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PAPER – 7 : DIRECT TAX LAWS

Working notes should form part of the answer.

Question No.1 is compulsory.

Attempt any **five** questions from the remaining **six** questions.

Question 1

- (a) X. Limited has transferred its Unit N to Y. Limited by way of slump sale on November 30, 2011. The summarised Balance Sheet of X. Limited as on that date is given below:

Liabilities	₹ (in lakhs)	Assets	₹ (in lakhs)
Paid up capital	1,700	Fixed Assets :	
Reserve & surplus	620	Unit L	150
Liabilities:		Unit M	150
Unit L	40	Unit N	550
Unit M	110	Other Assets:	
Unit N	90	Unit L	520
		Unit M	800
		Unit N	390
Total	2,560	Total	2,560

Using the further information given below, compute the capital gain arising from slump sale of Unit N and tax on such capital gain.

- (i) Cost inflation index for financial year 2004-05 and financial year 2011-12 are 480 and 785, respectively.
- (ii) Lump sum consideration on transfer of Unit N is ₹ 880 lakhs.
- (iii) Fixed assets of Unit N includes land which was purchased at ₹ 60 lakhs in the year 2004 and revalued at ₹ 90 lakhs as on March 31, 2011.
- (iv) Other fixed assets are reflected at ₹ 460 lakhs (i.e. ₹ 550 lakhs less value of land) which represents written down value of those assets as per books. The written down value of these assets under section 43(6) of the Income-tax Act, 1961 is ₹ 410 lakhs.
- (v) Unit N was set up by X. Limited in July, 2004. (6 Marks)

The Suggested Answers for Paper 7: - Direct Tax Laws are based on the provisions applicable for A.Y. 2012-13, which is the assessment year relevant for November, 2012 examination.

- (b) XYZ Limited purchased a machine on 1st April, 2011 for ₹ 10 crores by availing 70% loan facility from bank. The machine was required for extension of the business of the company and was put to use into effective production on 1st February, 2012. Interest on loan is charged at 12% per annum.

Advise XYZ Limited on the treatment of interest payment made on this loan and depreciation allowable for the Assessment Year 2012-13. Assume that this machine is the only machine in the related block of assets. (4 Marks)

- (c) State with reasons whether the following assets are chargeable to wealth tax under the Wealth-tax Act, 1957:

- (i) Factory building and godown leased out on rent.
- (ii) Silver and gold in the jewellers shop
- (iii) Jewellery purchased by Mr. X, a NRI out of balance lying in his Non Resident External Account on the date of his return to India two years back on permanent basis.
- (iv) Aircraft owned and used by a company for transportation of its goods.
- (v) Life interest in property. (5 Marks)

- (d) State the cases where the Assessing Officer can make an assessment of net wealth to the best of his judgement by exercising his powers under section 16(5) of the Wealth-tax Act, 1957. Is it necessary for the Assessing Officer to issue show cause notice before making such assessment? (5 Marks)

Answer

- (a) **Computation of capital gain on slump sale of Unit N under section 50B**

Particulars	₹ (in lacs)
Sale consideration for the slump sale of Unit N	880
Less: Net worth of Unit N (Refer Note 1 below)	<u>770</u>
Long term capital gain arising on slump sale	<u>110</u>

Computation of tax liability of X Ltd. on slump sale of Unit N

Particulars	₹ (in lacs)
Tax on capital gains@20%	22.00
Add: Surcharge@5%	<u>1.10</u>
	23.10
Add: Education cess@2% and Secondary and higher education cess@1%	<u>0.69</u>
Total tax liability on capital gain arising on slump sale of Unit N	<u>23.79</u>

Notes:

- The net worth of an undertaking transferred by way of slump sale shall be deemed to the cost of acquisition and cost of improvement for the purposes of section 48 and 49 [Section 50B(2)].

Computation of net worth of Unit N :

Particulars	₹ (in lacs)
(A) Book value of non-depreciable assets:	
(i) Land (Revaluation is to be ignored for computing net worth)	60
(ii) Other assets	390
(B) Written down value of depreciable assets under section 43(6)	<u>410</u>
Aggregate value of total assets	860
Less: Value of liabilities of Unit N	<u>90</u>
Net worth of Unit N	<u>770</u>

- Since Unit N is held for more than 36 months, the capital gains of ₹ 110 lacs arising on transfer of such unit would be a long term capital gain taxable under section 112. However, indexation benefit is not available in the case of a slump sale.

(b) (i) Interest on term loan for purchase of machinery

As per section 36(1)(iii), interest paid in respect of capital borrowed for acquisition of an asset for extension of existing business for a period beginning from the date of borrowal of loan for acquiring the asset till the date on which such asset is first put to use is not allowable as deduction. Interest for such period has to be capitalized, by adding the same to the cost of the asset. Therefore, interest@12% p.a. for a period of 10 months from 1st April, 2011 to 31st January, 2012 on ₹ 7 crores, being the amount of loan, has to be capitalized.

	₹
Cost of machinery	10,00,00,000
Add: Interest $[12\% \times 10/12 \times ₹ 7,00,00,000]$	<u>70,00,000</u>
Actual Cost of machinery	<u>10,70,00,000</u>
Interest @12% for two months (February, 2012 & March, 2012) after the asset is put to use is allowable as deduction under section 36(1)(iii) $[12\% \times 2/12 \times ₹ 7,00,00,000]$	14,00,000

(ii) Depreciation

	₹
Since the machinery is put to use for less than 180 days in the previous year 2011-12, the depreciation would be restricted to 50% of the amount calculated at the prescribed percentage of 15%. Therefore, depreciation = 50% × [15% × ₹ 10,70,00,000]	80,25,000
Likewise, the additional depreciation would also be restricted to 50% of the amount calculated at the prescribed percentage of 20%, assuming that XYZ Ltd. is engaged in the manufacture or production of any article or thing and that the machinery acquired is a new machinery. Therefore, additional depreciation = 50% × [20% × ₹ 10,70,00,000]	<u>1,07,00,000</u>
	<u>1,87,25,000</u>

(c) (i) Factory building and godowns leased out on rent

Section 2(ea)(i) of the Wealth-tax Act, 1957 provides for exceptions to the chargeability of building or land appurtenant thereto to wealth-tax. One such exception is the property in the nature of commercial establishments or complexes. Therefore, factory buildings and godowns, being in the nature of commercial establishments or complexes, are not assets within the meaning of section 2(ea)(i) and are accordingly not chargeable to wealth-tax.

(ii) Silver and gold used in the jewellers' shop

Jewellery is considered as an asset within the meaning of section 2(ea) of the Wealth-tax Act, 1957. However, if jewellery is used as stock-in-trade, the same shall be excluded from the assets chargeable to wealth-tax. Therefore, silver and gold used in the jewellers' shop represent his stock-in-trade and would, therefore, not be chargeable to wealth-tax.

(iii) Jewellery purchased by Mr.X, a NRI out of balance lying in his NRE A/c on the date of his return to India two years back on permanent basis

Any asset acquired by Mr.X out of money brought by him into India, within one year immediately preceding the date of his return or at any time thereafter, would be exempt for a period of seven successive assessment years following the year of his arrival in India on a permanent basis. Money standing to the credit of such person in a NRE A/c on the date of his return to India shall be deemed to be money brought by him into India on that date. Therefore, the jewellery acquired by Mr. X out of balance lying in his NRE A/c on the date of his return to India would not be chargeable to wealth-tax for the A.Y.2012-13, since Mr.X has come to India on a permanent basis only two years back.

(iv) Aircraft owned and used by a company for transportation of its goods

The definition of asset under section 2(ea) includes, *inter alia*, aircrafts, other than those used by the assessee for commercial purposes. Aircraft owned and used by a company for transportation of its goods is construed as used for "commercial purposes", since it is used for the business of the company. Hence, such aircraft is not chargeable to wealth-tax.

(v) Life interest in property

If the "property" in question is taxable under the Wealth-tax Act, 1957, then life interest in such property would be valued and charged to wealth-tax in the hands of the assessee who has life interest in such property. If the property is not taxable, then life interest in such property would also not be chargeable to wealth-tax.

(d) (i) The cases where the Assessing Officer can make an assessment of net wealth to the best of his judgment by exercising his powers under section 16(5) are as follows—

- (a) Where a person fails to furnish his return of wealth required to be filed under section 14(1) within the due date, and has also not filed a belated return or a revised return under section 15.
- (b) Where any person, having filed a return, fails to comply with all the terms of a notice issued under section 16(2) for making scrutiny assessment.
- (c) Where the assessee fails to comply with all the terms of a notice issued under section 16(4) for filing a return of net wealth or requiring production of accounts, records, or other documents as the Assessing Officer may require.
- (ii) The Assessing Officer, after taking into account all relevant material which he has gathered, can make a best judgment assessment only after giving the assessee an opportunity of being heard by serving a notice calling upon the assessee to show cause, on a date and time to be specified in the notice, why the assessment should not be completed to the best of his judgment.
- (iii) However, it will not be necessary to give such opportunity where a notice under section 16(4) has already been issued prior to making the best judgment assessment.

Question 2

The Profit & Loss Account of Indian Branch of **Bank of UK**, a bank incorporated in United Kingdom for the year ended 31st March, 2012 shows a net profit of ₹ 60 crores after debiting/crediting the following items:

	Particulars	₹ (in crores)
(i)	Depreciation	10
(ii)	Interest on fixed deposit from which tax was deducted at source	2

	<i>under section 194A, but was deposited in October, 2012</i>	
(iii)	<i>Interest on Government Securities accrued but not due on 31st March, 2012</i>	<i>3</i>
(iv)	<i>Reversal of interest income recognized in the previous year 2010-11 in respect of term loan which was classified as sub-standard asset in that year as per the prudential norms of Reserve Bank of India. The reversal of interest was made on the basis of inspection report of Reserve Bank of India in September, 2011</i>	<i>0.20</i>
(v)	<i>Profit on sale of a vacant land situated in Noida, Uttar Pradesh to a company incorporated in New Zealand pursuant to an agreement entered into in UK for which payment was also made in UK.</i>	<i>5</i>
(vi)	<i>Net depreciation on investments under "held for trading" and "available for sale" categories on lower of cost or market price as per the prudential guidelines of Reserve Bank of India.</i>	<i>12</i>
(vii)	<i>Bad debts written off in respect of advances classified as "loss assets"</i>	<i>13</i>
(viii)	<i>Provision for non-performing assets as per prudential norms of Reserve Bank of India</i>	<i>120</i>
(ix)	<i>Indian Branch's share of executive and general administration expenses as per debit note raised by the Head office.</i>	<i>4</i>

Other relevant information:

- Interest on Government Securities accrued but not due on 31st March, 2011 is ₹5 crores, which was credited to the Profit & Loss Account for the previous year 2010-11.*
- Depreciation allowable under the Income-tax Rules, 1962: ₹12 crores.*
- The assessee was allowed deduction of ₹10 crores for provision for bad debts under section 36(1)(viii) till Assessment Year 2011-12 and it wrote off bad debts for the first time in financial year 2011-12.*
- Interest on sub-standard and doubtful categories of advances not recognised as income as per prudential norms of Reserve Bank of India: ₹15 crores.*
- Land at Noida was acquired by the branch in the financial year 2007-08 at a cost of ₹9 crores. Cost inflation index for financial year 2007-08 and financial year 2011-12 are 551 and 785, respectively.*

Compute the total income and tax payable by the Indian Branch of Bank of UK for the Assessment Year 2012-13 ignoring the applicability of the provision relating to minimum alternate tax. Give explanation for treatment of each item.

(16 Marks)

Answer

**Computation of total income and tax liability of the Indian branch of Bank of U.K. for
A.Y.2012-13**

Particulars	₹ (in crores)	
Profits and Gains of Business or Profession		
Net Profit as per profit and loss account		60.00
<i>Add:</i> Expenses not allowable or treated separately		
Depreciation [Note (i)]	10.00	
Interest on fixed deposit on which tax deducted was deposited after due date of filing of return [Note (ii)]	2.00	
Bad debts [Note (vii)]	13.00	
Provision for non-performing assets [Note (viii)]	120.00	
Head Office expenses [Note (ix)]	4.00	149.00
		209.00
<i>Add:</i> Interest accrued but not due on Government Securities on 31.3.2011, credited to profit and loss account of the P.Y.2010-11, but not treated as income of that year, since such interest is taxable on due basis [Note (iii)]		5.00
		214.00
<i>Less:</i> Income not taxable in this year or under this head		
Interest accrued but not due on Government Securities on 31.3.2012 not to be treated as income of A.Y.2012-13 [Note (iii)]	3.00	
Profit on sale of vacant land [Note (v)]	5.00	8.00
		206.00
<i>Less:</i> Expenses allowable as deduction		
Depreciation allowable under the Income-tax Rules, 1962 [Note (i)]	12.00	
Provision for doubtful debts [Note (viii)]	9.56	
Head office expenses [Note (ix)]	4.00	25.56
Income chargeable under "Profits and Gains of Business or Profession"		180.44
Capital Gains [Note (v)]		
Sale consideration (of vacant land in Noida) (₹ 5 crores + ₹ 9 crores)	14.00	

Less: Indexed cost of acquisition [₹ 9 crores × 785/551]	12.82	1.18
Total Income		181.62
<u>Tax liability</u>		
Tax on capital gains@20% under section 112 [20% × ₹1.18 crores]		0.24
Tax on other income@40% (since it is a foreign banking company) [₹180.44 × 40%]		72.18
		72.42
Add: Surcharge@2%		1.45
		73.87
Add: Education cess@2% and secondary and higher education cess@1%		2.22
Total tax liability		76.09

Notes:

- (i) Depreciation debited in the books of account (i.e., ₹ 10 crores) has to be added back and depreciation calculated as per Income-tax Rules, 1962 (i.e. ₹ 12 crores) is allowable as deduction under section 32.
- (ii) Interest on fixed deposit would be disallowed under section 40(a)(ia) while computing the income of A.Y.2012-13 since tax deducted thereon under section 194A has been deposited after the due date of filing of return of income i.e. 30th September, 2012.
- (iii) Interest on government securities would accrue or arise under the Income-tax Act, 1961 only on the due date when it becomes receivable and not prior to that. Therefore, interest accrued but not due on 31.3.2012, credited to the profit and loss account for the year 2011-12, has to be deducted for computing business income, since such interest is neither received nor receivable during that year.

Likewise, interest accrued but not due on 31.3.2011 and credited to the profit and loss account for the year 2010-11 would not have been included in the total income of the A.Y.2011-12. Such interest accrued but not due as on 31.3.2011 should be included in the total income of the current previous year 2011-12 when it actually becomes receivable.

Therefore, ₹ 3 crores, being interest on government securities accrued but not due as on 31.3.2012, credited to the profit and loss account has to be deducted and ₹ 5 crores, being interest on government securities accrued but not due as on 31.3.2011 has to be added to compute the total income of the bank for A.Y.2012-13, assuming that such interest has fallen due in the F.Y.2011-12.

- (iv) Since the reversal of interest in respect of a term loan classified as a sub-standard asset as per the prudential norms of RBI, has been made on the basis of inspection report of

RBI, the deduction is allowable on the reasoning that reversal of interest partakes the character of loss arising in the normal course of banking business. Since the same has already been debited to profit and loss account, no further adjustment is required in this regard.

- (v) Since land at Noida is held by the company for more than 36 months, it is a long-term capital asset, and the gain arising from sale of such asset is taxable under the head "Capital Gains". Therefore, ₹ 5 crores, being the profit on sale of land credited to the profit and loss account has to be deducted for computing the business income of the bank. The indexed cost of acquisition has to be deducted from the sale consideration of ₹14 crores (₹ 9 crores + ₹ 5 crores) to arrive at the long-term capital gain, which is taxable@20% under section 112.
- (vi) Investments held under "held-for-trading" and "available-for-sale" categories are to be considered as stock-in-trade of the bank even though they are shown under the head "investments" in the balance sheet under the Banking Regulations Act, 1949, as held by Supreme Court in *United Commercial Bank v CIT (1999) 106 Taxman 601*. Hence, loss due to diminution in value of investments is allowed as deduction. As the effect has already been given in the accounts, no further adjustment is required.
- (vii) Section 36(1)(vii) provides that where the actual amount of bad debts exceeds the credit balance in the provision for bad and doubtful debts made under section 36(1)(viiia), such excess bad debts written off can be claimed as deduction. The provision for doubtful debts allowed as deduction under section 36(1)(viiia) till A.Y. 2011-12 is 10 crores and the current year provision is ₹ 9.56 crores. Therefore, since the bad debts of ₹13 crores written off does not exceed the credit balance of ₹ 19.56 (i.e. ₹ 10 crores + ₹ 9.56 crores) crores in provision for bad and doubtful debts, the entire bad debts has to be added back for computing business income.

Note – *The correct accounting treatment, in a case where there is a provision for doubtful debts account, is that the bad debts written off is routed through the provision for doubtful debts account, and only the bad debts in excess thereof is directly charged to the profit and loss account. However, in this question, the bad debts and provision for NPAs as per prudential norms of RBI have been directly debited to profit and loss account. The problem has been solved on the basis of the accounting treatment as given in the question.*

(viii) &

- (ix) Section 36(1)(viiia) restricts the allowability of provision for bad and doubtful debts to 5% of total income (before making any deduction under section 36(1)(viiia) and Chapter VI-A) in case of a bank incorporated outside India. Therefore, ₹ 120 crores, being provision for non-performing assets debited to profit and loss account as per prudential norms of RBI has to be added back. Thereafter, deduction is allowable upto 5% of the total income, after provision of head office expenses under section 44C.

However, head office expenses allowable under section 44C would be the actual expenditure of ₹ 4 crores or 5% of adjusted total income, whichever is lower. Adjusted total income would be the total income after deducting provision for doubtful debts allowable under section 36(1)(viiia).

The total income, before provision for doubtful debts under section 36(1)(viiia) and head office expenses under section 44C is ₹ 195.18 crores.

Let us take the deduction under section 36(1)(viiia) to be X and the deduction under section 44C to be Y.

$$X = \left[\frac{5}{100} \times (195.18 - Y) \right] \text{ or ₹ 120 crores, whichever is lower}$$

$$Y = \left[\frac{5}{100} \times (195.18 - X) \right] \text{ or ₹ 4 crores, whichever is lower}$$

In this case, the value of Y would be ₹ 4 crores. Substituting ₹ 4 crores for Y in the first equation, we can get the figure of X, representing the provision for doubtful debts allowable under section 36(1)(viiia), which would be ₹ 9.56 crores.

- (x) Interest of ₹ 15 crores on sub-standard and doubtful categories of advances is not recognized as income as per prudential norms of RBI. Since there is no real accrual of interest income in the hands of the bank, hence, it would not be chargeable to tax. Since the same has not been credited to profit and loss account, no adjustment is required.

Note – It was so held by the Delhi High Court in *DIT v. Brahmaputra Capital Financial Services Ltd.* (2011) 335 ITR 182. In the said case, the Delhi High Court observed that it was a prudent decision on the part of the assessee that the interest on the non-performing asset, whose recovery was doubtful, was not accounted for in the books of account. Also, the assessee was bound by the RBI guidelines, which required the said treatment of interest income. Therefore, the Court held that there was no real accrual of interest in the hands of the assessee and, hence, it would not be chargeable to tax under section 5.

Question 3

- (a) Mr. A's premises were searched under section 132. During the course of search, certain records belonging to Mr. B were found. Mr. A and Mr. B wish to know from you the consequences. Advise them. (5 Marks)
- (b) ABC LLP, a limited liability partnership in India is engaged in development of software and providing IT enabled services through two units, one of which is located in a notified Special Economic Zone (SEZ) in Chennai. The particulars relating to previous year 2011-12 furnished by the assessee are as follows:

Total Turnover: SEZ unit ₹ 120 lakhs and the other unit ₹ 100 lakhs

Export Turnover: SEZ unit ₹ 100 lakhs and the other unit ₹ 60 lakhs

Profit: SEZ unit ₹ 50 lakhs and the other unit ₹ 40 lakhs.

The assessee has no other income during the year.

- (i) Compute tax payable by ABC LLP for the Assessment Year 2012-13*
- (ii) Will the amount of tax payable change, if ABC LLP is an overseas entity? (6 Marks)*
- (c) KLM Limited has gone for pension scheme referred to in section 80CCD. It contributes 20% of basic salary to the account of each employee under the scheme. Dearness allowance paid is 40% of basic salary. 50% of dearness allowance forms part of pay for retirement benefits. Total basic salary of employees during the year ended 31st March, 2012 amounted to ₹ 100 lakhs. You are a finance executive of the company and get a basic salary of ₹ 20,000 per month and contribute 20% of basic salary to the pension scheme. On these facts:*
 - (i) Compute the amount admissible as deduction under section 36(1)(iva) and the amount inadmissible under section 40A(9) in computation of business income of KLM Limited.*
 - (ii) Explain the tax treatment in your hands. (5 Marks)*

Answer

- (a)** As per the provisions of section 132(4A), where any books of account or other documents, etc. are found in the possession or control of the person who is subject to search, then, it shall be presumed that such books of account or documents, etc., belong to such person. Hence, in the present case the records belonging to Mr. B found in the search of Mr. A's premises, shall be deemed to be of Mr. A.

In such a case, the Assessing Officer can seize such records. However, such records seized shall not be retained by the Assessing Officer for a period exceeding 30 days from the date of order of assessment under section 153A. The Assessing Officer may retain the same for a period exceeding 30 days provided he records the reasons for retaining the same in writing and obtains the approval of Chief Commissioner, Commissioner, Director General or Director for such retention.

However, as per section 153C, where the Assessing Officer is satisfied that any books of account or other documents, etc, seized belong to a person other than the person subject to search under section 132, then the books of account or documents, etc., seized shall be handed over to the Assessing Officer having jurisdiction over such other person and that Assessing Officer shall proceed against such other person and issue such other person notice and assess or reassess his income as per the provisions of section 153A.

Therefore, in the present case, if the Assessing Officer of Mr. A is satisfied that the records belonging to Mr. B found in the course of search have no bearing on the assessment of Mr. A, he shall hand over the same to the Assessing Officer having

jurisdiction over Mr. B. Such Assessing Officer shall proceed with the assessment of Mr. B under section 153A.

Also, penalty for concealment of income under section 271(1)(c) ranging from 100% to 300% may be imposed in case the Assessing Officer is satisfied that the assessee has concealed the particulars of income or has furnished inaccurate particulars of such income.

(b) (i) Computation of total income and tax liability of ABC LLP as per the normal provisions of the Act for A.Y. 2012-13

Particulars	₹ (in lakh)
Business income (before deduction under section 10AA) (₹ 50 lacs + ₹ 40 lacs)	90.00
Less: Deduction under section 10AA	
Profit of unit in SEZ $\times \frac{\text{Export turnover of unit in SEZ}}{\text{Total turnover of unit in SEZ}}$	
= ₹ 50 lacs $\times$ ₹ 100 lacs / ₹ 120 lacs	<u>41.67</u>
Total Income	<u>48.33</u>
Tax on total income @ 30%	14.50
Add: Education cess @ 2% & SHEC @ 1%	<u>0.435</u>
Tax liability (as per normal provisions)	<u>14.935</u>

Computation of Adjusted total income and Alternate Minimum tax of ABC LLP as per the provisions of section 115JC for A.Y. 2012-13

Particulars	₹ (in lakh)
Total income as per the normal provisions	48.33
Add: Deduction under section 10AA	<u>41.67</u>
Adjusted total income	<u>90.00</u>
Tax @ 18.5% of Adjusted total income	16.6500
Add: Education cess @ 2% & SHEC @ 1%	<u>0.4995</u>
Alternate minimum tax as per section 115JC	<u>17.1495</u>

Since the tax payable as per the normal provisions of the Act is less than the alternate minimum tax payable, the adjusted total income shall be deemed to be the total income of ABC LLP and the tax payable for A.Y. 2012-13 shall be ₹ 17.1495 lakh.

- (ii) In case ABC LLP is an overseas entity, the amount of tax payable shall change since the provisions of alternate minimum tax shall not be applicable to an overseas LLP.

The tax would be payable as per the normal provisions of the Act. The tax liability would, therefore, be ₹ 14.935 lakh.

Note - While computing the deduction under section 10AA, it has been assumed that A.Y. 2012-13 falls within first five year period commencing from the year of provision of services by the Unit in SEZ of ABC LLP and therefore, deduction @ 100% of the profit derived from export of such services has been provided.

- (c) (i) **Computation of deduction allowable under section 36(1)(iva) and disallowance under section 40A(9) while computing business income of KLM Ltd.**

Particulars	₹
Basic Salary	1,00,00,000
Dearness Allowance is 40% of basic salary, 50% of which forms part of pay for retirement benefits	<u>20,00,000</u>
Salary for the purpose of section 36(1)(iva) (Basic Salary + DA which forms part of pay for retirement benefits)	<u>1,20,00,000</u>
Actual contribution (20% of basic salary i.e., 20% of ₹ 100 lakh)	20,00,000
Less: Permissible deduction under section 36(1)(iva) (10% of salary computed as above = 10% of ₹ 1,20,00,000 = ₹ 12,00,000)	<u>12,00,000</u>
Excess contribution disallowed under section 40A(9)	<u>8,00,000</u>

- (ii) **Tax treatment in the hands of the finance executive in respect of employer's and own contribution to pension scheme referred to in section 80CCD.**

- (a) Employer's contribution to such pension scheme would be treated as salary since it is specifically included in the definition of "salary" under section 17. Therefore, ₹ 48,000, being 20% of basic salary of ₹ 2,40,000, will be included in salary.
- (b) Own contribution to pension scheme is allowable as deduction under section 80CCD(1). However, the deduction is restricted to 10% of salary. Salary, for this purpose, means basic pay plus dearness allowance, if it forms part of pay for retirement benefits. Therefore, salary for the purpose of deduction under section 80CCD, in this case, would be –

Particulars	₹
Basic salary (₹ 20,000 × 12)	2,40,000
Dearness allowance = 40% of ₹ 2,40,000 = ₹ 96,000	

50% of DA forms part of pay = 50% of ₹ 96,000	<u>48,000</u>
Salary for the purpose of deduction under section 80CCD	<u>2,88,000</u>
Deduction under section 80CCD(1) = 10% of ₹ 2,88,000 (as against actual contribution of ₹ 48,000, being 20% of basic salary of ₹ 2,40,000)	28,800
₹ 28,800 is allowable as deduction under section 80CCD(1). This would be taken into consideration and be subject to the overall limit of ₹ 1 lakh under section 80CCE.	

- (c) Employer's contribution to pension scheme would be allowable as deduction under section 80CCD(2), subject to a maximum of 10% of salary. Therefore, deduction under section 80CCD(2), would also be restricted to ₹ 28,800, even though the entire employer's contribution of ₹ 48,000 is included in salary under section 17.

However, this deduction of employer's contribution of ₹ 28,800 to pension scheme would be outside the overall limit of ₹ 1 lakh under section 80CCE i.e., this deduction would be over and above the other deductions which are subject to the limit of ₹ 1 lakh.

Question 4

Attempt any **four** questions out of the following questions:

- P. Limited has two divisions, engineering division and tea division. It has transferred engineering division to Q. Limited pursuant to a scheme of demerger which satisfies the conditions of section 2(19AA). P. Limited had a debt of ₹ 5 lakhs in engineering division which stood transferred to Q. Limited. The said debt has been written off as bad in the accounts of Q. Ltd. Can Q. Limited claim deduction on account of the bad debt? (4 Marks)*
- A Venture Capital Fund derived income of ₹ 17 lakhs comprising dividend of ₹ 4 lakhs from shares from a Venture Capital Undertaking and interest of ₹ 13 lakhs on loan granted to such undertaking. Mr. G receives income of ₹ 2 lakhs from such fund. Examine the taxability of the sum of ₹ 2 lakhs received by Mr. G. (4 Marks)*
- BCFS Limited is a Non-Banking Financial Company (NBFC). The company has not credited interest of ₹ 30 lakhs due on certain loan accounts which had become non-performing assets in its profit & loss account. As per NBFC Prudential Norms (RBI) Directions, 1998, which is binding on the company, interest or discount or any other charges on non-performing assets shall be recognised as income only when it is actually realised. Can the Assessing Officer make addition of such interest on the ground that the assessee, being a company, follows mercantile system of accounting? (4 Marks)*
- Mr. S, a lawyer by profession, incurred expenditure on his heart surgery. He claimed such expenditure arguing that the repair of vital organ i.e. the heart has directly impacted*

his professional competence as his gross income from profession increased manifold after the surgery, the heart should be treated as a plant and hence such expenses should be allowed under section 31 as current repairs to plant and machinery or section 37(1) as an expenditure incurred wholly and exclusively for the purpose of his profession. Is the claim of Mr. S tenable in law? (4 Marks)

- (e) *Pinewood Hotels and Resorts Limited is engaged in business of owning, operating and managing hotels. The tips are paid by the guests by way of charge to the credit cards in the bills. The company disburses the same to the employees at periodic intervals. Explain with reasons whether the company is responsible for deducting tax at source from disbursement of tips to its employees.* (4 Marks)

Answer

- (a) As per the provisions of section 36(1)(vii), bad debts written off as irrecoverable by the assessee shall be allowed as deduction while computing income under the head "Profit and gains from business or profession" in case such debt has been taken into account in computing the income of the assessee in the current previous year or any of the earlier previous year.

However, as per the Supreme Court's ruling in *CIT v. T. Veerabhadra Rao (1985) 115 ITR 152*, a successor to a business will be entitled to claim an allowance for bad debt under section 36(1)(vii) even though the debt was not incurred by it (i.e., the successor) but was incurred by the predecessor before takeover of the business by the successor.

Therefore, the claim for bad debts will be allowed even if the relevant debt had been taken into account in computing the income of the predecessor only and not in computing income of the successor assessee.

However, it is important that the identity of the business after succession remains the same.

Therefore in the present case, deduction under section 36(1)(vii) on account of bad debts of ₹ 5 lakh shall be allowed to Q. Limited in relation to a debt incurred by P. Limited for the engineering division transferred to Q. Limited, even though the same is not taken into account in computing the income of Q. Limited of the current previous year or any of the earlier previous years, provided the identity of the business in the hands of Q Ltd remains the same.

- (b) As per the provisions of section 115U, income received by a person from investments made in the venture capital fund shall be chargeable to income-tax in the same manner as if it were the income received by such person from an investment made directly in a venture capital undertaking.

The income paid by the venture capital fund shall be deemed to be of the same nature and in the same proportion in the hands of the person receiving such income as it had been received by, or had accrued to, the venture capital fund (VCF) during the previous year.

Therefore, the income of ₹ 2 lacs received by Mr. G from the venture capital fund shall be taxable in his hands as if he has made a direct investment in the venture capital undertaking (VCU).

Amount treated as dividend = ₹ 2,00,000 × 4/17 i.e. ₹ 47,059

Amount treated as interest from investment = ₹ 2,00,000 × 13/17 i.e. ₹ 1,52,941

Both these receipts will be income exempt under section 10(23FB) in the hands of the VCF.

As far as the investor is concerned, dividend will be exempt since the VCU would have paid the DDT on the same.

The interest income would be assessable as "Income from other sources".

- (c) The issue under consideration is whether in the case of an assessee following mercantile system of accounting, the interest from the NPA has in fact accrued to the assessee and whether such interest can be regarded as income accrued under section 5 of the Income-tax Act, 1961.

As per section 145, the income shall be computed in accordance with the method of accounting regularly followed by the assessee. In the case of a NBFC, it is bound by the RBI directives. The classification as NPA is as per prudential norms of the RBI.

In the case of NPAs, the recovery of the principal amount of loan itself is doubtful. Therefore, where the interest was not received on NPAs and possibility of recovery was almost nil, it could not be treated to have accrued in favour of the assessee. Accordingly, the assessee, on the basis of prudence, is justified in not accounting for interest in the books of account on the ground that there is no real accrual of interest from a NPA under section 5.

In the case of *DIT v. Brahmaputra Capital Financial Services Ltd. (2011) 335 ITR 182*, the High Court took a similar view.

Hence the Assessing Officer cannot make an addition on the premise that the company follows mercantile system of accounting.

- (d) The issues under consideration are whether the expenses incurred on heart surgery can be regarded as:
- (a) Current repairs to plant, allowable under section 31 or
 - (b) A revenue expenditure, incurred wholly and exclusively for the purposes of the assessee's profession and hence, allowable under section 37(1).

These issues came up before the Delhi High Court in the case of *Shanti Bhushan v. CIT (2011) 336 ITR 26*, wherein it was observed that to allow the heart surgery expenditure as repair expenses to plant, the heart should have been first included in the assessee's balance sheet as an asset in the previous year and in the earlier years. Also, a value needs to be assigned for the same. The assessee would face difficulty in arriving at the

cost of acquisition of such an asset for showing the same in his books of account. Though the definition of plant under section 43(3) is inclusive in nature but the plant must have been used as a tool for profession, which is not true in case of heart. Therefore, the heart cannot be said to be plant for the business or profession of the assessee. Therefore, the expenditure on heart surgery is not allowable as repairs to plant under section 31.

According to the provisions of section 37(1), *inter alia*, the said expenditure must be incurred wholly and exclusively for the purposes of the assessee's profession. As mentioned above, a healthy heart will increase the efficiency of human being in every field including its professional work. Therefore, there is no direct nexus between the expenses incurred by the assessee on the heart surgery and his efficiency in the professional field. Therefore, the claim for allowing the said expenditure under section 37(1) is also not tenable.

Therefore, applying the rationale of the above court ruling to the case on hand, the claim of S is not tenable in law.

- (e) The liability to deduct tax at source will arise only if the impugned payments disbursed to the employees by the assessee-company are regarded as "Salaries" under section 192.

When the tips were charged from the customers by the employer, the tips went into the receipt of the employer and was subsequently disbursed to the employees. As soon as such amounts were received by the employer, there was an obligation on the part of the employer to disburse them to the rightful persons, namely, the employees. Simultaneously, by virtue of the employer-employee relationship, a vested right accrued to the employee to claim the tips. Therefore, the tips constitute an additional income for the employees and thus, would be taxable under the head "Salaries". Therefore, the company was liable to deduct tax at source from such payments under section 192

This view was taken by the Delhi High Court in the case of *CIT (TDS) v. ITC Ltd [2011] 338 ITR 598*.

However, the liability to deduct tax will arise only if the amount of salaries after considering the permissible deductions, exceed the basic exemption limit in the hands of the recipient of such tips.

Question 5

- (a) *MSO Foundation, a charitable institution set up on 1st April, 2011 and registered under section 12AA with effect from that date, is engaged in providing education in hotel management. The organisation acquires a building for using the same for holding classes and office activities. It has approached you for your opinion on its eligibility to claim the cost of the building and also depreciation thereon in the current year and the subsequent year. Advise the institution indicating the reasons.* (4 Marks)

- (b) *HLI Private Limited is a company with three shareholders H (40%), L (20%) and I on behalf his HUF (40%). I (HUF) is a Hindu Undivided Family whose members are Mr. I, Mrs. I and their two sons, G and J. The company gave a loan of ₹ 9 lakhs to I (HUF) on 30th April, 2011, on which date the accumulated profits of the company was ₹ 6 lakhs. What is the tax consequence of this transaction?* (4 Marks)
- (c) *David, a foreign national and a cricketer came to India as a member of Australian cricket team in the year ended 31st March, 2012. He received ₹ 5 lakhs for participation in matches in India. He also received ₹ 1 lakh for an advertisement of a product on TV. He contributed articles in a newspaper for which he received ₹ 10,000. When he stayed in India, he also won a prize of ₹ 10,000 from horse racing in Mumbai. He has no other income in India during the year.*
- (i) *Compute tax liability of David for Assessment Year 2012-13.*
 - (ii) *Are the income specified above subject to deduction of tax at source?*
 - (iii) *Is he liable to file his return of income for Assessment Year 2012-13?*
 - (iv) *What would have been his tax liability, had he been a match referee instead of a cricketer?* (8 Marks)

Answer

- (a) (i) 15% of income from property held for charitable purposes is exempt from tax under section 11. The remaining 85% of such "income" would be exempt if it is "applied" for charitable purposes in India.
- (ii) There are many court rulings holding that "income" has to be computed in a commercial manner and hence, depreciation on assets used for earning the income in question, will have to be deducted.
- (iii) Application of the amount can be for revenue or capital purposes. As long as the expenditure is incurred out of income earned by the trust and for the purposes of carrying on the objects of the trust, it would be treated as application of income even if such expenditure is for capital purposes. Therefore, since the building is acquired by the organization for holding classes and office activities, which is for the purposes of carrying on the objects of the charitable institution i.e., for providing education in hotel management, the cost of the building would be treated as application of income.
- (iv) A charitable institution can claim depreciation on assets even if the cost of assets has been fully allowed while computing income (as application of income under section 11). Therefore, in this case, the charitable institution can claim the depreciation on building as deduction, even if the entire cost of building is separately treated as application of income.

Note :

- (1) *This view is supported by the Guidance Note issued by the ICAI on Audit of Public Charitable Institutions under the Income-tax Act, 1961. Even where the whole of the capital expenditure has been treated as application of income towards charitable purposes for exemption under section 11, the institution can claim depreciation in respect of the assets used by it for its business on the basis of normal commercial principles.*
 - (2) *A different view was taken by the Kerala High Court in Lissie Medical Institutions v. CIT (2012) 76 DTR (Ker) 377, where it was held that once the capital expenditure has been treated as application of income, the trust is not eligible to claim depreciation on such capital expenditure, in the current year or in the subsequent years.*
- (b) The issue under consideration in this case is whether, where the Karta is a shareholder (on behalf of his HUF) of a company in which public are not substantially interested, the loan advanced by the company to the HUF would constitute deemed dividend under section 2(22)(e) to the extent to which the company possesses accumulated profits.

There are two views on the basis of which this question can be answered.

First view

Section 2(22)(e) would be attracted if the loan is given by a company in which public are not substantially interested to a shareholder, being a person who is the beneficial owner of shares holding not less than 10% of voting power.

On a plain reading of section 2(22)(e), it appears that the said provision would be attracted only if the person to whom the loan is given is a registered shareholder as well as beneficial owner.

If this view is taken, then section 2(22)(e) would not be attracted in this case, since the registered shareholder is Mr. I (on behalf of his HUF), whereas the beneficial owner is his HUF.

Therefore, loan given to the HUF would not be deemed as dividend by applying section 2(22)(e).

Note – *This view was taken by the Supreme Court in Rameshwarlal Sanwamal v. CIT (1980) 122 ITR 1 (SC).*

Second view

Section 2(22)(e) would be attracted if the loan is given by a company in which public are not substantially interested to a shareholder, being a person who is the beneficial owner of shares holding not less than 10% of voting power.

Even though on a plain reading of section 2(22)(e), it appears that the said provision would be attracted only if the person to whom the loan is given is a registered shareholder as well as beneficial owner, the Delhi High Court, in *CIT v. National Travel*

Services (2011) 202 Taxman 327, has taken a view that where loan is given by a company to a firm, being the beneficial owner of shares held in the name of its partners, provisions of section 2(22)(e) would be attracted, since the essential condition to be satisfied is that of beneficial ownership and it is not necessary that the beneficial owner has to be a registered shareholder.

If this view is adopted, then section 2(22)(e) would get attracted in this case. The loan to the HUF, being the beneficial owner, would be deemed as dividend in the hands of the HUF.

It is, however, taxable only to the extent to which the company possesses accumulated profits on the date of loan i.e., in this case, ₹ 6 lakh.

(c) (i) **Computation of tax liability of David for the A.Y.2012-13**

Particulars	₹	₹
Income taxable under section 115BBA		
Income from participation in matches in India	5,00,000	
Advertisement of product on TV	1,00,000	
Contribution of articles in newspaper	10,000	
Total income	6,10,000	
Tax@10% under section 115BBA on ₹ 6,10,000		61,000
Tax@30% under section 115BB on income of ₹ 10,000 from horse races		3,000
		64,000
Add: Education cess@2% and Secondary and higher education cess@1%		1,920
Total tax liability of David for the A.Y.2012-13		65,920

(ii) Yes, the above income are subject to tax deduction at source.

Income referred to in section 115BBA (i.e., ₹ 6,10,000, in this case) is subject to tax deduction at source@10% under section 194E.

Income referred to in section 115BB (i.e., ₹ 10,000, in this case) is subject to tax deduction at source@30% under section 194BB.

Since David is a non-resident, the amount of tax to be deducted calculated at the prescribed rates mentioned above, would be increased by education cess@2% and secondary and higher education cess@1%.

(iii) Section 115BBA provides that if the total income of the non-resident sportsman comprises of only income referred to in that section and tax deductible at source has been fully deducted, it shall not be necessary for him to file his return of income. However, in this case, Mr. David has income from horse races as well.

Therefore, he cannot avail the benefit of exemption from filing of return of income as contained in section 115BBA. Hence, he would be liable to file his return of income for A.Y.2012-13.

- (iv) The Calcutta High Court has, in *Indcom v. CIT (TDS) (2011) 335 ITR 485*, held that match referees do not fall within the meaning of "sportsmen" to attract the provisions of section 115BBA. Therefore, although the payments made to non-resident match referees are "income" which has accrued and arisen in India, the same are not taxable under the provisions of section 115BBA. They are subject to the normal rates of tax.

Particulars	₹
Tax@30% under section 115BB on winnings of ₹ 10,000 from horse races	3,000
Tax on ₹ 6,10,000 at the rates in force	
Upto ₹ 1,80,000	Nil
1,80,000 – 5,00,000 @10%	32,000
5,00,000 – 6,10,000 @ 20%	<u>22,000</u>
	<u>54,000</u>
	57,000
Add: Education cess@2% and secondary and higher education cess@1%	1,710
	58,710

Question 6

- (a) The Assessing Officer completed the assessment of X. Limited for the assessment year 2008-09 under section 143(3) on 30th December, 2010. The Assessing Officer has initiated the proceeding for penalty under section 271(1)(c) on 30th December, 2010. What is the time limit for imposition of such penalty in the following cases:
- X. Limited did not contest the assessment order.
 - X. Limited contested the assessment order by filing appeal to the Commissioner (Appeals). The appeal was dismissed on 30th December, 2011, on which date the Commissioner received the appeal order.
 - The jurisdictional High Court stayed the penalty proceeding on 25th August, 2011 and the Supreme Court vacated the stay on 3rd November, 2011. (5 Marks)
- (b) The Finance Act 2011 has broadened the powers of the Transfer Pricing Officer under section 92CA. Examine the correctness of the statement. (4 Marks)
- (c) Poulomi, a chartered accountant, is presently working in a firm in India. She has received an offer for the post of Chief Financial Officer from a company at Singapore. As per the offer letter, she should join the company at any time between 1st September, 2012 and

31st October, 2012. She approaches you for your advice on the following issues to mitigate her tax liability in India: (4 Marks)

- (i) Date by which she should leave India to join the company;
 - (ii) Direct credit of part of her salary to her bank account in Kolkata maintained jointly with her mother to meet requirement of her family
 - (iii) Period for which she should stay in India when she comes on leave.
- (d) A company which is entitled to claim deduction under section 80-IB has received duty drawback under a scheme framed by the Central Government under the Customs Act, 1962. Can such duty drawback form part of the profit of eligible undertaking for the purpose of deduction under section 80-IB? (3 Marks)

Answer

- (a) Section 275(1) provides for the time limit for imposing penalty. According to this section, the time limit for imposition of penalty under section 271(1)(c) in the following cases would be :

(i) If X. Limited did not contest the assessment order

Where the relevant assessment order is not the subject matter of either appeal or revision, an order imposing penalty shall not be passed -

- (i) after the expiry of the financial year in which the proceedings, in the course of which action for the imposition of penalty has been initiated, are completed, i.e. 31st March, 2011, or
- (ii) six months from the end of the month in which action for imposition of penalty is initiated, i.e. 30th June, 2011

whichever is later.

Therefore, the time limit for imposing penalty in this case would be 30th June, 2011.

(ii) If X. Limited made an appeal to the Commissioner (Appeals) against the assessment order and the appeal was dismissed on 30th December, 2011, on which date the Commissioner received the appeal order

Where the assessment order or other order is the subject matter of an appeal to the Commissioner (Appeals) under section 246A, and the Commissioner (Appeals) passes the order disposing of such appeal, an order imposing penalty shall be passed –

- (a) before the expiry of the financial year in which the proceedings, in the course of which action for imposition of penalty has been initiated, are completed i.e. 31st March, 2011 or

- (b) within one year from the end of the financial year in which the order of the Commissioner (Appeals) is received by the Chief Commissioner or Commissioner i.e. 31st March, 2013,

whichever is later.

Therefore, the time limit for imposing penalty in this case would be 31st March, 2013.

- (iii) If the penalty proceeding is stayed by the High Court on 25th August, 2011 and the stay is vacated by the Supreme Court on 3rd November, 2011.**

As per the provisions of the *Explanation* below section 275(2), the period of stay is to be excluded from the time limit for imposition of penalty. However, in this case, the time limit for imposing penalty would expire on 30th June, 2011, being the date of expiry of six months from the end of the month in which action for imposition of penalty is initiated (since it is later than 31.3.2011, being the date of expiry of the financial year in which the assessment proceedings are completed). The passing of stay order after that date will not have any impact on the time limit for imposing penalty which would be 30th June, 2011.

- (b)** This statement is correct.

The Finance Act, 2011 has expanded the powers of the Transfer Pricing Officer under section 92CA to empower him to -

- (i) determine the arm's length price of other international transactions, identified subsequently in the course of proceedings before him. So far, his powers were restricted to determining the arm's length price of international transactions referred to him by the Assessing Officer.
 - (ii) conduct a survey by exercising the powers conferred upon an income-tax authority under section 133A for the purpose of determining the arm's length price.
- (c)** The following category of individuals will be treated as resident in India only if the period of their stay in India during the relevant previous year is 182 days or more :-
- (a) Indian citizens, who leave India in any previous year, *inter alia*, for purposes of employment outside India, or
 - (b) Indian citizen or person of Indian origin engaged outside India, *inter alia*, in an employment, who comes on a visit to India in any previous year.
 - (i) Since Poulomi is leaving India for the purpose of employment outside India, she will be treated as resident only if the period of her stay during the previous year amounts to 182 days or more. Therefore, Poulomi should leave India on or before 28th September, 2012, in which case, her stay in India during the previous year would be less than 182 days and she would become non-resident for the purpose of taxability in India. In such a case only the income

which accrues or arises in India or which is deemed to accrue or arise in India or received or deemed to be received in India shall be taxable.

The income earned by her in Singapore would not be chargeable to tax in India for A.Y. 2012-13, if she leaves India on or before 28th September, 2012.

- (ii) If any part of Poulomi's salary will be credited directly to her bank account in Kolkata then, that part of her salary would be considered as income received in India during the previous year under section 5 and would be chargeable to tax under Income-tax Act, 1961, even if she is a non-resident. Therefore, Poulomi should receive her entire salary in Singapore and then remit the required amount to her bank account in Kolkata in which case, the salary earned by her in Singapore would not be subject to tax in India.
- (iii) In case Poulomi visits India after taking up employment outside India, she would be covered in the exception provided in (b) above and she will be treated as resident only if the period of her stay during the relevant previous year amounts to 182 days or more.

Therefore, when Poulomi comes India on leave, she should stay in India for less than 182 days during the relevant previous year so that her status remains as a non-resident for the relevant previous year. Moreover, she should not visit India again during the current previous year i.e. P.Y. 2011-12.

- (d) Section 80-IB provides for allowing deduction in respect of profits and gains derived from eligible business of the industrial undertaking.

The issue under consideration is whether duty drawback can be regarded as "profits and gains derived from eligible business of the industrial undertaking".

For a receipt to be treated as having been "derived from" the industrial undertaking, the same should be directly and inextricably connected with the business of the industrial undertaking. The connection should be direct and not remote.

The facts of the case are similar to the facts of the case in *Liberty India v. CIT* (2009) 317 ITR 218, wherein the Supreme Court observed that duty drawback is an incentive which flows from the schemes framed by the Central Government or from the Customs Act, 1962. Profits derived by way of incentives such duty drawback cannot be credited against the cost of manufacture of goods debited in the profit and loss account and they do not fall within the expression "profits derived from industrial undertaking" under section 80-IB. They belong to the category of ancillary profits of such undertaking. Hence, duty drawback receipts cannot form part of the profits derived from the eligible business for the purpose of the deduction under section 80-IB.

Applying the same rationale to the present case, duty drawback would not form part of profit of eligible undertaking for the purpose of deduction under section 80-IB.

Question 7

- (a) If an assessee fails to make a claim for any deduction in the return of income, he loses his opportunity for claiming such deduction at the assessment stage or subsequent stage. Do you agree with the proposition? (4 Marks)

- (b) X and Y are partners of a partnership firm. The Assessing Officer of X is of the opinion that the income returned by X is actually taxable in the hands of Y.

The Assessing Officer, in order to safeguard the interest of the Revenue, assessed the income in the hands of both X and Y. The Assessing Officer recovered the tax due on the same from X and Y. He also imposed penalty under section 271(1)(c) on Y for concealing the same. Comment on the actions of the Assessing Officer. (5 Marks)

- (c) PA Consulting Ltd's total income during the previous year ended 31st March, 2012 is ₹ 10,50,000. Tax deducted at source by different payers amounted to ₹ 24,450 and tax paid in foreign country on a doubly taxed income amounted to ₹ 10,000 for which the company is entitled to relief under section 90 as per the double taxation avoidance agreement.

During the year the company paid advance tax as under:

Date of payment	Advance tax paid (₹)
15-06-2011	40,000
12-09-2011	65,000
15-12-2011	1,00,000
15-03-2012	62,000

The company filed its return of income for the Assessment Year 2012-13 on 15th October, 2012.

Compute interest, if any, payable by the company under sections 234A, 234B and 234C. Assume that transfer pricing provision is not applicable. (7 Marks)

Answer

- (a) (i) As per section 80A(5), where the assessee fails to make a claim in his return of income for any deduction under section 10AA or under any provision of Chapter VIA under the heading "C - Deductions in respect of certain incomes", no deduction shall be allowed to him thereunder at a later stage. However, it can be claimed through a revised return provided the time limit for filing the revised return as mentioned in section 139(5) has not expired.
- (ii) However, the restriction under section 80A(5) is not applicable for other deductions under Chapter VIA or to deductions under any particular head of income.

It may be noted that the Supreme Court in the case of *Goetze India Ltd. v. CIT 284 ITR 323* has held that a fresh claim for deduction can be made before the Assessing Officer only by filing a revised return of income.

The Supreme Court has, however, made it clear that the adjudication was only with reference to the power of the Assessing Officer to entertain a fresh claim for deduction otherwise than through a return of income and does not impinge on the power of the Tribunal under section 254.

Therefore, if an assessee fails to claim a deduction under Chapter VIA other than deductions mentioned in section 80A(5), it

- (1) can be claimed by him by making an application for rectification of a mistake apparent from record under section 154 before an Income-tax Authority or under section 254 before the Appellate Tribunal. The availability of the impugned deduction should be apparent from the details furnished in the return of income or in the statements/details filed in case of assessment under section 143(3).
- (2) can be claimed before Commissioner (Appeals) by raising the additional ground, if the Commissioner (Appeals) is satisfied that such a ground could not have been raised at the time of filing of return or at the time of making of the assessment order and such ground became available because of change in law or change in circumstances.
- (3) can be allowed by the Income-tax Appellate Tribunal even if such an issue was not raised before lower authorities. This can be done *suo moto* or an application made by the assessee.
- (4) can be claimed under section 264 before the Commissioner of Income-tax, if the same has not been allowed by the Assessing Officer.

Therefore, the proposition that **any deduction** not claimed in the return of income, cannot be claimed at the assessment stage or subsequent stage is not true.

- (b) When the ownership of the income is in dispute or is a matter of doubt, it is open to the Assessing Officer to assess a particular income in the case of the person who is considered as liable to tax and include the same income in the case of another person also as a protective measure. Such an assessment is known as protective assessment.

It must, however, be noted that while protective assessment is permissible, a protective order for recovery is not permissible. In making a protective assessment, the authorities are merely making an assessment and leaving it as a paper assessment until the matter is decided one way or another, in further proceedings like appeal or revision.

Further more, a protective order of assessment can be passed but not a protective order of penalty.

Therefore, though the Assessing Officer's action in assessing the income in the hands of both X and Y is valid, the recovery of tax due on the same from X and Y and imposition of penalty under section 271(1)(c) on Y for concealment of income is not valid.

(c) Interest under section 234A

Since the return of income has been furnished by PA Consulting Ltd. on 15th October, 2012 i.e. 15 days after the due date for filing return of income (30.9.2012), interest under section 234A will be payable for 1 month @ 1% on the amount of tax payable on the total income, as reduced by tax reliefs and prepaid taxes.

Particulars	₹
Tax on total income (₹ 10,50,000 x 30.9%)	3,24,450
Less: Advance tax paid	2,67,000
Less: Tax deducted at source	24,450
Less: Relief of tax allowed under section 90	<u>10,000</u>
Tax payable on self assessment	<u>23,000</u>
Interest = ₹ 23,000 x 1% = ₹ 230	

Interest under section 234B

Where the advance tax paid by the assessee is less than 90% of the assessed tax, the assessee would be liable to pay interest under section 234B.

Computation of Assessed tax:	₹
Tax on total income (₹ 10,50,000 x 30.9%)	3,24,450
Less: Tax deducted at source	24,450
Less: Relief of tax allowed under section 90	<u>10,000</u>
Assessed tax	<u>2,90,000</u>
90% of assessed tax = ₹ 2,90,000 x 90% = ₹ 2,61,000	

Since the advance tax paid by PA Consulting Ltd. (₹ 2,67,000) is more than 90% of the assessed tax (₹ 2,61,000), it is not liable to pay interest under section 234B.

Interest under section 234C

Particulars	₹
Tax on total income (₹ 10,50,000 x 30.9%)	3,24,450
Less: Tax deducted at source	24,450
Less: Relief of tax allowed under section 90	<u>10,000</u>
Tax due on returned income/Total advance tax payable	<u>2,90,000</u>

Calculation of interest payable under section 234C:

Date (a)	Advance tax paid till date (b) (₹)	Minimum % of tax due on returned income to be paid till date to avoid interest under section 234C (c)		Advance tax payable till date in case condition mentioned in (c) is not met	Shortfall (₹)	Interest (₹)
		%	Amount (₹)			
15.06.2011	40,000	12%	34,800	15%	-	Nil (See Note below)
15.09.2011	1,05,000	36%	1,04,400	45%	-	Nil (See Note below)
15.12.2011	2,05,000	75%	2,17,500	75%	12,500	$12,500 \times 1\% \times 3$ months = 375
15.03.2012	2,67,000	100%	2,90,000	100%	23,000	$23,000 \times 1\%$ = 230
Interest payable under section 234C						605

Note: Since the advance tax paid by PA Consulting Ltd. on 15th June, 2011 is more than 12% of the tax due on returned income (i.e. ₹ 2,90,000) and the advance tax paid on 12th September, 2011 is more than 36% of the tax due on returned income, it is not liable to pay any interest under section 234C in respect of these two quarters.