

The Suggested Answers for Paper – 5: Income-tax and Central Sales Tax are based on the provisions applicable for A.Y.2005-06, which is the assessment year relevant for November 2005 examinations.

PAPER – 5 : INCOME TAX AND CENTRAL SALES TAX

*Answer **all** questions*

Question 1

- (a) *Mr. Ashok owns a property consisting of two blocks of identical size. The first block is used for business purposes. The other block has been let out from 1.4.2004 to his cousin for Rs.10,000 p.m. The cost of construction of each block is Rs.5 lacs (fully met from bank loan), rate of interest on bank loan is 10% p.a. The construction was completed on 31.3.2004. During the year ended 31.3.2005, he had to pay a penal interest of Rs.2,000 in respect of each block on account of delayed payments to the bank for the borrowings. The normal interest paid by him in respect of each block was Rs.42,000. Principal repayment for each block was Rs.23,000. An identical block in the same neighbourhood fetches a rent of Rs.15,000 per month. Municipal tax paid in respect of each block was Rs.12,000.*

The income from business prior to adjustment towards depreciation on any asset is Rs.2,20,000. He follows Mercantile system of accounting.

Depreciation on equipments used for business is Rs.30,000.

On 23.3.2005, he sold shares of B Ltd., a listed share in BSE for Rs.2,30,000. The share had been purchased 10 months back for Rs.1,80,000. Security transaction tax paid may be taken as Rs.220.

Brought forward business loss of a business discontinued on 12.1.2004 is Rs.80,000. This loss has been determined in pursuance of a return of income filed in time and the current year is the seventh year.

The following payments were effected by him during the year:

- (i) LIP of Rs.20,000 on his life and Rs.12,000 for his son aged 22, engaged as a software engineer and drawing salary of Rs.25,000 p.m.*
- (ii) Medici claim premium of Rs.6,000 for himself and Rs.5,000 for above son. The premiums were paid by cheque.*

You are required to compute the total income for the assessment year 2005-06 and the tax payable. The various heads of income should be properly shown. Ignore the interest on bank loan for the period prior to 1.4.2004, as the bank had waived the same.

(16 Marks)

- (b) Following is the Profit & Loss account of Mr. A, a dealer in shares and securities for the year ended on 31st March, 2005:

	Rs.		Rs.
To Trading Expenses	62,60,000	By Sales	72,54,000
To Administrative Expenses	1,05,000	By Interest on FD with bank	16,500
To Financial Expenses	48,265	By Dividend from Indian Co.	64,360
To Demat and Delivery charges	4,350	By Interest on I.T. Refund (A.Y. 2004-05)	230
To Securities Transaction Tax	5,500		
To Net Profit before depreciation	9,11,975		
	<u>73,35,090</u>		<u>73,35,090</u>

Compute the rebate available under Section 88E.

(7 Marks)

- (c) Compute the total income of Mr. & Mrs. A from the following information:

	Rs.
(a) Salary Income (Computed) of Mrs. A	2,30,000
(b) Income from profession of Mr. A .	3,90,000
(c) Income of minor son B from company deposit	15,000
(d) Income of minor daughter C from special talent	32,000
(e) Interest from bank received by C on deposit made out of her special talent	3,000
(f) Gift received by C on 30.09.2004 from friend of Mrs. A	2,500

Brief working is sufficient. Detailed computation under various heads of income is NOT required.

(7 Marks)

Answer

- (a) Computation of total income of Mr. Ashok for the A.Y. 2005-06

Particulars	Rs.	Rs.	Rs.
Income from house property [See Note I]			
Gross Annual Value [GAV of the second block]		1,80,000	
Less: Municipal tax paid		12,000	
Net Annual Value (NAV)		<u>1,68,000</u>	
Less: Deductions under section 24			
(a) 30% of NAV	50,400		

(b) Interest on bank loan	50,000	1,00,400	67,600
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Profits and gains of business or profession [See Note II]

Income prior to adjustment for depreciation	2,20,000		
Less: Depreciation	80,000		
Business income	1,40,000		
Less: Set-off of brought forward business loss [See Note III]	80,000		60,000

Capital gains [See Note IV]

Short-term capital gains from sale of listed shares

Full value of consideration	2,30,000		
Less: Cost of acquisition	1,80,000		50,000
Gross total income (GTI)			1,77,600
Less: Deduction under section 80D			6,000
Total Income			1,71,600

Computation of tax payable of Mr. Ashok for A.Y.2005-06	Rs.
Tax on total income of Rs.1,21,600 (excluding STCG) at normal rates	13,320
Less: Tax rebate under section 88 (See Note V)	7,800
	5,520
Tax on short-term capital gains[10% of Rs.50,000]	5,000
	10,520
Education cess @2%	210
Total tax payable	10,730

Notes:

I – On computation of Income from house property

- (1) The annual value of the house property which is used for the purpose of the business or profession carried on by the assessee, the profits of which are chargeable to income-tax, does not fall under the head "Income from house property". Therefore, the annual value of the first block is not chargeable to tax under the head "Income from house property".

- (2) As regards the second block, the sum for which the property may be reasonably expected to be let is Rs.15,000 per month. The Gross Annual Value (GAV) of the block is the higher of fair rent (i.e. Rs.15,000 p.m.) or the actual rent received (Rs.10,000 p.m.) Hence, the GAV of the second block is Rs.1,80,000 (i.e. Rs.15,000 p.m.)
- (3) Under section 24(b), interest on bank loan for construction of house is deductible. However, penal interest is not deductible. Assuming that the principal repayment of Rs.23,000 was made at the end of the year, interest due during the year in respect of the second block is Rs.50,000 (i.e. 10% of Rs.5 lakhs), which is allowable as deduction under section 24(b). It is also possible to solve the problem assuming that the interest of Rs.42,000 paid during the year represents the interest due.

II – On computation of Profits and gains of business or profession

- (1) Mr. Ashok can claim depreciation @10% on the building used by him for business purposes. The depreciation on the first block is Rs.50,000 (being 10% of Rs.5,00,000) and depreciation on equipments used for business is Rs.30,000. Hence the depreciation allowable during the year is Rs.80,000.
- (2) Since Mr. Ashok follows mercantile system of accounting, outstanding bank interest would have been provided for already.

III – On set off of business loss

As per section 72, business loss can be carried forward for a maximum of 8 assessment years and be set-off against business income. Therefore, since the current year is the seventh year only and since the loss has been determined in pursuance of a return of income filed in time, the brought forward business loss can be set-off against business income of the current year. It is not necessary that the business in respect of which the loss was incurred should be in existence for carry forward and set-off of loss of such business.

IV – On treatment of short-term capital gains (STCG)

The listed shares have been sold after 1-10-2004. The tax payable on the STCG from listed shares sold on or after 1-10-2004, on which securities transaction tax has been paid, is 10% as per section 111A. For the purpose of providing deduction under Chapter VIA, the gross total income should be reduced by the STCG on listed shares. Rebate under section 88 is to be allowed from the income-tax on total income as reduced by such STCG.

V – On computation of rebate under section 88 and deduction under section 80D

Tax rebate under section 88 can be claimed in respect of life insurance premium paid for major son, even though he is not dependent on the assessee. However, deduction under section 80D cannot be claimed in respect of mediclaim premium paid for non-dependant son.

Qualifying amount for rebate under section 88:	Rs.
Life insurance premium (Rs.20,000 + Rs.12,000)	32,000
Principal repayment in respect of the second block subject to a maximum of Rs.20,000	20,000
Total	52,000

Rebate under section 88 is to be calculated at 15% of qualifying amount, since Ashok's Gross Total Income exceeds Rs.1.5 lakhs. Therefore, rebate is Rs.7,800 (i.e. 15% of Rs.52,000).

(b) Computation of rebate under section 88E in case of Mr.A for A.Y. 2005-06

Particulars	Rs.	Rs.
Profits and gains of business or profession		
Net Profit as per Profit & Loss Account		9,11,975
<i>Add: Expenses not allowable</i>		
Securities transaction tax		5,500
		<u>9,17,475</u>
<i>Less: Income not includible under this head</i>		
Interest on FD with bank	16,500	
Dividend from an Indian company	64,360	
Interest on Income-tax refund	230	81,090
Income from business		<u>8,36,385</u>
Income from other sources		
Interest on fixed deposit with bank	16,500	
Dividend from Indian company [Exempt u/s 10(34)]	-	
Interest on Income-tax refund	230	16,730
Gross Total Income		<u>8,53,115</u>
Less: Deduction under Chapter VIA		
Under section 80L (Interest on FD with bank)		12,000
Total Income		<u>8,41,115</u>
Total Income (rounded off)		8,41,120
 Tax on total income		 2,26,336

Rebate under section 88E in respect of securities transaction tax – Where the total income of an assessee in a previous year includes any income, chargeable under the head “Profits and gains of business or profession”, arising from taxable securities transactions, he shall be entitled to a deduction, from the amount of income-tax on such income arising from such transactions, to the extent of the lower of the following two amounts –

- (1) Securities transaction tax paid i.e. Rs.5,500 in this case.
- (2) Average rate of income-tax x business income from such taxable securities transactions = 26.909% x Rs.8,36,385 = Rs.2,25,063.

Therefore, rebate under section 88E = Rs.5,500.

$$\text{Average rate of income-tax} = \frac{\text{Total tax}}{\text{Total income}} \times 100 = \frac{2,26,336}{8,41,120} \times 100 = 26.909\%$$

Note - Chapter VII of the Finance (No.2) Act, 2004, providing for levy of securities transaction tax on the value of taxable securities transactions came into force on 1.10.2004 only. However, this question does not specifically indicate the dates of purchase/sale of shares and securities for the purpose of determining the extent of applicability of securities transaction tax. This problem has been solved on the assumption that the entire business income of Mr. A has arisen from taxable securities transactions.

It is also possible to assume that income has accrued evenly throughout the year and therefore one half of business income (i.e. 4,18,193, being half of Rs.8,36,385) represents income from taxable securities transactions (i.e. income earned after 1.10.2004). In such a case, rebate under section 88E would be the lower of the following two amounts:

- (1) Securities transaction tax paid i.e. Rs.5,500.
- (2) Average rate of income-tax x business income from such taxable securities transactions = 26.909% x Rs.4,18,193 = Rs.1,12,532.

Therefore, rebate under section 88E = Rs.5,500.

- (c) As per the provisions of section 64(1A) of the Income-tax Act, 1961, all the income of a minor child has to be clubbed in the hands of that parent whose total income (excluding the income of the minor) is greater. The income of Mr. A is Rs.3,90,000 and income of Mrs. A is Rs.2,30,000. Since the income of Mr. A is greater than that of Mrs. A, the income of the minor children have to be clubbed in the hands of Mr. A. It is assumed that this is the first year when clubbing provisions are attracted.

Income derived by a minor child from any activity involving application of his/her skill, talent, specialized knowledge and experience is not to be clubbed. Hence, the income of minor child C from exercise of special talent will not be clubbed. However, interest from

bank deposit has to be clubbed even when deposit is made out of income arising from application of special talent.

The total income of Mrs. A is Rs.2,30,000. The total income of Mr.A giving effect to the provisions of section 64(1A) is as follows -

Computation of total income of Mr.A for the A.Y.2005-06

Particulars	Rs.	Rs.
Income from profession		3,90,000
Income of minor son B from company deposit	15,000	
Less: Exemption u/s 10(32)	1,500	13,500
Income of minor daughter C		
from special talent – not to be clubbed	-	
Interest from bank	3,000	
Gift of Rs.2,500 received from a non-relative on 30.9.2004 (not taxable u/s 56(2)(v), since it is lesser than Rs.25,000)	-	
	3,000	
Less: Exemption u/s 10(32)	1,500	1,500
Gross Total Income		4,05,000
Less: Deduction under section 80L (bank interest)		1,500
Total Income		4,03,500

Question 2 (First Alternative)

- (a) *In computing income under certain heads of income, method of accounting is irrelevant, while in some it is relevant. Comment.* (4 Marks)
- (b) *State the activities and operations, income from which is not deemed to accrue or arise in India.* (4 Marks)
- (c) *Mr.A is a resident Indian. During the F.Y. 2004-05, interest of Rs.92,000 was credited to his Non-resident (External) Account with the SBI. Rs.20,000 being interest on fixed deposit with SBI was credited to his savings bank account during this period. He also earned Rs.4,000 as interest on this savings account. Is Mr. A required to file return of income?*

What will be your answer, if he owns one shop in Mumbai of area 130 sq. ft? (4 Marks)

Answer

- (a) Section 145(1) of the Income-tax Act, 1961 states that income chargeable under the head "Profit and gains of business or profession" or "Income from other sources" shall be

computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee.

This implies that the income under the remaining heads of income, namely Salaries, Income from house property and Capital gains, should be computed as per the relevant provisions contained in the Income-tax Act. In such cases, the income has to be computed as laid down by the provisions of the Act, irrespective of the method of accounting employed by the assessee.

The Central Government, under section 145(2), is empowered to notify accounting standards to be followed by any class of assesses or in respect of any class of income. So far, the CBDT has notified two accounting standards which are required to be followed by all assesses following the mercantile system of accounting.

Hence, it could be said that the method of accounting is irrelevant while computing income under certain heads of income, whereas in some others it is relevant.

- (b) According to *Explanation 1* to section 9(1)(i) of the Income-tax Act, 1961, income from the following activities and operations shall not be deemed to accrue or arise in India-

1. **In case of a business of which all the operations are not carried out in India [Explanation 1 (a) to section 9(1)(i)]**

In the case of a business of which all the operations are not carried out in India, the income of the business deemed to accrue or arise in India shall be only such part of income as is reasonably attributable to the operations carried out in India. Therefore, it follows that such part of income which cannot be reasonably attributed to the operations in India is not deemed to accrue or arise in India.

2. **Purchase of goods in India for export [Explanation 1(b) to section 9(1)(i)]**

In the case of a non-resident, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in India for the purpose of export.

3. **Collection of news and views in India for transmission out of India [Explanation 1(c) to sec. 9(1)(i)]**

In the case of a non-resident, being a person engaged in the business of running a news agency or of publishing newspapers, magazines or journals, no income shall be deemed to accrue or arise in India to him through or from activities which are confined to the collection of news and views in India for transmission out of India.

4. **Shooting of cinematograph films in India [Explanation 1(d) to sec. 9(1)(i)]**

In the case of a non-resident, no income shall be deemed to accrue or arise in India through or from operations which are confined to the shooting of any cinematograph film in India, if such non-resident is –

- (i) an individual, who is not a citizen of India; or
- (ii) a firm which does not have any partner who is a citizen of India or who is

resident in India; or

- (iii) a company which does not have any shareholder who is a citizen of India or who is resident in India.

(c) **Computation of total income of Mr.A for A.Y. 2005-06**

Particulars	Rs.
Income from other sources	
Interest earned from Non-Resident (External) Account [Exempt u/s 10(4)(ii), assuming that Mr.A has been permitted by RBI to maintain the aforesaid account]	-
Interest on bank fixed deposit	20,000
Interest on savings bank account	4,000
Gross Total Income	24,000
Less: Deduction u/s 80L	12,000
Total Income	12,000

An individual is required to furnish a return of income u/s 139(1) if his total income exceeds the maximum amount not chargeable to tax. i.e. Rs. 50,000. Hence, Mr. A is not required to file a return of income since his total income is below Rs.50,000.

However, if he owns a shop of area 130 sq. ft. in Mumbai, he is required to file a return of income in Form No.2C as per the first proviso to section 139(1). It is presumed that he resides in an area notified by the CBDT in this behalf.

Question 2 (Second Alternative)

- (a) "Loss can be carried forward only by the person who has incurred the loss" - Discuss.
(4 Marks)
- (b) Briefly discuss about the provisions relating to claiming of exemption in respect of short-term capital gains, in order to reduce tax liability.
(4 Marks)
- (c) Briefly discuss about the provisions relating to deductibility of interest on capital borrowed for the purpose of business or profession.
(4 Marks)

Answer

- (a) As per section 78(2), where any person carrying on business or profession has been succeeded in such capacity by another person otherwise than by inheritance, then the successor cannot have the loss of the predecessor carried forward and set off against his income. However, there are certain exceptions, which are briefed hereunder:
- (i) Carry forward and set off of accumulated business loss of the amalgamating company against the income of the amalgamated company, if the amalgamation is within the meaning of section 72A;

- (ii) Carry forward and set off of accumulated business loss of the demerged company in the hands of the resulting company, in a scheme of demerger, subject to fulfillment of certain conditions which the Central Government may for this purpose notify, to ensure that the demerger is for genuine business purposes;
 - (iii) In the case of reorganisation of business, where a firm is succeeded by a company as per the provisions of section 47(xiii), or a sole proprietary concern is succeeded by a company as per the provisions of section 47(xiv), the accumulated loss of the firm or sole proprietor shall be deemed to be the loss of the successor company for the previous year in which the business reorganization was effected and the carry forward provisions shall be applicable to the successor company;
 - (iv) Where a business carried on by one person is acquired by another person through inheritance, then the successor can carry-forward and set-off the loss of the predecessor against his income.
- (b) Exemption under sections 54B, 54D and 54G can be claimed in respect of income from short term capital gains in order to reduce tax liability.
- (1) Under section 54B, if an individual transfers his agricultural land which has been used by him or his parents for agricultural purposes for a period of two years immediately preceding the date of transfer and he purchases another agricultural land within a period of two years from the date of such transfer, the amount of capital gain or the actual amount invested in purchasing the new agricultural land, whichever is lower, is allowed as exemption.
 - (2) Under section 54D, deduction is allowable to any assessee, being an industrial undertaking on compulsory acquisition of land and building forming part of the industrial undertaking. Such land and building should have been used for the purpose of the business of the undertaking for at least two years immediately preceding the date of compulsory acquisition and another land or building should be purchased or constructed within a period of three years for the use of the existing or newly set-up industrial undertaking. In such a case, the capital gain or the amount invested in the new land and building, whichever is lower, would be exempt.
 - (3) Section 54G exempts capital gain on transfer of assets, being machinery, plant, building or land, used for the business of an industrial undertaking situated in an urban area consequent to shifting of the industrial undertaking to any area other than an urban area. The assessee, being an industrial undertaking, should, within a period of one year before or three years after the date of transfer, purchase machinery, plant or acquire building or land or construct building and complete shifting to the new area. In such a case, the capital gain would be exempt to the extent of the cost of the new assets and expenses incurred for shifting.
- (c) Under section 36(1)(iii), deduction is allowed in respect of interest on capital borrowed for the purposes of business or profession while computing income under the head "Profits and gains of business or profession".

Capital may be borrowed for several purposes like for acquiring a capital asset, or for paying off a trading debt or loss etc. The scope of the expression 'for the purposes of business' is very wide. Capital may be borrowed in the course of the existing business as well as for acquiring assets for extension of existing business. *Explanation 8* to section 43(1) clarifies that interest relatable to a period after the asset is first put to use cannot be capitalized. Interest in respect of capital borrowed for any period from the date of borrowing to the date on which the asset was first put to use should, however, be capitalized in the case of extension of existing business or profession. The proviso to section 36(1)(iii) provides that no deduction shall be allowed in respect of any amount of interest paid, in respect of capital borrowed for acquisition of a new asset for extension of existing business or profession (whether capitalized in the books of account or not) for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use.

Question 3

- (a) *Fill in the blanks having regard to the provisions of the Income-tax Act, 1961 (All sub-divisions relate to the assessment year 2005-06) :*
- (i) *The due date for filing of return under Section 139(1) by a company having a turnover of less than Rs.40 lakhs is.....* (1 Mark)
 - (ii) *No order of assessment or reassessment shall be made under Section 147 after the expiry of from the end of* ($\frac{1}{2} + \frac{1}{2}$ Mark)
 - (iii) *Deduction under Section 80GGC in respect of contribution to approved political parties given by a local authority partly funded by the Government is* (1 Mark)
 - (iv) *Where a person transfers capital asset to a firm in which he becomes partner, the full value of consideration in the context of capital gain computation, will be* (1 Mark)
 - (v) *The first item in the order of priority of set off as between current year capital expenditure on scientific research, current year depreciation and brought forward business loss is* (1 Mark)
- (b) *State whether True or False, with reasons, having regard to the provisions of the Income-tax Act, 1961 (Answers without reasoning will not be given any mark; all sub-divisions relate to the assessment year 2005-06):*
- (i) *Where an urban agricultural land owned by an individual, continuously used by him for agricultural purposes for a period of two years prior to the date of transfer, is compulsorily acquired under law and the compensation is fixed by the State Government, resultant capital gain is exempt.*
 - (ii) *Where the Commissioner of Income-tax is satisfied that the activities of the charitable trust, which has been accorded registration is not genuine, he can cancel the registration by passing an order in writing.*

- (iii) *An existing assessee engaged in trading activities, can claim additional depreciation under Section 32(1)(ia) in respect of new plant acquired and installed in the trading concern, where the increase in value of such plant as compared to the approved base year is more than 10%.*
- (iv) *A Hindu Undivided Family resident in India having total income of Rs.55,000 is eligible to claim eligible tax rebate under Section 88D.*
- (v) *Where an individual repays a sum of Rs.30,000 towards principal and Rs. 14,000 as interest in respect of loan taken from a bank for pursuing eligible higher studies, the deduction allowable under Section 80E is Rs.40,000, and not Rs.30,000 (principal component only). (5x2=10 Marks)*

Answer

- (a) (i) 31st October, 2005.
- (ii) One year; the financial year in which the notice under section 148 was served
- (iii) Nil / not allowed .
- (iv) The amount recorded in the books of account of the firm as the value of the capital asset
- (v) Current year depreciation / Current year capital expenditure on scientific research.
- (b) (i) **False.** As per section 10(37), where an individual owns urban agricultural land which has been used for agricultural purposes for a period of two years immediately preceding the date of transfer, and the same is compulsorily acquired under any law and the compensation is determined or approved by the Central Government or the Reserve Bank of India, resultant capital gain will be exempt. In this case, however, the compensation has been fixed by the State Government and hence the exemption will not be available.
- (ii) **True.** As per sub-section (3) of section 12AA, inserted by the Finance (No.2) Act, 2004, the Commissioner has been granted the power to cancel the registration of the trust, by passing a written order, where he is satisfied, inter alia, that the activities of the trust are not genuine. However, the trust should be given a reasonable opportunity of being heard.
- (iii) **False.** Additional depreciation can be claimed in respect of eligible plant and machinery acquired and installed by an assessee engaged in the business of manufacture or production of any article or thing. However, in this case, the assessee is engaged in trading activities and the new plant has been acquired and installed in a trading concern. Hence, the assessee will not be entitled to claim additional depreciation under section 32(1)(ia).
- (iv) **False.** Tax rebate under section 88D can be claimed only by an individual resident in India. In the given problem, the assessee is a resident HUF. Hence, the assessee cannot claim rebate under section 88D.

- (v) **True.** Deduction under section 80E is available in respect of principal as well as interest on loan taken for pursuing eligible higher education, subject to a ceiling of Rs. 40,000.

Question 4

Write short notes on any **three** of the following:

- (a) Valuation of paid holidays for perquisite purposes under section 17(2);
- (b) Deductibility of contributions for Rural Development Programmes under section 35CCA;
- (c) Set off and carry forward of loss arising under the head "Income from other sources";
- (d) Powers of income-tax authorities under section 131 as regards discovery, production of evidence, etc. (6x3=18 Marks)

Answer

(a) Valuation of paid holidays for perquisite purposes under section 17(2):

- (i) The value of travelling, touring, stay and any other expenses paid for or borne or reimbursed by the employer for any holiday availed by the employee or any member of his household shall be the sum equal to the amount of the expenditure incurred by the employer in that behalf. This provision applies in respect of trips other than those exempt under section 10(5) read with Rule 2B.
- (ii) If the facility is maintained by the employer, and is not available uniformly to all employees, the value of benefit shall be taken to be the value at which such facilities are offered by other agencies to the public.
- (iii) Where the employee is on official tour and the expenses are incurred in respect of any member of his household accompanying him, the amount of expenditure so incurred shall also be a fringe benefit or amenity.
- (iv) However, if the official tour is extended as a vacation, the value of such fringe benefit will be limited to the expenses incurred in relation to such extended period of stay or vacation.
- (v) The amount so determined as above shall be reduced by the amount, if any, paid by or recovered from the employee for such benefit or amenity.

(b) Deductibility of contributions for rural development programmes under section 35CCA

Under section 35CCA, deduction is allowed in respect of the following expenditure incurred by an assessee during the previous year -

- (1) Payment to an association or institution, which has as its object the undertaking of any programme of rural development. Such payment must be used for carrying out any programme of rural development approved by the prescribed authority; or
- (2) Payment to an association or institution, which has as its object the training of persons for implementing programmes of rural development; or

- (3) Payment to a rural development fund set up and notified by the Central Government in this behalf; or
- (4) Payment made to the National Urban Poverty Eradication Fund (NUPEF) set up and notified by the Central Government in this behalf.

Where a deduction under this section is claimed and allowed for any assessment year in respect of any such expenditure referred to above, no deduction in respect of such expenditure shall be allowed under any other provision of the Act for the same or any other assessment year.

(c) Set off and carry forward of loss arising under the head "Income from other sources"

In the case of an assessee, being the owner of horses maintained by him for running in horse races, the amount of loss incurred by the assessee in such activity cannot be set-off against income from any source other than the activity of owning and maintaining race horses in that year. However, such loss can be carried forward under section 74A and set off against income from the activity of owning and maintaining race horses in any subsequent year. No such loss can, however, be carried forward beyond 4 assessment years from the end of the assessment year in which the loss is first computed.

For this purpose, the "amount of loss incurred by the assessee in the activity of owning and maintaining race horses" means -

- (i) in a case where the assessee has no income by way of stake money, the amount of revenue expenditure laid out or expended by him wholly and exclusively for the purposes of maintaining race horses;
- (ii) in a case where the assessee has income by way of stake money, the amount by which such income falls short of the amount of revenue expenditure laid out or expended by the assessee wholly and exclusively for the purposes of maintaining race horses.

(d) Powers of income-tax authorities under section 131 as regards discovery, production of evidence etc. :

Section 131 of the Income-tax Act, 1961 deals with the powers regarding discovery, production of evidence, etc.

The Assessing Officer, Joint Commissioner, Commissioner (Appeals), and Chief Commissioner or Commissioner shall have the same powers as are vested in a court under the Code of Civil Procedure, 1908 while trying a suit in respect of the following matters, namely -

- (i) discovery and inspection;
- (ii) enforcing the attendance of any person, including any officer of a banking company and examining him on oath;
- (iii) compelling the production of any books of account and other documents; and

- (iv) issuing commissions.

Further, the said income-tax authorities are vested with the power to impound or retain in their custody for such period as they may think fit, any books of accounts or other documents produced before them in any proceeding under this Act. However, an Assessing Officer or Deputy Director shall not impound any such books of account or documents without recording reasons and shall not retain in his custody such books of account and documents for a period exceeding 15 days (excluding holidays) without the approval of the Director General or Chief Commissioner or Commissioner or Director of Income-tax.

Question 5

- (a) *Choose the correct answer with regard to the provisions of the Central Sales-tax Act:*
- (a) *The collection of Central Sales-tax is effected by*
- (i) *the State where the goods are produced;*
 - (ii) *the State where the movement of goods begins;*
 - (iii) *the State where the goods are delivered;*
 - (iv) *the Central Government directly from the dealer.*
- (b) *The levy of Central Sales-tax is on*
- (i) *purchase of goods;*
 - (ii) *sale of goods;*
 - (iii) *purchase or sale of goods;*
 - (iv) *None of the above.*
- (c) *G effected inter-state sale of declared goods to H, charging correct CST of 3%. G should obtain from H*
- (i) *Form 'D';*
 - (ii) *Form 'C';*
 - (iii) *Form 'G';*
 - (iv) *No form.*
- (d) *R of Coimbatore, Tamil Nadu sold to a Malaysian ship at Kochi port in Kerala, some goods for consumption on board the ship. Such sale will be*
- (i) *inter-state sale;*
 - (ii) *export sale as it is a foreign ship;*
 - (iii) *intra-state sale;*
 - (iv) *sale in the course of import.*

- (e) A dealer engaged in effecting inter-state sale is required to get himself registered where his turnover exceeds
- (i) Any amount
 - (ii) Rs.1,00,000
 - (iii) Rs.2,50,000
 - (iv) Rs.3,00,000. (5x1=5 Marks)
- (b) Fill up the blanks, having regard to the provisions of the Central Sales-tax Act:
- (i) D, a dealer in Maharashtra has sold goods to G in Gujarat for which the sales tax rate in Maharashtra is 2% and the rate in Gujarat is 3%. The CST leviable is ----- (1 Mark)
 - (ii) The application for compulsory registration should be submitted by a dealer within ----- days of making an inter-state sale. (1 Mark)
 - (iii) C of Karnataka sends goods to T of Tamil Nadu for doing some job work. T adds some materials of his own, completes the job and returns the same to C. The above transaction ----- (attracts/does not attract) liability to CST. (1 Mark)
 - (iv) The dealer aggrieved by an appealable order should normally file appeal within ----- days from the date of ----- (1+1 Mark)
- (c) State with reasons whether the statements are true or false as per the provisions of the CST Act:
- (i) If a dealer applies for amendments to his certificate of CST registration, the amendment will be effective from the date on which the dealer makes an application for amendment.
 - (ii) The certificate of CST registration is non-transferable.
 - (iii) One Form 'C' issued by the buyer to seller can cover all transactions in one financial year.
 - (iv) In case of penultimate seller making sales to the actual exporters, the actual exporters shall issue a certificate to the penultimate seller in Form H.
 - (v) The directors of a private company in liquidation are jointly and severally liable personally for any sales tax liability of the company in liquidation. (5x1 = 5 Marks)

Answer**(a) Sub-division****Answer**

- (a) (ii) the State where the movement of goods begins
- (b) (ii) sale of goods

- (c) (ii) Form C [assuming that H is a registered dealer and the declared goods are covered in the registration certificate of such dealer]
- (d) (i) inter-State sale
- (e) (i) Any amount

(b) Sub-division

Answer

- (i) 2% [assuming that G is a registered dealer and the goods are covered in the registration certificate of such dealer and Form C is furnished]
- (ii) 30
- (iii) Attracts **(See Note below)**
- (iv) 45; service of such order upon him.

Note – If the job worker does not use his own material, there is no transfer of property in goods involved in works contract, and consequently, CST is not payable. However, in this case, since T adds some materials of his own, tax may be leviable on material used by T in execution of job work, as it will be goods involved in execution of works contract.

- (c) (i) **True.** If a dealer applies for amendment of his certificate of CST registration and the amendment is allowed by the CST authority, it becomes effective from the date on which the application for this purpose was made by the dealer.
- (ii) **True.** Certificate of registration is not transferable. If the dealer sells his business, the new buyer has to apply for fresh registration. However, in case of retirement or death or addition of a partner, only amendment to the certificate of registration is necessary.
- (iii) **True.** One Form 'C' can cover all transactions in one financial year irrespective of the total value of transactions during the year. If, however, a transaction covers more than one financial year, separate Form 'C' is required for each financial year.
- (iv) **True.** The actual exporter has to issue a certificate to the penultimate seller in Form H. Form H can be obtained from sales tax authority by the exporter.
- (v) **True.** As per section 18, if a private company is wound up and any tax assessed on the company cannot be recovered, then every person who was a director of the private company at any time during the period for which tax is due shall be jointly and severally liable for the payment of such tax, unless he proves that the 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.

Question 6

- (a) What is meant by "document of title" in the context of inter-State sale under the CST Act?
(3 Marks)

- (b) Mr. D, a first stage dealer in packing machinery in the State of Gujarat furnishes the following data:

	Rs.
(i) Total inter-state sales during F.Y. 2004-05	92,50,000
CST not shown separately	
(ii) Above sales include:	
Excise duty	9,00,000
Freight	1,50,000
(Of this Rs.50,000 is not shown separately in invoices)	
Insurance charges incurred prior to delivery of goods	32,000
Installation and commissioning charges shown separately	15,000
Incentive on sales received from manufacturer	30,000

Determine the turnover and CST payable, assuming that all transactions were covered by valid 'C' Forms. (7 Marks)

Answer

- (a) The term "documents of title to goods" is defined under section 2(4) of the Sale of Goods Act, 1930, as: "Document of title to goods" includes a bill of lading, dock warrant, warehouse-keeper's certificate, wharfinger's certificate, railway receipt, warrant or order for the delivery of goods and any other document used in the ordinary course of business as proof of possession or control of goods, or authorising or purporting to authorise, either by endorsement or by delivery, the possessor of the document to transfer or receive goods thereby represented. Some examples of documents of title are Lorry Receipt, Railway Receipt, Air Way Bill and Bill of Lading.

As per section 3(b), a sale or purchase of goods shall be deemed to take place in the course of inter-State trade or commerce if the sale or purchase is effected by a transfer of documents of title to goods during their movement from one State to another. Endorsement can be made on the "document of title" any time after the goods are handed over to the carrier but before physical delivery is taken from the carrier.

- (b) **Computation of Mr.D's turnover and central sales tax payable**

Particulars	Rs.	Rs.
Total inter-State sales		92,50,000
Less: Freight shown separately in the invoices	1,00,000	
Installation and commissioning charges shown separately	15,000	
		1,15,000
Turnover including CST (A)		91,35,000

CST payable (91,35,000 x 4/104) (B)	3,51,346
Turnover excluding CST (A-B)	<u>87,83,654</u>
 Central sales tax payable	 3,51,346

Note –

1. Excise duty forms part of the sale price and is not deductible.
2. Freight not shown separately in the invoices and insurance charges incurred prior to delivery of goods are not deductible in calculating the turnover.
3. Sale price includes incentive on sales received from manufacturer.
4. The CST on transactions covered by valid 'C' forms is 4% or the State sales-tax rate, whichever is lower. It has been assumed that in this case, the State sales-tax rate is higher than 4%. Therefore, the rate of CST is taken as 4%.