

CA PCC/PCE :: TAXATION : MAY 2007

Total No. of Questions— 8

Time Allowed : 3 Hours

Maximum Marks : 100

Answers to questions are to be given only in English except in the cases of candidates who have opted for Hindi medium. If a candidate who has not opted for Hindi medium, answers in Hindi, his answers in Hindi will not be valued.

Answer all Questions.

Q1. State with reasons, whether the following statements are true or false, with regard to the provisions of the Income-tax Act, 1961: [Answer any five out of six sub-divisions] **5 × 2 = 10**

- (i) Only individuals and HUFs can be resident, but not ordinarily resident in India; firms can be either a resident or non-resident.
- (ii) In respect of voluntary contributions in excess of Rs.20,000 received by a political party, exemption under section 13A is available where proper details about the donations are maintained; there is no need to maintain books of account.
- (iii) Payment made in respect of a business expenditure incurred on 16th February, 2007 for Rs.25,000 through a cheque duly crossed as "& Co." is hit by the provisions of section 40A(3).
- (iv) For grant of deduction under section 80-IB, filing of audit report in prescribed form is must for a corporate assessee; filing of return within the due date laid down in section 139(1) is not required.
- (v) From 1.6.2006 onwards, the Assessing Officer has the power, inter alia, to allot PAN to any person by whom no tax is payable.
- (vi) Where the Karta of a HUF is absent from India, the return of income can be signed by any male member of the family.

Sol.

- (i) **True:** A person is said to be "not-ordinarily resident" in India if he satisfies either of the conditions given in sub-section (6) of section 6. This sub-section relates to only individuals and Hindu Undivided Families. Therefore, only individuals and Hindu undivided families can be resident, but not ordinarily resident in India. All other classes of assesseees can be either a resident or non-resident for the purpose of income-tax. A firm can, therefore, either be a resident or non-resident.
- (ii) **False:** The obligation under section 13A to maintain proper details of voluntary contributions in excess of Rs.20,000 is over and above the obligation to maintain such books of account and other documents as would enable the Assessing Officer to properly deduce its income there from.
- (iii) **True:** In order to escape the disallowance specified in section 40A(3), payment in respect of the business expenditure ought to have been made through an account payee cheque. Payment through a cheque crossed as "& Co." will attract disallowance under section 40A(3).
- (iv) **False:** Section 80AC stipulates compulsory filing of return of income on or before the due date specified under section 139(1), as a pre-condition for availing the benefit of deduction, *inter alia*, under section 80-IB.

- (v) **True:** Section 139A(2) has been substituted w.e.f. 1.6.2006, to provide that the Assessing Officer may, having regard to the nature of transactions as may be prescribed, also allot a PAN to any other person, whether any tax is payable by him or not, in the manner and in accordance with the procedure as may be prescribed.
- (vi) **False:** Section 140(b) provides that where the karta of a HUF is absent from India, the return of income can be signed by any other adult member of the family; such member can be a male or female member.

Q2. Mr. Pankaj, aged 58 years, who retired from the services of the Central Government on 30.6.06, furnishes particulars of his income and other details as under: **20**

- Salary @ Rs.6,000 p.m.
- Pension @ Rs.3,000 p.m. for July' 06 to Nov' 06.
- On 1.12.2006, he got 1/3rd of his pension commuted for Rs.1,20,000.
- A house plot at Ernakulam sold on 1.2.07 for Rs.5,00,000 had been purchased by him on 3.11.79 for Rs.10,000. The stamp valuation authority had assessed the value of said house plot at Rs.6,00,000 which was neither disputed by the buyer nor by him. The value of this house plot as on 1.4.81 was Rs.15,000 (The cost inflation index for the year 2006- 07 is 519).
- Received interest on bank FDRs of Rs.72,500, dividend on mutual fund units of Rs.15,000 and interest on maturity of NSC of Rs.50,000 out of which an amount of Rs.40,000 was already disclosed by him on accrual basis in the returns upto Asst. Year 2006-07.
- Investment in purchase of NSC for Rs.30,000 and payment for mediclaim insurance for self and wife of Rs.12,500. Made investment in Tax Magnum units of Mutual Fund of SBI of Rs.80,000.

Compute the total income of Mr. Pankaj for A.Y. 2007-08.

In the event of Mr. Pankaj being ready to make appropriate investment for availing exemption in respect of capital gain arising from sale of house plot, what will be the amount to be invested and the period within which the same should be invested?

- (a) if he wishes to avail exemption under section 54F by constructing a new residential house;
- (b) if he wants to avail exemption under section 54EC.

Sol.

Computation of total income of Mr. Pankaj for A.Y.2007-08

Particulars	Rs.
Income from salaries (See Working Note 1)	41,000
Capital gains (See Working Note 2)	5,22,150
Income from other sources (See Working Note 3)	82,500
Gross Total Income	6,45,650
Less: Deductions under Chapter VI-A (See Working Note 4)	1,10,000
Total Income	5,35,650

1. Income from salaries

Particulars	Rs.
Salary for 3 months received from Government of India (6000 x 3)	18,000
Pension for 5 months from July'06 to Nov'06 @ Rs.3000 p.m. (3000 x 5)	15,000
Pension for 4 months from Dec'06 to March'07 @ Rs.2,000 p.m.(2,000 x 4)	8,000
	41,000

Note - Commuted value of pension of Rs.1,20,000/- received from the Central Government is fully exempt under section 10(10A)

2. Capital gains

Particulars	Rs.
Long term capital gains on sale of house plot at Ernakulam on 01.02.2007	
Sale consideration received is Rs.5,00,000. However, since the value assessed by the stamp valuation authority (i.e. Rs.6,00,000) is higher than the sale consideration, such value assessed is deemed to be the full value of the consideration received or accruing as a result of such transfer as per section 50C	6,00,000
Less: Indexed cost of acquisition	77,850
$15,000 \times \frac{519}{100}$	
	5,22,150

3. Income from other sources

Particulars	Rs.	Rs.
Interest on bank FDRs		72,500
Dividend of Rs.15,000 on units of Mutual Fund [exempt under section 10(35)]		-
Interest on maturity of NSC	50,000	
Less: Interest already shown on accrual basis in the past returns	40,000	10,000
		82,500

4. Deductions under Chapter VI-A

Particulars	Rs.	Rs.
Under section 80C		
Purchase of NSC	30,000	
Tax Magnum units of Mutual Fund of SBI	80,000	
Total	1,10,000	

Maximum deduction available under section 80C	1,00,000
Under section 80D	
Medical insurance premium paid Rs.12,500/- but maximum allowable is Rs.10,000/- (assumed to have been paid by cheque)	10,000
	1,10,000

Investment in approved modes

Section 54F (by constructing a new house)

In order to avail exemption under section 54F by constructing a new residential house, the assessee should construct a residential house within three years from the date of transfer of house plot. To avail the maximum exemption, the entire net consideration of Rs.5,00,000 received from sale of house plot should be invested. Value determined under section 50C is not relevant. If only part of the net consideration is invested, then proportionate exemption of long term capital gains would be available i.e.

$$\text{Long term capital gain} \times \frac{\text{Amount invested in new residential house}}{\text{Net sale consideration}}$$

Section 54EC

In order to avail maximum exemption under section 54EC, the assessee should invest the entire long-term capital gain arising from transfer of the house plot, i.e. Rs.5,22,150, within six months from the date of sale of house plot, i.e. on or before 31.7.2007 in bonds of National Highways Authority of India (NHAI) or Rural Electrification Corporation Ltd. (RECL). If only part of the capital gain is invested, then the exemption would be restricted to the amount invested in such bonds.

- Q3.** (a) The broad break-up of tax and allied details of Mrs. Rinku, born on 30th March, 1942 are as under:

9

	Rs.
Long-term capital gains on sale of house	2,00,000
Short-term capital gains on sale of shares in B Pvt. Ltd	30,000
Prize winning from a T.V. show	20,000
Business income	2,20,000
Net agricultural income	40,000
Mrs. Rinku has paid the following:	
LIC premium of self	40,000
LIC premium of husband	20,000
Premium for annuity contract with LIC in the name of her husband	25,000
Repayment of housing loan principal (loan taken by her son dependent on her)	30,000

Compute the tax payable by Mrs. Rinku for the assessment year 2007-08.

- (b) Swadeshi Ltd., which follows mercantile system of accounting, obtained licence on 1.6.2005 from the Department of telecommunication for a period of 10 years. The total licence fee payable is Rs.18,00,000. The relevant details are:

Year ended 31st March	Licence fee Payable for the year	Payments made	
		Date	Amount
	Rs.		Rs.
2006	10,00,000	30.3.06	3,70,000
		15.05.06	6,30,000
2007	8,00,000	28.02.07	5,40,000

Balance of Rs.2,60,000 is pending as on 31.3.2007.

Compute the amount of deduction available to the assessee under section 35ABB for the assessment years 2006-07 and 2007-08. Can any deduction be claimed under section 32 also?

Sol.

(a) Computation of tax payable by Mrs. Rinku for the A.Y.2007-08

Particulars	Rs.	Rs.
Step 1		
Add Agricultural income and Non-agricultural income		4,50,000
(Rs.40,000 + Rs.4,10,000) [For computation of nonagricultural income, see Note 1 below]		
Tax on the above income		
(i) Tax on long-term capital gain of Rs.2,00,000 @ 20%	40,000	
(ii) Tax on winnings of Rs.20,000 from a T.V. show @ 30%	6,000	
(iii) Tax on balance income of Rs.2,30,000	<u>9,000</u>	
Total tax on Rs.4,50,000	55,000	
Step 2		
Add Basic exemption limit to agricultural income (Rs.1,85,000 + Rs.40,000)		2,25,000
Tax on Rs.2,25,000		8,000
Step 3		
Tax on non-agricultural income (Tax under step 1 – Tax under step 2) (Rs.55,000 – Rs.8,000)		47,000
Add: Education cess @ 2%		<u>940</u>
Tax payable by Mrs. Rinku		47,940

Notes -

1. Computation of total income of Mrs. Rinku for the A.Y.2007-08

Particulars	Rs.	Rs.
Business income		2,20,000
Long term capital gains on sale of house		2,00,000
Short term capital gains on sale of shares in B Pvt. Ltd		30,000
Prize winnings from a T.V. show		<u>20,000</u>
Gross Total Income		4,70,000
Less: Deduction under section 80C		
Life insurance premium of self		40,000
Life insurance premium of husband	20,000	<u>60,000</u>
Total Income		4,10,000

2. Mrs. Rinku has completed 65 years of age on 30th March, 2007 (P.Y.2006-07). Therefore, she is entitled to the higher basic exemption limit of Rs.1,85,000.
 3. Short-term capital gains on sale of shares in B Pvt. Ltd. is taxable at normal rates.
 4. Premium for annuity contract with LIC in husband's name and repayment of housing loan taken by dependent son are not eligible for deduction under section 80C.
- (b) As per section 35ABB, any amount actually paid for obtaining licence to operate telecommunication services, shall be allowed as deduction in equal installments during the number of years for which the licence is in force. Therefore, the year of actual payment is relevant and not the previous year in which the liability for the expenditure was incurred according to the method of accounting regularly employed by the assessee.

1. Rs.3,70,000 paid on 30.03.2006 [P.Y.2005-06]

Unexpired period of licence 10 years

Hence Rs.37,000 [i.e. Rs.3,70,000/10] can be claimed under section 35ABB for period of 10 years commencing from A.Y.2006-07.

2. Rs.11,70,000 paid during year ended 31.03.07 [P.Y.2006-07]

Unexpired period of licence 9 years

Hence Rs.1,30,000 [i.e. Rs.11,70,000/9] can be claimed under section 35ABB for a period of 9 years commencing from A.Y.2007-08.

3. Amount of deduction u/s 35ABB

Assessment year	Amount (Rs.)
2006-07	37,000
2007-08	37,000 + 1,30,000 = 1,67,000

4. Where deduction under section 35ABB is claimed and allowed, deduction under section 32(1) cannot be allowed for the same previous year or any subsequent previous year.

Q4. (First Alternative)**14**

Miss Charlie, an American national, got married to Mr. Radhey of India in USA on 2.3.06 and came to India for the first time on 16.3.06. She remained in India up till 19.9.06 and left for USA on 20.9.06. She returned to India again on 27.3.07. While in India, she had purchased a show room in Mumbai on 22.4.06, which was leased out to a company on a rent of Rs.25,000 p.m. from 1.5.06. She had taken loan from a bank for purchase of this show room on which bank had charged interest of Rs.97,500 upto 31.3.07. She had received the following gifts from her relatives and friends during 1.4.06 to 30.6.06 :

From parents of husband	Rs.51,000
Fro married sister of husband	Rs.11,000
From two very close friends of her husband, Rs.1,51,000 and Rs.21,000	Rs.1,72,000

Determine her residential status and compute the total income chargeable to tax alongwith the amount of tax payable on such income for the Asst. Year 2007-08.

Q4. (a) (Second Alternative)**8**

A newly qualified Chartered Accountant Mr. Dhaval, commenced practice and has acquired the following assets in his office during F.Y. 2006-07 at the cost shown against each item. Calculate the amount of depreciation that can be claimed from his professional income for A.Y. 2007-08:

Sl. No.	Description	Date of acquisition	Date when put to use	Amount Rs.
1.	Computer	27 Sept., 06	2 Oct., 06	35,000
2.	Computer software	2 Oct., 06	4 Oct., 06	8,500
3.	Computer printer	2 Oct., 06	3 Oct., 06	12,500
4.	Books (of which books being annual publications are of Rs.12,000)	1 Apr., 06	1 Apr., 06	13,000
5.	Office furniture (Acquired from practising C.A.)	1 Apr., 06	1 Apr., 06	3,00,000
6.	Laptop	26 Sep., 06	4 Oct., 06	43,000
7.	Fire extinguisher	1 Apr., 06	No instance arose to use during F.Y. 2006-07	2,500
8.	Purchased practising CA's office in April '06 who had run it for 4 years, for Rs.5 lacs which includes Rs.2 lacs for goodwill and Rs.3 lacs for cost of furniture (included in 5 above)			

Note: Depreciation is to be provided at the applicable rates.

- (b) Simran, engaged in various types of activities, gives the following particulars of her income for the year ended 31.3.2007:

		Rs.
(a)	Profit of business of consumer and house-hold products	50,000
(b)	Loss of business of readymade garments	10,000
(c)	Brought forward loss of catering business which was closed in Asst. Year 2006-07	15,000
(d)	Short-term loss on sale of securities and shares	15,000
(e)	Profit of speculative transactions entered into during the year	12,500
(f)	Loss of speculative transactions of Asst. Year 2002-03 not set off till Asst. Year 2006-07	15,000

Compute the total income of Simran for the A.Y. 2007-08.

4. Answer

Under section 6(1), an individual is said to be resident in India in any previous year, if he satisfies any one of the following conditions:

- (i) He has been in India during the previous year for a total period of 182 days or more, or
- (ii) He has been in India during the 4 years immediately preceding the previous year for a total period of 365 days or more and has been in India for at least 60 days in the previous year.

If an individual satisfies any one of the conditions mentioned above, he is a resident. If both the above conditions are not satisfied, the individual is a non-resident.

Therefore, the residential status of Miss Charlie, an American National, for A.Y.2007-08 has to be determined on the basis of her stay in India during the previous year relevant to A.Y. 2007- 08 i.e. P.Y.2006-07 and in the preceding four assessment years.

Her stay in India during the previous year 2006-07 and in the preceding four years are as under:-

P.Y.2006-07

01.04.2006 to 19.09.2006	-	172 days
27.03.2007 to 31.03.2007	-	5 days
Total		177 days

Four preceding previous years

P.Y.2005-06 [1.4.05 to 31.3.06]	-	16 days
P.Y.2004-05 [1.4.04 to 31.3.05]	-	Nil
P.Y.2003-04 [1.4.03 to 31.3.04]	-	Nil
P.Y.2002-03 [1.4.02 to 31.3.03]	-	Nil
Total		16 days

The total stay of the assessee during the previous year in India was less than 182 days and during the four years preceding this year was for 16 days. Therefore, due to non-fulfillment of any of the two conditions for a resident, she would be treated as non-resident for the Assessment Year 2007-08.

Computation of total income of Miss Charlie for the A.Y. 2007-08

Particulars	Rs.	Rs.
Income from house property		
Show room located in Mumbai remained on rent from 01.05.06 to 31.03.07 @ Rs.25,000/- p.m.		
Gross Annual Value [25,000 x 11] (See Note 1 below)	2,75,000	
Less: Municipal taxes	-	
Net Annual Value (NAV)	2,75,000	
Less: Deduction under section 24		
30% of NAV	82,500	
Interest on loan	97,500	1,80,000
		95,000
Income from other sources		
Gifts received from non-relatives on or after 1.4.2006 is chargeable to tax as per section 56(2)(vi) if the aggregate value of such gifts is in excess of Rs.50,000.		
- Rs.50,000 received from parents of husband would be exempt, since parents of husband fall within the definition of relative and gifts from a relative are not chargeable to tax.		Nil
- Rs.11,000 received from married sister of husband is exempt, since sister falls within the definition of relative and gifts from a relative are not chargeable to tax.		Nil
- From two friends of husband Rs.1,51,000 and Rs.21,000 aggregating to Rs.1,72,000. Since the aggregate of Rs.1,72,000 exceeds Rs.50,000, the entire amount is taxable under section 56(2)(vi).	1,72,000	1,72,000
Total income		2,67,000

Computation of tax payable by Miss Charlie for the A.Y. 2007-08

Particulars	Rs.	Rs.
Tax on total income of Rs.2,67,000		30,100
Add: Education cess@2%		602
Total tax payable		30,702

Notes –

- Actual rent received has been taken as the gross annual value in the absence of other information (i.e. Municipal value, fair rental value and standard rent) in the question.
- If the aggregate value of taxable gifts received from non-relatives on or after 1.4.2006 exceeds Rs.50,000 during the year, the entire amount received (i.e. the aggregate value of taxable gifts received) is taxable. Therefore, the entire amount of Rs.1,72,000 is taxable under section 56(2)(vi).

3. The increased basic exemption limit of Rs.1,35,000 is available only for resident women. In this case, since the assessee is a non-resident, she cannot avail the benefit of higher basic exemption limit of Rs.1,35,000.

Question 4 (Second Alternative)

(a) Computation of depreciation allowable for A.Y.2007-08			
	Asset	Rate	Depreciation
Block 1	Furniture	10%	30,000
Block 2	Plant (Computer, computer software, laptop & books)	60%	37,050
Block 3	Plant (Books)	100%	12,000
Block 4	Plant (Fire Extinguisher and Printer)	15%	2,250
Total depreciation allowable			81,300

Notes -

1. Computation of depreciation

Block of Assets	Rs.
Block 1: Furniture – rate 10%	
Put to use for more than 180 days [Rs.3,00,000@10%]	30,000

Block 2: Plant – rate 60%

(a) Computer (put to use for more than 180 days) [35,000 @ 60%]	21,000
(b) Laptop (put to use for less than 180 days) [43,000 @ 30%]	12,900
(c) Computer Software (put to use for less than 180 days) [8,500 @ 30%]	2,550
(d) Books (other than annual publications) (Put to use for more than 180 days) [1,000 @ 60%]	600
	37,050

Block 3: Plant – Rate 100%

Books (being annual publications) put to use for more than 180 days [12,000 @100%]	12,000
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Block 4: Plant – Rate 15%

Computer printer (Put to use for 180 days) [12,500 @15%]	1,875
Fire extinguisher [2,500 @ 15%]	375
	2,250

2. Where an asset is acquired by the assessee during the previous year and is put to use for the purposes of business or profession for a period of less than 180 days, the deduction on account of depreciation would be restricted to 50% of the prescribed rate. In this case, since Mr.Dhaval commenced his practice in the P.Y.2006-07 and acquired the assets during the same year, the restriction of depreciation to 50% of the prescribed rate would apply to those assets which have been put to use for less than 180 days in that year, namely, laptop and computer software.
3. Goodwill is not an intangible asset entitled to depreciation.
4. In case of fire extinguishers, it is sufficient if they are kept ready for use. Actual use is not essential.

(b) Computation of total income of Simran for the A.Y. 2007-08

Particulars	Rs.	Rs.
Profit of business of consumer and house-hold products	50,000	
Less: Loss of business of readymade garments for the year adjusted under section 70(1)	10,000	
	40,000	
Less: Brought forward loss of catering business closed in A.Y. 2006- 07 set off against business income for the year as per section 72(1)	15,000	25,000
Profit of speculative transaction		12,500
Total Income		37,500

Notes –

1. Loss of speculative transaction of A.Y. 2002-03 is not allowed to be set off against the profit of speculative transaction of the A.Y.2007-08, since, as per the provisions of section 73(4), such loss can be carried forward for set-off for a maximum period of 4 years only i.e. up to A.Y.2006-07
2. Short term capital loss of Rs.15,000 on sale of securities and shares has to be carried forward as per section 74 since there is no income under the head Capital Gains for the A.Y.2007-08. The loss is to be carried forward for set off in future years against income chargeable under the head Capital Gains. Such loss can be carried forward for a maximum period of 8 assessment years.

Q5. Answer any four out of the following five sub-divisions, relating to the provisions of the Income-tax Act, 1961:

4 × 4 = 16

- (a) Discuss briefly about the scheme to facilitate submission of return of income through Tax Return Preparers.
- (b) Briefly discuss about the provisions relating to deductibility of expenditure incurred in relation to income not includible in assessee's total income.
- (c) How does the Income-tax Act, 1961 deal with conversion of a self-acquired property into the property of a Hindu Undivided Family?
- (d) What are the consequences of failure to deduct tax at source or pay the tax deducted at source to the credit of Central Government?
- (e) State the factors to be borne in mind relating to carry forward and set off of losses in case of change in constitution of firm or succession under section 78.

Sol.

(a) Scheme to facilitate submission of return of income through Tax Return Preparers [Section 139B]

- (1) Section 139B provides that, for the purpose of enabling any specified class or classes of persons to prepare and furnish their returns of income, the CBDT may notify a Scheme to provide that such persons may furnish their returns of income through a Tax Return Preparer authorized to act as such under the Scheme.

- (2) The Tax Return Preparer shall assist the persons furnishing the return in a manner that will be specified in the Scheme, and shall also affix his signature on such return.
 - (3) A Tax Return Preparer can be an individual, other than -
 - (i) any officer of a scheduled bank with which the assessee maintains a current account or has other regular dealings.
 - (ii) any legal practitioner who is entitled to practice in any civil court in India.
 - (iii) a chartered accountant.
 - (iv) an employee of the 'specified class or classes of persons'.
 - (4) The "specified class or classes of persons" for this purpose means any person, other than a company or a person, whose accounts are required to be audited under section 44AB or under any other existing law, who is required to furnish a return of income under the Act.
- (b) Deductibility of expenditure incurred in relation to income not includible in total income [Section 14A]**
- (i) As per section 14A, expenditure incurred in relation to any exempt income is not allowed as a deduction while computing income under any of the five heads of income.
 - (ii) However, the Assessing Officer is not empowered to reassess under section 147 or to pass an order increasing the liability of the assessee by way of enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154, for any assessment year beginning on or before 1.4.2001 i.e. for any assessment year prior to A.Y. 2002-03.
 - (iii) The Assessing Officer is empowered to determine the amount of expenditure incurred in relation to such income which does not form part of total income in accordance with such method as may be prescribed by the CBDT in this regard.
 - (iv) Such method should be adopted by the Assessing Officer if he is not satisfied with the Correctness of the claim of the assessee, having regard to the accounts of the assessee.
 - (v) Further, the Assessing Officer is empowered adopt such method, even where an assessee claims hat no expenditure has been incurred by him in relation to income which does not form part of total income.
- (c) Conversion of a self-acquired property into the property of a Hindu Undivided Family [Section 64(2)]**
- Section 64(2) deals with the case of conversion of self-acquired property into property of a Hindu undivided family.
- (i) Where an individual, who is a member of the HUF, converts at any time after 31-12- 1969, his individual property into property of the HUF of which he is a member or throws such property into the common stock of the family or otherwise transfers such individual property, directly or indirectly, to the family otherwise than for adequate consideration, the income from such property shall continue to be included in the total income of the individual.
 - (ii) Where the converted property has been the subject-matter of a partition (whether partial or total) amongst the members of the family, the income derived from such converted property as is received by the spouse on partition will be deemed to arise to the spouse from assets transferred indirectly by the individual to the spouse and consequently, such income shall also be included in the total income of the individual who effected the conversion of such property.

(iii) Where income from the converted property is included in the total income of an individual under section 64(2), it will be excluded from the total income of the family or, as the case may be, of the spouse of the individual.

(d) Consequences of failure to deduct tax at source or pay such tax deducted to the credit of the Central Government [Section 201]

(1) The following persons shall be deemed to be an assessee in default, if they do not deduct the whole or any part of the tax or after deducting, fail to pay the tax -

(i) any person referred to in section 200; and

(ii) the principal officer and the company of which he is the principal officer, in the cases referred to in section 194.

(2) However, no penalty shall be charged under section 221 from such person, principal officer or company unless the Assessing Officer is satisfied that such failure to deduct or pay the tax deducted, was without good and sufficient reasons.

(3) Such person, principal officer or company shall also be liable to pay simple interest at 12% p.a. on the amount of such tax from the date on which such tax was deductible to the date on which such tax is actually paid.

(4) Such interest should be paid before furnishing the quarterly statement for each quarter in accordance with section 200(3).

(5) Where the tax has not been paid after it is deducted, the amount of the tax together with the amount of simple interest thereon shall be a charge upon all the assets of the person or the company, as the case may be.

(e) Carry forward and set off of losses in case of change in constitution of firm or succession [Section 78]

(i) Where there is a change in the constitution of a firm, so much of the loss proportionate to the share of a retired or deceased partner remaining unabsorbed shall not be allowed to be carried forward by the firm. However, unabsorbed depreciation can be carried forward.

(ii) Where any person carrying on any business or profession has been succeeded in such capacity by another person otherwise than by inheritance, such other person shall not be allowed to carry forward and set off against his income, any loss incurred by the predecessor.

(iii) Where there is a succession by inheritance, the legal heirs [assessable as body of individuals (BOI)] are entitled to set off the business loss of the predecessor. Such carry forward and set off is possible even if the legal heirs constitute themselves as a partnership firm. In such a case, the firm can carry forward and set off the business loss of the predecessor.

Q6. .Answer any five out of the following six sub-divisions:–

5 × 2 = 10

(a) Is an unincorporated association, formed after 1st June, 2006, liable to pay any service tax?

(b) Is e-filing of service tax return permitted?

(c) Should service tax be paid even if not collected from the client or service receiver?

(d) Will the payment to a hotelier of Rs.10,000 on behalf of an architect by a service receiver be included in the value of taxable services?

(e) Which is the most popular and common method for computing VAT liability and at what stage is the tax imposed?

- (f) Is it correct to state that VAT usually increases the retail price, as the tax is payable on the first sale price?

Sol.

- (a) With effect from 01.05.2006, the Finance Act, 2006 has inserted an explanation after section 65(121) of the Finance Act, 1994. The explanation states that taxable service includes any taxable service provided or to be provided by any unincorporated association or body of persons to a member thereof, for cash, deferred payment or any other valuable consideration.
Thus, an unincorporated association providing service to its members can also be a “person” for purpose of service-tax, and be liable to pay service tax.
- (b) Yes, e-filing of service tax returns is permitted under service tax law. E-filing is a facility for the electronic filing of service tax returns by the assessee from his office, residence or any other place of choice, through the internet, by using a computer.
E-filing of returns is an assessee facilitation measure of the Department in continuation of its modernization and simplification programme. It is an alternative to the manual filing of return. This facility is available to all service providers.
- (c) Section 68 of the Finance Act, 1994 casts the liability to pay service tax upon the service provider or upon the person liable to pay service tax as per rule 2(1)(d) of the Service Tax Rules, 1994. This liability is not contingent upon the service provider realizing or charging the service tax at the prevailing rate. The statutory liability does not get extinguished if the service provider fails to realize or charge the service tax from the service receiver.
- (d) Service tax chargeable on any taxable service is on the basis of gross amount charged by service provider for such service provided or to be provided by him. It is not necessary that the service receiver should pay the consideration only to the service provider; any money paid to the third party is also includible. Hence, the hotel bill met by the client would be includible in the value of taxable services.
- (e) Invoice method is the most common and popular method for computing the tax liability under the VAT system. Under this method, tax is imposed at each and every stage of sales on the entire sale value, and the tax paid at the earlier stage is allowed as set-off.
- (f) The statement is not correct as VAT is a multi-point tax where tax is imposed at each and every stage of sales and tax paid at the earlier stage is allowed as set-off.

	Rs.
Contract for services entered into on 31.8.2006	
Advance received in September, 2006 towards all services	60,000
Total value of services, billed in February, 2007	2,10,000
Above includes non-taxable services of	70,000
Balance amount is received in March, 2007	

When does the liability to pay service tax arise and for what amount? Contract contains clear details of services; consideration and service tax are charged separately, as mutually agreed upon.

Sol.

The liability to pay service tax arises at the time of receipt of advance in September, 2006 and at the time of receipt of balance consideration in March 2007. Service tax is payable as soon as any advance is received as the taxable service includes "service to be provided" and payments received, before during or after the provision of taxable services form part of the gross amount charged for the taxable services. Further, the liability to pay service tax arises only upon the receipt of the value of taxable services and not when the bill is raised.

Advance portion

	Rs.
Advance received towards all services in September, 2006	= 60,000
Amount billed for taxable services	= 2,10,000 – 70,000 = 1,40,000
Advance received towards taxable services	= 60,000 × (1,40,000 / 2,10,000) = 40,000
Service tax @ 12% (since, service tax is charged separately)	= 40,000 × 12%
	= 4,800
Education Cess @ 2%	= 96
Total service tax liability	= 4,896

In this case, the due date for payment of service tax will be 5th October, 2006.

Balance portion

	Rs.
Balance amount received in March 2007	= 2,10,000 – Rs.60,000 = 1,50,000
Amount received towards taxable services	= 1,50,000 × (1,40,000/2,10,000) = 1,00,000
Service tax @ 12%	= 1,00,000 × 12%

	= 12,000
Education Cess @ 2%	= 240
Total service tax liability	= 12,240

In this case, the due date for payment of service tax will be 31st March, 2007.

Q8. Answer any three out of the following four sub-divisions: **3 × 3 = 9**

- (a) An assessee who has collected service tax from a client is unable to perform the service. Briefly explain the situations in which and the conditions subject to which he can adjust the service tax relating to above, against his forthcoming service tax liability.
- (b) Can Vignesh & Co., providing services from different locations and billing the clients from each location, opt for centralized service tax registration?
- (c) Can it be said that if the taxable service is not capable of ascertainment, the same cannot form part of value of taxable services from May, 2006 onwards?
- (d) In case of import of services, is a recipient of such services in India liable to pay service tax?

Sol.

- (a) An assessee may adjust excess payment of service tax against his liability of service tax for subsequent periods. Where an assessee has deposited service tax in respect of a taxable service which is not so provided by him either wholly or partially for any reason, he may adjust the excess service tax so paid by him (calculated on a *pro rata* basis) against his service tax liability for the subsequent period.

However, for carrying out such adjustment, the assessee must have refunded the value of taxable service and the service tax thereon to the person from whom it was received.

In such cases of adjustment, the assessee is required to file the details in respect of such *suo moto* adjustments done by him at the time of filing the service tax returns. The return Form ST – 3 also provides for enclosure of documentary evidence for adjustment of such excess service tax paid.

It is to be noted that adjustment of excess payment of service tax is not allowed *per se*, say due to clerical mistake etc. In such cases, the assessee has to claim the refund of excess tax paid.

- (b) Sometimes an assessee provides taxable service from more than one premises. Rule 4(2) of the Service Tax Rules 1994 provides that in such cases, the assessee can obtain centralized registration at his option if

- (a) he has centralized billing or centralized accounting in respect of such service, and
- (b) such centralized billing or centralized accounting systems are located in one or more offices or premises.

The assessee can register such offices or premises where centralized accounting or centralized billing systems are located.

In the given situation, centralized billing is not adopted. Hence, Vignesh & Co. cannot opt for centralized service tax registration.

- (c) No, it cannot be said so since with effect from 18.4.2006, the Finance Act, 2006 has introduced detailed provisions for valuation of taxable services. The provisions of section 67, as amended, state clearly that if the consideration for a taxable service is not ascertainable, the value of such service shall be the amount as may be determined in the prescribed manner.
- (d) Clause (iii) of rule 2(1)(d) of the Service Tax Rules, 1994 provides that in relation to any taxable service provided or to be provided by any person from a country other than India and received by any person in India, the person liable to pay service tax is the recipient of such service. Thus, in case of import of services, recipient of such services in India shall be liable to pay service tax.