

**MOCK TEST PAPER – 1**  
**FINAL COURSE: GROUP – II**  
**PAPER – 7: DIRECT TAX LAWS**  
**SUGGESTED ANSWERS / HINTS**

1. (a) Computation of total income and tax liability of Merchant LLP as per the normal provisions for assessment year 2013-14

| Particulars                                                                | ₹ in lacs        |                         |
|----------------------------------------------------------------------------|------------------|-------------------------|
| <b>Net profit as per Profit and Loss A/c</b>                               |                  | 54,00,000               |
| <i>Less: Income exempt or taxable under different heads</i>                |                  |                         |
| Dividend (Exempt under section 10(34))                                     | 1,00,000         |                         |
| Profit on sale of vacant site (taxable under Capital Gains)                | <u>7,00,000</u>  | <u>8,00,000</u>         |
|                                                                            |                  | 46,00,000               |
| <i>Add: Working partner's salary (considered separately)</i>               | 12,00,000        |                         |
| Provision for income-tax (not a deductible expenditure)                    | 14,00,000        |                         |
| Depreciation                                                               | <u>12,00,000</u> | <u>38,00,000</u>        |
|                                                                            |                  | 84,00,000               |
| <i>Less: Depreciation allowable under section 32</i>                       |                  | <u>8,00,000</u>         |
| Book profit                                                                |                  | 76,00,000               |
| <i>Less: Working partners' salary (Refer Working Note below)</i>           |                  | <u>12,00,000</u>        |
| <b>Income under the head "Profits and Gains of business or profession"</b> |                  | 64,00,000               |
| Long term capital gain (computed)                                          |                  | <u>5,00,000</u>         |
| <b>Gross total income</b>                                                  |                  | <b>69,00,000</b>        |
| <i>Less: Deduction under section 80-1A</i>                                 |                  | <u>20,00,000</u>        |
| <b>Total Income</b>                                                        |                  | <b>49,00,000</b>        |
| Tax thereon : On ₹ 44 lacs @ 30%                                           |                  | 13,20,000               |
| On ₹ 5 lacs @ 20% (LTCG)                                                   |                  | <u>1,00,000</u>         |
|                                                                            |                  | 14,20,000               |
| <i>Add: Education cess &amp; secondary and higher education cess @ 3%</i>  |                  | <u>42,600</u>           |
| <b>Total tax liability</b>                                                 |                  | <b><u>14,62,600</u></b> |

### Computation of Alternate Minimum Tax under section 115JC

| Particulars                                                       | ₹                       |
|-------------------------------------------------------------------|-------------------------|
| Total income                                                      | 49,00,000               |
| Add: Income from undertaking eligible for section 80-IA deduction | <u>20,00,000</u>        |
| Adjusted Total Income                                             | <u>69,00,000</u>        |
| Tax thereon @ 18.5%                                               | 12,76,500               |
| Add: Education cess & secondary and higher education cess @ 3%    | <u>38,295</u>           |
| <b>Total tax liability</b>                                        | <b><u>13,14,795</u></b> |
| <b>Rounded off</b>                                                | <b><u>13,14,800</u></b> |

As the tax liability under section 115JC is less than regular income tax payable, Merchant LLP has to pay tax as per the regular provisions i.e. ₹ 14,62,600.

#### Working Note:

Working partners' salary of ₹ 12 lakhs is to be restricted to the limits under section 40(b)(v) i.e.

|                                      |                                     |                           |
|--------------------------------------|-------------------------------------|---------------------------|
| First ₹ 3,00,000 of Book Profit      | 90% or ₹ 1,50,000 whichever is more | ₹ 2,70,000                |
| Remaining ₹ 73,00,000 of Book Profit | 60%                                 | ₹ <u>43,80,000</u>        |
|                                      |                                     | ₹ <u><b>46,50,000</b></u> |

Since the actual salary of ₹ 12 lakhs is less than ₹ 46,50,000, actual salary is allowable as deduction.

#### (b) Computation of Net Wealth of Sigma Limited as on the valuation date 31.03.2013

| Particulars                 | Reasons                                                      | Value<br>(₹ in crores) |
|-----------------------------|--------------------------------------------------------------|------------------------|
| <b>Assets:</b>              |                                                              |                        |
| (i) <b>Fixed Assets:</b>    |                                                              |                        |
| Plant & Machinery           | Not an asset under section 2(ea)                             | Nil                    |
| Factory building            | Commercial property. Hence, not an asset under section 2(ea) | Nil                    |
| Urban land (350 sq. meters) | It is an asset under section 2(ea) <b>(Refer Note 2)</b>     | 100                    |

|                                                                           |                                                             |                                                                                                                                 |            |
|---------------------------------------------------------------------------|-------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------|------------|
|                                                                           | Motor cars                                                  | Used for running on hire. Hence, not an asset under section 2(ea)                                                               | Nil        |
| (ii)                                                                      | <b>Investments:</b>                                         |                                                                                                                                 |            |
|                                                                           | Jewellery                                                   | It is not a stock-in-trade. Hence, an asset under section 2(ea)                                                                 | 30         |
|                                                                           | Plot of land in Mumbai                                      | An asset under section 2(ea). <b>(Refer Note 2)</b>                                                                             | 50         |
|                                                                           | Equity shares in subsidiary companies                       | Not an asset under section 2(ea)                                                                                                | Nil        |
| (iii)                                                                     | <b>Current assets:</b>                                      |                                                                                                                                 |            |
|                                                                           | Inventories (Jewellery)                                     | Stock-in-trade. Hence, not an asset under section 2(ea)                                                                         | Nil        |
|                                                                           | Sundry Debtors                                              | Not an asset under section 2(ea)                                                                                                | Nil        |
|                                                                           | Cash and bank balances (includes cash balance of ₹2,50,000) | Bank balance – not an asset under section 2(ea).<br>Cash in hand – recorded in books – hence, not an asset under section 2(ea). | Nil        |
| <b>Value of assets as per Schedule III of the Wealth-tax Act, 1957(A)</b> |                                                             |                                                                                                                                 | <b>180</b> |
|                                                                           | <b>Liabilities:</b>                                         |                                                                                                                                 |            |
| (i)                                                                       | Current Liabilities                                         | Not incurred in relation to an asset under section 2(ea). Hence, not eligible for deduction.                                    | Nil        |
| (ii)                                                                      | Loan for purchase of urban land                             | Since urban land is included in the net wealth, loan taken for its purchase is eligible for deduction.                          | 30         |
| <b>Liabilities eligible for deduction (B)</b>                             |                                                             |                                                                                                                                 | <b>30</b>  |
| <b>Net wealth [(A) – (B)]</b>                                             |                                                             |                                                                                                                                 | <b>150</b> |

**Notes:**

- In respect of the business assets of Sigma Ltd. chargeable to wealth tax, the value as per Schedule III exceeds the book value by 20%, therefore, the Schedule III value has been taken to be the value for levy of wealth tax.

2. Plot of land not exceeding 500 sq. meters is exempt only in the case of an individual or HUF and not in the case of a company.

**2. Computation of total income of Star India Private Ltd. for the A.Y. 2013-14**

| Particulars                                                                                        | ₹               | ₹        |
|----------------------------------------------------------------------------------------------------|-----------------|----------|
| <b>Income from House Property (Note 1)</b>                                                         |                 |          |
| Gross Annual Value (GAV) (Rental income has been taken as GAV in the absence of other information) | 5,00,000        |          |
| Less: Municipal Taxes (not deductible since it has not been paid)                                  | <u>Nil</u>      |          |
| Net Annual Value (NAV)                                                                             | 5,00,000        |          |
| Less: Deduction under section 24 (30% of NAV)                                                      | <u>1,50,000</u> | 3,50,000 |
| <b>Profits and gains of business or profession</b>                                                 |                 |          |
| Net profit as per profit and loss account                                                          | 1,20,00,000     |          |
| Add: <b>Items debited but to be disallowed or to be considered separately</b>                      | 16,00,000       |          |
| Licence fee for obtaining franchise (Note 2)                                                       |                 |          |
| Municipal taxes in respect of let-out part of office premises (Note 1)                             | 12,000          |          |
| Contribution to approved and notified university (treated separately) (Note 4)                     | 1,60,000        |          |
| Loss due to destruction of machinery by fire (Note 5)                                              | 2,40,000        |          |
| Amount payable to contractor not having PAN (Note 6)                                               | 80,000          |          |
| Short-term capital loss on sale of shares of P. Ltd. (Note 7)                                      | 16,000          |          |
| Depreciation on tangible fixed assets (Note 8)                                                     | <u>80,000</u>   |          |
|                                                                                                    | 1,41,88,000     |          |
| Less: <u>Depreciation under section 32 (Note 8)</u>                                                |                 |          |
| Tangible fixed assets (Note 8)                                                                     | 1,40,000        |          |
| Intangible asset (Franchise)                                                                       |                 |          |
| 25% of ₹ 16,00,000 (Note 2)                                                                        | <u>4,00,000</u> | 5,40,000 |
| Weighted deduction under section 35(1)(ii) (Note 4)                                                |                 | 2,80,000 |
| Rental income to be taxed under "Income from house property" (Note 1)                              | 5,00,000        |          |

|                                                                                                     |               |                           |
|-----------------------------------------------------------------------------------------------------|---------------|---------------------------|
| Dividend credited to profit and loss account to be excluded <b>(Note 7)</b>                         | 8,000         |                           |
| Waiver of interest on bank loan credited to profit and loss account but not taxable <b>(Note 9)</b> | <u>80,000</u> | 1,27,80,000               |
| <b><u>Capital Gains (Note 7)</u></b>                                                                |               |                           |
| Short-term capital loss (₹ 20 x 1000 shares)                                                        | 16,000        |                           |
| <b>Less:</b> Dividend exempt under section 10(34)                                                   | <u>8,000</u>  |                           |
| Short-term capital loss to be carried forward to A.Y. 2014-15                                       | <u>8,000</u>  |                           |
| <b><u>Income from Other Sources (Note 10)</u></b>                                                   |               |                           |
| Deemed dividend under section 2(22)(e)                                                              |               | <u>40,000</u>             |
| <b>Total Income</b>                                                                                 |               | <b><u>1,31,70,000</u></b> |

**Notes:**

- (1) Rental income from letting out a part of the office premises is taxable under "Income from house property". Therefore, it has to be deducted while calculating business income, since the income has been credited to profit and loss account. Likewise, municipal taxes due in respect of such property, debited to profit and loss account has to be added back to compute business income

**Note** - There is an alternate view that rental income from letting out part of the excess premises by an assessee who is engaged in business is only exploitation of the commercial asset by an assessee who is engaged in business and hence, the same constitutes business income only. In such a case also, municipal taxes is not allowable as deduction since the same has not been paid on or before the due date of filing of return of income as required under section 43B.

- (2) Franchise is an intangible asset eligible for depreciation @ 25%. Since one-time licence fees of ₹ 16 lakh paid to a foreign company for obtaining franchise has been debited to profit and loss account, the same has to be added back. Depreciation @ 25% has to be provided in respect of the intangible asset since it has been used for more than 180 days during the year.
- (3) ₹ 20,500 paid to M/s Sodhi Transporters, a goods transport operator in cash is deductible while computing business income, since the limit above which disallowance under section 40A(3) would be attracted in case of payment to a transport contractor engaged in the business of plying, leasing goods carriages is ₹ 35,000. Since it is already debited to profit and loss account, no further adjustment is required.
- (4) Contribution to a university approved and notified under section 35(1)(ii) is eligible for a weighted deduction of 175%. Therefore, the contribution of ₹ 1,60,000 debited

to profit and loss account has been added back and ₹ 2,80,000 (being 175% of ₹ 1,60,000) has been deducted while computing business income.

- (5) Loss of ₹ 2,40,000 due to destruction of machinery caused by fire is not deductible since it is capital in nature.
- (6) Non-furnishing of PAN to deductor results in attracting provisions of section 206AA, which require tax to be deducted at a higher rate of 20%. Since the company has not deducted tax at source, disallowance under section 40(a)(ia) would be attracted in respect of payment of ₹ 80,000 made to contractor.
- (7) As per section 94(7), where any person buys any shares within 3 months prior to the record date and sells such shares within 3 months after such date and the dividend received on such shares is exempt, then the loss arising out of such purchase and sale of shares shall be ignored to the extent of dividend income.

|                                                                 | ₹            |
|-----------------------------------------------------------------|--------------|
| Loss on purchase and sale of shares (₹ 100 - ₹ 80) x 800 shares | 16,000       |
| Less: Dividend exempt under section 10(34) [₹ 10 x 800 shares]  | <u>8,000</u> |
| Short-term capital loss                                         | <u>8,000</u> |

Since short term capital loss can be set-off only against income under the head "Capital Gains", the short-term capital loss of ₹ 8,000 has to be carried forward to the next year. Dividend of ₹ 8,000 credited to profit and loss account has to be deducted and short-term capital loss of ₹ 16,000 debited to profit and loss account has to be added back.

- (8) Depreciation as per Income-tax Rules, 1962, is deductible while calculating business income. Therefore, ₹ 1.40 lakh depreciation on tangible fixed assets and ₹ 4 lakh on intangible assets is deducted. The amount of ₹ 80,000 depreciation debited to profit and loss account has been added back.
- (9) Waiver of principal amount of loan taken for trading activity is a benefit in respect of a trading-liability by way of remission or cessation thereof and is, hence, taxable under section 41(1). It has been so held in *Solid Containers v. DCIT (2009) 308 ITR 417 (Bom.)*. Since the loan waiver has already been credited to profit and loss account, no adjustment is required.

Since the loan is for meeting working capital requirement, it is logical to assume that is taken for trading activity.

However, the treatment is different in respect of interest of loan. Since interest on such loan would have not been allowed as deduction in the earlier years as per section 43B due to non-payment of such interest, waiver of interest will not be taxable. Since ₹ 80,000 representing interest waiver has already been credited to profit and loss account, the same has to be deducted for computing business income.

- (10) As per section 2(22)(e), any payment by a company in which the public are not substantially interested by way of loan to a shareholder, who is the beneficial owner of shares holding not less than 10% of voting power, is deemed as dividend to the extent to which the company possesses accumulated profits. Accordingly, in this case, ₹ 40,000 would be deemed as dividend under section 2(22)(e).
3. (a) (1) As per section 10(1), agricultural income is exempt from tax. The meaning and scope of agricultural income is defined in section 2(1A). According to *Explanation 2* to section 2(1A), any income derived from any building from the use of such building for any purpose (including letting for residential purposes or for the purpose of any business or profession) other than agriculture shall not be agricultural income. In this case, the house was occupied for residential purposes. Therefore, the rent of ₹ 60,000 from letting out of houses constructed on agricultural land shall not be treated as agricultural income by virtue of *Explanation 2* to section 2(1A). Hence, such income would be chargeable to tax.
- (2) The entertainment allowance received by the Minister of Surface Transport is taxable under the head "Salaries". However, deduction under section 16(ii) is allowable to the extent of least of the following –
- 1/5<sup>th</sup> of the salary
  - ₹ 5,000
  - Actual entertainment allowance received, i.e., ₹ 24,000 in this case.
- (3) As per section 25AA, unrealised rent would be deemed to be the income chargeable under the head "Income from house property". Accordingly, it would be chargeable to income-tax as income of that previous year in which such rent is realised whether or not the assessee is the owner of that property in that previous year. Therefore, in this case, unrealized rent of ₹ 55,000 would be charged to tax in the P.Y. 2012-13 under the head "Income from house property" even though he is no longer the owner of the house property.
- (b) (i) When a company is converted into LLP fulfilling the conditions laid down in section 47(xiiib), the LLP is eligible for amortization of expense in five equal annual instalments. If the expenditure was incurred in the previous year 2012-13, then 1/5<sup>th</sup> being ₹ 50 lakhs is deductible under section 35DDA in the hands of the LLP.
- (ii) Advertisement in souvenirs of political party is not deductible as per section 37(2B). Donation to registered political parties is eligible for deduction under section 80GGB. Further, the word "contribute" in section 80GGB has the meaning assigned to it in section 293A of the Companies Act, 1956 and accordingly, it includes the amount of expenditure incurred on advertisement in a souvenir of a political party. Therefore, ₹ 5,50,000 incurred on advertisement in a souvenir of a

political party and ₹ 3,00,000 given as a donation to a registered political party is deductible under section 80GGB.

- (iii) Cash payment for purchase of fish products is not attracted by section 40A(3) in view of the relief provided in Rule 6DD. However, the relief will not be available on the payment for the purchase of fish products from a trader, broker or middleman, by whatever name called.
  - (c) (i) Under section 43B, interest on term loans and advances to scheduled banks shall be allowed only in the year of payment of such interest irrespective of the method of accounting followed by the assessee. *Explanation 3D* to section 43B provides that if any interest payable by the assessee is converted into a loan, the interest so converted and not actually paid shall not be deemed as actual payment, and hence would not be allowed as deduction. Therefore the interest of ₹ 2 lakhs converted into loan cannot be claimed as deduction.
  - (ii) According to the *Explanation 5* to Section 32(1), allowance of depreciation is mandatory. Therefore, depreciation has to be provided mandatorily while calculating income from business /profession whether or not the assessee has claimed the same while computing the total income.
4. (a) Section 119(2)(b) empowers the CBDT to authorise any income tax authority to admit an application or claim for any exemption, deduction, refund or **any other relief under the Act** after the expiry of the period specified under the Act, to avoid genuine hardship in any case or class of cases. The claim for carry forward of loss in case of late filing of a return is relatable to a claim arising under the category of “any other relief available under the Act”. Therefore, the CBDT has the power to condone delay in filing of such loss return due to genuine reasons.

The facts of the case are similar to the case of *Lodhi Property Company Ltd. v. Under Secretary, (ITA-II), Department of Revenue (2010) 323 ITR 0441*, where the Delhi High Court held that the Board has the power to condone the delay in case of a return which was filed late and where a claim for carry forward of losses was made. The delay was only one day and the assessee had shown justifiable reason for the delay of one day in filing the return of income. If the delay is not condoned, it would cause genuine hardship to the assessee. Therefore, the Court held that the delay of one day in filing of the return had to be condoned.

Applying the rationale of the above court ruling to the case in hand, the CBDT has the power to condone the delay in filing the return of income of Mr. Harish and permit carry forward of business loss of ₹ 1 lakh, since the delay of one hour was due to a genuine and justifiable reason i.e., network problem while e-filing the return.

- (b) The Delhi High Court, in *Lachman Dass Bhatia Hingwala (P) Ltd. v. ACIT (2011) 330 ITR 243 (Delhi)(FB)* observed that the justification of an order passed by the Tribunal recalling its own order is required to be tested on the basis of the law laid

down by the Apex Court in *Honda Siel Power Products Ltd. v. CIT* (2007) 295 ITR 466, dealing with the Tribunal's power under section 254(2) to recall its own order where prejudice has resulted to a party due to an apparent omission, mistake or error committed by the Tribunal while passing the order. Such recalling of order for correcting an apparent mistake committed by the Tribunal has nothing to do with the doctrine or concept of inherent power of review. It is a well settled provision of law that the Tribunal has no inherent power to review its own judgment or order on merits or reappreciate the correctness of its earlier decision on merits. However, the power to recall has to be distinguished from the power to review. While the Tribunal does not have the inherent power to review its order on merits, it can recall its order for the purpose of correcting a mistake apparent from the record.

When prejudice results from an order attributable to the Tribunal's mistake, error or omission, then, it is the duty of the Tribunal to set it right. The Delhi High Court observed that the Tribunal, while exercising the power of rectification under section 254(2), can recall its order in entirety if it is satisfied that prejudice has resulted to the party which is attributable to the Tribunal's mistake, error or omission and the error committed is apparent.

- (c) This issue was considered by the Delhi High Court in *CIT (TDS) v. ITC Ltd.* (2011) 338 ITR 598.

The Delhi High Court observed that once the tips were paid by the customers either in cash directly to the employees or by way of charge to the credit cards in the bills, the employees gained additional income, which was by virtue of their employment. When the tips were received by the employees directly in cash, the employer hardly had any role and it may not even know the amount of tips collected by the employees. That would be out of the purview of responsibility of the employer under section 192.

However, when the tips were charged to the bill either by way of a fixed percentage on the total bill, or where no percentage was specified, the amount was indicated by the customer on the bill as a tip, the tip went into the receipt of the employer and was subsequently disbursed to the employees. As soon as such amounts were received by the employer, there was an obligation on the part of the employer to disburse them to the rightful persons, namely, the employees. Simultaneously, a right accrued to the employees to claim the tips from the employer. By virtue of the employer-employee relationship, a vested right accrued to the employee to claim the tips. The High Court, therefore, held that the tips would constitute income within the meaning of section 2(24) and are, thus, taxable under section 15. Consequently, it was obligatory upon the company to deduct tax at source from such payments under section 192.

Applying the ratio of the above case, Ashoka Ltd. is liable to deduct tax under section 192 from the tips collected by it directly and disbursed to its employees, by treating the same as salary.

- (d) The issue as to whether exemption under section 54F can be claimed in respect of capital gains arising from sale of a depreciable asset held for more than 36 months came up before the Delhi High Court in *CIT v. Rajiv Shukla (2011) 334 ITR 138*.

In that case, the assessee had claimed benefit of exemption under section 54F in respect of capital gain arising on the sale of property, being a depreciable asset held for more than 36 months. However, the department contended that no exemption under section 54F would be available, as the said exemption is granted in respect of capital gain arising from the transfer of a long-term capital asset whereas the capital gain arising from transfer of a depreciable asset is deemed to be capital gain arising from transfer of short-term capital asset by virtue of provisions of section 50.

The Delhi High Court, relying on the decision of the Bombay High Court in the case of *CIT v. Ace Builders P. Ltd. (2006) 281 ITR 210* and the decision pronounced by Gauhati High Court in *CIT v. Assam Petroleum Industries P. Ltd. [2003] 262 ITR 587*, in relation to erstwhile section 54E, held that the deeming fiction created by section 50 that the capital gain arising on transfer of a depreciable asset shall be treated as capital gain arising on transfer of short-term capital asset is only for the purpose of sections 48 and 49 and not for the purpose of any other section.

In effect, the benefit of indexation as per the second proviso to section 48 would not be available in respect of depreciable assets. Further, the written down value of the block at the beginning of the year, as increased by the actual cost of the asset purchased during the year in that block will be reduced from the net sale consideration for determining the taxable capital gains.

Section 54F, being an independent section, will not be bound by the provisions of section 50. The depreciable asset, if held for more than 36 months, shall be a long-term capital asset as per the provisions of section 2(29A). Therefore, the exemption under section 54F cannot be denied on account of the fiction created by section 50, if the depreciable asset which is transferred is held for more than 36 months and the net consideration is invested in purchase of a new residential house.

Applying the above rationale of the Delhi High Court ruling to this case, Mr. Rajiv can invest the net consideration on sale of building for purchasing a new residential house and claiming exemption under section 54F, since the building is held for more than 36 months. Thus, we can conclude that the contention of the Assessing Officer is not correct.

5. (a) Section 139(5) stipulates that when a return is furnished under section 139(1) or in response to notice issued under section 142(1), and later on, the assessee

discovers any omission or wrong statement therein, he may furnish a revised return at any time before the expiry of one year from the end of the relevant assessment year or before the completion of the assessment, whichever is earlier.

Though the return is a belated return filed in December 2013, since the return was filed in response to a notice issued under section 142(1), the assessee can file a revised return before the expiry of one year from the end of the relevant assessment year i.e. by 31<sup>st</sup> March, 2015

As the revised return is contemplated in January, 2014, he could do so.

- (b) The proviso to section 92C(2) provides that where more than one price is determined by the most appropriate method, the arm's length price (ALP) shall be taken to be the arithmetical mean of such prices.

However, if the arithmetical mean, so determined, is within such percentage of the transfer price as notified by the Central Government, then, the transfer price shall be deemed to be the arm's length price and no adjustment is required to be made.

The arithmetical mean of the prices =  $(₹ 96 + ₹ 112) / 2 = ₹ 104$  lacs.

The rate of permissible variation prescribed by the Central Government is 2% i.e. ₹ 2 lacs ( $₹ 100 \text{ lacs} \times 2\%$ ).

Since the variation between the arm's length price of ₹ 104 lacs and the transfer price of ₹ 100 lacs is not within the limit of 2% of TP (i.e., ₹ 2 lacs), the arm's length price shall be ₹ 104 lacs.

The Assessing Officer may compute the total income of the Indian company having regard to the arm's length price of ₹ 104 lacs so determined. No deduction shall be allowed under Chapter VI-A or section 10AA in respect of ₹ 4 lacs, being the amount of income by which the total income of the Indian company is enhanced after application of the arm's length price of ₹ 104 lacs.

- (c) Section 90(2) makes it clear that where the Central Government has entered into a Double Taxation Avoidance Agreement with a country outside India, then **in respect of an assessee to whom such agreement applies, the provisions of the Act shall apply to the extent they are more beneficial to the assessee.** This means that where tax liability is imposed by the Act, the Double Taxation Avoidance Agreement may be resorted to for reducing or avoiding the tax liability.

However, as per section 90(4) inserted by Finance Act, 2012, the assessee, in order to claim relief under the agreement, has to obtain a certificate [Tax Residence Certificate (TRC)] from the Government of that country containing such particulars as may be prescribed, declaring the residence of the country outside India. The submission of TRC containing the prescribed particulars shall be necessary but not a sufficient condition for availing benefits of the agreement. In effect, further conditions can be stipulated for claiming treaty benefits in addition to the requirement of submission of the TRC.

The Supreme Court has held, in *CIT v. P.V.A.L. Kulandagan Chettiar* (2004) 267 ITR 654, that in case of any conflict between the provisions of the Double Taxation Avoidance Agreement and the Income-tax Act, 1961, the provisions of the Double Taxation Avoidance Agreement would prevail over those of the Income-tax Act. X is, therefore, not liable to pay tax on the income earned by him provided he submits the Tax Residence Certificate obtained from the government of the other country and fulfills such other conditions as may be prescribed for claiming the treaty benefits.

- (d) In this case, tax is deductible@10% under section 194J in respect of fees for professional services. Since there has been a delay in deduction and deposit of tax, interest under section 201(1A) is attracted.

As per the provisions of section 201(1A), if a person who is liable to deduct tax at source fails to deduct tax at source or after deducting such tax, fails to pay the tax as required by the Act, then he is liable to pay interest as follows -

- (i) 1% for every month or part of month on the amount of such tax from the date on which such tax was deductible to the date on which such tax is actually deducted.
- (ii) 1½% for every month or part of month on the amount of such tax from the date on which such tax was deducted to the date on which tax is actually paid.

Therefore, in the given case, interest under section 201(1A) would be computed as follows –

|                                                                         | ₹            |
|-------------------------------------------------------------------------|--------------|
| 1% on tax deductible but not deducted i.e., 1% on ₹ 9,000 for 8 months  | 720          |
| 1½% on tax deducted but not deposited i.e. 1½% on ₹ 19,500 for 4 months | 1,170        |
| <b>Total interest payable under section 201(1A)</b>                     | <b>1,890</b> |

6. (a) (i) Penalty under section 271C is attracted for failure to deduct tax at source. The penalty would be a sum equal to the amount of tax which such person has failed to deduct. Such penalty can be imposed only by the Joint Commissioner. Therefore, ABC Ltd. shall be liable for penalty under section 271C equal to the amount of tax which they have failed to deduct under section 194C from the payments made to the contractors.
- (ii) Section 133(6) empowers the Income-tax authority to require any person to furnish information in relation to such points or matters which will be useful for or relevant to any enquiry or proceeding under the Act. Failure on the part of an assessee to furnish the information in relation to such points or matters as required, makes him liable for penalty under section 272A(2) of ₹ 100 for every day during which the failure continues.

**Note** – In a case where no proceeding is pending, the Income-tax authority can exercise this power only after obtaining the approval of the Director or Commissioner, as the case may be. In this case, it is presumed that the Income-tax authority has obtained the approval of the Director or Commissioner before exercising this power.

- (b) Clause (b) of section 245A has restricted the cases eligible to appear before the Settlement Commission. The term 'case' would mean any proceeding for assessment under the Act of any person in respect of any assessment year or years which is pending before the Assessing Officer and which alone shall be eligible for settlement by the settlement commission.

The following shall, however, not be a proceeding for the purpose of filing an application under section 245C -

- (i) a proceeding for assessment or reassessment or re-computation under section 147;
- (ii) a proceeding for making fresh assessment in pursuance of an order under section 254 or section 263 or section 264 setting aside or cancelling an assessment.

Therefore, search cases are eligible for settlement through the Settlement Commission. A proceeding shall be deemed to have been commenced on the date of issue of notice initiating assessment under section 153A or section 153C and would get concluded on the date on which the assessment is made. During this period, application for settlement of the case could be filed by the assessee. The monetary limit prescribed in respect of additional amount of income-tax payable is also be kept in mind in view of proviso to section 245C(1).

**(c) Computation of "Income from other sources" of Mr. Suresh for the A.Y.2013-14**

|     | Particulars                                                                                                                                                                                                                         | ₹               |
|-----|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|
| (1) | Cash gift received on 31.08.2012 is taxable under section 56(2)(vii)                                                                                                                                                                | 60,000          |
| (2) | Fair market value of shares of Beta Ltd. is taxable                                                                                                                                                                                 | 1,20,000        |
| (3) | Purchase of land for inadequate consideration on 5.01.2013 would not attract the provisions of section 56(2)(vii), since there is a consideration and <b>only where the consideration is fully absent, it is chargeable to tax.</b> | Nil             |
|     | <b>Income from other sources</b>                                                                                                                                                                                                    | <b>1,80,000</b> |

**Computation of "Capital Gains" of Mr. Suresh for the A.Y.2013-14**

| Particulars                                                           | ₹        |
|-----------------------------------------------------------------------|----------|
| Sale Consideration (07.03.2013)                                       | 1,50,000 |
| Less: Cost of acquisition [deemed to be the fair market value charged |          |

|                                  |               |
|----------------------------------|---------------|
| to tax under section 56(2)(vii)] | 1,20,000      |
| <b>Short-term capital gains</b>  | <b>30,000</b> |

- (d) In the case of a company which is wound up, the tax due will have to be recovered only from the liquidator of the company. The liquidator is debarred from parting with the assets of the company until it is notified by the Assessing Officer of the amount which will be sufficient to provide for any tax which is then payable by the company.

In the case of private company, which is wound up, the directors of the company are jointly and severally liable for the payment of tax.

Where a private company is converted into a public company and the tax assessed in respect of any previous year during which such company was a private company cannot be recovered, such tax is recoverable from every person who was a director of the private company at any time during the relevant previous year. The liability of a director is joint and several unless he proves that non recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the company.

**7. (a) Computation of total income of Mr. Jatin for the Assessment Year 2013-14**

| Particulars                                                                                                                                                     | ₹        | ₹               |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------|----------|-----------------|
| <b>Salaries</b>                                                                                                                                                 |          |                 |
| Gross salary received                                                                                                                                           | 3,60,000 |                 |
| Add: Shares allotted at concessional price – fair market value less the amount recovered from the employee [Section 17(2)(vi)] (i.e. ₹ 1,20,000 minus ₹ 24,000) | 96,000   |                 |
|                                                                                                                                                                 | 4,56,000 |                 |
| Less: Conveyance allowance exempt under section 10(14)                                                                                                          | 36,000   | 4,20,000        |
| <b>Capital gains</b>                                                                                                                                            |          |                 |
| Sale consideration of equity shares sold on 2.03.2013                                                                                                           | 2,16,000 |                 |
| Less: Fair Market Value of shares on the date of exercise of option ( i.e., 4.06.2012)                                                                          | 1,20,000 | 96,000          |
| <b>Gross Total Income</b>                                                                                                                                       |          | <b>5,16,000</b> |
| <b>Less: Deduction under Chapter VIA</b>                                                                                                                        |          |                 |
| <b>Under section 80C</b>                                                                                                                                        |          |                 |
| For investment in notified bonds of NABARD                                                                                                                      | 48,000   |                 |
| <b>Under section 80CCD</b>                                                                                                                                      |          |                 |
| For deposit in pension scheme notified by Central Government [₹ 36,000 but restricted to 10% of salary i.e. 10% of ₹ 3,24,000]                                  | 32,400   |                 |

|                                                                               |        |                 |
|-------------------------------------------------------------------------------|--------|-----------------|
| <b>Under section 80D</b>                                                      |        |                 |
| For payment of health insurance premium by credit card                        | 10,800 |                 |
| <b>Under section 80E</b>                                                      |        |                 |
| For payment of interest on loan taken from bank for higher studies of his son | 72,000 | 1,63,200        |
| <b>Total Income</b>                                                           |        | <b>3,52,800</b> |

**Notes:**

- (i) Conveyance allowance received for official duties is fully exempt under section 10(14).
- (ii) Section 80CCD provides for deduction of employee's and employer's contribution to pension scheme notified by the Central Government. This deduction has also been extended to individuals employed by any other employer on or after 1.1.2004. However, if the amount contributed exceeds 10% of salary, then, the deduction would be restricted to 10% of salary. [As per *Explanation* to section 80CCD, salary for this purpose would include dearness allowance if the terms of employment so provide, but excludes all other allowances and perquisites]. Therefore, "salary" for the purpose of section 80CCD would be ₹ 3,24,000 (₹ 3,60,000 – ₹ 36,000).
- (iii) The deduction under section 80E available to an individual in respect of interest on loan taken for his higher education has been extended to include interest on such loan taken for higher education of his relative i.e. his or her spouse and children. Hence, interest on loan taken by Mr. Jatin from bank for the higher studies of his son is eligible for deduction under section 80E.
- (iv) For claiming deduction under section 80D, the payment of medical insurance premium has to be made by any mode other than cash. Hence, payment of ₹ 10,200 made in cash will not qualify for deduction under section 80D.
- (v) Subscription to notified bonds issued by NABARD will qualify for deduction under section 80C(2)(xxii).
- (vi) The value of any specified security or sweat equity shares allotted or transferred by the employer, free of cost or at a concessional rate to the employee would be treated as a perquisite in the hands of the employee. The value would be the fair market value of the specified security or sweat equity shares on the date on which the option is exercised by the employee as reduced by the amount actually paid by, or recovered from the employee in respect of such securities or shares.

Consequently, section 49(2AA) provides that for the purpose of computing capital gains in the hands of the employee at the time of sale of such

securities/shares by the employee, the cost of acquisition shall be the fair market value which has been taken into account for the purpose of computing the perquisite value in the hands of the employee.

- (b) (i) Under section 64(1)(iv), where any asset is transferred directly or indirectly to the spouse by an individual, otherwise than for adequate consideration or in connection with an agreement to live apart, the income arising therefrom is included in the hands of the transferor. The term "income" in this context includes "loss" as well. Therefore, the loss sustained by Mrs. Verma in the business carried on by her with gifted funds by her husband can be set off by her husband.
- (ii) Section 78(2) stipulates that where any person carrying on any business or profession is succeeded in such capacity by another person otherwise than by inheritance, no person other than the person incurring the loss is entitled to carry forward the loss and set off against his income.

The facts of the case seem to indicate that Mrs. Radha has succeeded to the business by inheritance and is not affected by the provisions of section 78(2). Therefore she is eligible to carry forward and set off the loss of her husband against her own income. Succession by inheritance is an exception to the general bar against carry forward and set off of losses contained in section 78(2).