

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 2009-10m 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 having regard to the provisions of the relevant direct tax laws :*
- (i) *Income-tax in India is charged at the rate(s) prescribed by —*
 - (a) *The Finance Act*
 - (b) *The Income-tax Act*
 - (c) *The Central Board of Direct Taxes*
 - (d) *The Ministry of Finance.*
 - (ii) *Under the Income-tax Act, 1961, depreciation on machinery is charged on —*
 - (a) *Purchase price of the machinery*
 - (b) *Market price of the machinery*
 - (c) *Written down value of the machinery*
 - (d) *All of the above.*
 - (iii) *Income accruing in India in previous year is taxable for —*
 - (a) *Resident*
 - (b) *Not ordinarily resident*
 - (c) *Non-resident*
 - (d) *All of the above.*
 - (iv) *Sandeep purchased a house for his residential purpose after taking a loan in January, 2007. During the previous year 2008-09, he paid interest on loan Rs. 1,67,000. While computing income from house property, the deduction is allowable to the extent of —*
 - (a) *Rs.30,000*
 - (b) *Rs.1,00,000*
 - (c) *Rs.1,67,000*
 - (d) *Rs.1,50,000.*

- (v) Which of the following is an 'asset' under section 2(ea) of the Wealth-tax Act, 1957 —
- (a) Equity shares in a company
 - (b) Balance in provident fund
 - (c) Motor car held as stock-in-trade
 - (d) Jewellery for personal use. (1 mark each)
- (b) Re-write the following sentences after filling-in the blank spaces with appropriate word(s)/figure(s) :
- (i) Deduction for bad debt is allowed to an assessee carrying on business in the year in which the debt is _____ as bad.
 - (ii) Deduction available under section 80GG towards rent paid shall not exceed Rs. _____ per month.
 - (iii) It is obligatory for an assessee to pay advance tax where the amount of tax payable is Rs. _____ or more.
 - (iv) A belated return of income can be filed at any time before the expiry of _____ from the end of relevant assessment year.
 - (v) Wealth-tax is levied on the net wealth of a person as on 31st March, this date is known as _____ date. (1 mark each)
- (c) Rajan is an employee of a private limited company and gets the following emoluments during the previous year ended on 31st March, 2009 :
- Salary : Rs.96,000;
- Salary in lieu of leave : Rs.6,000;
- Entertainment allowance: Rs.10,000; and
- Commission : Rs.8,000.
- Rajan's son studies in a school which is owned and maintained by the company. The cost of education in a similar school in the locality is Rs.22,000 per year, but the company charges Rs.4,000 from Rajan. Salary of a domestic servant provided to Rajan by the company is Rs.6,000 and the same is paid by the company. The company purchases a computer on 1st April, 2008 for Rs.50,000 which is given to Rajan for office and private use. The company purchases a refrigerator for Rs.20,000 on 30th June, 2008 for personal use of Rajan. Rajan and the company both contribute Rs.12,000 towards recognised provident fund. Rajan deposits Rs.40,000 towards public provident fund. Rajan earns Rs.1,00,000 by way of rent from a vacant plot of land. Compute the taxable income and tax liability of Rajan for the assessment year 2009-10. (5 marks)

Answer 1(a)(i)

- (a) The Finance Act

Answer 1(a)(ii)

- (c) Written down value of the machinery

Answer 1(a)(iii)

- (d) All of the above

Answer 1(a)(iv)

- (d) Rs.1,50,000

Answer 1(a)(v)

- (d) Jewellery for personal use.

Answer 1(b)

- (i) Deduction for bad debt is allowed to an assessee carrying on business in the year in which the debt is **Written off** as bad.
- (ii) Deduction available under section 80GG towards rent paid shall not exceed **Rs. 2,000** per month.
- (iii) It is obligatory for an assessee to pay advance tax where the amount of tax payable is **Rs. 5,000** or more.
- (iv) A belated return of income can be filed at any time before the expiry of **one year** from the end of relevant assessment year.
- (v) Wealth-tax is levied on the net wealth of a person as on 31st March, this date is known as **Valuation** date.

Answer 1(c)

**Computation of Taxable income of Mr. Rajan
for the Assessment Year 2009-10**

	<i>Rs.</i>
1. Income from salary :	
Salary	96,000
Salary in lieu of leave not availed	6,000
Entertainment Allowance	10,000
Commission	8,000
Educational facility to Rajan's son* [22,000 – 1,000 x 12 – 4,000]	6,000
Free use of computer	—
Facility of Refrigerator [20,000 x 10% x 9/12]	1,500
Salary of domestic servant	6,000
Employer's Contribution to RPF in excess of 12% of salary [12,000 – 12% of 96,000]	480
Gross Salary	1,33,980
Less : Deduction under section 16	—
Income from salary	1,33,980
Income from other sources	1,00,000

Gross Total Income	2,33,980
Less deduction under section 80C [12,000 + 40,000]	<u>52,000</u>
Contribution to PF PPF	
Taxable Income	<u>1,81,980</u>
Computation of Tax :	
On First Rs. 1,50,000	—
On balance [1,81,980 – 1,50,000] @ 10%	3,198
Add EC & SHEC (3%)	96
	<u>3,294</u>
Tax liability rounded off	<u>3,290</u>

Note: There are two views regarding valuation of education facilities. According to another view the entire amount of Rs. 18,000/- may included in the total income.

Question 2

- (a) From the following profit and loss account of Vinay for the year ended 31st March, 2009, compute his total income and tax liability for the assessment year 2009-10 :

	Rs.		Rs.
Interest on capital	12,000	Gross profit	5,10,000
Insurance	2,000	Brokerage	30,000
Bad debts	30,000	Bad debts recovered	15,000
Depreciation	34,000	(earlier allowed as deduction)	
Advance tax	25,000	Sundry receipts	18,000
General expenses	12,000	Interest on debentures	
Advertisement	5,000	(gross)	
Salary (including salary to Vinay Rs. 20,000)	85,000	[TDS Rs. 4,120]	40,000
Interest on loan	8,000		
Net profit	4,00,000		
	<u>6,13,000</u>		<u>6,13,000</u>

Additional information :

- The amount of depreciation allowable as per income-tax rules is Rs. 42,000.
 - General expenses include Rs. 5,000 given as contribution to a political party.
 - Vinay pays Rs. 5,200 as premium on his own life insurance policy of Rs. 50,000.
 - Loan was obtained for payment of income-tax. (4 marks)
- (b) Write short notes on any two of the following :
- Taxation of zero coupon bonds

- (ii) *Share of profit from partnership firm*
- (iii) *Exemption of income of newly established units in special economic zone.*
(3 marks each)
- (c) *State, with reasons in brief, whether the following statements are correct or incorrect:*
- (i) *Unabsorbed depreciation of any year can be carried forward for set-off for an unlimited period of time.*
- (ii) *An individual is not liable to pay fringe benefit tax.*
- (iii) *The entire amount of winning from lotteries is taxable at a special rate of income-tax.*
- (iv) *Income of minor child is included in the income of his parents under the Income-tax Act, 1961 in all cases.*
- (v) *When the prize is given partly in cash and partly in kind, income-tax will be deducted from cash only.*
(1 mark each)

Answer 2(a)

**Computation of total income of Mr. Vinay
for the Assessment Year 2009-10**

	<i>Rs.</i>	<i>Rs.</i>
(i) Income from business :		
Net profit as per Profit & Loss A/c		4,00,000
Add : Inadmissible Expenditure		
Interest on Capital	12,000	
Advance Tax	25,000	
Contribution to a political party	5,000	
Salary to Vinay	20,000	
Interest on Loan	<u>8,000</u>	<u>70,000</u>
		4,70,000
Less : Dep. Undercharged (42,000 – 34,000)		<u>8,000</u>
		4,62,000
Less non-business income credited to P&L A/c		
Interest on debentures		<u>40,000</u>
Income from business		4,22,000
Income from other sources (Interest on debentures)		40,000
Gross Total Income		4,62,000
Less : Deduction U/s 8-C		
Life Insurance premium	5,200	
Contn. To political parties	<u>5,000</u>	<u>10,200</u>
Total Income :		<u>(4,51,800)</u>

	<i>Rs.</i>	<i>Rs.</i>
Computation of Tax :		
On First Rs.1,50,000		—
On Next rs.1,50,000 @ 10%		15,000
On Balance Rs.(1,51,800) @ 20%	<u>30,360</u>	<u>30,360</u>
		45,360
Add EC & SHEC (3%)		<u>1,391</u>
Total amount of Tax		46,721
Less : Advance Tax & TDS [25,000+4,120]		<u>29,120</u>
		17,601
Tax Payable rounded off		<u>17,600</u>

Answer 2(b)(i)**Taxation of zero coupon bonds**

The Finance Act, 2005 has introduced the procedure regarding the taxation of the income on the Zero Coupon Bonds issued on or after 1.6.2005. According to Section 2(48) Zero Coupon Bonds means a bond :

- (i) Issued by any infrastructure capital company fund or public sector company;
- (ii) In respect of which no payment or benefit is received or receivable before maturity or redemption from the above companies/funds.
- (iii) Which the Central Government may by notification in the Official Gazette specify in this behalf.

The payment of and benefit from zero coupon bond shall be received or receivable from the issuing company/fund only at the time of maturity or redemption. If such zero bonds are held for less than 12 months, the gain on such bonds shall be short-term capital gain and if these bonds are held for more than 12 months the gain shall be long-term capital gain. Long-capital gain on these bonds shall be chargeable to tax at minimum of the following :

- (i) 20% of long-term capital gain after indexation of cost of such bonds;
- (ii) 10% of long-term capital gain before indexation of cost of such bonds.

Answer 2(b)(ii)**Share of profit from partnership firm**

Share income of a person being a partner of a firm which is separately assessed as such is exempt from tax. For the purposes of this clause, the share of a partner in the total income of a firm separately assessed as such shall be an amount which bears to the total income of the firm the same proportion as the amount of his share in the profits of the firm in accordance with the partnership deed bears to such profits.

Answer 2(b)(iii)**Exemption of income of newly established units in special economic zone**

According to Section 10AA of the Income Tax Act a newly established unit in a Special Economic Zone (SEZ) shall be eligible for deduction of such profit and gain as are derived from export of articles or things or providing any service, as the case may be, during the previous year relevant to any assessment year commencing on or after the 1st April, 2006. The deduction under this Section shall be allowed for a total period of 15 relevant assessment years as per the limits given below :

- (a) 100% of the profit and gain derived from the export of such articles or things or from services for the first 5 consecutive assessment years beginning with the Assessment Years relevant to the previous year in which the unit begins to manufacture such articles or thing or provide services.
- (b) 50% of such profits or gains in the next 5 consecutive Assessment Years.
- (c) So much of the amount not exceeding 50% of the profits as is debited to profit & loss account of the previous year in respect which the deduction is to be allowed and credited to Special Economic Zone Reinvestment Reserve Account to be created and utilized for the purpose of the business of the Assessee in the manner laid down in sub-section (2) of Section 10AA for the next five consecutive Assessment Years.

Answer 2(c)(i)**Correct**

Under Section 32(2) of the Income-tax Act unabsorbed depreciation of any year can be set-off against any income (Except income from salary) of the assessee without time limit whether the business is carried on or not.

Answer 2(c)(ii)**Correct**

An individual is not liable to pay Fringe Benefit Tax as its application does not cover individual employers.

Answer 2(c)(iii)**Correct**

The entire amount of winning from lotteries without deduction of any expenditure or allowance will be taxable. Winning from lotteries is taxable at a special rate of income tax i.e., 30% + Surcharge + cess 3%.

Answer 2(c)(iv)**Incorrect**

Under Section 64(1A) of Income Tax Act all incomes which arises or accrues to the minor child (not being a minor child suffering from any disability) shall be clubbed in the income of his parent whose total income, excluding the minor's income is greater.

Once the income of the minor child is included in the total income of any one parent clubbing of income of minor child with the same parent will continue in subsequent years also. However, where any income is derived by the minor from manual work or from any activity involving application of his skill, talent or specialized knowledge and experience, it will not be clubbed in the income of the parent.

Answer 2(c)(v)

Correct

Under Section 194B of the Income Tax Act when the prize is given partly in cash and partly in kind income tax will be deducted from cash prize with reference to the aggregate amount of the cash price and the value of the price in kind.

Question 3

(a) *Distinguish between any three of the following :*

- (i) *'Gross total income' and 'total income'.*
- (ii) *'Recognised provident fund' and 'statutory provident fund'.*
- (iii) *'Compulsory best judgment assessment' and 'discretionary best judgment assessment'.*
- (iv) *'Exemptions' and 'deductions'. (4 marks each)*

(b) *What is the time-limit for deposit of 'tax deducted at source' (TDS) to the credit of Central Government ? (3 marks)*

Answer 3(a)(i)

'Gross total income' and 'total income'

Gross total income means aggregate amount of taxable incomes computed under five heads of income i.e. salaries, house property, business and profession, capital gains and other sources. While total income means the total amount of income referred to in section 5 computed in the manner laid down in the Income Tax Act. Accordingly after allowing deductions under Section 80-C to 80-U from gross total income the remaining amount is called total income :

Total income is more important than GTI since tax calculation is done on total income.

GTI can remain more than or equal to total income while total income remains equal to or less than GTI.

In GTI rounding-off procedure does not apply, while total income shall be rounded-off to the nearest multiple of ten Rs.

Due to exemption agricultural income shall not be included in Gross Total Income but for tax purpose agricultural income shall be added to Total Income.

Answer 3(a)(ii)

'Recognised provident fund' and 'statutory provident fund'

Recognized Provident Fund is set-up under the provisions of Employee's Provident Fund Act, 1952. This fund is maintained by the private sector organizations and factories.

Apart from this where provident fund maintained by other organization is recognized by the income-tax authorities, such fund is also deemed as recognized provident fund. On the other hand statutory provident fund is set-up under the provisions of Provident Fund Act, 1925. This fund is applicable to the employees of Central Government, State Government and Semi-Government. Under this fund only the employee's contribution is deposited. The Government does not contribute any amount while in case of RPF both employer and employee can deposit the contribution. Employer's contribution to RPF up to 12% of salary is exempted and any amount in excess of 12% is included in gross salary of the employee. Interest up to 9.5% p.a. is exempted and any amount of interest in excess of 9.5% p.a. included in the gross salary of the employee.

Answer 3(a)(iii)

'Compulsory best judgement assessment' and 'discretionary best judgement assessment'

The Assessing officer, after taking into account all relevant material which he has gathered, is under an obligation to make an assessment of the total income or loss to the best of his judgement and determine the tax payable by the Assessee. This is referred as best judged assessment.

Best Judgement assessments are of two types :

- (i) Compulsory best judgement assessment; and
- (ii) Discretionary best judgement assessment.

Compulsory best judgement assessment shall be made by the Assessing Officer in cases of non-co-operation on the part of the assessee or when the assessee is in default as regards supplying information. According to Section 144, in the following circumstances compulsory best judgement assessment shall be made :

Where any person :

- (i) fails to file any return required to be filed under Section 139(1) or has not filed a belated return or a revised return of his income; or
- (ii) fails to comply with all the terms and conditions of the notice issued by the Assessing Officer under Section 142 requiring the assessee to produce such accounts or documents that he might desire; or
- (iii) fails to get the accounts audited by an accountant nominated by the Commissioner or fails to submit a report of such audit in the prescribed time;
- (iv) fails to comply with the accounting standards prescribed by the Central Government in terms of Section 145(2).
- (v) Having filed a return, fails to comply with all the terms and conditions of the notice issued to him, requiring the presence of the assessee or the production of evidence on which the assessee may rely in support of the return.

Discretionary best judgement assessment (Section 145) : The Income-tax Act empowers the Assessing Officer to make a best judgement assessment even in cases where the Assessing Officer is not satisfied :

- (i) about the correctness or the completeness of the accounts of the assessee; or

- (ii) where no method of accounting has been regularly and consistently employed by the assessee.

Answer 3(a)(iv)**‘Exemptions’ and ‘deductions’**

Under Section 10 of the Income Tax Act several incomes are exempt from tax. Such incomes are not included in the computation of total income. For example scholarship for education is exempted from tax. So if a person receives scholarship it will be tax free and not included in his income. Any income which is wholly exempted from tax has two characteristics :

- (i) Income tax is not payable on such income; and
- (ii) Such income is not included in total income of the Assessee.

While under Section 80 of Income Tax Act the deductions specified in Section 80C to 80U are allowed from the Gross Total Income to arrive at the total income. However, the aggregate amount of the deductions cannot exceed the gross total income. The main point of difference between exemption and deductions are as below :

- (a) Exempted income means income not to be added in GTI while deductions is made from GTI.
- (b) Exempted items have been given in Section 10 while deductions have been given under Section 80C to 80U.
- (c) Tax is to be calculated on the Total Income (GTI—Deduction under Section 80C to 80U) while exemptions are not considered while calculating GTI.

Answer 3(b)

Tax deducted at source (TDS) is required to be paid to the credit of Central Government within the time limit stated below :

- (i) When payment is made by the Government or when payment is made on behalf of the Government; tax should be deposited on the date of payment itself.
- (ii) When TDS is done by a non-Government body under Section 193, 194A, 194C, 194D, 194E, 194G, 194H, 194-I, 194J, 195, 196A, 196B, 196C and 196D and the amount is credited to the account of the recipient as on the last date of the accounting year, tax should be deposited within two months from the last date of the accounting year.
- (iii) When Assessing Officer has permitted to make quarterly payment which is covered by Sections 194A, 194D and 194H, TDS is required to be deposited upto July 15, October 15, January 15 and April 15 for respective quarters.
- (iv) When Assessing Officer has permitted to make quarterly payment relating to payment of salary, TDS has to be credited to Government treasury upto June 15, Sept. 15, Dec. 15 and March 15 for respective quarters.
- (v) In any other case, TDS is to be credited within one week from the last date of the month in which deduction is made.

Question 4

- (a) What are the special provisions for computing profits and gains of retail business?
(5 marks)
- (b) What are the provisions relating to clubbing of income arising to spouse from the assets transferred ?
(5 marks)
- (c) Alka is carrying on textile business. Compute her net wealth from the following details of her assets and also determine her wealth-tax liability for the assessment year 2009-10 :

	Market Value (Rs.)
(i) Land in rural area (it lies within 8 kms. from a municipality having a population of more than 10,000; land was purchased in 1990; construction is permissible)	48,00,000
(ii) Land in urban area (held as stock-in-trade since 2001)	35,50,000
(iii) Motor cars	8,60,000
(iv) Aircraft for use of employees and auditors	1,25,00,000
(v) Bank balance	12,00,000
(vi) Guest house situated in rural area	10,50,000
(vii) Residential flats of identical size provided to employees near the factory (salary of employees does not exceed Rs. 5,00,000 in a year)	30,00,000
(viii) Residential house given to general manager (whose annual salary is Rs. 15,00,000)	25,00,000
(ix) Cash in hand as per cash book	2,00,000
(x) Two residential houses let-out on rent (value of each being Rs.22 lakh; one is let-out for 250 days during the financial year 2008-09).	

Alka has taken a loan of Rs.24,00,000 for acquiring the aircraft; Rs.5,50,000 for urban land; and Rs.4,00,000 for residential house given to general manager.

(5 marks)

Answer 4(a)**Provisions for computing profits and gains of retail business (Section 44AF)**

The broad features of the scheme are as under :

- (a) Notwithstanding anything to the contrary contained in section 28 to 43C, in the case of an assessee engaged in retail trade in any goods or merchandise, a sum equal to 5% of the total turnover in the previous year on account of such business shall be deemed to be profits and gains of such business chargeable under the head profits and gains of business or profession. The assessee has to declare a higher income if it is more than the aforesaid amount of 5%.

The scheme shall not be applicable if the total turnover of such retail trade exceeds Rs.40 lakhs in the previous year.

(b) The other features of the scheme are as given below :

- (i) Any deduction allowable under the provisions of Sections 30 to 38 shall for the purpose of above income be deemed to have been already given full effect to and no further deduction under these sections shall be allowed. However, remuneration to working partner and interest paid or payable to partners shall be allowed as deduction from the income computed under this section. Such deduction shall however be subject to conditions and limits specified under section 40(b).
- (ii) The written down value of any asset used for the purpose of the business shall be deemed to have been calculated as if the assessee had claimed and had been actually allowed the deduction in respect of depreciation for each of the relevant assessment years.
- (iii) The provisions of sections 44AA and 44AB shall not apply in so far as they relate to this business and in computing the monetary limits under these sections, the total turnover or as the case may be, the income from said business shall be excluded.
- (iv) The assessee may choose not to opt for this scheme and may declare an income lower than the specified amount. In this case, the assessee shall have to keep and maintain books of account as per Section 44AA and get his accounts audited as per Section 44AB.

Answer 4(b)

Income from assets transferred to the spouse [Section 64(1)(iv)]

In computing the total income of an individual, all such income as arises directly or indirectly, subject to the provision of Section 27(i), to the spouse of such individual from assets transferred directly or indirectly to the spouse of such individual otherwise than for adequate consideration or in connection with an agreement to live apart shall be included.

As per this provision, if an individual transfers any asset other than house property to his/her spouse, the income from such an asset shall be included in the total income of the transferor. This provision is not applicable to house property because in that case the transferor is deemed to be the owner of the house property and the annual value of the property is taxed in the hands of the transferor as per Section 27.

The income from the transferred assets shall not be clubbed in the following cases:

- (i) If the transfer is for adequate consideration;
- (ii) The transfer is under an agreement to live apart;
- (iii) If the relationship of husband and wife does not exist, either at the time of transfer of such asset or at the time of accrual of the income

Where a gift has been made, prior to the solemnization of the marriage, to the would be wife, the provisions of Section 64(1)(iv) cannot be attracted for the assessment year in respect of the income derived from such gifted amount.

Extent of inclusion under sections 64(1)(iv), (vi), (vii) and (viii) in cases of inadequate consideration : There may be cases where the transfer of assets to spouse is for consideration passed, but the amount of the consideration is not adequate. Property worth Rs.1,50,000 may have been transferred for a consideration of Rs.1,00,000 only. In such cases, the income from the property includible in the spouse would be in the proportion of the inadequacy of the consideration, i.e., Rs.50,000. Thus, if the income from the property is Rs.3,000, only Rs.1,000 will be included under these provisions in the transferor's income.

Answer 4(c)

Computation of Net Wealth of Mrs. Alka for the Assessment Year 2009-10

<i>Particulars</i>	<i>Amount (Rs.)</i>
Land in rural area	48,00,000
Land in Urban Area (Exempt for 10 years)	Nil
Motor Cars	8,60,000
Aircraft [being used for business]	Exempt
Bank balance [not an asset]	Nil
Guest House	10,50,000
Residential flats [Salary of employees does not exceed Rs.5 lac]	Exempt
Residential House to Managing Director	25,00,000
Let out residential house [one let out for less than 300 days]	22,00,000
Cash in hand [Rs.2,00,000 – Rs.50,000] being an individual	1,50,000
Gross Wealth	1,15,60,000
Less amount of loan used in acquiring residential house	
Given to Managing Director	4,00,000
Net Wealth	1,11,60,000
Wealth Tax @ 1% on (Rs.1,11,60,000 – Rs.15,00,000)	
Rs. 96,60,000 = Rs.96,600	

Note : Loans in respect of exempted assets are not deductible.

Question 5

- (a) Anurag sells a plot of land on 8th July, 2008 for Rs.40 lakh and paid brokerage on its sale @ 1%. He purchased this plot on 19th December, 1986 for Rs.4,20,000. On 1st February, 2009, he purchased a residential house for Rs.15 lakh. He owns one residential house on 8th July, 2008. The cost inflation index for 1986-87 was 140 and for 2008-09 is 582. Find out the amount of capital gains chargeable

to tax for the assessment year 2009-10. Suppose Anurag sells the new residential house before 1st February, 2012, what will be the taxable amount of capital gains and in which year it will be charged to tax ? If Anurag purchases any other residential house before 1st February, 2011, what will be the taxable amount of capital gains and in which year it will be charged to tax ? (5 marks)

(b) Danny has the following investments in the previous year ended 31st March, 2009:

- (i) Rs.7,160 received as interest on securities of Karnataka government.
- (ii) Rs.9,000 received as interest on securities of a listed paper manufacturing company.
- (iii) Rs.7,200 received as interest on the unlisted securities of a sugar company.
- (iv) Rs.30,000, 11% securities (unlisted) of a textile company.
- (v) Rs.20,000, 10% Tamil Nadu government loan.
- (vi) Rs.50,000, 13.5% listed debentures of Dolly Ltd.

Interest on all securities is payable on 30th June, and 31st December. The bank charges 1.5% commission on net realisation of interest as collection charges.

Danny also received Rs.15,000 as director's fee from a company. His other incomes are — winnings from horse race : Rs.25,000 (gross); and interest on post office savings bank account : Rs.6,000.

Find out taxable income of Danny from other sources for the assessment year 2009-10. (5 marks)

(c) "Loss under any head of income for any assessment year can be set-off against the income from other heads of income but when it has to be carried forward for being set-off, it can only be set-off from income under the same head." Explain. (5 marks)

Answer 5(a)

Computation of Income from Capital Gains of Mr. Anurag for the Assessment Year 2009-10.

Particulars	Amount (Rs.)
Sales consideration	40,00,000
Less : Brokerage on Sales @ 1%	40,000
Net sales consideration	39,60,000
Less : Indexed Cost of Acquisition $4,20,000 \times 582/140$	17,46,000
LTCG	22,14,000
Less : Exemption under section 54F	8,38,636
$(22,14,000 \times 15,00,000/39,60,000)$	13,75,364
Taxable Income from Capital Gains	13,75,364

If Mr. Anurag sells the new house before February, 2012 then Rs.(8,38,636) being the amount of capital gains exempted during the Assessment Year 2009-10 under

section 54F will be chargeable to tax for the year in which the house is sold as long-term capital gains.

If Mr. Anurag purchases any other residential house before February 1, 2011 but after July 8, 2010 then he will not have any tax liability on account of Capital Gain. If Mr. Anurag purchases any other residential house before July 8, 2010 (i.e., within two years from the date of transfer of the original asset) then Rs. 8,38,638 will be taxable as long-term capital gains for the year in which another house is purchased.

Answer 5(b)

Computation of Income from other sources of Mr. Danny for the Assessment Year 2009-10.

<i>Particulars</i>	<i>Amount (Rs.)</i>
Karnataka Government Securities (No TDS)	7,160
Paper Company Securities (9,000 x 100/89.7)	10,034
Sugar Mill Company Securities (7,200 x 100/79.4)	9,068
Textile Company Securities	3,300
Tamilnadu Government Loan (No TDS)	2,000
DCM Ltd. Debentures (listed)	6,750
Director's Fee	15,000
Winnings from Horse races	25,000
Interest on Post Office Saving Bank A/c	Exempt
Gross Receipts	78,312
Less: Deduction under Section 57 for collection charges	511
Taxable Income from other sources	7,7801

Computation of Collection Charges

<i>Particulars</i>	<i>Amount (Rs.)</i>
Amount of Collection from securities :	
Karnataka Government Securities (No TDS)	7,160
Paper Company Securities	9,000
Sugar Mill Company Securities	7,200
Textile Company Securities [3,300 x 79.4/100]	2,620.20
Tamilnadu Government Loan	2,000
DCM Ltd. Debentures [6,750 x 89.7/100]	6054.75
Total Net Collection :	34,034.95
Collection Charges @ 1.5%	
34,034.95 x 1.5/100	= Rs. 510.52
	= Rs. 511

Answer 5(c)

As per Section 70, the general rule is that if the net result in respect of any source under any head of income is loss, the assessee can set it off from his income from any other source under the same head of income for the same assessment year barring a few cases of exceptions.

Likewise, as per Section 71, the general rule is that where there is a loss under any head of income, the same can be set-off against the income from other heads during the same assessment year barring a few exceptional cases.

When a loss cannot be set-off either under the same head or under different heads because of absence or inadequacy of the income of the same year, it may be carried forward for being set-off from the income of subsequent year/years. However, set-off of losses during the subsequent year/years can be made only from the same head of income from which the loss accrued during previous year/years. This is clear from the rules given under Section 71B, 72, 73, 74 and 74A :

- (i) Carried forward loss under the head "Income from house property" as per Section 71B, can only be set-off from income under this head only upto a maximum period of 8 assessment years.
- (ii) Carried forward business loss of non-speculative business, as per Section 72, can be set-off from income from business only upto a maximum of 8 assessment years.
- (iii) Carried forward loss of speculative business, as per Section 73, can be set off from income from speculative business only over a maximum period of 4 Assessment Years.
- (iv) Carried forward capital loss, as per Section 74, can be set-off from income from capital gains of subsequent year's upto a maximum period of 8 assessment years. However, long-term capital loss can only be set-off from long-term capital gains; short-term capital loss can be set-off from both-short-term as well as long-term capital gains.
- (v) Carried forward loss from activity of owning and maintaining race horses can be set-off from income from this business activity only chargeable to tax under the head "income from other sources" upto a maximum period of 4 assessment years.

Question 6

- (a) Rohit is the owner of a house property, its municipal valuation is Rs.80,000. It has been let-out for Rs.1,20,000 per annum. The local taxes payable by the owner amount to Rs. 16,000, but as per agreement between the tenant and the landlord, the tenant has paid the amount direct to the municipality. The landlord, however, bears the following expenses on tenant's amenities :

	Rs.
Extension of water connection	3,000
Water charges	1,500
Lift maintenance	1,500

<i>Salary of gardener</i>	<i>1,800</i>
<i>Lighting of stairs</i>	<i>1,200</i>
<i>Maintenance of swimming pool</i>	<i>750</i>
<i>The landlord claims the following deductions :</i>	
<i>Repairs and collection charges</i>	<i>7,500</i>
<i>Land revenue paid</i>	<i>1,500</i>

Compute the taxable income of Rohit from the house property for the assessment year 2009-10. (10 marks)

(b) What are 'capital assets' ? What items are not included in capital assets ? (5 marks)

Answer 6(a)

Computation of income from house property for the assessment year 2010-11

Gross annual value : to be higher of the following:

	<i>Rs.</i>	<i>Rs.</i>	<i>Rs.</i>
(a) Municipal valuation Rs. 80,000			
Or			
(b) De facto rent (Rs. 1,20,000 less value of amenities)			
Rent Received:			1,20,000
Less : Value of the amenities provided by the assessee:			
(i) Extension of water connection not deductible as it is capital expenditure			
(ii) Water charges	1,500		
(iii) Lift maintenance	1,500		
(iv) Salary of gardener	1,800		
(v) Lighting of stairs	1,200		
(vi) Maintenance of swimming pool	750	(6,750)	
Gross annual value			1,13,250
Less : Local tax Rs. 16,000 :			
No deduction is permissible as the taxes have been paid by the tenant			—
Net annual value			1,13,250
Less : Deduction from net annual value: 30% of Net Annual Value			33,975
Taxable Income			<u>79,275</u>

Answer 6(b)

Section 2(14) of the Income-tax Act defines the term “capital asset” to mean :

Property of any kind held by an assessee whether or not connected with his business or profession but does not include :

- (i) Any stock-in-trade, consumable stores or raw-materials held for the purposes of his business or profession;
- (ii) Personal effects that is to say, movable property (including wearing apparel and furniture but excluding jewellery) held for personal use by the assessee or any member of his family dependent on him. Jewellery includes ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals, whether or not containing any precious or semi-precious stone, and whether or not worked or sewn into any wearing apparel and precious or semi-precious stones, whether or not set in any furniture, utensil or other article or worked or sewn into any wearing apparel;
- (iii) Agricultural land in India, not being land situate (a) within the jurisdiction of a municipality or a cantonment board and which has a population of not less than 10,000 according to the last preceding census, or (b) in any area within such distance, not being more than eight kilometers from the local limits of any Municipality or cantonment board, as the Central Government may, having regard to the extent of any scope for urbanisation of that area and other relevant considerations, specify in this behalf by notification in the Official Gazette;
- (iv) 6½ per cent Gold Bonds, 1977 or 7 per cent Gold Bonds, 1980 or National Defence Gold Bonds, 1980 issued by the Central Government;
- (v) Special Bearer Bonds 1991 issued by the Central Government.
- (vi) Gold Deposit Bonds issued under the Gold Deposit Scheme, 1999 notified by the Central Government.

PART B**Question 7**

Attempt any four of the following :

- (a) *“Service tax is generally payable by the service provider, but there are certain situations in which service receiver is liable to pay service tax.” Explain.*
(5 marks)
- (b) *What are the due dates for payment of service tax by different assessees ?*
(5 marks)
- (c) *Indicate the amount of interest payable for late payment of service tax and the amount of penalty payable for late filing of return of service tax.* (5 marks)
- (d) *Explain the provisions regarding submission of return under service tax.*
(5 marks)
- (e) *What is the basis of calculation of service tax payable ? Explain the provisions governing valuation of taxable services.*
(5 marks)

- (f) Choose the most appropriate answer from the given options in respect of the following :
- (i) What would be the value of taxable service, if gross amount charged by a service provider on 5th March, 2009 is Rs.9,000 —
- (a) Rs. 8,010
 - (b) Rs. 8,160
 - (c) Rs. 9,000
 - (d) Rs. 8,100.
- (ii) If Raj has collected any amount of service tax from Brij which is not required to be collected, Raj shall pay the amount so collected to —
- (a) Brij
 - (b) The Central Government
 - (c) Keep it with himself
 - (d) None of the above.
- (iii) E-payment of service tax is compulsory in the case of an assessee who had paid service tax in the preceding financial year equal to at least —
- (a) Rs. 10 lakh
 - (b) Rs. 40 lakh
 - (c) Rs.50 lakh
 - (d) Rs. 1 crore.
- (iv) Upto what amount, the value of all taxable services provided by a service provider during a financial year is exempt from payment of service tax —
- (a) Rs. 4 lakh
 - (b) Rs. 8 lakh
 - (c) Rs. 10 lakh
 - (d) Rs. 12 lakh.
- (v) If a corporate assessee has paid Rs. 15,000 as excess service tax during the previous half-year ending period, this excess amount can be adjusted against its subsequent tax liability —
- (a) Equally every month
 - (b) Equally per quarter
 - (c) In one lump-sum
 - (d) Equally on half-yearly basis.

(1 mark each)

Answer 7(a)

Service tax is generally payable by the service provider but in situations referred to in Rule 2(1)(d), the person receiving the service is liable to pay service tax in the notified cases as is clear from the following table :

<i>Sl.No.</i>	<i>Person liable to pay service tax</i>	<i>Notified service</i>
1.	The DG of Posts & Telegraph, Chairman MTNL, a licence holder under Indian Telegraph Act	Telecommunication service
2.	Insurer or re-insurer	General insurance business
3.	Person carrying on business of general insurance or life insurance	Insurance auxiliary services provided by insurance agent
4.	Person who pays or is liable to pay freight himself or through his agent in road goods carriage	Services in relation to transport of goods by road
5.	Recipient of service	Services provided or to be provided by any person from abroad to any person in India
6.	Mutual fund or asset management company	Business auxiliary service of distribution of mutual fund
7.	Body corporate or firm who receives sponsorship services	Sponsorship services provided in India.

The persons liable to pay service tax will have to get themselves registered.

Answer 7(b)

In the case of individuals, proprietary firms and partnership firms, service tax is paid quarterly—April to 1 to June 30; July 1 to Sep.30; Oct. 1 to Dec.31 and Jan. 1 to March 31. In their case the due date for payment of service tax is 5th day of the month immediately following the relevant quarter. Therefore, on this basis July 5 will be the due date for service tax related to the first quarter; Oct. 5 for the second quarter and Jan 5, for the third quarter. There is one exception to this rule which provides that service tax received during the month of March or the quarter ending March shall be paid to the credit of Central Government by March 31 of the Calendar year. Therefore, for the last quarter Jan. 1 to March 31, March 31 is the due date of payment of service tax. Also when tax is deposited electronically through internet banking, the due date will be 6th day of the month immediately following the end of relevant quarter. So, July 6, Oct. 6 and Jan. 6 will be the due dates for payment of service tax when tax is deposited through internet in regard to the first three quarters but due to the above exception March 31 will be the due date for the last quarter even in this case.

In the case of companies and HUF, the due date of payment of service tax is 5th of the month immediately following every calendar month and 6th of the month immediately following every calendar month when service tax is paid through internet. In the case of

these assesses, service tax is paid every month and not quarterly as is the case with other assesses. For example, the due date for payment of service for the first calendar month of the financial year, which is April, will be May 5 (May 6 when tax is paid through internet) and so on. But for last month of the Financial Year, which is March, March 31 will be the due date for payment of service tax due to the exception as stated above. If the last day of payment of service tax is a public holiday, tax can be paid on the succeeding day which should be a working day.

Answer 7(c)

According to Section 75 of the Service Tax Act, simple interest @ 13% is payable for late payment of service tax. Interest is payable only for the period of delay beginning with first day after the due date and ending with the actual date of payment of service tax. For example, suppose the due date of service tax is May 6 and actual date of payment is May 21. Interest in this case will be paid for 15 days @ 13% per annum simple interest.

Rule 7C provides for the amount of penalty imposable by the Central Government for late filing of return of service tax. If the delay is upto 15 days, a penalty of Rs.500/-, if the delay is for 15 days to 30 days, a penalty of Rs.1,000; if delay is for 31 days or more, a penalty of Rs.1,000 plus Rs.100 per day from 31st day onwards subject to a maximum of Rs.2,000 shall be imposed.

Answer 7(d)

Provisions regarding returns are given below :

- (i) Every person liable to pay the service tax needs to self assess the tax due on the services provided by him. Further a return must be furnished to the superintendent of Central Excise in Form ST-3.
- (ii) The return is to be filed on half year basis i.e., (1st April to 30 Sept. & 1 Oct to March 31).
- (iii) The half yearly return should be filed in triplicate on or before the 25th of the month following the particular half year.
- (iv) Return under Section 70 contains general information like financial year, half yearly period, name of the assessee, registration number of premises and categories of taxable services for which the return is filed. Besides it contains month wise details of payment of service tax etc.
- (v) Copies of TR 6 Challan indicating the payment of Service Tax and Memorandum in Form ST-3A should be submitted along with the return.
- (vi) At first time of filing of return every assessee must furnish a list of all accounts maintained by the assessee.
- (vii) Assessee can file ST-3 Return by registered post with concerned divisional office on or before due date.
- (viii) If the assessee is providing more than one taxable service he should file only one return. In this case service wise details should be given in the return instead of a single total figure for all the services.

- (ix) Even if no services have been provided during a half year and no service tax is payable the assessee may file a nil return within the prescribed time limit.
- (x) Within 60 days from the date of filing of original return an assessee can file revised return to rectify mistakes.
- (xi) Electronic filing of return of service tax, facility is also available to file service tax return.

Answer 7(e)

According to Section 67 of the Finance Act, 1994 the amount of service tax is calculated on the basis of value determined under this Section. If value cannot be determined as per Section 67 valuation shall be made on the basis of valuation Rules, 2006. The provisions of Section 67 regarding valuation of taxable services are as follows:

- (i) The consideration for a taxable service shall be the gross amount charged by the service provider for the service provided or to be provided;
- (ii) If the consideration for a taxable service is in term of money the value of such service shall be the gross amount charged by the service provider for such service provided or to be provided.
- (iii) If the consideration for a taxable service is not received wholly or partly in money the value of taxable service shall be the amount of money as with addition of service tax charged is equivalent to the consideration.
- (iv) If consideration for a taxable service is not ascertainable value of such service will be on the basis of valuation rules;
- (v) If the gross amount charged by the service provider is inclusive of service tax payable the value of taxable service shall be calculated in the manner that with addition of service tax payable the total is equal to the gross amount charged.
- (vi) The gross amount charged for the taxable service can be received before during or after the provision of taxable service.
- (vii) Money includes any currency, cheque promissory notes, letter of credit, draft pay order, travelers cheque money order etc. but does not include currency that is held for its numismatic value;
- (viii) Gross amount paid includes payment by cheque, credit card, deduction from account and any form of payment by issue of credit notes or debit notes and book adjustment.

Answer 7(f)(i)

- (a) Rs. 8,160 (w.e.f. 24.02.2009)

Answer 7(f)(ii)

- (b) Central Government

Answer 7(f)(iii)

- (c) Rs.50 lac

Answer 7(f)(iv)

- (c) Rs.10 lac

Answer 7(f)(v)

- (a) Equally every month

PART C**Question 8**

Attempt any four of the following :

- (i) How would you take input tax credit when goods purchased are transferred by the dealer to his branch in any other State ?*
- (ii) "A registered dealer can set-off the amount of input tax against the amount of his output tax." Explain.*
- (iii) Explain the procedure of registration under 'value added tax' (VAT).*
- (iv) In what purchases input tax credit is not allowed under VAT ?*
- (v) What are the deficiencies in the design of VAT that has been adopted by the States in India ? Give your opinion.*
- (vi) "Tax credit or invoice method has been adopted universally because of the inherent advantages in the credit method of calculating tax liability." Explain.
(5 marks each)*

Answer 8(i)

In case of stock transfer of output outside, the State, input tax credit paid in excess of 2%, shall be eligible for tax credit. Since inter-State sale carries CST @ 2% and this not VAT-able in the importing State, corresponding tax incidence has to be kept for inter-state stock transfers.

Answer 8(ii)

VAT aims at providing set-off for the tax paid earlier and this is given effect through the concept of input tax credit. Set-off of the input tax credit in relation to any period means setting off the amount of input tax by a registered dealer against the amount of his output tax.

Tax paid on the inputs is termed as input tax. This amount is adjusted against the tax payable by the purchasing dealer on his sales. This credit availability is called input tax credit. Input tax is the tax paid or payable in the course of business on purchase of any goods made from a registered dealer of the State. Output tax means the tax charged or chargeable under the Act by a registered dealer for the sale of goods, in the course of business. In other words input tax is the tax a dealer pays on his local purchases of business inputs, which include the goods that he purchases for resale, raw material, capital goods as well as other inputs for use directly or indirectly in his business and output tax is the tax that a dealer charges on his sales that are subject to tax. The input tax credit is to be given for both manufacturers and traders for purchases of inputs,

supplies meant for both sale within the state as to other states, irrespective of when these were utilized or sold. This also reduces immediate tax liability. It is also to be noted that in certain cases partial input of tax credit is available in respect of input used for manufacture of exempted goods.

Input tax credit is allowable to a registered dealer for purchase of any goods made within the state from a dealer having a valid certificate of registration under the Act. Input tax credit on capital goods is available for traders and manufacturer.

Answer 8(iii)

Every dealer upto the retailer level is required to be registered with the sales tax department to avail the credit of input tax. However, there would be a threshold turnover level. The retailers with turnover below the threshold can opt not to register but to pay a nominal composition tax. However, such dealers are not entitled to take credit of prior stage tax, nor can they pass the credit to their buyers. In effect the VAT chain breaks at their stage. Those opting not to register under VAT can opt for general registration.

Registration of dealers with gross annual turnover above the prescribed limit will be compulsory. There will be a provision for voluntary registration for dealers with gross annual turnover of less than the prescribed limit. All existing dealers will be automatically registered under the VAT Act. A new dealer will be allowed 30 days time from the date of his being liable to get registered. Small dealers with gross annual turnover not exceeding the prescribed limit will not be liable to pay VAT. States will have flexibility to fix threshold limit within the prescribed limit. Small dealers with annual gross turnover not exceeding Rs.50 lakh who are otherwise liable to pay Vat shall however have the option for a composition scheme with payment of tax at a small percentage of gross turnover. The dealers opting for the composition scheme will not be entitled to input tax credit.

Answer 8(iv)

Input tax credit is not allowed under VAT in respect of the following purchases :

- (a) The dealers opting for the composition scheme will not be entitled to input credit on their purchases;
- (b) When a certain sale is exempted from tax, the dealer effecting the exempted sale will not be entitled to any Vat credit on the inputs purchased by him;
- (c) Input tax credit is not available on the purchases made from an unregistered dealer.
- (d) Input tax credit is not available if the final product are not sold but given as free sample.

Answer 8(v)

Some crucial deficiencies of VAT design adopted by states in India are as follows :

- (i) It does not cover all goods and services that comprise in the final consumption. Services are not at all included. The Central Government has not yet delegated the powers to tax services to States.
- (ii) Under continuous pressure from various forces the list of exempted commodities from VAT is quite big.

- (iii) The states have no power of going above or below the “floor rates” even though floor rate implies that discretionary rates may as well can be adopted by states. Also, no rebate is given for tax on purchases of goods of exempted category at the time of sale to a final consumer.
- (iv) The general rate of VAT which is 12.5% is too high. It is not possible to see this rate to be “revenue neutral” for all states. Rate of Sales Tax of only a few States was as high as 12.5%.
- (v) Classification of goods is arbitrary and leaves high chances of disputes as to whether a particular item comes within the lower rate category or not.
- (vi) “Capital goods” and “industrial inputs” have been included in the 4% list. Concessional rate of VAT is not warranted for inputs because the end use of a product by the customer should not affect the VAT to be charged and paid by a seller “set off” automatically takes care of it. Also, reduced rates on inputs increases revenue loss from undeclared sales of finished products.

Answer 8(vi)

Under tax credit method of VAT, amount of VAT payable is arrived at by subtracting total tax paid to the suppliers on inputs/purchases from the amount of total tax charged on the outputs/sales. The other methods—addition method and subtraction method are not practicable in the case of a manufacturer when the rate of tax is different on inputs and output.

The following are the advantages of using tax credit method :

- (a) Since under this method dealers are required to state the amount of tax in invoices, it makes cross-checking of tax paid at earlier stages more practicable.
 - (b) Dealers at intermediate stages do not have any interest in tax rate because burden of tax is dependent on the tax rate at the final stage;
 - (c) Under this method, through zero rating of exports, exports can easily be relieved of domestic indirect taxes.
-