in India for at least 60 days in that year.

In this case, X has been in India only from 1.4.2011 to 30.04.2011 i.e. for 30 days. Therefore, he does not satisfy either of the conditions in (i) or (ii) and is, hence, a non-resident. Y, who left India one week before X's departure, is also a non-resident for the same reasons.

Section 9(1)(v) provides that income by way of interest payable by a non-resident in respect of any debt incurred, or moneys borrowed and used, for the purposes of a business or profession carried on by such person in India shall be deemed to accrue or arise in India.

Therefore, interest payable by a non-resident in respect of any debt incurred, or moneys borrowed and used, for the purpose of making or earning any income from

any source other than a business or profession carried on by him in India, shall not be deemed to accrue or arise in India. Therefore, interest payable by X on money borrowed from Y to invest in shares of an Indian company shall not be deemed to accrue or arise in India and hence, is not taxable in India in the hands of Y.

- (c) Computation of taxable value of services provided by the C.J. Professionals for the half year ending on 30.09.2011:

Particulars	₹
Total bills raised(Note 1)	7,65,000
Less: Bill raised on an approved International Organisation (Note 2)	<u>65,000</u>
	7,00,000
Add: Advance received for the services to be provided in October '11 (Note 3)	<u>1,50,000</u>
Taxable value of services	<u>8,50,000</u>
Computation of service tax payable	
Taxable value of services	8,50,000
Service tax @ 10%	85,000
Add: Education cess @ 2%	1,700
Add: Secondary and higher education cess @ 1%	<u>850</u>
Total service tax payable	87,550

Notes:

- Point of taxation is date of issue of invoice or receipt of payment whichever is earlier [Rule 3 of Point of Taxation Rules, 2011]
 - Services provided to an International Organisation are exempt from the service tax *vide Notification No. 16/2002 ST dated 02.08.2002*.
 - Any advance received for providing any taxable services forms part of the value of taxable service [Section 67 of the Finance Act, 1994]. Further in case of advance, point of taxation is the date of receipt of advance.[Rule 3 of Point of Taxation Rules, 2011].
3. (a) There are two units of the house. Unit I with 2/3rd area is used by Manoj for self-occupation throughout the year and no benefit is derived from that unit, hence it will be treated as self-occupied and its annual value will be nil. Unit 2 with 1/3rd area is let-out through out the previous year and its annual value has to be determined as per section 23(1).

Computation of Income from house property of Mr. Manoj for A.Y. 2012-13

Particulars	Amount in rupees
Unit I (2/3 rd area – self-occupied)	

Annual Value		Nil
Less: Deduction u/s 24(b) 2/3 rd of ₹ 1,20,000		80,000
Income from Unit I (self-occupied)		-80,000
Unit II (1/3rd area – let out)		
Computation of Gross Annual Value		
Step I – Compute Annual Value		
Annual Value = Higher of municipal value and fair rent, restricted to standard rent. However, in this case, standard rent of ₹ 1,20,000 (1/3 rd of ₹ 3,60,000) is more than the higher of municipal value of ₹ 80,000 (1/3 rd of ₹ 2,40,000) and fair rent of ₹ 1,00,000 (1/3 rd of ₹ 3,00,000). Hence the higher of municipal value and fair rent is the Annual Value. In this case, it is the fair rent.	1,00,000	
Step 2 – Compute actual rent received/ receivable ₹ 7,500 × 12 = ₹ 90,000	90,000	
Step 3 –Gross Annual Value is the higher of Annual Value and actual rent received/receivable i.e. higher of ₹ 1,00,000 and ₹ 90,000	1,00,000	
Gross Annual Value (GAV)		1,00,000
Less: Municipal taxes paid by the owner during the previous year relating to let-out portion 1/3 rd of (12.5% of ₹ 2,40,000) = ₹ 30000/3 = ₹ 10,000		10,000
Net Annual Value (NAV) = (₹ 1,00,000-₹ 10,000)		90,000
Less: Deductions under section 24		
(a) 30% of NAV = 30% of ₹ 90,000	27,000	
(b) Interest paid on borrowed capital (relating to let out portion) 1/3 rd of ₹ 1,20,000	40,000	67,000
Income from Unit II (let-out)		23,000
Loss under the head “Income from house property” = -₹ 80,000 + ₹ 23,000		-57000

- (b) (i) **True** : As per section 2(48), ‘Zero Coupon Bond’ means a bond issued by any infrastructure capital company or infrastructure capital fund or a public sector company on or after 1st June 2005, in respect of which no payment and benefit

is received or receivable before maturity or redemption from such issuing entity and which the Central Government may notify in this behalf.

- (ii) **False** : The exemption under section 54EC has been restricted, by limiting the maximum investment in long term specified assets (i.e. bonds of NHAI or RECL, redeemable after 3 years) to ₹50 lakh during any financial year. Therefore, in this case, the exemption under section 54EC can be availed only to the extent of ₹50 lakh, provided the investment is made before 1.11.2011 (i.e., within six months from the date of transfer).
- (c) The VAT is a system based simply on transactions. Thus there is no need to go through complicated definitions like sales, sales price, turnover of purchases and turnover of sales. The tax is also broad-based and applicable to all sales in business leaving little room for different interpretations. Thus, this system brings certainty to a great extent.

Also, under a VAT system, the buyer knows, out of the total consideration paid for purchase of material, what is tax component. Thus, the system ensures transparency also. This transparency enables the State Governments to know as to what is the exact amount of tax coming at each stage. Thus, it is a great aid to the Government while taking decisions with regard to rate of tax etc.

4. (a) 1. As per section 35(2AB), where a **company** engaged in, inter alia, the business of biotechnology incurs any expenditure on scientific research during the current year, it is eligible for claiming weighted deduction of a sum equal to 200% of the eligible expenditure. However this weighted deduction is not available to any assessee other than company.

The eligible expenditure and quantum of deduction will be:

Any expenditure incurred during earlier 3 years immediately preceding the date of commencement of business on payment of salary or purchase of materials, or capital expenditure incurred other than expenditure on acquisition of land [actual expenditure qualifies for deduction under section 35(1)].

The deduction available under section 35 for scientific research will, therefore, be:

	Particulars	₹
(a)	Land	Nil
(b)	Building	22,80,000
(c)	Revenue expenses of last 3 years	4,40,000
(d)	Capital expenditure of last 3 years: Plant and machinery	5,00,000
(e)	Current year revenue expenditure	1,80,000

Total deduction under section 35

34,00,000

2. Section 41(3) provides that where a capital asset used for scientific research is sold, without having been used for other purposes, the lower of sale proceeds or the total amount of deduction earlier allowed under section 35 will be considered as income from business of the previous year in which the sale took place.

Therefore, the income chargeable to tax under section 41(3) should be lower of the following:

- (1) Sale proceeds i.e. ₹ 8,00,000
 - (2) Total amount of deduction earlier allowed under section 35 i.e. ₹ 5,00,000 will be deemed to be the income chargeable to tax under section 41(3).
3. The difference between sale proceeds and business income under section 41(3) will be treated as short-term capital gain.

₹

Sale proceeds of plant and machinery	8,00,000
Less: Business Income as per section 41(3)	<u>5,00,000</u>
Short-term capital gain	<u>3,00,000</u>

- (b) Section 44AA(1) requires every person carrying on any profession, notified by the Board in the Official Gazette (in addition to the professions already specified therein), to maintain such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of the Income-tax Act, 1961.

As per the provisions of Rule 6F of the Income-tax Rules, 1962, a person carrying on a notified profession shall be required to maintain specified books of accounts :

- (i) if his gross receipts in all the three years immediately preceding the relevant previous year has exceeded ₹ 1,50,000; or
- (ii) if it is a new profession which is setup in the relevant previous year, it is likely to exceed ₹ 1,50,000 in that previous year.

In the present case, Mohit is a person carrying on profession as technical consultant, which is a specified profession. Since his gross receipts have not exceeded ₹ 1,50,000 in financial year 2008-09, the requirement under section 44AA to compulsorily maintain the prescribed books of account is not applicable to him.

- (b) As per section 64(1) of the Finance Act, 1994 as amended, service tax provisions do not extend to the State of Jammu and Kashmir. Therefore, service tax will not be payable if service is provided in Jammu & Kashmir. However, since service tax is a destination based consumption tax, if a person from Jammu & Kashmir provides the

taxable service outside Jammu & Kashmir in any other part of India, the service will be liable to service tax, as the location where service is provided is relevant. Hence, the services provided by a person having a place of business in the State of Jammu and Kashmir providing services in any other place in India are taxable under the Finance Act, 1994 as amended.

5. (a) Computation of taxable capital gain of Mr. Pankaj for A.Y. 2012-13

Particulars	₹	₹
Sale consideration received on sale of 20,000 shares @ ₹ 175 each		35,00,000
Less: Indexed cost of acquisition		
(a) 10,000 shares received as gift from father on 5.4.1981		
Indexed cost $10000 \times ₹ 25 \times 785/100$	19,62,500	
(b) 5,000 bonus shares received from XYZ Ltd	Nil	
Bonus shares are acquired on 17.3.1986 (i.e after the year 1979-80 when the original shares were purchased). Hence, the cost is Nil.		
(c) 5000 shares purchased on 31.12.1993@₹ 75 per share. The indexed cost is $5000 \times ₹ 75 \times 785/244$	<u>12,06,455</u>	<u>31,68,955</u>
Long term capital gain		3,31,045
Less : Exemption under section 54F (See Note below)		
₹ 3,31,045 x ₹ 25,00,000 / ₹ 35,00,000		<u>2,36,461</u>
Taxable long term capital gain		<u>94,584</u>

Note:

Exemption under section 54F can be availed by the assessee subject to fulfillment of the following conditions :

- The assessee should not own more than one residential house on the date of transfer of the long-term capital asset;
- The assessee should purchase a residential house within a period of 1 year before or 2 years after the date of transfer or construct a residential house within a period of 3 years from the date of transfer of the long-term capital asset.

In this case, the assessee has fulfilled the two conditions mentioned above. Therefore, he is entitled to exemption under section 54F.

(b) **Computation of total income of Mr. P for A.Y.2012-13**

Particulars		₹	₹
Income from Other Sources			
Basic Pay		2,40,000	
Constituency allowance (₹ 9,500x12)	1,14,000		
Electricity allowance (₹ 5,000x6)	30,000		
Telephone allowance (₹ 5,000x12)	60,000		
	2,04,000		
Less: Exempt u/s 10(17)[₹ 9,500 p.m. being constituency allowance]	1,14,000	90,000	3,30,000
Income from Other Sources / Total Income			3,30,000

Note : The pay and allowances of a member of the State Assembly would be taxable under the head "Income from other sources", since there is no employer-employee relationship in this case.

- (c) Yes, the given proposition is true. The consumption variant is convenient from the point of administrative expediency as it simplifies tax administration by obviating the need to distinguish between purchases of intermediate and capital goods on the one hand and consumption goods on the other hand.

Besides, it does not affect decisions regarding investment because the tax on capital goods is also set-off against the VAT liability. Hence, the system is tax neutral in respect of techniques of production (labour or capital-intensive).

6. (a) Section 64(1) of the Income-tax Act, 1961 provides for the clubbing of income in the hands of the individual, if the income earned is from the assets transferred directly or indirectly to the spouse of the individual, otherwise than for adequate consideration. In this case Smt. Jaya received a gift of ₹ 2,00,000 from her husband which she invested in her business. The income to be clubbed in the hands of Smt. Jaya's husband for A.Y.2012-13 is computed as under :

Particulars	Smt.Jaya's Capital Contribution	Capital Contribution Out of gift from husband	Total
	₹	₹	₹
Capital as at 1.4.2010	2,50,000	--	2,50,000
Investment on 04.05.2010 out of gift received from her husband		2,00,000	2,00,000
Profit for F.Y. 2010-11 to be	2,50,000	2,00,000	4,50,000

apportioned on the basis of capital employed on the first day of the previous year i.e. on 1.4.2010	2,00,000		2,00,000
Capital employed as at 1.4.2011	4,50,000	2,00,000	6,50,000
Profit for F.Y.2011-12 to be apportioned on the basis of capital employed as at 1.4.2011 (i.e. 45 : 20)	2,70,000	1,20,000	3,90,000

Therefore, the income to be clubbed in the hands of Smt.Jaya's husband for A.Y.2012-13 is ₹ 1,20,000.

(b) Computation of total income of Rashmi for the A.Y. 2012-13

Particulars	₹	₹
Profit from sugar business	75,000	
Less: Loss from textile business for the year adjusted under section 70(1)	<u>25,000</u>	
	50,000	
Less: Brought forward loss of catering business closed in A.Y. 2011-12 set off against business income for the current year as per section 72(1)	<u>30,000</u>	20,000
Profit of speculative transaction		<u>17,500</u>
Total Income		<u>37,500</u>

Notes :

1. Loss of speculative transaction of A.Y. 2007-08 is not allowed to be set off against the profit of speculative transaction of the A.Y.2012-13, since, as per the provisions of section 73(4), such loss can be carried forward for set-off for a maximum period of 4 years only i.e. up to A.Y.2011-12.
 2. Short term capital loss of ₹ 10,500 on sale of securities and shares has to be carried forward as per section 74 since there is no income under the head Capital Gains for the A.Y.2012-13. The loss is to be carried forward for set off in future years against income chargeable under the head Capital Gains. Such loss can be carried forward for a maximum period of 8 assessment years.
- (c)** Yes, the person liable to pay service tax in relation to purchase or sale of foreign currency, including money changing, provided by a foreign exchange broker, including an authorised dealer in foreign exchange or an authorized money changer, referred to in section 65(105)(zm) and section 65(105)(zzk) as amended has the option to pay an amount at the following rates instead of paying service tax @ 10%:-

S.No.	For an amount	Service tax shall be calculated at the rate of
1.	Upto ₹ 100,000	0.1 % of the gross amount of currency exchanged or ₹ 25 whichever is higher
2.	Exceeding ₹ 1,00,000 and upto ₹ 10,00,000	₹ 100 + 0.05 % of the gross amount of currency exchanged
3.	Exceeding ₹ 10,00,000	₹ 550 + 0.01 % of the gross amount of currency exchanged or ₹ 5,000 whichever is lower

However, the person providing the service shall exercise such option for a financial year and such option shall not be withdrawn during the remaining part of that financial year

7. (a) (i) The liability to deduct tax at source under section 194A is not attracted in respect of interest paid to a banking company. Therefore, XYZ Ltd. is not liable to deduct tax at source on interest payment to the corporation bank.
- (ii) Freight Payment to Flyking not subject to TDS as the value of contract does not exceed ₹ 30,000. Again, payment to Railways is exempt from TDS;
- (iii) Provisions for deduction of tax at source under section 194J are attracted in respect of payment of fees for professional services, if the amount of such fees exceeds ₹ 30,000 in the relevant financial year. The service rendered by a commentator in relation to sports activities has been notified by the CBDT as professional service for the purpose of section 194J vide its *Notification No. 88 dated 21st August, 2008*. Therefore, tax is required to be deducted@10% from the fee of ₹ 2.5 lacs payable to the former cricketer.
- (iv) Under section 194G, the person responsible for paying to any person stocking, distributing, purchasing or selling lottery tickets shall at the time of credit of the commission or payment thereof, whichever is earlier, amounting to more than ₹ 1,000, deduct income-tax at 10%.

Therefore, the State Government shall deduct tax at source@10% on payment of commission made to the agent on sale of lottery tickets.

- (b) (i) **True :** Section 139A(2) provides that the Assessing Officer may, having regard to the nature of transactions as may be prescribed, also allot a PAN to any other person, whether any tax is payable by him or not, in the manner and in accordance with the procedure as may be prescribed.

- (ii) **False** : Section 140(b) provides that where the Karta of a HUF is absent from India, the return of income can be signed by any other adult member of the family; such member can be a male or female member.
- (c) Yes, in the instant case, Durga Consultants Ltd. is required to file its return electronically. Service Tax Rules, 1994 have been amended to provide that with effect from 01.10.2011, every assessee will have to submit half-yearly service tax return electronically, irrespective of the amount of service tax paid by him in the preceding financial year. Hence, now all assesses are required to file service tax returns electronically. Therefore, for the half year ended September 30, 2011, Durga Consultants Ltd. shall file its return electronically.