# CA-PCC NOV 2008

**Answer All Questions**
**Wherever required, suitable assumptions may be made by the candidate and stated clearly in the answer. Working notes should form part of the answer**

**Q1.** State with reason, any five sub-divisions, whether the following statements are true or false with regard to the provisions of the Income-tax Act, 1961 for the AY 2008-2009.

**(5 x 2 = 10 marks)**

**(a)** Compensation on account of disaster received from local authority by an individual or his/her legal heir is taxable.
**(b)** Filing belated return u/s 139(4) of the Income-tax Act, 1961 will debar an assessee from claiming deduction u/s 80ID or 80IE of the Act
**(c)** Rural branches of the cooperative banks are not allowed to claim provision for bad and doubtful debts
**(d)** Income to a non-resident by way of interest, royalty and fee for technical services deemed to accrue or arise in India is taxable in India irrespective of territorial nexus.
**(e)** Depreciation is allowed only when it is claimed.
**(f)** Capital gain of Rs. 75 lakh arising from transfer of long term capital assets will be exempt from tax if such capital gain is invested in the bonds redeemable after three years, issued by NHAI u/s 54EC of the Act.

**Solution:**
**Q1 (a): FALSE**
**As per section 10(10BC) introduced w.e.f AY 2008-2009,** compensation received or receivable by an individual or his legal heir on account of disaster from central government, state government or local authority is exempt from tax. However if the loss due to disaster has been claimed as deduction while calculating PGBP income then such compensation shall not be exempt.

**Q1 (b): TRUE.**
As per section 80AC to claim deduction under section 80ID and 80IE the assessee has to file income tax return as per the time period mentioned under section 139(1). If the assessee could not file the income tax return till the due date then the benefit of filling belated income tax return under section 139(4) shall not be available.

**Q1 (c): FALSE.**
As per section 36(1) In case of co-operative banks other than primary agricultural credit society or a primary co-operative agricultural deduction for the provision of bad debts is allowed. For this limits are 7.5% of the gross total income, but in case of rural branches limit is 10% of the aggregate average advances made.

**Q1 (d): TRUE.**
**WEF Assessment year 2008-2009** incomes such as Interest income under Section 9(1)(v), Royalty income under Section 9(1)(vi) and Income of Technical Fee under Section 9(1)(vii) if are deemed

to accrue or arise in India, then such incomes shall be included in the total income of a non-resident, whether or not the non-resident has a residence or place of business or business connection in India.

**For Example:** Interest payable by the government shall be deemed to accrue or arise in India even is a non resident recipient has no connection (residence/place of business/business connection) with India.

This amendment nullifies the decision of **Supreme Court in the case of Ishika Wajima-Harima Heavy Industries Ltd. V DIT given in 2007,** where it was held that deeming provision comes into play when there is sufficient nexus between income and territory of India.

**Q 1(e) FALSE.**
WEF AY 2002-2003 to claim depreciation has been made mandatory. So depreciation has to be deducted while calculating PGBP income even if assessee is maintaining books on the cash basis of accounting. If assessee has not claimed depreciation then assessing officer will have to calculate and allow the depreciation to the assessee.

**Q 1(f) FALSE.**
The investment in the bonds should not exceed Rs. 50 lakhs w.e.f 1/4/2007. Further, investment can be made in any bonds which are redeemable after the period of 3 years and which have been issued on or after 1/4/2007 by NHAI or RECI.

**Q2.** Dr. Smt. Niranjana, a resident individual, aged 60 years is running a clinic. Her Income and Expenditure Account for the year ending 31/3/2008 is as under: **(20 marks)**

| **Expenditure** | **Amount in Rs.** | **Income** | **Amount in Rs.** |
|---|---|---|---|
| To Medicines consumed | 538400 | By Consultation and medical charges | 1885850 |
| To Staff salary | 380000 | By Income-tax refund (principal 5000 interest 450) | 5450 |
| To Clinic consumables | 110000 | By Dividend from units of UTI | 10500 |
| To Rent paid | 90000 | By Winning from game show on TV net of TDS (TDS 16830) | 33170 |
| To Administrative expenses | 255000 | By Rent | 27000 |
| To amount paid to scientific research association approved u/s 35 | 150000 | | |
| To Net profit | 438570 | | |
| **Total** | 1961970 | **Total** | 1961970 |

Additional information if given to you:
**(a)** Rent paid includes Rs. 30,000 paid by cheque towards rent for her residential house.
**(b)** Clinic equipments are:

| | | |
|---|---|---|
| 1/4/2007 | Opening W.D,V | Rs. 5,00,000 |
| 7/12/2007 | Acquired cost | Rs. 2,00,000 |

**(c)** Rent received relates to a property situated at Surat. Gross annual value Rs. 27,000. The municipal tax of Rs. 2,000 paid in December 2007 has been included in "administrative expenses".

**(d)** She received salary Rs. 7,500 p.m. from "Full Care Hospital" which has not been included in the "consultation and medical charges".

**(e)** Dr. Niranjana availed loan of Rs. 5,50,000 from a bank for higher education of her daughter. She repaid principal of Rs. 1,00,000 and interest thereon Rs. 55,000 during the year PY 2007-2008.

**(f)** She paid Rs. 1,00,000 as tuition fee (not in the nature of development fees / donation) to the university for full time education of her daughter.

**(g)** An amount of Rs. 18,000 has also been paid by cheque on 27th March 2008 for her medical insurance premium.

From the above compute the total income and tax payable thereon by Dr. Smt. Niranjana for the AY 2008-2009.

**Solution: Calculation of PGBP income of Dr. Smt. Niranjana for the AY 2008-2009.**

| | | |
|---|---|---|
| **Net profits** | | 438570 |
| **ADD:** | | |
| Rent paid for own residential house | 30000 | |
| Municipal taxes included in administrative expenses | 2000 | 32000 |
| **LESS:** | | |
| Deduction for the sum paid to scientific research association is 125% of sum donated. (125% of 150000 – 150000) | 37500 | |
| Income tax refund | 5450 | |
| Dividends from UTI | 10500 | |
| Winnings from game shows | 33170 | |
| Rent received | 27000 | |
| Depreciation under section 32 for assets<br>500000 X 15% = 75000<br>200000 X 15% / 2 = 15000 | 90000 | 203620 |
| **PGBP income** | | 266950 |

**Calculation of house property income of Dr. Smt. Niranjana for the AY 2008-2009.**

| | |
|---|---|
| Actual rent received | 27000 |
| Gross annual value of the property | 27000 |
| Less: Municipal taxes paid by the landlord on or before 31/3/2008 | 2000 |
| Net annual value of the property | 25000 |
| Less: statutory deduction under section 24(a) | 7500 |
| Less: interest on the borrowed capital under section 24(b) | NIL |
| Taxable house property income | 17500 |

**Calculation of other sources of Dr. Smt. Niranjana for the AY 2008-2009.**

| | |
|---|---|
| Interest on the income tax refund | 450 |
| Dividends income from UTI | Exempt from tax under section 10(35) |
| Winnings from game shows | 50000 |

| | |
|---|---|
| Taxable income from other sources | 50450 |

**Calculation of total income of Dr. Smt. Niranjana for the AY 2008-2009.**

| | |
|---|---|
| Income under the head salary | 90000 |
| Income under the head house property | 17500 |
| Income under the head business and profession | 266950 |
| Income under the head capital gains | NIL |
| Income under the head other sources | 50450 |
| Gross total income | 424900 |
| Less: Deductions under section | |
| Section 80C (Education expenses for full time education) | 100000 |
| Section 80E (interest on the higher education loan of family member) | 55000 |
| Section 80D (medical insurance premium) | 15000 |
| Section 80GG***: Deduction for rent paid is least of<br>(i) Rent paid in excess of 10% of Adjusted Gross Total Income = 4510<br>(ii) 25% of the Adjusted Gross Total Income = 63725<br>(iii) 2,000 per month. = 24000 | 4510 |
| Taxable income rounded off under section 288A | 250390 |

**Note***:** We have assumed that Dr. Smt. Niranjana is not paying rent for the residential accommodation in the city of Surat, where she has a let out house.

**Calculation of Adjusted Gross Total Income**

| | |
|---|---|
| GTI | 424900 |
| Less: all deduction except Section 80GG | |
| Section 80C | 100000 |
| Section 80E | 55000 |
| Section 80D | 15000 |
| AGTI | 254900 |

**Calculation of tax liability of Dr. Smt. Niranjana for the AY 2008-2009.**

| | | |
|---|---|---|
| Total income | | 250390 |
| Tax on winnings from lottery | 50000 X 30% | 15000 |
| Tax on the normal incomes at slab rate | First 145000<br>Next upto 5000 @ 10%<br>Next upto 100000 @ 20% = 50390 X 20% | nil<br>500<br>10078 |
| Total Income Tax | | 25578 |
| Add: Surcharge | | NIL |
| Income tax plus surcharge | | 25578 |
| Add: Primary education cess | 2% of 25578 | 511.56 |
| Add: secondary and higher education cess | 1% of 25578 | 255.78 |
| Income tax | | 26345.34 |
| Less: TDS on winnings from game shows u/s 194B | | 16830 |
| Tax payable under section 288B | | 9520 |

**Q 3. (a)** Mr. M is an area manager of M/S N. Steels Co. Ltd. During the PY 2007-2008 he gets following emoluments from his employer: **(Marks 6)**

| | |
|---|---|
| Basic salary<br>Upto 31/8/2007<br>From 1/9/2007 | <br>Rs. 20,000 p.m.<br>Rs. 25,000 p.m. |
| Transport Allowance | Rs. 2,000 p.m. |
| Contribution to recognized provident fund | 15% of basis salary and D.A. |
| Children education allowance | Rs. 500 p.m. for two children |
| City Compensatory Allowance | Rs. 300 p.m. |
| Hostel expenses allowance | Rs. 380 p.m. for two children |
| Tiffin allowance (actual expenses 3,700) | Rs. 5,000 p.a. |
| Tax paid on employment | Rs. 2,500 |

Compute taxable salary of Mr. M for the AY 2008-2009.

**Solution:** **Calculation of income from salary of Mr. M for the PY 2007-2008**

| | | | |
|---|---|---|---|
| Basic salary<br>Upto 31/8/2007<br>From 1/9/2007 | <br>20,000 X 5<br>25,000 X 7 | <br>100000<br>175000 | <br><br>275000 |
| Transport Allowance<br>Less: Exempt | 2,000 X 12<br>800 X 12 | 24000<br>9600 | <br>14400 |
| Contribution to RPF | 15% X 275000<br>Less: Exempt 12% X 275000 | 41250<br><br>33000 | <br><br>8250 |
| Children education allowance | 500 X 12<br>Less: Exempt: 100 X 12 X 2 | 6000<br>2400 | <br>3600 |
| City Compensatory Allowance | 300 X 12 | | 3600 |
| Hostel expenses allowance | 380 X 12<br>Less: exempt: 190 X 2 X 12 | 4560<br>4560 | <br>NIL |
| Tiffin allowance | | | 5000 |
| Tax paid on employment | | | 2500 |
| Gross salary | | | 312350 |
| Less: Deductions u/s 16 (iii) | | | 2500 |
| Taxable Salary | | | 309850 |

**(b)** Mr. X owns one residential house in Mumbai. The house is having two units. First unit of the house is self-occupied by Mr. X and another unit is rented for 8,000 p.m. The rented unit was vacant for 2 months during the year. The particulars of house for the PY 2007-2008 are as under: **(Marks 9)**

| | |
|---|---|
| Standard rent | Rs. 162000 p.a. |
| Municipal valuation | Rs. 190000 p.a. |
| Fair rent | Rs. 185000 p.a. |

| | |
|---|---|
| Municipal tax | 15% of municipal value |
| Light and water charges | Rs. 500 pm |
| Interest on borrowed capital | Rs. 1500 pm |
| Lease money | Rs. 1200 pa |
| Insurance charges | Rs. 3000 pa |
| Repairs | Rs. 12000 pa |

Compute the income from house property of Mr. X for the AY 2008-2009.

**Solution:** **Calculation of income from house property for Mr. X**

| **Nature of the property** | **50% is SO** | **50% is LO** |
|---|---|---|
| Municipal valuation | 95000 | 95000 |
| Fair rent | 92500 | 92500 |
| Standard rent | 81000 | 81000 |
| Expected rent | 81000 | 81000 |
| Less: Loss of rent due to vacancy | Nil | 16000 |
| | 81000 | 65000 |
| Actual rent | Nil | 80000 |
| Gross annual value of the property | Nil | 80000 |
| Less: Municipal taxes | Nil | 14250<br>(assumed to be paid in the PY) |
| Net annual value of the property | Nil | 65750 |
| Less: statutory deduction under section 24(a) | Nil | 19725 |
| Less: interest on the borrowed capital under section 24(b) | 9000 | 9000 |
| Taxable house property income | (9000) | 37025 |
| Net house property income after adjustment of loss | | 28025 |

**Q 4 (a)** Mr. P is a resident individual and furnishes you the following particulars of his and other details for the PY 2007-2008: **(6 marks)**

| | |
|---|---|
| Income from salary | Rs. 18000 |
| Net annual value taxable under the income from house property | Rs. 70000 |
| Income from business | Rs. 80000 |
| Income from speculation business | Rs. 12000 |
| LTCG on sale of land | Rs. 15800 |
| Loss on the maintaince of race horse | Rs. 9000 |
| Loss on the gambling | Rs. 8000 |
| Depreciation allowable under the act comes out to 8000 for which no treatment has been given above.<br>The other details of unabsorbed depreciation and brought forward losses are: | |
| Unabsorbed depreciation | Rs. 9000 |
| Loss from speculation business | Rs. 16000 |
| Short term capital loss | Rs. 7800 |
| Unrealized rent | Rs. 17000 |

Compute the GTI of Mr. P for the AY 2008-2009 and the amount of loss that can or can't be carried forward.

**Solution:** **Calculation of GTI of Mr. P for the AY 2008-2009**

| | | | |
|---|---|---|---|
| Income from salary | | | 18000 |
| Income from house property<br>NAV<br>Less: statutory deduction u/s 24(a) | <br>70000<br>21000 | | <br><br>49000 |
| Income from PGBP<br>Normal business<br>Less: depreciation for current year<br>Less: BF depreciation<br><br>Speculation business<br>Less: BF loss of speculation business | <br>80000<br>8000<br>9000<br><br>12000<br>12000 | <br><br><br>63000<br><br><br>NIL | <br><br><br><br><br><br>63000 |
| LTCG on sale of land<br>Less: BF STCG | 15800<br>7800 | | <br>8000 |
| **Gross total income** | | | **138000** |

**NOTES:**

**1.** BF loss of speculation business of Rs. 4000 shall be carry forwarded to the next financial year.
**2.** Loss on the maintaince of race horses of Rs. 9000 shall be carry forwarded to the next financial year.
**3.** Loss on the gambling activities shall be ignored for the purposes of total income.

**Q 4 (b)** Mr. Prasad is a karta of a HUF. The family declares GTI of Rs. 400000 for the AY 2008-2009. The GTI includes taxable LTCG of Rs. 65000 and STCG of Rs. 35000 which is taxable under section 111A. The details of HUF funds investment made during the PY 2007-2008 are as follows: **(8 marks)**

| | |
|---|---|
| Amount deposited in PPF in the name of members of HUF | Rs. 10000 |
| Medical insurance premium paid by cheque<br>**(a)** in the name of the karta<br>**(b)** in the personal name of Mr. Prasad | <br>Rs. 4000<br>Rs. 5000 |
| Contributions made to:<br>**(a)** Indra Gandhi Memorial Trust<br>**(b)** Delhi university (declared as an institution of national eminence)<br>**(c)** Zila saksharta samiti<br>**(d)** An approved charitable institution<br>**(e)** Government for the promotion of family planning.<br>**(f)** Hunuman temple in the local mohalla | <br>Rs. 7000<br>Rs. 3000<br>Rs. 5000<br>Rs. 30000<br>Rs. 10000<br>Rs. 20000 |

Compute the total income of HUF which is chargeable to tax for the AY 2008-2009.

**Solution:** **Calculation of the total income of HUF for the AY 2008-2009**

| | |
|---|---|
| LTCG income | 65000 |
| STCG income on sale of listed equity shares | 35000 |
| Other income | 300000 |
| Gross total income | 400000 |
| Less: Deduction under section 80C (deposit in the name of member of HUF) | 10000 |
| Less: Deduction under section 80D (medical insurance premium paid by cheque in the name of karta) | 4000 |
| Less: Deduction under section 80G | 30800 |
| Total income of HUF | 355200 |

**Calculation of deduction under section 80G**

| **Category** | **Donation to** | **Amount donated** | **Amount qualifying u/s 80G** |
|---|---|---|---|
| A: 100% of amt donated | Delhi university<br>Zila saksharta samiti | 3000<br>5000 | **8000** |
| B: 50% of amt donated | Indra Gandhi Memorial Trust | 7000 | **3500** |
| C: 100% of amt donated, within a limit | Government for the promotion of family planning. | 10000 | **10000**<br>(100% of 10000 or 28600 whichever is lower) |
| D: 50% of amt donated, within a limit | An approved charitable institution | 30000 | **9300**<br>(50% of 30000 or 18600 whichever is lower)<br><br>(28600-10000 = 18600) |
| Total deduction u/s 80G | | | **30800** |

**Limit for the deduction in category C and D is 10% of AGTI**

| | |
|---|---|
| Gross total income | 400000 |
| Less: LTCG income | 65000 |
| Less: STCG income on sale of listed equity shares | 35000 |
| Less: deduction u/s 80C | 10000 |
| Less: Deduction u/s 80D | 4000 |
| AGTI | 286000 |
| 10% of AGTI | 28600 |

**Q 5** Answer any four of the following five subdivisions with the regard to the provisions of the income tax act 1961 **(4 X 4 = 16 marks)**

**(a)** Mrs. X an individual resident woman wanted to know whether Income tax is attracted on the sale of gold and jewellery gifted to her by her parents at the occasion of her marriage in the year 1979 which was purchased at a total cost of Rs. 200000.

**(b)** Can an assessing officer make a request for the withdrawal of approval which has been granted to an institution by a National Committee for carrying out eligible project or scheme, eligible u/s 35AC of the income tax act 1961?

**(c)** Explain the concept of marginal relief under the income tax act 1961.

**(d)** Briefly explain the provisions of section 80U of the income tax act 1961 in respect of deduction available on permanent physical disability.

**(e)** Explain with brief reasons whether the return of income can be revised u/s 139(5) of the income tax act 1961 in the following cases:

1) defective or incomplete return which has been filed u/s 139(9)
2) belated return which has been filed u/s 139(4)
3) return which has already been revised once u/s 139(5)
4) return of loss which has been filed u/s 139(3)

**Solution:**

**Q 5 (a)** Yes, Mrs. X is liable to LTCG on the sale of gold and jewellery which has been gifted to her by her parents. For the purposes of calculation of LTCG:

**1.** Cost of acquisition shall be taken as higher of actual cost to previous owner i.e. Rs. 200000 or FMV as on 1/4/1981.
**2.** Cost inflation index shall be taken as 100 and 551
**3.** Period of holding is more than 36 months so asset is LTCA

**Q 5 (b)** No assessing officer can not make a request for the withdrawal of approval. Approval can be withdrawn if project or scheme of such approved association, institution etc.

(1) Is not being carried on in accordance with conditions of its approval; or
(2) A report in respect of such project or scheme has not been furnished after the end of each financial year in prescribed form then the National Committee may withdraw the approval of such association.

**Q 5 (c) MARGINAL RELIEF**

Surcharge is imposed on individuals if their total income is more than Rs. 10 lakhs. Sometimes additional tax including surcharge but before education cess on the total income exceeding Rs. 10 lakhs will be more than the difference between the total income and Rs. 10 lakhs. In such a case marginal relief will be provided which will be equal to increase in tax less increase in Income. For the AY 2008-2009 Marginal Relief would be applicable in respect of the taxpayers whose total income falls in the following range.

| **Assessee** | **AY 2008-2009** |
|---|---|
| Resident Women who is less than 65 years of age | Rs. 1,000,000-- Rs. 10,36,640 |
| Resident Senior citizen | Rs. 10,00,000-- Rs. 10,35,220 |
| Any other individual or any HUF/AOP/BOI | Rs. 10,00,000-- Rs. 10,37,160 |
| Partnership Firms and domestic companies | Rs. 10447760. |
| Foreign companies | Rs. 10169490 |

These income ranges will remain valid only if there is no rebate under section 88E and the taxpayer does not have any income which is chargeable to tax at special rates. (e.g. Long term capital gains, lottery income etc.)

**EXAMPLE:** Total income of Mr. J being a resident of India is Rs. 10,51,000. He has donated Rs. 11000 to PMNRF and has deposited Rs. 20000 in PPF account. Calculate his total income, tax liability after marginal relief for the AY 2008-2009.

**CALCULATION OF MARGINAL RELIEF**

| | |
|---|---|
| Tax if total income would have been Rs. 1000000 | 249000 |
| Tax when total income is Rs. 1020000 | 280500 |
| Increase in Tax is | 31500 |
| Increase in total income is | 20000 |
| Difference of incremental total income and incremental tax | 11500 |

**CALCULATION OF TOTAL INCOME AND TAX LIABILITY FOR THE AY 2008-2009**

| | |
|---|---|
| Gross Total Income | 1051000 |
| Less: deduction under section 80C | 20000 |
| Less: deduction under section 80G | 11000 |
| Total Income | 1020000 |
| Tax on this total income | 255000 |
| Add: Surcharge @ 10% | 25500 |
| Tax payable | 280500 |
| Less: Marginal relief | 11500 |
| Tax payable<br>Add: Education cess<br>@ 2% for primary education<br>@ 1% for higher and secondary education | 269000<br><br>5380<br>2690 |
| Tax liability payable to government | 277070 |

**Q 5 (d): DEDUCTION ALLOWED TO PHYSICALLY HANDICAPPED: SECTION 80U**

**a)** The assessee claiming the deduction should be an Individual (can be Indian or a foreign national) being a resident and a person with a disability.

**b)** The disability should be more then 40%.

**c)** Deduction shall be given only when he could satisfy the assessing officer that the disability has the effect of reducing considerably his capacity to do normal work or engaging in gainful employment or occupation.

**d)** He is certified by a medical authority to be a person with the disability at any time during the PY and this certificate has to be furnished along with the ROI. Further this certificate has to be furnished every year in which this deduction is claimed.

**e)** The amount of deduction shall be Rs.50000 in case of a person with a disability and Rs.75000 in case of a person with a severe disability (having disability of over 80%).

**f)** Meaning of disability under this section is Blindness, Low vision, Leprosy-cured---meaning person who has been cured of leprosy but is suffering from loss of sensation in feet or hands, Hearing impairment, Locomotors disability---means disability of bones, joints or muscles leading to substantial restriction of the movement of the limbs.

**Q 5 (e): Solution:**

1. No, defective return of section 139(9) can not be revised until the defects have been removed. If the assessing officer considers that return is defective he may give an assessee an opportunity to rectify the defect within 15 days of receipt of intimation. If the defect is not rectified within the time allowed assessing officer might treat the return as invalid and such return can not be revised.
2. No, belated return can't be revised as was decided by Supreme Court in case of **KUMAR JAGDISH CHANDRA SINHA.** The return filed under section 139(1) or section 142(1) can only be revised and not the return submitted under section 139(4).
3. Yes, the revised return can also be revised under section 139(5). . ROI can be revised
   **i)** Before the end of one year from the end of the relevant assessment year OR
   **ii)** Before the completion of assessment **whichever is earlier.**
4. Yes it can be and as many number of times as one desires but if done within the time limit specified. ROI can be revised
   **i)** Before the end of one year from the end of the relevant assessment year OR
   **ii)** Before the completion of assessment **whichever is earlier.**

**Q 6** Answer any five of the following: **(2 X 5 = 10 marks)**

**(a)** Can we say that levy of VAT will have effect on the retail price of goods?
**(b)** Explain as to how and when the amendments made in the finance bill in respect of the service tax matters come into the force.
**(c)** Who is responsible to pay service tax when the recipient of sponsorship services is located outside India.
**(d)** Whether free service after the sale of motor vehicle given by the authorized dealer for which they are reimbursed by the vehicle manufacturer are subject to the service tax.
**(e)** Who is liable to pay E-payment of service tax
**(f)** Whether life insurer carrying on the life insurance business has option to calculate service tax at some different rate?

**Q 6: Solution:**

**a)** No, VAT does not affect the retail price. Under the old system of sales tax , a single point sales tax was charged on the last sale transaction but under the system of VAT the amount of sales tax gets distributed over all dealers in the chain. Since the amount collected by the state government remains the same so we can say that VAT does not reduces retail price. This can be explained with the help of the following example:
A manufacturer sells good to wholesaler for Rs. 200. Wholesales adds profit margin of Rs. 300 and sells it to the retailer. Retailer adds profit margin of Rs. 500 and the sells the product for Rs. 1000 to a customer. Assume the rate of sales tax is 4%.

**OLD SYSTEM OF SALES TAX:** Under the old system sales tax @ 4% would be charged at Rs. 1000 (last point sales) i.e. Rs. 40.
**SYSTEM OF VAT:**

| Transaction | Sale price | Output sales tax | Input sales tax | Net sales tax payable |
|---|---|---|---|---|

| | | | | |
|---|---|---|---|---|
| Manufacturer to wholesaler | 200 | 8 | 0 | 8 |
| Wholesaler to retailer | 500 | 20 | 8 | 12 |
| Retailer to consumer | 1000 | 40 | 20 | 20 |

Under both systems the retail price remains unchanged but under the system of VAT sales tax gets distributed over the chain.

**b)** The law relating to service tax is not governed by any Service Tax Act, but it is governed by chapter V of Finance Act 1994. After the introduction of the finance bill in the parliament, it is approved by the President of India within the period of 75 days. When finance bill is approved by the president then it becomes Finance Act and the corresponding changes are made every year to the Finance Act 1994. Further, tax on the services does not become effective from the date of passing finance act but becomes effective from the date which is notified by CBEC. In addition to notifications, CBEC issues circulars and clarifications for the effective implementation of service tax.

**C) SPONSORSHIP SERVICES** In case of sponsorship, reverse charge mechanism is applicable, i..e, service provider is not liable for payment of service tax rather the service recipient is liable for payment of service tax to the Govt. however, that reverse charge mechanism is applicable only when the service recipient is in India *(amendment to that effect was made in year 2007)*. In the given situation, since the service recipient is outside India reverse charge mechanism is not applicable; hence, service provider is liable for payment of service tax.

**d) FREE SERVICES:** As per section 67 (1) if the services are free services and where no consideration has been received then there shall be no service tax. In case of the authorized dealer who has provided services to client but has not charged anything from the client, but he is fully reimbursed by the manufacturer, can not be said to have been providing free services. In this case services are free for the client but the service provider has got the remuneration from the manufacturer so in this sense it is not free services and service tax is liable to be paid.

**e) E-PAYMENT OF SERVICE TAX:** WEF 1/10/2006, an assessee who has paid service tax of Rs. 50 lakhs or above in the preceeding financial year or has already paid service tax of Rs. 50 Lakhs in the current financial year has to compulsorily deposit the service tax liable to be paid by him electronically, through internet banking.

**f) LIFE INSURER CARRYING LIFE INSURANCE BUSINESS:** An insurer carrying on the life insurance business that is liable for paying service tax has the option to pay an amount calculated @ 1% of the gross amount of the premium charged by him towards the discharge of his service tax liability instead of paying service tax @ 12%.

**Q 7 (a)** Mr. X is the owner of the property had entered into an agreement with a bank. The agreement was entered into on 1/4/2007 to give the ground floor of the property on monthly rent of Rs. 75000. The bank had taken the property for the commercial use. Explain whether Mr. X is liable to pay service tax on the transaction with the bank? **(3 marks)**

**Solution:** WEF 1/6/2007 the services of renting immovable property have become taxable services. Therefore in this case services of Mr. X for the period of April and May 2007 are not taxable services but from June to March 2008 services of Mr. X are taxable services.
Mr. X is providing taxable services to a bank. Since rent of June to March 2008 is Rs. 7.5 lakhs, which is less than Rs. 10 lakhs therefore Mr. X will get basic exemption and no service tax shall be payable by him.

**(b)** Mr. Y is a consulting engineer raised a bill of Rs. 224720 (including service tax) on his client for the consulting services rendered by him in the month of June 2007. A partial payment of Rs. 168540 was received by him in the month of March 2008. Compute the service tax amount payable by Mr. Y and the due date by which service tax can be deposited. **(3 marks)**
**Solution: SERVICE TAX AT REALIZATION OF PAYMENT:** Service tax is payable at the time of realization of the amount for services rendered and not at the time when billing was done. Thus charge of service tax is on the event of providing services but payment of service tax to the Government is deferred till the receipt of the value of taxable services.
In other words, under the law of service tax, we follow cash system of accounting. This means service tax shall be payable to the government for the amount which has been realized from the client. In this case services have been rendered for Rs. 224720 but the payment have been received for Rs 168540, so the service tax shall be payable only for Rs. 168540. Since this amount is inclusive of service tax, the amount of service tax shall be calculated as follows:

| | | |
|---|---|---|
| Amount of services | 168540 / 112.36 X 100 | Rs. 150000 |
| Service tax @ 12% | | Rs. 18000 |
| Add: PEC @ 2% | | Rs. 360 |
| Add: SHEC @ 1% | | Rs. 180 |
| Total amount of service tax payable to the government | | Rs. 18540 |

Since this amount has been received in the month of March so this amount should be paid to the credit of the central government on or before 31/3/2008.

**Q 8** Answer any three of the following: **(3 X 3 marks)**

- **(a)** Can service tax return be revised by a person?
- **(b)** Explain input tax credit in the context of VAT
- **(c)** What are the exceptions to the input tax credit
- **(d)** What are the due dates for the payment of service tax?

**Solution:**
**(a) REVISION OF RETURN: RULE 7B:** Yes, return of the service tax can be revised by the person. An assessee may submit the revised return in for ST-3 in triplicate to correct a mistake or omission, within a period of 90 days from the date of submission of original return.

**(b) CONCEPT OF INPUT TAX CREDIT:** The main feature of system of VAT is that it provides the benefit of set off of input tax from the main output tax. The value added tax is based on the value addition to the goods, and the related VAT liability of the dealer is calculated by deducting input tax credit from the tax collected on sales during a particular period.

**EXAMPLE:** Mr. X purchases raw material worth Rs. 100000 in month of Jan 2008 and records the sales at Rs. 160000 during the same month. Input and output rate of VAT is 4%. So In this case, Input tax paid on raw material purchased is Rs. 4000 (100000 X 4%) and tax collected on sales is Rs. 6400 (160000 X 4%). So VAT payable by Mr. X during the month of Jan 2008 shall be Rs. 2400

**(c) EXCEPTIONS TO INPUT TAX CREDIT:** Input tax credit is generally given for the entire VAT paid within the state on the purchase of taxable goods meant for resale or manufacture of taxable goods. However no credit is available for the following purchases:

- **(1)** Goods purchased from unregistered dealer.
- **(2)** Goods purchased from other states.
- **(3)** Goods purchased from outside India.
- **(4)** Purchase of capital goods.
- **(5)** Purchase from a dealer who has opted from a composition scheme.
- **(6)** Purchase of goods in cases where the dealer does not have invoices showing amounts of tax charged separately by the selling dealer.

**(d) DUE DATES FOR THE PAYMENT OF SERVICE TAX:**

- **(a)** If the assessee is an individual or proprietary firm or partnership firm, the service tax shall be paid to the Central Government by the 5th of the month immediately following the quarter in which the payments are received, towards the value of taxable services. **In case e-payment is made, due date is 6th.**
- **(b)** In all other cases service tax received during any calendar month shall be paid to the Central Government by the 5th of the month immediately following the calendar month in which payments are received, towards value of taxable services. **In case e-payment is made, due date is 6th.**
- **(c)** If the service tax on the value of taxable services is received during the month of March, or the quarter ending in March, as the case may be, shall be paid to the Government by the 31st day of March of the calendar year.