

PAPER – 7 : DIRECT TAXES

QUESTIONS

1. The assessee was a manufacturer of textiles who made contribution towards export development fund. The assessee claimed that in order to augment its own export sales and give competitive edge to its marketing, it had contributed to the fund in its own business expediency, with the object of increasing opportunity of export of goods manufactured by it and to earn the subsidy. The assessee, therefore, claimed deduction on account of the same. Is the contention of the assessee correct?
2. Find out the taxable value of perquisite from the following particulars in case of an employee to whom the following assets held by the company were sold on 17.7.2004:

	Amount in Rs.		
	Car	Laptop	Furniture
Cost of purchase (June, 2002)	6,50,000	1,50,000	50,000
Sale price	4,00,000	20,000	25,000

The assets were put to use by the company from the day these were purchased.

3. Rallis Ltd. was situated in a remote place and its employees were the members of a club. The club was the only source of recreation to the employees. Rallis Ltd. paid a sum of Rs.5 lakhs to the club for renovation and repairs of the club building which had been damaged. Rallis Ltd. claimed deduction of the same as business expenditure. Discuss whether its claim is tenable in law?
4. Treaty Shopping is illegal and should be necessarily forbidden – Discuss the correctness of this statement.
5. Mr.Zavier, an American national, is a resident in India during the previous year ended on 31.3.2005. He is the owner of a building located in Detroit. The same was given on rent @ US \$ 10,000 p.m. The Municipal Corporation of Detroit was paid taxes on such building of US \$ 7,500 on 13.3.2005. Besides the above property, he purchased a piece of land at Mumbai for construction of a house. The said land was given on rent for running of a dairy @ Rs 7,500 p.m. w.e.f. 01.12.2004. The value of one US \$ in Indian rupee throughout the year remained at Rs.46. Compute Mr.Zavier's taxable income for assessment year 2005-06.
6. ABC Pvt. Ltd. had in the course of carrying on of its business, obtained unsecured loans from various creditors. In the light of the financial difficulties faced by the company, the creditors approached the High Court by filing various company petitions. During the course of those proceedings, a compromise was reached between the company and its creditors wherein, as per the terms of the compromise, certain creditors remitted unsecured loans amounting to Rs.1,77,052 and interest amounting to Rs.2,96,171. ABC Pvt. Ltd. declared such remitted interest as income liable to tax under section 41(1), while filing its return of income. The ITO, however, contended that the remittance of unsecured loan was also a benefit accruing to the company during the course of its business activity and brought the same to tax. Discuss the correctness of the contention of the ITO, keeping in mind that there was no allowance or deduction in any of the previous years in respect of such unsecured loan.
7. Rajdhani Ltd. deposited the share application money with its banker and earned interest thereon. The Assessing Officer sought to tax the interest earned on the deposit as income for the relevant assessment year, when the allotment process was not yet complete. The allotment process was completed only in the next assessment year. Is the Assessing Officer right in bringing to tax interest earned on such deposit in the current assessment year when the allotment process was not complete?
8. The WDV of Plant & Machinery on 01.04.2004 of Rallis Ltd. engaged in manufacturing of PVG granules is Rs.2,500 lakhs. The company purchased additional plant and machinery for Rs.1,000 lakhs on 20.06.2004 inclusive of a second-hand machine imported from Japan of Rs.400 lakhs to increase its installed capacity of production from 2000 TPA to 2500 TPA. The

production from new machine started w.e.f. 1.1.2005. Workout by giving reasons, the amount of allowable depreciation.

9. SFS Ltd. was engaged in the sale and export of sea food. It obtained a permit to fish in the Exclusive Economic Zone of India. In order to exploit the said fishing rights, it entered into an agreement chartering two fishing vessels, with a non-resident company. As per the terms of the agreement, SFS Ltd. had to pay 85% of fish catch towards the hire charges to the said non-resident company. This receipt in the form of 85% of the fish catch by the non-resident company was in India and all the formalities were completed in India. The assessing authority held that the assessee had made the payment to the non-resident company within the meaning of section 195 and was liable to deduct tax at source therefrom. Is the contention of the assessing authority correct? Discuss.
10. Is it necessary for the Assessing Officer to issue show-cause notice or give an opportunity for the assessee to be heard before issuing directions for conduct of special audit under section 142(2A)?
11. The assessee, Mr. Ram, declared the cost of construction of cinema theatre at Rs.10.53 lakhs, based on the registered valuer's report. The Assessing Officer accepted the value of the theatre as declared by the assessee and completed the assessment. However, the CIT, on enquiry, found that the assessee had availed a loan of Rs.17 lakhs from a leasing company declaring the value of the theatre at Rs.27.40 lakhs. Therefore, the CIT, after giving the assessee an opportunity of being heard, set aside the order of assessment and directed the Assessing Officer to make fresh assessment after verification and enquiry. On appeal before the Tribunal, the assessee questioned the order of the CIT by contending that the invocation of the provision under section 263 is not sustainable in law, since there was no information relating to any proceedings under the Income-tax Act available before the Assessing Officer which show that the assessment was erroneous and prejudicial to the Revenue. Discuss the correctness of the assessee's contention.
12. An educational institution eligible for exemption under section 10(23C) contends that it is not required to file a return of income, since its income is exempt from tax. Is the contention of the educational institution correct? Discuss.
13. Discuss the correctness of the following statements -
 - (i) Long term capital loss can be set-off against short-term capital gains arising in that year.
 - (ii) Business loss can be set-off against salary income arising in that year.
14. Cheran Cine Arts of Chennai is engaged in distribution of cinematography films. It started construction of a multiplex theatre and convention hall in Chennai in June 2004 and completed the construction in November, 2004. The profits for the year ended 31.03.2005 of all the activities are:

	<i>Rs. in lakhs</i>
(i) Distribution of cinematography films	10
(ii) Convention Centre	4
(iii) Multiplex theatre	2

Compute the taxable income for the A.Y. 2005-06 with reasons

15. Rajesh owns a residential house which is self-occupied. He also owns a house plot. He sells the house on 15.3.2005 for Rs.10 lakhs and the house plot on 25.3.2005 for Rs.8 lakhs. The house was purchased on 12.12.97 for Rs.6 lakhs and the plot on 1.2.98 for Rs.4 lakhs. Rajesh purchased a new residential house on 15.5.2005 for Rs.12 lakhs. Compute the income chargeable under the head "Capital Gains" for A.Y.2005-06. Cost Inflation Index for the financial year 1997-98 is 331 and financial year 2004-05 is 480.
16. The Settlement Commission had passed an order under section 245D(4) waiving and/or reducing interest levied on the assessee under sections 234A, 234B and 234C in accordance

with the state of law at the relevant point of time. Thereafter, the Settlement Commission, after a period of less than four years served notice upon the assessee stating that in view of the decision of the Supreme Court in the case of *CIT v. Anjum M.H. Ghaswala (2001) 252 ITR 1*, the aforesaid order required rectification. After considering the reply of the assessee, the Settlement Commission passed an order under section 154 withdrawing the reduction/waiver of interest granted by it earlier. Discuss the following with reference to the facts of the case stated above -

- (a) Is the Settlement Commission vested with the powers of an Income-tax Authority to give effect to the judgment of the Supreme Court?
 - (b) Is the scope and ambit of section 245F wide enough to enable the Settlement Commission to rectify an order passed by it under section 245D(4)?
17. Discuss the provisions of section 194LA relating to TDS from compensation paid on acquisition of immovable property other than agricultural land.
 18. What is an Annual Information Return? Elucidate the provisions of section 285A regarding Annual Information Return.
 19. In order to make the Indian shipping industry more competitive, a tonnage tax scheme for taxation of shipping profits has been introduced. A new Chapter XII-G has been inserted in the Income-tax Act containing sections 115V to 115VZC which provides for special provisions relating to taxation of the income of shipping companies. With reference to this scheme, explain the meaning of the following terms -
 - (a) Operating ship
 - (b) Qualifying company
 - (c) Relevant shipping income.
 20. Mr. Suresh, a Not Ordinarily Resident in India seeks your advice with regard to the furnishing of his Wealth-tax return. The value of assets held on 31.03.2005 is indicated below. You are requested to compute the taxable wealth of Mr. Suresh giving justification for the inclusion or exclusion of each item. The valuation date as indicated above is 31st March, 2005:

Particulars	Rs.
(i) Motor cars of foreign make held as Fixed Assets	10,00,000
(ii) Gold bonds under Gold Deposit Scheme, 1999	20,00,000
(iii) Residential House Property at Nagpur let out w.e.f. 8 th April, 2004	10,00,000
(iv) Jewellery held	5,00,000
(v) Lands purchased for industrial purpose:	
On 21 st Feb, 2000	4,00,000
On 20 th June, 2004	8,00,000
(vi) Loan against the purchase of lands:	
On 21 st Feb, 2000	3,00,000
On 20 th June, 2004	5,00,000
(vii) Wealth-tax liability	15,000
(viii) Cash on hand	60,000
(ix) Cash at bank	2,00,000
(x) Fixed Assets located in London	30,00,000
(xi) Value of Assets held by Mrs. Suresh acquired out of the gifts received from her husband:	

Shares and Securities	3,00,000
Residential House Property at Pune	15,00,000

21. Ganesh furnishes the following particulars for the compilation of his Wealth Tax return for A.Y. 2005-06:

	Rs.
i Gifts of jewellery made to wife from time to time aggregating Rs.50,000. Market value on valuation date	1,50,000
ii Flat purchased under installment payment scheme in February, 1980 for Rs.5,00,000, used for purposes of his residence. Market value as on 31.3.2005. (Installment remaining unpaid Rs.70,000)	15,00,000
iii Urban land transferred to minor handicapped child valued on 31.3.2005.	4,00,000

Explain how you will deal with these items. Make suitable assumptions, if required.

SUGGESTED ANSWERS/HINTS

- This question came up for consideration before the Rajasthan High Court in *Additional Commissioner of Income-tax v. Rajasthan Spinning & Weaving Mills Ltd. (2004) 137 Taxman 367*. The Court observed that the fund was set up to promote export of textiles and therefore contribution to such fund had direct nexus to the advancement of the assessee's business. Participation in any trade, association or fund set up for advancement of business, which is also carried on by the assessee, is primarily for advancing assessee's own business and not for philanthropic purposes. The High Court held that such expenses were incurred and laid out wholly and exclusively for the purpose of the assessee's business, and hence were allowable as deduction under section 37(1).

Therefore, in this case, the contention of the assessee is correct.

- Computation of taxable value of perquisite**

Sl. No.	Description of assets	Value of perquisite (Rs).
1.	Car	16,000
2.	Laptop	17,500
3.	Furniture	<u>15,000</u>
	Total	<u>48,500</u>

Working Note -

Description	Nature of Asset		
	Car - 20% (WDV)	Laptop – 50% (WDV)	Furniture – 10% (SLM)
Sale Price (A)	<u>4,00,000</u>	<u>20,000</u>	<u>25,000</u>
Cost of purchase (June 2002)	6,50,000	1,50,000	50,000
Less: Normal wear & tear in the first year	<u>1,30,000</u>	<u>75,000</u>	<u>5,000</u>
Reduced actual cost (in June 2003)	5,20,000	75,000	45,000
Less: Normal wear & tear in the second year	<u>1,04,000</u>	<u>37,500</u>	<u>5,000</u>
Reduced actual cost (in June 2004) (B)	<u>4,16,000</u>	<u>37,500</u>	<u>40,000</u>
Taxable perquisite (B) – (A)	<u>16,000</u>	<u>17,500</u>	<u>15,000</u>

Note: According to Rule 3(7), the value of perquisite in respect of transfer of moveable asset shall be the difference between sale price and the actual cost as reduced by specified rate for normal wear and tear for each completed year of usage.

3. This issue came up for consideration before the Calcutta High Court in *Assam Brook Ltd. v. Commissioner of Income-tax (2004) 139 Taxman 229*. The High Court observed that since the company was situated in a remote place, the club was the only source of recreation for its employees, who were also members of the club. So, if the assessee-company paid some amount for the upliftment/running of the club in an effective way, then such payment was made in the interest of the assessee, so that its employees remained happy and, consequently, the work of the assessee was not hampered in any way due to dissatisfaction on the part of the employees. As the payment of Rs.5 lakhs was made by the assessee to the club keeping its business interest in mind, the said payment must be held to be business expenditure, and accordingly, as per section 37 the assessee-company was entitled to get deduction.

The claim of Rallis Ltd. is, therefore, tenable in law.

4. Treaty shopping is a process by which a resident of a third country takes advantage of a fiscal treaty between two countries. The Supreme Court in *Union of India v. Azadi Bachao Andolan (2003) 132 Taxman 373*, observed that many developed countries tolerate or encourage "treaty shopping", even if it is unintended, improper or unjustified, for other non-tax reasons, unless it leads to significant loss of tax revenue. The Court cannot judge the legality of "treaty shopping" merely because one section of thought considers it improper. The Supreme Court recognized that the Treaties are negotiated and entered into at political level and have several considerations as their bases. This was an important principle to be kept in mind in the interpretation of the provisions of an international treaty. The Court observed that if it was intended that a national of a Third State should be precluded from the benefits of a DTAA, then a suitable limitation to that effect must find place in the DTAA itself. In the absence of a limitation specifically provided in the DTAA, the same cannot be read into it.
5. For the previous year 2004-05, Mr. Xavier, an American National, is resident in India. Accordingly, the income received by him by way of rent of the house property located in USA is subject to tax in India. Municipal taxes so paid in the country where the property is situated are also to be allowed as deduction. This was held in the case of *CIT v. R. Venugopala Reddiar (1965) 58 ITR 439* by the Madras High Court. The income chargeable to tax will be as under:

Particulars	Amount in Rs.	Amount in Rs.
I. Income from House Property		
Income from property situated in USA		
Annual rental value being actual rent received of US\$10,000 p.m. converted into Indian rupees @ Rs.46		
- (US\$ 10,000 x 12 x 46)	55,20,000	
Less: Municipal taxes paid (US\$ 7500 x 46)	<u>3,45,000</u>	
Net annual value (NAV)	51,75,000	
Less: Deductions u/s.24 – 30% of NAV	<u>15,52,500</u>	36,22,500
II. Income from Other Sources		
Rent from letting out of vacant land at Mumbai for 4 months (Rs.7,500 x 4)		<u>30,000</u>
Taxable Income		<u>36,52,500</u>

Note:

1. Rental income from vacant land given on rent is chargeable to tax under the head "Income from other sources".
 2. In case the Double Taxation Avoidance Agreement provides for tax relief in respect of such income then section 90 would apply. In such a case, the income from house property in foreign country will be taxed subject to the terms of such agreement.
6. This issue came up for consideration before the Gujarat High Court in *CIT v. Chetan Chemicals (P.) Ltd. (2004) 139 Taxman 301*. The High Court observed that section 41(1) can be invoked only when an allowance or a deduction has been granted during the course of assessment for any year in respect of loss, expenditure or trading liability which is incurred by the assessee, and subsequently, during any previous year, the assessee obtains, whether in cash or in any other manner, any amount in respect of such trading liability by way of remission or cessation of such liability. In that case, either the amount obtained by the assessee or the value of the benefit accruing to the assessee can be deemed to be the profits and gains of a business or profession and can be brought to tax as income of the previous year in which such amount or benefit is obtained. In this case, since there had been no allowance or deduction in any of the preceding years in respect of the unsecured loan, the provisions of section 41(1) cannot be applied to such loan.

Therefore, the amount of Rs.1,77,052 arising as a result of remission of unsecured loans is not taxable in the hands of ABC Pvt Ltd.

7. The Madras High Court in *CIT v. Henkel Spic India Ltd. (2004) 139 Taxman 40* observed that until the allotment process was complete, the application money and the interest due thereon would remain with a trust in favour of the general body of the applicants. The prohibition incorporated in section 73(3A) of the Companies Act, 1956 was absolute and the amount so deposited cannot be transferred to any other account. The amount of interest earned on application money, to the extent to which it is not required for being paid to the applicants to whom moneys have become refundable by reason of delay in making refund, will belong to the company only when the trust terminates and it is only at that point of time that the amount can be said to have accrued to the company.

In this case, since the process of allotment was completed only in the next year, the interest can be said to have accrued in the next year only. Therefore, the Assessing Officer was not correct in bringing to tax interest earned on such deposit in the current assessment year.

8. **Calculation of allowable depreciation in the case of Rallis Ltd. for A.Y. 2005-06**

Particulars	Rs. in lakhs
WDV as at 01.04.2004	2,500
Add: Addition during the year (put to use for less than 180 days)	<u>1,000</u>
Total	<u>3,500</u>
Normal depreciation	
- On opening WDV of Rs.2,500 lakhs @ 25%	625
- On Addition of Rs.1,000 lakhs @ 25% * 50%	125
Additional depreciation	
- On Addition of Rs.600 lakhs @15% *50%	<u>45</u>
Total depreciation allowable	<u>795</u>

Note: In the case of an existing undertaking, additional depreciation @ 15% of actual cost will be allowed in the previous year in which it achieves substantial expansion by way of increase in the installed capacity by not less than 10%. Such additional depreciation will also be restricted to 50% of 15%, if the assets are put to use for a period of less than 180 days.

However such additional depreciation is not available for second-hand machinery. Hence, additional depreciation is not allowable on imported second hand machinery of Rs.400 lakhs.

For claiming additional deduction as above, the assessee should furnish details of machinery or plant and increase in the installed capacity of production in the prescribed Form No. 3AA along with the return of income, and the report of an accountant certifying that the deduction has been correctly claimed.

9. The Andhra Pradesh High Court settled this issue in *Kanchanganga Sea Foods Ltd. v. CIT (2004) 136 Taxman 8*, where it was held that 85% of fish catch which was adjusted in discharge of liability of the assessee towards hire charges, would be receipt in the hands of non-resident company under section 5(2). Further, this receipt in the form of 85% of the fish catch by the non-resident company was in India since all the formalities were completed in India. It was further held that payment contemplated under section 195 not only includes cash payment or payment by cheque or draft, but also a payment given by any other mode. Therefore, the payment of hire charges made by the assessee by giving 85% of fish catch to the non-resident company amounted to payment as contemplated under section 195.

Therefore, the contention of the assessing authority is correct.

10. This question has been answered by the Allahabad High Court in *Jhunjhunwala Vanaspati Ltd. v. Asstt. CIT (2004) 137 Taxman 214*. The High Court observed that the Income-tax Act confers powers on revenue officials to direct special audit of accounts in complex cases. The Court held that it is not necessary for the Assessing Officer to give show-cause notice or give an opportunity for the assessee to be heard before issuing directions under section 142(2A) for conduct of special audit, since such direction is a purely administrative matter, the sole purpose of which is to ensure a correct assessment.
11. This issue was resolved by the Madras High Court in *CIT v. Dr. K. Ramachandran (2004) 139 Taxman 320*. The High Court observed that the *Explanation* to section 263 provides that the term "record" shall include and shall be deemed always to have included all records relating to any proceeding under the Act available at the time of the examination by the CIT. In *CIT v. Shree Manjunathesware Packing Products & Camphor Works (1998) 231 ITR 53(SC)*, the Apex Court made it clear that section 263 enables the CIT to call for and examine the records of any proceedings under the Act and pass such orders thereon as the circumstances of the case justify, including an order enhancing or modifying the assessment or canceling the assessment and directing a fresh assessment, if he considers that the order passed by the Assessing Officer is erroneous and prejudicial to the interest of the Revenue. For this purpose, record would include not only record which was available to the ITO at the time of passing the assessment order, but would include the records available with the CIT at the time of passing of the order by the CIT.

The High Court also relied on its earlier decision in the case of *CIT v. M.N. Sulaiman (1999) 238 ITR 139*, wherein it followed the above decision of the Supreme Court. The High Court further held that the *Explanation* added to section 263(1) in the year 1988 has to be regarded as declaratory.

Therefore, since the term "record" includes all records available at the time of passing of order under section 263 by the CIT and is not restricted to information available to the ITO at the time of passing the assessment order, the assessee's contention is not correct.

12. Under section 10(23C), any income received by any person on behalf of an educational institution existing solely for educational purposes and not for purpose of profit is exempt. Such income is excluded from total income and does not enter into computation of total income.

Earlier, there was no provision in the Income-tax Act requiring such institutions, whose income was exempt under section 10(23C), to file a return of income. Section 139(1) covered only persons whose income was assessable under the Act.

However, the Finance Act, 2002 has w.e.f. 1.4.2003 inserted sub-section (4C) in section 139 requiring such institutions to file a return of income, if their total income, without giving effect to the provisions of section 10, exceeds the maximum amount which is not chargeable to tax.

Therefore, if the income of the educational institution, without giving effect to the provisions of section 10(23C), exceeds the maximum amount which is not chargeable to tax, then it is required to file its return of income in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed. All the provisions of the Act, will apply as if it were a return to be furnished under section 139(1).

13. (i) This statement is incorrect. Long-term capital loss can be set-off only against long term capital gain arising in that year. Where such loss cannot be wholly so set off, the amount of loss not so set off can be carried forward up to 8 assessment years and set off only against long term capital gains.
- (ii) This statement is incorrect. The Finance (No.2) Act, 2004 has amended section 71 to disallow set-off of business loss against income under the head "Salaries".
14. The provisions of section 80-IB(7A) and (7B) are applicable in the case of income derived by Cheran Cine Arts from Multiplex Theatre and Convention Centre, respectively. 50% of the profits of the Multiplex Theatre, if located other than in Delhi, Kolkata, Mumbai & Chennai are exempt under section 80-IB(7A). In this case, since the multiplex theatre is located in Chennai, it is not eligible for deduction under sub-section (7A). However, 50% of the profits derived from the Convention Hall are eligible for deduction under section 80-IB(7B), subject to fulfillment of other conditions laid down in clause (b) of section 80-IB(7B), which are as follows –
 - (i) The convention hall should have been constructed during the period 1.4.02 to 31.3.05;
 - (ii) The business of the convention hall should not have been formed by the splitting up, or the reconstruction, of a business already in existence or by the transfer to a new business of any building or of any machinery or plant previously used for any purpose;
 - (iii) The assessee should furnish alongwith the return of income, the audit report in the prescribed form, duly signed and verified by an accountant, certifying that the deduction has been correctly claimed.

Computation of taxable income of Cheran Cine Arts for the A.Y. 2005-06

Particulars	Rs. in lakhs
Income from distribution of cinematography films	10
Income from convention centre	4
Income from Multiplex theatre	<u>2</u>
	16
Less: Deduction under section 80-IB	
For convention centre – 50% of the profit for initial 5 years	2
For multiplex theatre	<u>Nil</u> <u>2</u>
Taxable income	<u>14</u>

15. **Computation of taxable capital gains of Rajesh for A.Y.2005-06**

Particulars	Amount in Rs.
1. Sale of House	
Sale consideration	10,00,000
Less: Indexed cost of acquisition [6,00,000x480/331]	8,70,091
Long term capital gain	1,29,909

Less: Exemption under section 54	1,29,909
[Cost of the new house or LTCG, whichever is lower]	

Taxable capital gain	Nil
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2. Sale of house plot

Sale consideration	8,00,000
Less: Indexed cost of acquisition $[4,00,000 \times 480/331]$	5,80,060

Long term capital gain	2,19,940
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Less: Exemption under section 54F:	2,19,940
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Investment for the purpose of section 54F=

$12,00,000 - 1,29,909 = 10,70,091$, which is more than the net consideration of Rs.8 lakhs. Therefore, the long term capital gain on sale of house plot is fully exempt.

Taxable Capital gain	Nil
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16. The above questions have been answered by the Gujarat High Court in *Sanjaybhai R. Patel v. Assessing Officer (2004) 135 Taxman 210*. In this case, the Gujarat High Court observed that section 245F(1) vests the Settlement Commission with all the powers which are vested in an income-tax authority under the Act, in addition to the powers that the Commission has under Chapter XIX-A.

Section 154 contemplates that the powers of rectification thereunder can be exercised only with a view to rectify a mistake apparent from record and that the said powers can be exercised by an income-tax authority referred to in section 116. Section 154(7) prescribes the time-limit for exercise of such powers and it says that no amendment under this section shall be made after the expiry of 4 years from the end of the financial year in which the order sought to be amended was passed.

In the instant case, the Settlement Commission had waived or reduced the interest under sections 234A, 234B and 234C despite the fact that it had no such power under the Act and it was contrary to the law laid down by the Supreme Court. The High Court took into consideration the decision in *Standard Radiators v. CIT (1987)165 ITR 178 (Guj.)* and held that in the instant case, the Settlement Commission had committed an error apparent on the face of the record in reducing/waiving the interest chargeable under sections 234A, 234B and 234C. As far as the issue as to whether the Settlement Commission is an income-tax authority or not is concerned, section 245F(1) specifically states that the Settlement Commission has got all the powers of the income-tax authority, over and above the powers under Chapter XIX-A.

The Settlement Commission cannot issue circulars for which the issuing powers are vested with the CBDT under section 119, but it is certainly an Income-tax authority to confer the benefit available to the assessee under the circular and for this purpose, section 245F can be pressed into service. If such powers are exercised by the Settlement Commission within 4 years from the date of original order passed under section 245D, the same is in accordance with the provisions contained in section 154. Therefore, there was no infirmity in the order passed by the Settlement Commission while exercising the powers under section 154 for the purpose of rectifying the mistake committed by it in the original order under section 245D, which was a mistake apparent from record.

17. TDS from compensation paid on acquisition of immovable property other than agricultural land [Section 194LA]

- (i) Section 194LA provides for deduction of tax at source by a person responsible for paying to a resident any sum in the nature of –
 - (1) compensation or the enhanced compensation or
 - (2) the consideration or the enhanced consideration
 on account of compulsory acquisition, under any law for the time being in force, of any immovable property (other than agricultural land).
- (ii) The amount of tax to be deducted is 10% of such sum mentioned in (i) above.
- (iii) The tax should be deducted at the time of payment of such sum in cash or by issue of a cheque or draft or by any other mode, whichever is earlier.
- (iv) No tax is required to be deducted where the amount of such payment or, as the case may be, the aggregate amount of such payments to a resident during the financial year does not exceed Rs.1 lakh.

18. Annual Information Return [Section 285BA]

- (a) Section 285BA had been inserted by the Finance Act, 2003, to provide that any assessee, who enters into any financial transaction, as may be prescribed, with any other person, shall furnish, within the prescribed time, an annual information return in such form and manner, as may be prescribed, in respect of such financial transactions entered into by him during any previous year.
- (b) Since the existing provisions of the section do not cast any obligation to furnish such a return on the Government agencies and other authorities, who are valuable sources of information and further, no mechanism has been provided to enforce furnishing of such a return, this section has been substituted with the new section 285BA.
- (c) Sub-section (1) of the new section casts responsibility on –
 - an assessee or
 - the prescribed person in the case of an office of Government or
 - certain other authorities,
 who are responsible for registering or maintaining books of account or other documents containing a record of any specified financial transaction, to furnish an annual information return.
- (d) Such annual information return should be furnished to the prescribed income-tax authority or such other authority or agency as may be prescribed in respect of –
 - (i) such transactions registered or recorded by him during any financial year beginning on or after 1st April, 2004, and
 - (ii) information relating to which is relevant and required for the purposes of this Act
- (e) The annual information return has to be furnished within the prescribed time after the end of such financial year in such form and manner (including on a floppy, diskette, magnetic cartridge tape, CD-ROM or any computer readable media) as may be prescribed.
- (f) The expression “specified financial transaction” has been defined to include the following transactions, which may be prescribed by the CBDT –
 - (1) a transaction of purchase, sale or exchange of goods or property or right or interest in a property, or
 - (2) a transaction for rendering any service, or
 - (3) a transaction under a works contract, or
 - (4) a transaction by way of an investment made or an expenditure incurred, or

- (5) a transaction for taking or accepting any loan or deposit.
- (g) The CBDT may prescribe different values for different transactions in respect of different persons, having regard to the nature of such transactions.
- (h) The value or the aggregate value of such transactions during a financial year so prescribed referred to above should not be less than fifty thousand rupees.
- (i) Where the prescribed income-tax authority considers that the annual information return is defective he may intimate such defect to the person who has furnished such return and give him an opportunity to rectify the same within one month or such further period as he may allow in his discretion.
- (j) If the defect is not rectified within such period, such return would be treated as an invalid return and the provisions of the Act would apply as if such person had failed to furnish the annual information return.
- (k) Where a person referred to in sub-section (1) has not furnished the annual information return within the prescribed time, the prescribed income-tax authority may serve a notice requiring him to furnish such return within a period of sixty days from the date of service of such notice. Such person should furnish such return within the time specified in the notice.
- (l) This amendment will apply to the specified financial transactions entered into on or after 1st April, 2004.
- (m) To provide a penalty for not furnishing a return as required under new section 285BA(1), a new section 271FA has been inserted. Penalty of Rs.100 is attracted for every day during which failure continues, if a person who is required to furnish an annual information return fails to furnish such return within the time prescribed.

19. (a) Operating ship [Section 115VB]

- (1) A company shall be regarded as operating a ship if it operates any ship whether owned or chartered by it.
- (2) Even if only a part of the ship has been chartered in by it in an arrangement such as slot charter, space charter or joint charter, the company would be regarded as operating a ship.
- (3) However, a company will not be regarded as the operator of a ship which has been chartered out on bareboat charter-cum-demise terms or on bareboat charter terms for a period exceeding three years.
- (4) "Bareboat charter" means hiring of a ship for a stipulated period on terms which give the charterer possession and control of the ship, including the right to appoint the master and crew;
- (5) "Bareboat charter-cum-demise" means a bareboat charter where the ownership of the ship is intended to be transferred after a specified period to the company to whom it has been chartered.

(b) Meaning of "Qualifying company" [Section 115VC]

- (1) A company will be a qualifying company if -
 - (a) it is an Indian company;
 - (b) the place of effective management of the company is in India;
 - (c) it owns at least one qualifying ship; and
 - (d) the main object of the company is to carry on the business of operating ships.
- (2) The expression "place of effective management of the company" has been defined in the *Explanation* to the section to mean -
 - (a) the place where the board of directors of the company or its executive directors make their decisions; or

- (b) in a case where the board of directors routinely approve the commercial and strategic decisions made by the executive directors or officers of the company, the place where such executive directors or officers of the company perform their functions.

(c) Meaning of “Relevant shipping income”[Section 115V-I]

- (1) The “relevant shipping income” of a tonnage tax company means its profits from core activities and its profits from incidental activities
- (2) Where the aggregate of income from incidental activities exceeds one-fourth per cent of the turnover from core activities, such excess will not form part of relevant shipping income for the purposes of this Chapter and shall be taxable under the other provisions of this Act.
- (3) The core activities of a tonnage tax company are –
 - (i) its activities from operating qualifying ships; and
 - (ii) Other ship-related activities, being,
 - (a) shipping contracts in respect of –
 - (1) earnings from pooling arrangements i.e.
 - (i) agreement between two or more persons for providing services through a pool or
 - (ii) operating one or more ships and sharing earnings or operating profits on the basis of mutually agreed terms;
 - (2) contracts of affreightment i.e. a service contract under which a tonnage tax company agrees to transport a specified quantity of specified products at a specified rate, between designated loading and discharging ports over a specified period.
 - (b) Specific shipping trades, being, -
 - (1) on-board or on-shore activities of passenger ships comprising of fares and food and beverages consumed on board;
 - (2) slot charters, space charters, joint charters, feeder services, container box leasing of container shipping.
- (4) The incidental activities of the tonnage tax company are the activities which are incidental to the core activities and which may be prescribed for the purpose.

20. Computation of taxable wealth of Mr. Suresh as on 31.3.2005

Sl. No.	Description of Assets	Notes	Amount
i)	Motor cars	(a)	10,00,000
ii)	Gold bonds under Gold Deposit Scheme, 1999	(b)	Nil
iii)	Residential House Property – Let-out	(c)	Nil
iv)	Jewellery held	(d)	5,00,000
v)	Lands purchased for industrial purpose	(e)	4,00,000
vi)	Cash on hand	(f)	10,000
vii)	Cash at bank – Not an asset		Nil
viii)	Fixed Assets located in London	(g)	Nil
	Add: Deemed assets u/s.4	(h)	<u>Nil</u>
			19,10,000
	Less: Debts incurred in relation to assets	(i)	<u>3,00,000</u>
	Taxable wealth		<u>16,10,000</u>

Note:

- a) Motor cars held as fixed asset is taxable irrespective of whether it is foreign make or Indian make.
 - b) Gold bonds under Gold Deposit Scheme 1999 are not assets within the meaning of sec. 2(ea).
 - c) Residential house property is let out for more than 300 days during the year 2004-05. Therefore, it is not an asset as provided u/s.2(ea).
 - d) According to Sec.2(ea), jewellery is a taxable asset.
 - e) Any unused land held by the assessee for industrial purposes for a period of 2 years from the date of its acquisition is not an asset chargeable for Wealth tax. In the given case, land purchased on 21.2.2000 is chargeable to tax. On the other hand land purchased on 20.6.2004 is not taxable since the two year period lapses only on 19.6.2006.
 - f) Cash in hand in excess of Rs.50,000 is chargeable to wealth tax.
 - g) According to sec.6, assets owned outside India by an individual who is not ordinarily resident in India is not taxable.
 - h) According to Sec.4, assets transferred to spouse without adequate consideration will have to be clubbed in the hands of the assessee. In the given case Mrs. Suresh invested in shares and residential property out of gifts received from her husband. Shares are not taxable, since they are not assets, whereas, residential property at Pune is taxable. However, the residential property at Pune is eligible for exemption u/s.5.
 - i) Loan against purchase of land is a debt, which is eligible for net off against the respective asset. In this case, land purchased on 20.06.2004 is exempt. Therefore, the debt relating to this asset is not eligible for net off. However, the land purchased on 21.2.2000 is subject to wealth tax and therefore, the corresponding debt can be adjusted.
- 21.** On the basis of the information furnished by Ganesh, the manner in which the assets are to be dealt with for the compilation of his net wealth is indicated here under:
- i) The jewellery gifted to his wife from time to time shall be included in his net wealth under the provisions of sec.4. As regards the value, Rule 18 provides for adopting the market value as on the valuation date and therefore Rs.1.50 lakhs will be included in the net wealth of Ganesh.
 - ii) In the case of any one residential unit which is occupied by the assessee throughout the period of 12 months preceding the valuation date, Rule 3 of Schedule III read with sec.7 provide for pegging down of the value as on the valuation date immediately following the date on which the assessee becomes the owner or on the valuation date 31.3.71, whichever date is later. In this case, Ganesh has purchased the flat in February, 1980 for Rs.5 lakhs and an installment of Rs.70,000/- is still remaining to be paid as on the valuation date. For pegging down the value, the value is required to be computed as per Schedule III. Assuming that the value as on 31.3.1980 is Rs.5 lakhs as per Schedule III, the amount to be considered is Rs.4.30 lakhs (i.e.after reducing the liability incurred in relation to this asset Rs.70,000/-). Ganesh should also note that he is eligible for exemption of one house u/s. 5 of the Wealth Tax Act. He can avail such exemption for this flat.
 - iii) Under the Wealth Tax Act, urban land is an asset which is liable to wealth tax. According to sec.4, the net wealth of a minor child shall be included in the net wealth of a parent, whose net wealth before such inclusion is greater. However, there is an exception where by the net wealth of a minor child suffering from any disability as specified u/s.80U of the Income-tax Act shall not be so included. In such a case, the minor child shall be chargeable to wealth tax in accordance with the provisions of the Wealth Tax Act and the parent shall not be liable. In the case of Ganesh, the urban land is transferred to his minor handicapped child. In view of the exception stated above, the value of the urban land shall not be included in Ganesh's wealth, assuming that the minor child suffers from disability of the nature specified u/s 80U.
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