

TAX LAWS

Time allowed : 3 hours

Maximum marks : 100

NOTE : All references to sections mentioned in Part - A of the Question Paper relate to the Income-tax Act, 1961 and the relevant Assessment Year 2008-09 unless stated otherwise.

PART A

*(Answer Question No. 1 which is COMPULSORY
and ANY THREE of the rest from this part)*

Question 1

- (a) *Choose the most appropriate answer from the given options in respect of the following :*
- (i) *Which of the following is not an example of capital receipt —*
 - (a) *Money received on issue of shares*
 - (b) *Money received on sale of land*
 - (c) *Money received on sale of goods*
 - (d) *None of the above.*
 - (ii) *Maximum qualifying limit for deduction under section 80C is —*
 - (a) *Rs.50,000*
 - (b) *Rs.1,00,000*
 - (c) *Rs.1,10,000*
 - (d) *Rs.1,50,000.*
 - (iii) *In certain cases, income of other person is included in the income of assessee. It is called —*
 - (a) *Clubbing of income*
 - (b) *Increase in income*
 - (c) *Addition to income*
 - (d) *Set-off of income.*
 - (iv) *Remuneration for rendering services on a foreign ship is exempt in the case of —*
 - (a) *A resident*
 - (b) *A non-resident who is not a citizen of India*
 - (c) *Not ordinarily resident*
 - (d) *A citizen of India.*
 - (v) *Which of the following is not an asset under section 2(ea) of the Wealth-tax Act, 1957 —*
 - (a) *Motor car*
 - (b) *Boats and aircrafts*

- (c) *Guest house*
 (d) *Cash at bank.*
- (vi) *Any rent or revenue derived from land may be treated as agricultural income if —*
 (a) *It is derived from land*
 (b) *The land is situated in India*
 (c) *The land is used for agricultural purpose*
 (d) *All the above conditions are satisfied.*
- (vii) *Which of the following is covered under section 80D of the Income-tax Act, 1961 —*
 (a) *Repayment of loan taken for higher education*
 (b) *Medical treatment of handicapped dependent*
 (c) *Medical insurance premium*
 (d) *Reimbursement of medical expenses.*
- (viii) *The incidence of taxation depends on the —*
 (a) *Residential status of the assessee*
 (b) *Accommodation of the assessee*
 (c) *Citizenship of the assessee*
 (d) *Marital status of the assessee.* (1 mark each)
- (b) *Mrs. Vidya received the following amounts during the financial year 2007-08 :*

	<i>Rs.</i>
<i>Gross salary</i>	<i>6,00,000</i>
<i>Family pension @ Rs.1,500 p.m.</i>	<i>18,000</i>
<i>Income of a minor child</i>	<i>6,000</i>
<i>Accumulated balance in provident fund of her husband after his death</i>	<i>1,00,000</i>
<i>Gratuity received after the death of her husband</i>	<i>80,000</i>

Calculate taxable income of Mrs. Vidya for the assessment year 2008-09.

(4 marks)

- (c) *What is meant by 'pay-as-you-earn' scheme ?* (3 marks)

Answer 1(a)

- (i) (c) *Money received on sale of goods.*
 (ii) (b) *1,00,000*
 (iii) (a) *Clubbing of income*
 (iv) (b) *A non-resident who is not a citizen of India*
 (v) (d) *Cash at bank*

- (vi) (d) All the above conditions are satisfied.
- (vii) (c) Medical insurance premium
- (viii) (a) Residential status of the assessee.

Answer 1(b)**Computation of Taxable Income of Mrs. Vidya for the Assessment Year 2008-09**

		<i>Rs.</i>
Gross Salary		6,00,000
Less : Standard deduction		—
Income from Salary		<u>6,00,000</u>
Income from other sources :		
Family Pension		18,000
Income from Minor Child under section 64	6,000	
Less : Exemption under section 10(32)	<u>1,500</u>	<u>4,500</u>
Gross Total Income		6, 22,500
Less : Deduction under Section 57 in respect of family pension(1/3rd of 18,000)		<u>6,000</u>
Taxable Income		<u>6, 16,500</u>

Note : Gratuity received by Mrs. Vidya on the death of her husband is not taxable in her hands vide Circular No.573 dated August 21, 1990

Answer 1(c)**‘Pay-as-you-earn’ Scheme**

Sections 207 to 219 of the Income-tax Act lay down the provisions relating to advance payment of income-tax. The scheme of advance payment of tax is also known as ‘Pay as you earn’. The income on which the assessee is required to pay advance tax is commonly known as ‘income subject to advance tax’ and the tax payable on such income is known as ‘advance tax’.

The liability to pay advance tax arises during any financial year, in accordance with the provisions of Sections 208 to 219 (both inclusive), in respect of the total income of the assessee which would be chargeable to tax for the assessment year immediately following that financial year. Such income is, in Section 207, referred to as current income.

As per Section 208, advance tax shall be payable during a financial year in every case where the amount of such tax payable by the assessee during that year, as computed in accordance with the provisions of this Chapter, is five thousand rupees or more.

Assessee is liable to Pay advance tax, if liability for tax exceeds Rs. 50,000.

Question 2

- (a) *Re-write the following sentences after filling-up the blank spaces with appropriate word(s)/figure(s) :*
- (i) *Profit and gains arising from the transfer of a capital asset are taxable as _____.*
 - (ii) *Income accrued and received outside India is taxable in case of a _____.*
 - (iii) *If an asset is put to use for less than 180 days in the previous year, the depreciation is charged at _____ of normal rate.*
 - (iv) *Salary received by a Member of Parliament is taxable under the head _____.*
 - (v) *Unabsorbed part of the loss from house property can be carried forward and set-off within the subsequent _____ years.*
 - (vi) *Remuneration earned by a member of HUF for the services rendered by him is _____ income of the member.*
 - (vii) *One house or part of house belonging to an individual is _____ under the Wealth-tax Act, 1957. (1 mark each)*
- (b) *State, with reasons in brief, whether the following statements are correct or incorrect:*
- (i) *Sandeep, a trader, purchases standing crops and sells it after harvesting. His income will be treated as agricultural income.*
 - (ii) *Suresh receives Rs. 10 lakh from statutory provident fund on his retirement. This amount is taxable under the head income from salary.*
 - (iii) *Sarita paid Rs. 30,000 as interest @ 30% per annum on loan taken for the construction of a house. No deduction shall be allowed for payment of interest, as in the opinion of Assessing Officer, the rate of interest is very high.*
 - (iv) *Ashok Exports Ltd. realised surplus of Rs. 1,00,000 consequent to change in exchange rate of currency. This surplus is a revenue receipt. (2 marks each)*

Answer 2(a)

- (i) Capital gains
- (ii) Resident and Ordinarily resident
- (iii) 50 per cent or $\frac{1}{2}$
- (iv) Income from other sources.
- (v) Eight
- (vi) Exempt
- (vii) Exempt.

Answer 2(b)(i)**Incorrect**

Income accruing to Sandeep, a trader, by selling crops after harvesting is not agricultural income, because he has no interest in land except a mere licence to enter upon the land and gather upon the produce, since the land is not the direct, immediate or effective source of income. [*CIT v. Maddi Venkata Subbayya* (1951) 20 ITR 151 Mad].

Answer 2(b)(ii)**Incorrect**

Under Section 10(11) of the Income Tax Act any payment received from statutory provident fund would be exempted from income tax without any monetary limit.

Answer 2(b)(iii)**Incorrect**

Under Section 24(b) of the Income Tax Act the Assessing Officer is not empowered to question an assessee about the rate of interest on loan. So the assertion of the Assessing Officer is not tenable.

Answer 2(b)(iv)**Correct**

If by virtue of exchange operations profits be made during the course of business and in connection with business transactions, the excess receipt on account of conversion of one currency into another would be revenue receipts; otherwise they would be capital receipts.

Question 3

(a) Attempt the following :

- (i) *"Income-tax is a tax on income and not a tax on every item of money received." Explain this statement with reference to capital and revenue receipts.*
- (ii) *"Expenditure on scientific research is allowed as deduction even if contribution is made to other institutions for scientific research." Explain the statement.*
- (iii) *A person receives money from an insurer on account of damage to a capital asset resulting from accidental fire. Whether such money shall be taxable as capital gains ? Explain. (3 marks each)*

(b) Distinguish between any two of the following :

- (i) *'House rent allowance' and 'rent free house'.*
- (ii) *'Cost of acquisition' and 'cost of improvement'.*
- (iii) *'Fair rent' and 'annual rent'. (3 marks each)*

Answer 3(a)(i)

Income tax as the name implies, is a tax on income and not a tax on every item of money received. Therefore, unless the receipt in question constitutes income as

distinguished from capital, it cannot be charged to tax. For this purpose income should be distinguished from capital which give rise to income. Receipts are of two types viz., capital receipts and revenue receipts. The distinction between the two is vital because capital receipts are exempt from tax unless they are expressly taxable (for e.g., capital gains' are taxable under Section 45 even if they are capital receipts. On the other hand revenue are taxable unless they are expressly exempt from tax. for example income exempt under section 10. As the Income Tax Act does not define the term 'capital receipts' and 'revenue receipts', one has to depend upon the meaning of the concepts as well as the decided cases.

Answer 3(a)(ii)

According to Section 35(1) of the Income-tax Act, where the assessee does not himself carry on scientific research but makes contribution to other institutions such expenditure is allowed while computing income from business and profession. Accordingly where the assessee does not himself carry on scientific research but makes contribution to other institutions for this purpose, deduction is allowed if :

- (i) The payment is made to an approved scientific research association which has as its object undertaking of scientific research related or unrelated to the business of assessee or to a university college or other institution to be used for scientific research;
- (ii) The amount of deduction shall be allowed to the extent of 125% of the sum paid if the payment is made to an approved university college or institution.
- (iii) The approval of the scientific research association, university, college or institution is required to be obtained from Central Government as provided by Finance Act, 1999.

Answer 3(a)(iii)

Section 45(1A) of Income Tax Act, provides that where any person receives at any time during the previous year any money or other asset under an insurance from an insurer on account of damage to, or destruction of, any capital asset, as a result of flood, typhoon, hurricane, cyclone, earthquake or other convulsion of nature; or riot or civil disturbance; or accidental fire or explosion; or by action by enemy or action by an enemy or action taken in combating an enemy (whether with or without a declaration of war), then, any profit or gain arising from receipt of such money or other asset shall be chargeable to tax under the head capital gains. The income shall be deemed to be the income for the previous year in which such money or other asset is received. For computing capital gains the value of any money or the fair market value of asset received on the date of receipt shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of damaged asset.

Answer 3(b)(i)

'House rent allowance' and 'rent free house'

<i>House Rent Allowance</i>	<i>Rent Free House</i>
1. It is dealt under Section 10(13A) and Rule 2A.	It is a kind of perquisite. It is dealt under section 17(2)(i) of the Act.

<i>House Rent Allowance</i>	<i>Rent Free House</i>
2. While calculating 'salary' and basic pay, dearness allowance and commission (if terms of employment provide) is included.	Under calculation of 'salary', apart from basic pay, DA and Commission; Bonus, fees and other taxable allowances are also included.
3. Only taxable portion (after deduction) is added to the Gross Salary of the assessee.	In this case, it included in the Gross Salary of the assessee, as perquisite.

Answer 3(b)(ii)

The distinction between 'Cost of acquisition' and 'Cost of improvement' can be explained in following lines. The above two terms are associated with capital assets.

Cost of acquisition

Cost of acquisition of an asset is the value for which it was acquired by the assessee. Expenses of capital nature for completing or acquiring the title to the property are includible in the cost of acquisition. Cost of acquisition always precedes cost of improvement.

Cost of improvement

It is the capital expenditure incurred by the assessee in making any additions/ improvement to the capital asset. It also includes any expenditure incurred to protect or complete the title to the capital assets or cure such title. Any expenditure incurred to increase the value of the capital asset is treated as cost of improvement. Any cost of improvement incurred before 1.4.1981 is not taken into consideration for calculating capital gains chargeable to tax.

Answer 3(b)(iii)**'Fair rent' and 'Annual rent'**

Fair rent means the sum of for which the property might reasonably be expected to let from year to year. This rent is also known as notional rent. It will be equal to the rent which a similar property fetches in the neighborhood.

Whereas annual rent means the actual rent. This happens only where the house property has been actually let. Again annual rent means (i) if property is let out throughout the previous year the annual rent received or receivable for that year and (ii) if the property is let out for a part of the year the amount which bears the same proportion to actual rent received or receivable for the period of letting as the period of twelve month bears to the period of letting.

Quesiton 4

- (a) Ram, who is 28 years of age, is a businessman in Delhi. On the basis of the following profit and loss account for the financial year 2007-08, compute his taxable income :

	<i>Rs.</i>		<i>Rs.</i>
<i>Opening stock</i>	<i>20,700</i>	<i>Sales</i>	<i>15,00,000</i>
<i>Purchases</i>	<i>10,00,000</i>	<i>Closing stock</i>	<i>25,200</i>

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	Rs.	Rs.
<i>Household expenses</i>	10,000	
<i>Income-tax for the financial year 2007-08</i>	30,000	
<i>Interest on capital</i>	8,400	
<i>Depreciation on furniture</i>	12,000	
<i>Reserve for bad debts</i>	1,200	
<i>Salaries and wages</i>	60,000	
<i>Rent and rates</i>	25,000	
<i>Net profit</i>	3,57,900	
	<u>15,25,200</u>	<u>15,25,200</u>

Other relevant particulars are as follows :

- (i) *Opening stock and closing stock have consistently been valued at 10% below cost price.*
- (ii) *Household expenses include a contribution of Rs.1,500 towards public provident fund.*
- (iii) *Amount of depreciation on furniture as per income-tax provisions is Rs.10,000. (6 marks)*
- (b) *Write short notes on any three of the following :*
 - (i) *The activities of a co-operative society which are eligible for deduction under section 80P.*
 - (ii) *Essential conditions for claiming exemption under section 11 in the case of a charitable trust.*
 - (iii) *Liability to pay fringe benefit tax.*
 - (iv) *Banking cash transaction tax. (3 marks each)*

Answer 4(a)

Computation of Taxable Income of Mr. Ram for the Assessment Year 2008-09

<i>Particulars</i>	<i>Rs.</i>	<i>Rs.</i>
Income from business :		
Net Profit as per Profit & Loss A/c		3,57,900
Add : Inadmissible Expenses :		
Household Expenses	10,000	
Income Tax	30,000	
Interest on Capital	8,400	
Excess depreciation (12,000 – 10,000)	2,000	

<i>Particulars</i>	<i>Rs.</i>	<i>Rs.</i>
Reserve for Bad-debt	<u>1,200</u>	<u>51,600</u>
		4,09,500
Add : Undervaluation of closing stock ($1/9 \times 25,200$)		<u>2,800</u>
		4,12,300
Less : Under Valuation of opening stock ($1/9 \times 20,700$)		<u>2,300</u>
Income from business		4,10,000
Income from other sources		---
Gross Total Income		4,10,000
Less : Deduction u/s 80C (Contribution to PPF)		<u>1,500</u>
Taxable Income		<u>4,08,500</u>

Answer 4(b)(i)

The activities of a co-operative society which are eligible for deduction under Section 80P are as follows:

- (i) Income from banking business [Section 80P(2)(a)(i)]
- (ii) Cottage Industry [Section 80P(2)(a)(ii)]
- (iii) Marketing agricultural produce [Section 80P(2)(a)(iii)]
- (iv) Purchase of agricultural implements [Section 80P(2)(a)(iv)]
- (v) Processing of agricultural produce of its member [Section 80P(2)(a)(v)]
- (vi) Collective disposal of Labour [Section 80P(2)(a)(vi)]
- (vii) Primary Society engaged in supply of milk, oilseeds, fruits etc. [Section 80P(2)(b)]
- (viii) Investment activities
- (ix) Letting of Godowns [Section 80P(2)(e)]

Answer 4(b)(ii)

The essential conditions for availing exemption under Section 11 are :

- (a) The property should be held under a trust or other legal obligation.
- (b) The property should be held for charitable or religious purposes. Also the trust should not be created for the benefit of any particular religious community; no part of the income should vest for benefit of the settler or other specified person.
- (c) The income of the trust should be applied to charitable or religious purposes or is accumulated within the permitted limits for applying to such purposes.
- (d) Income is applied to charitable or religious purposes in India.
- (e) The trust should be registered with the Commissioner of Income Tax.
- (f) If the income exceeds the exemption limit, the accounts of the trust should be audited.
- (g) The funds of the trust should be invested or deposited in any of the modes or forms specified under Section 11(5).

Answer 4(b)(iii)**Liability to pay fringe benefit tax**

'Fringe benefit tax' (FBT) is payable by an 'employer' on the 'fringe benefits' provided or deemed to have been provided by him to his employees. FBT means the tax chargeable under Section 115WA. In addition to the income tax charged for every assessment year commencing on or after 1.4.2006, additional income tax (in this Act referred to as fringe benefit tax) in respect of fringe benefits provided or deemed to have been provided by an employer to his employees during the previous year @ 30% (plus applicable surcharge and education cess of 3% on the aggregate of additional income tax and surcharge) on the value of such fringe benefits.

Even loss making concerns will have to pay fringe benefit tax although there is no income tax payable by him. An employer who is eligible for deductions under Section 10A, 10AA, 10B, 10BA shall also be liable to pay FBT, even though he is allowed deduction or exemption under the aforesaid sections.

Answer 4(b)(iv)**Banking Cash Transaction Tax (BCTT)**

BCTT is a concept introduced by the Finance Act, 2005, under Chapter VII. According to Section 94(3) of the Income Tax Act, BCTT means, the tax leviable on the taxable banking transactions under the provisions of the Chapter. From 1.6.2005, every taxable banking transaction be charged at 0.1%. The BCTT shall be payable as per provision of section 94(8) of the Act and there is no surcharge and education cess on this tax. The value of taxable banking transaction under Section 94(8)(9) is the amount of cash withdrawn. The value of taxable banking transaction under section 94(8)(b) is the amount of cash received on encashment of term deposit or deposits. The exemption limit for bank withdrawal is Rs.50,000 for individual or HUF and Rs.1,00,000 for other persons in respect of cash withdrawal on a day from a Bank.

Question 5

- (a) *Gulshan submits the following information relevant for the financial year 2007-08 :*

	<i>Profit (Rs.)</i>	<i>Loss (Rs.)</i>
<i>Salary income</i>	<i>8,00,000</i>	<i>—</i>
<i>Income from house property :</i>		
<i>House - A</i>	<i>25,000</i>	<i>—</i>
<i>House - B</i>	<i>—</i>	<i>30,000</i>
<i>Profits and gains of business or profession :</i>		
<i>Business - A</i>	<i>12,000</i>	<i>—</i>
<i>Business - B</i>	<i>—</i>	<i>20,000</i>
<i>Business - C (Speculative)</i>	<i>22,000</i>	<i>—</i>
<i>Business - D (Speculative)</i>	<i>—</i>	<i>35,000</i>
<i>Capital gains :</i>		
<i>Short term capital gains</i>	<i>10,000</i>	<i>—</i>
<i>Short term capital loss</i>	<i>—</i>	<i>30,000</i>

Long-term capital gains on sale of building	16,000	—
Income from other sources :		
Loss on maintenance of race horses	—	15,000
Determine the net income of Gulshan for the assessment year 2008-09.		

(7 marks)

(b) Suresh is the owner of a house. The actual rent of this house is Rs.9,000 per month and municipal valuation of this house is Rs.7,500 per month. Other informations about the house are —

- (i) Municipal taxes are Rs. 10,000 out of which the tenant has paid Rs.6,000.
- (ii) Suresh has accepted a deposit of Rs.1,00,000 from the tenant on which Suresh has paid interest @ 6% per annum.
- (iii) The tenant is also liable for meeting the expenses on repairs of the house.
- (iv) The tenant has paid Rs.25,000 as premium for the house. The premium is non-refundable. The lease period of the house is 5 years.

Assuming that the house is built on free-hold land, determine the value of the house under the provisions of the Wealth-tax Act, 1957 for the assessment year 2008-09.

(8 marks)

Answer 5(a)**Computation of Taxable Income of Mr. Gulshan for the Assessment Year 2008-09**

Particulars	Rs.	Rs.
Inter-source adjustment :		
(A) Income from Salary		8,00,000
(B) Income from House Property :		
House A Rs. 25,000		
House B <u>Rs. 30,000</u> (Loss)	(-) 5,000	
(C) Profits and Gains of		
Business or profession :		
Business A Rs. 12,000		
Business B <u>Rs. 20,000</u> (Loss)	(-) 8,000	
Speculative Business :		
Business C Rs. 22,000		
Business D <u>Rs. 35,000</u> (Loss)	(-)13,000	
(D) Capital Gains :		
Short-term Capital Gains Rs. 10,000		
Short-term Capital Loss (-) Rs. 30,000		
(-) Rs. 20,000		
Long-term Capital Gain <u>Rs. 16,000</u>	(-) 4,000	
Income from other Sources:		
Loss on maintenance of Race Horses	(-)15,000	
Net Income = Rs. 8,00,000 – Rs. 5,000 = Rs. 7,95,000		

Notes :

- (i) The house property loss can be set-off against salary income.
- (ii) Loss from business and profession cannot set-off against salary income [Section 71(2A)].
- (iii) Loss from speculative business cannot be set-off in the assessment year under any other head and it has to be carried forward to next assessment year [Section 73].
- (iv) Short-term capital loss will be carried forward to the next assessment year.
- (v) As per section 74A, the loss incurred by the assessee, in the activity of owning and maintaining race horses, shall only be set-off against the income of such activity. It cannot be set-off against income from any other source.

Answer 5(b)

Computation of the Value of the house under the provisions of the Wealth Tax Act, 1957 for the Assessment Year 2008-09

	<i>Rs.</i>	<i>Rs.</i>
Actual rent paid by the tenant Rs. 9,000 x 12	1,08,000	
<i>Add :</i>		
(i) 1/9th of repair expenses are borne by the tenant i.e., 1/9th x 1,08,000		12,000
(ii) Municipal Tax paid by tenant		6,000
(iii) Interest on deposit 15% of 1,00,000 = 15,000 Less : Interest paid 6,000		9,000
(iv) Annual premium 25,000/5		5,000
(iv) Annual Rent (a)		<u>1,40,000</u>
Municipal Value (b) 7,500 x 12 = Rs. 90,000		
Gross Maintainable Rent (a) or (b) whichever is higher		1,40,000
Less : Municipal Taxes 10,000		
15% of 1,40,000	<u>21,000</u>	<u>31,000</u>
Net Maintainable Rent (NMR)		<u>1,09,000</u>
Capitalized Value of the house:		
House is constructed on freehold		
Land = NMR x 12.5		
= 1,09,000 x 12.5 = Rs.13,62,500		

Question 6

(a) Nikhil, Gagan and Suman are partners in a firm with equal shares. The profit and loss account for the year ending 31st March, 2008 shows a net profit of Rs.42,300 after debiting the following items :

- (i) Salary of Rs. 24,000 each to Nikhil and Gagan.
- (ii) Bonus to Suman Rs. 18,000.
- (iii) Commission of Rs. 9,000, Rs. 10,000 and Rs. 15,000 to Nikhil, Gagan and Suman respectively.
- (iv) Interest on capital @ 15% amounting to Rs. 4,500, Rs. 6,000 and Rs. 15,000 paid to Nikhil, Gagan and Suman respectively.

Assuming that all partners are working partners and the firm fulfils the conditions of section 184, compute the total income of the firm and taxable income of the partners in the firm. (8 marks)

(b) Indicate the amount of deduction available to an assessee from his gross total income under section 80GG in respect of rent paid. Point out the circumstances when the deduction will be denied. (7 marks)

Answer 6(a)**Computation of total Income of the Firm**

				Rs.
Net Profit as per Profit & Loss Account				42,300
Add : Disallowed items :				
Salary to Partners : Nikhil	24,000			
Gagan	24,000	48,000		
Bonus to Suman			18,000	
Commission to Partners : Nikhil	9,000			
Gagan	10,000			
Suman	15,000	34,000		1,00,000
Interest on Capital in Excess of 12% =				
Nikhil = $(4,500 \times 3) \div 15 =$	900			
Gagan = $(6,000 \times 3) \div 15 =$	1,200			
Suman = $(15,000 \times 3) \div 15 =$	3,000			5,100
Book Profit				<u>1,47,400</u>
Less : Remuneration under section 40(b)				
Actual Remuneration		1,00,000		
OR				
90% of Book profit on				
First 75,000 =	67,500			
60% of Book profit on				
Balance of Rs.72,400 =	43,440	1,10,940		1,00,000
Total Income of the Firm				<u>47,400</u>

Computation of income of Partners from Firm

	<i>Nikhil</i>	<i>Gagan</i>	<i>Suman</i>
Interest on Capital (12%)	3,600	4,800	12,000
Salary	24,000	24,000	---
Bonus	---	---	18,000
Commission	9,000	10,000	15,000
	<u>36,600</u>	<u>38,800</u>	<u>45,000</u>

Answer 6(b)

Deduction in respect of Rent Paid (Section 80 GG)

Deductions admissible under this Section is:

- Actual rent paid less 10% of 'Adjusted Total Income'.
- 25% of such 'Adjusted Total Income'.
- Amount calculated at Rs. 2,000 p.m.

whichever is least.

Adjusted Total Income is the adjusted Gross Total Income under Section 80G except exempted income less long term capital gain.

However, certain conditions as given below are required to be fulfilled/satisfied for claiming deduction u/s 80GG

- The assessee should not be receiving any house rent allowance exempt u/s 10(13A) or rent free accommodation.
- The accommodation should be occupied by the assessee for the purpose of his own residence.
- The assessee fulfills such other conditions or limitations as may be prescribed having regard to the area or place in which such accommodation is situated and other relevant consideration.
- The assessee or his spouse or his minor child or an HUF of which he is a member does not own any accommodation at the place where he ordinarily resides or performs duties of his office or employment or carries on his business or profession.
- If the assessee owns any accommodation at any place other than that referred to above, such accommodation should not be in the occupation of the assessee and its annual value is not required to be determined under Section 23(2)(a)(i) or Section 23(2)(b).
- Allowed only to an individual assessee after furnishing Form 10BA along with return of income.

PART B**Question 7**

Attempt any four of the following :

- (a) What do you mean by 'taxable services' in the context of service tax ? How is the value of taxable services determined ? (5 marks)

- (b) *Explain the procedure of registration for paying service tax.* (5 marks)
- (c) *Under certain circumstances, the service receivers are liable to pay service tax. Indicate such cases.* (5 marks)
- (d) *Choose the most appropriate answer from the given options in respect of the following :*
- (i) *Tax on service is —*
 - (a) *a direct tax*
 - (b) *an indirect tax*
 - (c) *multipoint tax*
 - (d) *None of the above.*
 - (ii) *Appeal to Customs, Excise and Service Tax Appellate Tribunal can be filed within —*
 - (a) *One month*
 - (b) *Two months*
 - (c) *Three months*
 - (d) *Four months.*
 - (iii) *Service tax is administered by the Department of —*
 - (a) *Central Sales Tax*
 - (b) *Central Excise*
 - (c) *Revenue*
 - (d) *Customs.*
 - (iv) *Service tax collected by mistake is required to be deposited under section 73A of the Finance Act, 1994 to the —*
 - (a) *Central Government*
 - (b) *Account of the person who paid such tax*
 - (c) *National Defence Fund*
 - (d) *Chief Minister's Relief Fund.*
 - (v) *Service tax is applicable in the case of —*
 - (a) *All Company Secretaries*
 - (b) *Company Secretaries in Practice*
 - (c) *Company Secretaries below the age of 65 years*
 - (d) *All services rendered by a Practising Company Secretary other than representation services before any statutory authority. (1 mark each)*
- (e) *Re-write the following sentences after filling-up the blank spaces with appropriate word(s)/figure(s) :*
- (i) *The Superintendent of Central Excise is bound to grant certificate of registration for service tax within _____ days of the receipt of application.*

- (ii) *Taxable services provided to any person by the Reserve Bank of India is _____ from service tax.*
- (iii) *Under section 77 of the Finance Act, 1994, a maximum penalty of Rs. _____ is payable for late filing of service tax return.*
- (iv) *The threshold limit for service tax exemption applicable in the case of small service providers has been increased to _____.*
- (v) *When there is no consideration received for services rendered freely, the service tax _____ apply. (1 mark each)*
- (f) *State, with reasons in brief, whether the following statements are correct or incorrect:*
 - (i) *Service tax is to be paid to the credit of Central Government by the 5th of the month immediately following the calendar month in which the payments are received.*
 - (ii) *In case the taxable services are provided from more than one premises/offices, the assessee can opt for registration of only one premises.*
 - (iii) *The facility for e-filing of returns is not applicable to service tax.*
 - (iv) *There is no system of getting advance ruling in respect of service tax matters.*
 - (v) *The CENVAT credit rules do not extend its scope to service tax paid in respect of input services. (1 mark each)*

Answer 7(a)

According to Section 67 of Chapter V of Finance Act, 1994, the value of any taxable service shall be the 'gross amount' charged by the service provider for such service rendered by him. "Gross amount" means the amount actually charged by the service provider without making any deduction. The service provider will have to make a bill on the receiver of service showing clearly the gross amount charged.

For determining the value of taxable service, the following factors regarding identification of services have to take into consideration.

- (a) Services to be included;
- (b) Services to be excluded;
- (c) Items which are statutorily includible or excludible;
- (d) Items which are includible or excludible according to departmental clarifications;
- (e) If permissible, reimbursement of out of pocket expenses have to be excluded;
- (f) Inclusion of service tax element separately in the bills;
- (g) General and specific exemptions services on which no service tax is leviable at all are not required to be considered for determining the value of taxable service. Such services are the services which are not covered under Section 65(105) of the act and also those services which are provided in the State of Jammu & Kashmir where a service provider is providing more than one taxable service, the gross amount in respect of all the services should be determined separately in respect of each such service so that specific exemptions applicable to each service can be availed.

As per Section 67 of the act, if the consideration for a taxable service is in terms of money, the value of such service shall be the gross amount charged by the service provider for such service. If the consideration is not received in money, the value of taxable service shall be the amount of money (together with service tax) equivalent to the total consideration thus arrived at.

If the gross amount charged by service provider is inclusive of service tax payable, the value of taxable service will be equal to = Gross amount charged $\times$ 100/100 + Rate of Service Tax.

Gross amount charged includes payment by cheque, credit card deduction from account and any form of payment by issue of credit or debit notes and book adjustments.

Answer 7(b)

Procedure of registration under service tax

Section 69 of the Finance act deals with the procedure of registration for paying service tax. The procedure of registration is as follows :

- (i) Every person responsible for collecting service tax has to register with Central Excise authorities. He has to apply in Form ST-1.
- (ii) The application for registration is to be made within a period of 30 days from the date on which the service tax is liable.
- (iii) ST-1 Form shall be accompanied with copy of PAN, an affidavit declaring the commencement of services, proof of residence, photograph of the assessee etc.
- (iv) If the assessee is a partnership firm copy of certificate registration and partnership deed must be attached to Form No.1.
- (v) Where the assessee is providing more than one taxable service he can obtain registration by making a single application mentioning all the taxable services provided by him.
- (vi) The Central Excise Officer shall after satisfying himself that the applications form is in conformity with the prescribed guidelines shall grant a certificate of registration in Form ST-2 within 7 days of the date of receipt of the application.

Answer 7(c)

Service receivers are liable to pay service tax

Though the service provider is primarily liable for payment of service tax, there is one exception when the service receiver is liable for payment of service tax. As per Section 68(2) read with Rule 2(d) of the Service Tax Rules, 1994, in case of non-resident service provider who does not have any office in India, the service receiver is liable for payment of service tax. Moreover, Finance Act, 2008 changed the recipient name from 'client' or 'customer' to 'any person'. CBE&C TRU Letter F.No.34/1/TRU dated 29.2.2000 clarifies as follows. In number of taxable services, recipient of service is specified as 'client' or 'customer'. Service tax is levied on services received in India. For example, some musicians under a entity (established abroad) performs in India through a Indian

entity. The musicians are of foreign nationality. The service receiver in India who are conducting the show has to pay the service tax. Other examples are : insurance companies paying service tax in respect of service provided by insurance agents. Service provided by mutual fund distributor—service receiver to pay service tax on brokerage/ commission received.

Answer 7(d)

- (i) (b) An indirect tax
- (ii) (c) Three months
- (iii) (b) Central Excise
- (iv) (a) Central Government
- (v) (d) All services rendered by a Practising Company Secretaries other than representation services before any statutory authority.

Answer 7(e)

- (i) 7 days
- (ii) Exempt
- (iii) Rs.1,000
- (iv) Rs.10,00,000
- (v) Will not

Answer 7(f)(i)**Correct**

Rule 6 of the Service Tax Rules 1994 provided that any assessee who is providing taxable services and receives payment for the services, shall pay service tax to the credit of Central Government account by the 5th of that month immediately following the month in which the payments are received.

Answer 7(f)(ii)**Correct**

Section 69 of the Finance Act provides that in case the taxable services are provided from more than one premises/offices the assessee can opt for registration for only one premises if there is a system of centralized billing accounting with permission from department.

Answer 7(f)(iii)**Incorrect**

Service tax providers can avail the benefit of e-filing of returns through internet. The assessee can go to the e-filing site 'Home page' by typing the address <http://servicetaxefiling.nic.in> in the address bar of the browser. Assessee having a 15 digit STP code and falling under certain categories can avail the facility of e-return.

Answer 7(f)(iv)**Incorrect**

Chapter VA has been added to the Finance Act, 1994 by the Finance Act, 2003 to provide for advance rulings in service tax on the lines of the similar provisions contained in the Central Excise Act, 1944 and Customs Act, 1962.

Answer 7(f)(v)**Incorrect**

Under CENVAT Credit Rules, 2004, now credit can be taken for inputs, capital goods as well as for input services used in or in relation to manufacture or production of final products or for providing of any taxable services.

PART C**Question 8**

Attempt any four of the following :

- (a) *What are the different modes of computation of value added tax (VAT) and what are the advantages of adoption of tax credit method ?* (5 marks)
- (b) *"In the old sales tax structure, there were problems of double taxation of commodities and multiplicity of taxes, resulting in a cascading burden." In the light of this statement, explain how VAT is an improvement over the old sales tax structure.* (5 marks)
- (c) *Dinesh purchases raw material from Ram and Shyam for manufacturing goods. Dinesh sells goods to wholesaler Mohan. Mohan sells goods to Trilok, a retailer, who sells goods to consumers. Calculate the amount of VAT collected by the government from the following particulars based on the fact that Shyam charges VAT @ 4% and other sellers charge VAT @ 12.5% :*

	Price without VAT (Rs.)
<i>Raw material supplied :</i>	
Ram to Dinesh	5,000
Shyam to Dinesh	8,000
<i>Manufactured goods sold :</i>	
Dinesh to Mohan	18,000
Mohan to Trilok	25,000
Trilok to consumers	30,000
	(5 marks)
(d) <i>"Input tax credit is generally given for the entire VAT paid within the State on purchases of taxable goods meant for resale or manufacture of taxable goods". In the light of this statement, enumerate the cases of purchases of goods in respect of which tax credit is not available.</i>	(5 marks)
(e) <i>Write a brief note on rates of VAT.</i>	(5 marks)

- (f) *State, with reasons in brief, whether the following statements are correct or incorrect:*
- (i) *Zero rating transaction is the same as an exempt transaction.*
 - (ii) *VAT helps in checking tax evasion and in achieving neutrality.*
 - (iii) *The departmental audit also helps to check tax evasion.*
 - (iv) *Introduction of VAT has increased the professional development opportunities for the Company Secretaries.*
 - (v) *As a result of introduction of VAT, the central sales tax will be phased out in due course.* (1 mark each)

Answer 8(a)

There are three different modes of computation of VAT :

- (i) *Addition Method* : Under this method identification of value added is estimated by adding values of all the elements of production wages, profits, rent and interest. Under this method, the incidence of tax evasion is greater because it does not require matching of invoices.
- (ii) *Subtraction Method* : In this method value added is computed by subtracting inputs from outputs. This is also known as the product approach.
- (iii) *Tax Credit Method* : Under this method, Vat payable by a dealer is arrived at by deducting tax on inputs from the tax on sales. This method is known as the invoice method. This method is universally used because of the advantages of computing tax liability under this method. As rate of tax is different in respect of inputs and outputs, the addition method and the subtraction method are not practicable in the case of a manufacturer.

The advantages of using tax credit method in estimating VAT liability are :

- (i) Under this method exports are exempted from levy of domestic indirect taxes as exports are taxed at Zero rate and refund of input taxes paid.
- (ii) Under this method, dealers at intermediate stage are indifferent to tax rates because burden of VAT is dependent upon rate of Tax at the final stage.
- (iii) Under this method, cross-checking of tax paid at earlier stages is comparatively easier because of the fact that dealers are required to specify the amount of tax in their invoices.

Answer 8(b)

In the old sales tax structure, there were problems of double taxation of commodities and multiplicity of taxes, resulting in a cascading burden”.

Earlier the local sales tax was based on single point tax. The single point tax was either at first point or at last point. The First point tax (FPT) was convenient to the revenue but had inbuilt cascading effect. The Last Point Tax (LPT) is an ideal system but it was evasion prone resulting into loss of revenue to the government. The VAT system on the other hand reduces the disadvantages of both FPT and LPT and at the same time draws the advantages from resulting into both. The VAT system obviously is more transparent,

uniform and less prone to tax evasion. The following illustration may show the difference between first point tax and last point tax.

Assume the base price of the commodity is Rs. 1000 and the government wishes to collect sales tax of 10% on base price i.e. Rs. 100.

Taxation

<i>F.P.T.</i>	<i>Rs.</i>	<i>L.P.T.</i>	<i>Rs.</i>
Price paid by A	1,000	Price paid by A	1,000
Tax paid by A	100	Tax paid by A	Nil
Total	1,100	Total	1,000
Margin @ 50% added by A	550	Margin added by A @ 50%	500
Price paid by B	1,650	Price paid by B	1,500
Margin @ 50% added by B	825	Margin @ 50% added by B	750
	2,475		2,250
Tax	Nil	Tax	100
Price paid by Consumer	2,475	Price paid by Consumer	2,350

In both the cases as above, the tax collected by the government is Rs. 100 but consumer would pay more under F.P.T. than under L.P.T. Under VAT, the consumer would pay the same amount as under F.P.T. but the government would get the tax of Rs. 225/- instead of Rs. 100/-

States continue to tax declared goods on single point basis under the existing system subject to a rate of 4%. Under VAT, declared goods will also suffer tax at multiple levels.

Under the existing Sales tax systems, inputs used for manufacture, whether capital or otherwise, are eligible for concessional rate of tax on furnishing the requisite forms. However, under the VAT system, there is no place for concessions. Goods will be taxed at their respective rates, of course, with a provision for set off in future. There will be no incentive schemes under VAT, barring those carried forward from the existing system.

Note : Students may give any other alternative example.

Answer 8(c)

Computation of Amount of VAT collected by the Government

<i>Particulars of Sales</i>	<i>Price without VAT</i>	<i>Gross VAT</i>	<i>Net VAT payable by dealer</i>
	<i>Rs.</i>	<i>Rs.</i>	<i>Rs.</i>
Sales of Raw materials :			
Ram to Dinesh Ltd. [VAT 12.5%]	5,000	625	625
Shyam to Dinesh Ltd. [VAT 4%]	8,000	320	320

<i>Particulars of Sales</i>	<i>Price without VAT</i>	<i>Gross VAT</i>	<i>Net VAT payable by dealer</i>
	<i>Rs.</i>	<i>Rs.</i>	<i>Rs.</i>
Sales of Goods :			
Dinesh to Mohan [VAT 12.5%]	18,000	2,250	
Less : VAT Credit to Dinesh Ltd. [Rs.625+Rs.320]		945	1,305
Mohan to Trilok [VAT 12.5%]	25,000	3,125	
Less VAT Credit to Mohan Ltd.		2,250	875
Trilok to Consumers [VAT 12.5%]	30,000	3,750	
Less VAT Credit to Trilok		3,125	625
Total VAT collected by the Government			3,750

Answer 8(d)

Input tax credit means setting off the amount of input tax by a registered dealer against the amount of his output tax liability. Input tax is the tax a dealer pays on his local purchases of business inputs which include the goods he purchases for resale, raw-materials, capital goods as well as other inputs for use in his business directly or indirectly. Output tax is the tax that a dealer charges on his sales. Adjustment of input tax from the amount of output tax is known as input tax credit.

The input tax credit is to be given for both manufacturers and traders for purchase of inputs meant for both sales within the state as well as to other states.

The essence of VAT lies in providing set-off for the tax paid earlier through the system of input tax credit. For example, suppose a dealer purchases raw material worth Rs.5 lac and sells his output for Rs.8 lakhs. Input tax rate and output tax rate being 12.5%, input tax credit shall be computed as follows :

Input tax paid on raw material = Rs.62,500 [Rs.5 lakhs x 12.5%]

Output tax collected on sales = Rs.1.00,000 [Rs.8 lakhs x 12.5%]

VAT payable = (Rs.1,00,000 – Rs.62,500 = Rs.37,500

This shows that the assessee has availed input tax credit equal to Rs.62,500.

However, credit for payment of taxes on capital goods may not be immediately available from output tax as it is available in respect of input tax on raw materials. Input tax credit on capital goods may be granted over a certain period of time in order to soften the burden on states due to high value of the capital goods. Also, input tax credit on capital goods may not be available to a trader because he does not use the capital goods for manufacture.

Purchases in respect of which no tax credit is available :

Input tax credit is generally given for the entire VAT paid within the state on purchases

of taxable goods meant for resale/manufacture. However, input tax credit is not available in respect of the following purchases :

- (i) Purchases of goods from unregistered dealers.
- (ii) Purchases of goods from other states.
- (iii) Goods purchased for manufacture of exempted goods.
- (iv) Purchases of capital goods where credit is available in some cases in instalments.
- (v) Goods purchased for use as fuel in generation of power.
- (vi) Goods purchased for being dispatched to outside states as branch transfers.
- (vii) Goods purchased for use in manufacture of goods to be dispatched outside any state as branch transfer.
- (viii) Goods purchased where invoices do not show amounts of tax charged separately by the dealer who sold goods.
- (ix) Purchase of non-creditable goods.
- (x) Purchases from a dealer who has opted for composition scheme.

Answer 8(e)

Rates of VAT : Under the VAT system five different rates are applicable as follows:

- (i) Zero percent in the case of unprocessed agricultural goods and goods' of social implications. This rate is also applicable in case of items which are legally barred from taxation.
- (ii) One percent in the case gold and silver ornaments and other precious and semi-previous metals.
- (iii) Four per cent in the case of inputs used for manufacturing i.e., industrial goods, declared goods; capital goods and other essential items;
- (iv) Twelve and half per cent in the case of all the remaining goods other than luxury goods.
- (v) Twenty per cent in the case of luxury goods.

Answer 8(f)(i)

Incorrect

Reasons : Zero rating means that the tax payable on sale of a commodity is fixed at 0%. Though apparently, it looks similar to an exempt transaction, there is significance difference between the two. While in an exempt transaction, the tax paid on inputs lapse i.e., it cannot be set-off under the Zero rated sales, prior stage tax is set-off against the 0% tax paid and effectively the entire tax paid on purchases is eligible for refund.

Answer 8(f)(ii)

Correct

Reasons : A cross checking through computerized system shall be done on the basis of coordination between tax authorities of the State Governments and the authorities

of Central excise to compare constantly the tax returns and set-off documents of VAT System of the States and those of Central Excise. This comprehensive cross checking system helps in reduction in tax evasions and also leads to significant growth of tax revenue

Answer 8(f)(iii)**Correct**

Departmental Audit is conducted on the basis of sample checking in case of self assessment cases. If some disparities are noted, then audit of those cases is done thoroughly. It helps in checking tax evasions.

Answer 8(f)(iv)**Correct**

With the inception of VAT, Company Secretaries are now able to act as authorized representative of their clients in some states, through statutory provisions provided in the respective VAT Acts.

Answer 8(f)(v)**Correct**

With the introduction of VAT in majority of states in our country, Central Sales Tax Act, 1956 will be phased out by 2010, it becomes imperative for our economy that the VAT system should be implemented all over the country
