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PAPER – 4 : TAXATION

Question No.1 is compulsory.

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

Wherever required, suitable assumptions may be made and disclosed by way of a note.

Working notes should form part of the answer.

All questions pertaining to Income-tax relate to assessment year 2013-14, unless stated otherwise in the question.

Question 1

- (a) Mrs. Rani a resident aged 50 years is running an acupuncture clinic. Her Income and Expenditure Account and other relevant information for the year ending 31st March, 2013 are given below:

Expenditure	Amount (₹)	Income	Amount (₹)
To Staff Salary	2,40,000	By Fees receipts	10,00,000
To Clinic rent	1,20,000	By Dividend from Indian Companies	10,500
To Medicines and needles	1,05,000	By Winning from Lotteries	7,000
To Depreciation	81,000	Net of TDS (TDS ₹3,000)	1,750
To Administrative expenses	1,52,000	By Income-tax Refund	
To Donation to Prime Minister's National Relief Fund	20,000		
To Excess of Income over Expenditure	3,01,250		
	10,19,250		10,19,250

- (i) Depreciation in respect of all assets has been ascertained at ₹ 60,000 as per Income-tax Rules, 1962.
- (ii) Medicines and needles of ₹ 22,000 have been used for her family.
- (iii) Fees receipts include ₹ 24,000, being honorarium for valuing acupuncture examination answer books.
- (iv) She has also received ₹ 57,860 on maturity of one LIC Policy, not included in the above Income and Expenditure Account.

The Suggested Answers for Paper 4: Taxation are based on the provisions of law as amended by the Finance Act, 2012 and applicable for A.Y. 2013-14 (in the case of Income-tax), which is the assessment year relevant for May, 2013 examination.

(v) She has paid an LIC premium of ₹12,000 for self (Sum Assured ₹50,000).

(vi) She has paid ₹2,500 for purchase of lottery tickets.

From the above, compute the total income and tax payable thereon of Mrs. Rani for the Assessment year 2013-14. (10 Marks)

- (b) Q Ltd. is engaged in providing the taxable services. Ascertain the amount of service tax payable by it in the month of September, 2012 from the information given below:

Particulars	Amount (₹)
Supply of farm labour for agriculture purpose	1,00,000
Service to people free of cost	60,000
Advance received in September, 2012 from clients for which no services has been rendered till date	85,000
Amount received for the services rendered in June, 2012 (bills for the same were issued on 25 th June, 2012)	90,000
Bill raised for the services rendered in the month of September, 2012 against which no amount is received so far.	75,000

The above amounts are exclusive of service tax. Q. Ltd. is not eligible for small service provider's exemption in the financial year 2012-13. (5 Marks)

The rate of service tax is 12% Education Cess is 2% and Higher Education cess is 1%.

- (c) Mr. Bansilal of Punjab is a manufacturer, registered under VAT. He provides the following particulars for the financial year 2012-13.

		₹
1.	Purchases from local registered dealer (excluding VAT 4%)	1,15,000
2.	Purchases from a dealer having opted composition scheme (includes VAT 4%)	2,20,000
3.	Purchases of machinery eligible for input credit on 1-10-2012 (excluding VAT 4%) Depreciation rate 15% p.a.	5,00,000
4.	Other direct & indirect expenses – 30% of total purchases (excluding depreciation)	
5.	Profit margin – 20% of the total cost.	
6.	Unutilized balance of VAT input credit as on 1-4-2012.	7,500
7.	90% of the production is sold during the year.	
8.	VAT rate for sales is 12.5%	

Find the taxable turnover, net VAT payable and input credit for the year 2012-13. (5 Marks)

Answer**(a) Computation of total income and tax liability of Mrs. Rani for the A.Y. 2013-14**

Particulars	₹
Income from business (Working Note – 1)	3,21,000
Income from other sources (Working Note – 2)	<u>34,000</u>
Gross Total Income	3,55,000
Less: Deduction under Chapter VI-A (Working Note – 3)	<u>25,000</u>
Total Income	<u>3,30,000</u>
Tax on total income (Working Note - 4)	15,000
Add: Education cess @ 2% and SHEC @1%	<u>450</u>
Total tax liability	15,450
Less: Tax deducted at source (TDS)	<u>3,000</u>
Tax payable	<u>12,450</u>

Working Notes:**1. Computation of income under the head “Profits and gains of business or profession”**

Particulars	₹	₹
Net Income as per Income and Expenditure Account		3,01,250
Add: Expenses disallowed:		
Depreciation (81,000 - 60,000)	21,000	
Cost of medicines etc. for personal use	22,000	
Donation to Prime Minister's Relief Fund	<u>20,000</u>	<u>63,000</u>
		3,64,250
Less: Income not taxable/exempt under the Income-tax Act, 1961/ Income not taxable under this head		
Dividend from Indian companies	10,500	
Income-tax refund	1,750	
Winning from Lotteries	7,000	
Honorarium for valuing answer books	<u>24,000</u>	<u>43,250</u>
Income under the head “Profits and gains of business or profession”		<u>3,21,000</u>

2. Computation of income under the head “Income from other sources”

Particulars	₹	₹
Dividend from Indian Companies [Exempt u/s 10(34)]		-

Honorarium for valuing answer books		24,000
Winning from Lotteries (Net)	7,000	
Add: TDS	<u>3,000</u>	<u>10,000</u>
Income from other sources		<u>34,000</u>

Note - As per section 58(4), no deduction in respect of any expenditure or allowance is allowable in respect of winnings from lotteries. Hence, ₹ 2,500 paid for purchase of lottery tickets is **not** allowable as deduction.

3. Computation of deduction under Chapter VI-A

Particulars	₹
U/s 80C Life Insurance Premium (maximum 10% of sum assured)	5,000
U/s 80G Donation to Prime Minister's Relief Fund [100% deduction without qualifying limit]	<u>20,000</u>
Total deduction under Chapter VI-A	<u>25,000</u>

4. Computation of tax on total income

Particulars	₹
Tax on winnings from lotteries [₹ 10,000 @ 30%]	3,000
Tax on balance income of ₹ 3,20,000 [10% of (₹ 3,20,000 – ₹ 2,00,000, representing the basic exemption limit)]	<u>12,000</u>
Tax on total income	<u>15,000</u>

5. Maturity proceeds of life insurance policy

Any sum received under a life insurance policy is wholly exempt from tax under section 10(10D).

Note: The above solution has been worked out on the basis of the following assumptions:

- (1) The life insurance policy, in respect of which premium of ₹ 12,000 is paid, is issued on or after 1st April, 2012. Hence, deduction under section 80C has been restricted to 10% of actual capital sum assured.
- (2) The maturity proceeds of LIC have been taken as exempt under section 10(10D) presuming that the premium paid during any of the years of the policy does not exceed the specified percentage of the actual capital sum assured.

(b) Computation of service tax payable by Q Ltd. :

Particulars	Amount (₹)
Supply of farm labour for agricultural purpose (Note-1)	Nil
Services to people free of cost (Note-2)	Nil
Advances received in September, 2012 from clients for which no service has been rendered till date (Note-3)	85,000
Amount received for the services rendered in June, 2012 (Note-4)	Nil
Bills raised for the services rendered in the month of September, 2012 against which no amount is received so far (Note-5)	<u>75,000</u>
Value of taxable services	<u>1,60,000</u>
Service tax @ 12% = ₹1,60,000 × 12%	19,200
Education cess @ 2% = ₹19,200 × 2%	384
Secondary and higher education cess @ 1% = ₹19,200 × 1%	<u>192</u>
Service tax payable	<u>19,776</u>

Notes:

1. Services relating to agriculture or agricultural produce by way of supply of farm labour are included in the negative list of services. Hence, they are not taxable.
2. Service tax is chargeable on the value of service. Thus, service tax is not payable in case of free services as there is no consideration in such a case.
3. Point of taxation in case of receipt of an advance is the date of receipt of each such advance.
4. Since, point of taxation (POT) for a service is the date of issue of invoice or receipt of payment, whichever is earlier, POT for services rendered in June, 2012 would be June 25, 2012. Hence, receipts of ₹90,000, having been already charged to service tax in the month of June, 2012, will not be chargeable to service tax again in September, 2012.
5. Since, POT for a service is the date of issue of invoice or receipt of payment, whichever is earlier, bills raised for the services rendered in the month of September, 2012 would be chargeable to service tax in the month of September, irrespective of no amount, in relation to the same, being received so far.

(c) Computation of input tax credit for the year 2012-13:

Input tax credit	Amount (₹)
Unutilized balance of VAT input credit as on 01.04.2012	7,500
Add : VAT @ 4% on purchases from local registered dealer	

$= ₹1,15,000 \times \frac{4}{100}$	4,600
Add : Purchases from a dealer having opted composition scheme [Purchases made from composition dealers are not eligible for input tax credit]	Nil
Add : VAT @ 4% on purchases of machinery eligible for input tax credit $= ₹ 5,00,000 \times \frac{4}{100}$ [It has been assumed that entire VAT credit can be availed during year 2012-13]	<u>20,000</u>
Input tax credit available for the year 2012-13	<u>32,100</u>

Computation of taxable turnover and net VAT payable for the year 2012-13:

Particulars	Amount (₹)
Purchases from local registered dealer	1,15,000
Add : Purchases from a dealer having opted composition scheme	2,20,000
Add: Depreciation on the machinery for the half year $₹ 5,00,000 \times \left[\frac{15}{100} \times \frac{1}{2} \right]$ [Depreciation cannot be claimed on the value of VAT]	37,500
Add: Direct and indirect expenses = 30% of ₹ 1,15,000 + ₹ 2,20,000 + ₹ 5,00,000]	<u>2,50,500</u>
Total cost	<u>6,23,000</u>
Profit @ 20% of the total cost	1,24,600
Production during the year	<u>7,47,600</u>
Taxable turnover [90% of the production]	<u>6,72,840</u>
Output VAT payable @ 12.5%	84,105
Less: Input tax credit available (computed in the above table)	32,100
Net VAT payable	52,005

Question 2

- (a) Devesh and Siddhant are brothers and they earned the following incomes during the financial year 2012-13. Devesh settled in America in the year 1985 and Siddhant settled in Mumbai. Devesh visits India for 20 days every year. Siddhant also visits America

every year for a month. Compute their total income for the Assessment year 2013-14 from the following information.

Sl. No.	Particulars	Devesh ₹	Siddhant ₹
1.	Interest on American Development bonds, 50% of interest received in India.	46,000	18,000
2.	Dividend from a Japanese Company received in America.	10,000	15,000
3.	Profit on sale of shares of an Indian company received in India	45,000	75,000
4.	Profit from a business in Mumbai, but managed directly from America.	10,000	-
5.	Income from a business in Mumbai.	32,000	28,000
6.	Fees for technical services rendered in America and received in America. The services were, however, utilized in India	1,50,000	-
7.	Interest on savings bank deposit in State Bank of India, Mumbai	4,500	12,000
8.	Rent received in respect of house property at Mumbai.	96,000	55,000
9.	Life Insurance Premium paid.	-	25,000

(8 Marks)

(b) What is "Negative list of services"? Which services by Government or a local authority are not included in the negative list of services? (4 Marks)

(c) One of the merits of VAT is 'Neutrality'. Explain (4 Marks)

Answer

(a) Computation of total income of Devesh & Siddhant for the A.Y. 2013-14

S. No.	Particulars	Devesh (₹)	Siddhant (₹)
		(Non-Resident)	(Resident)
1.	Interest on American Development Bonds (See Note 2)	23,000	18,000
2.	Dividend from Japanese Company received in America (See Note 4)	-	15,000
3.	Profit on sale of shares of an Indian company received in India (See Note 2)	45,000	75,000
4.	Profit from a business in Mumbai but managed directly from America (See Note 2)	10,000	-
5.	Income from a business in Mumbai (See Note 2)	32,000	28,000

6.	Fees for technical services rendered in America, and received in America, but services utilized in India (See Note 3)	1,50,000	-
7.	Interest on savings bank deposit in State Bank of India, Mumbai (See Note 2)	4,500	12,000
8.	Income from house property at Mumbai (See Note 5)	67,200	38,500
	Gross Total income	3,31,700	1,86,500
	Less: Deduction under Chapter VI-A		
	Section 80C - Life insurance premium paid	-	25,000
	Section 80TTA (See Note 6)	4,500	10,000
	Total Income	3,27,200	1,51,500

Notes:

- Devesh is a non-resident since he has been living in America since 1985. Siddhant, who is settled in Mumbai, is a resident.
- In case of a resident, his global income is taxable as per section 5(1). However, as per section 5(2), in case of a non-resident, only the following income are chargeable to tax:
 - Income received or deemed to be received in India during the previous year; and
 - Income accruing or arising or deemed to accrue or arise in India during the previous year.

The income referred to in Sl. No. 3, 4, 5 and 7 are taxable in the hands of both Devesh and Siddhant, since they accrue or arise in India.

Interest on American Development Bonds would be fully taxable in the hands of Siddhant, whereas only 50% which is received in India is taxable in the hands of Devesh.

- Income by way of fees for technical services rendered outside India and received outside India, would be deemed to accrue and arise in India in the case of a non-resident, if the services are utilised in India. Such income would, accordingly be included in the total income of Devesh.
- Dividend received from Japanese company in America by Devesh is not taxable since it accrues and is received outside India. However, dividend received by Siddhant is taxable, since he is a resident. Exemption under section 10(34) would not be available in respect of dividend received from a foreign company.

5. Income from house property	Devesh	Siddhant
	(₹)	(₹)
Rent received	96,000	55,000

Less: Deduction under section 24@ 30%	<u>28,000</u>	<u>16,500</u>
Net income from house property	<u>67,200</u>	<u>38,500</u>

The net income from house property in India would be taxable in the hands of both Devesh and Siddhant, since the accrual and receipt of the same are in India.

6. In case of an individual, interest upto ₹ 10,000 from savings account with, *inter alia*, a bank is allowable as deduction under section 80TTA.

Note - The above solution has been worked out on the basis of the following assumptions:

- (i) The profit on sale of shares of an Indian company is not exempt under section 10(38).
- (ii) Life insurance premium paid is fully allowable as deduction under section 80C on the assumption that the same is within the limit of 10% or 20% of actual capital sum assured, as the case may be (20%, in case the policy is issued before 1.4.2012 and 10% if the policy is issued on or after 1.4.2012).
- (iii) The savings bank deposit is not a time deposit with a bank.
- (iv) Rent received has been taken as the annual value in the absence of other information relating to municipal value, fair rent and standard rent.

- (b) The seventeen services which are specified in section 66D of the Finance Act, 1994, are termed as 'Negative List of services'. Section 66B, the charging section of the Finance Act, 1994, *inter alia*, provides that service tax shall be levied on all services, except the services specified in the negative list. Hence, all the services covered in the Negative list of services are not chargeable to service tax. The 'Negative List' is of paramount importance because every activity not covered under this list is chargeable to service tax.

The following services provided by the Government or a local authority to the extent they are not covered elsewhere are excluded from the negative list of services:-

- (i) Services by the Department of Posts by way of speed post, express parcel post, life insurance, and agency services provided to a person other than Government;
 - (ii) Services in relation to an aircraft or a vessel, inside or outside the precincts of a port or an airport;
 - (iii) Transport of goods or passengers; or
 - (iv) Support services, other than services covered under clauses (i) to (iii) above, provided to business entities.
- (c) The greatest advantage of VAT system is that it does not interfere in the choice of decision for purchases. This is because the system has anti-cascading effect. How much value is added and at what stage it is added in the system of production/distribution is of no consequence. The system is neutral with regard to choice of production technique, as well as business organization.

All other things remaining the same, the issue of tax liability does not vary the decision about the source of purchase. VAT facilitates precise identification and rebate of the tax on purchases and thus ensures that there is no cascading effect of tax. In short, the allocation of resources is left to be decided by the free play of market forces and competition.

Question 3

- (a) (i) *Rajesh went to Shrinagar on a holiday on 15.11.2012 with his wife and two children (one son – age 6 years; twin daughters – age 3 years). They went by aeroplane (economy class) and the total cost of tickets by his employer was ₹ 58,000 (₹ 43,000 for adults and ₹ 15,000 for the three minor children). Compute the amount of Leave Travel Concession exempt.*
- Will the answer be any different if, among his three children, the twins are 6 years old and son 3 years old? Discuss.* (4 Marks)
- (ii) *Mr. Gobind received retrenchment compensation of ₹ 10,00,000 after 30 years 4 months of service. At the time of retrenchment, he was receiving basic salary of ₹ 20,000 p.m. and dearness allowance of ₹ 5,000 p.m. Compute his taxable retrenchment compensation.* (4 Marks)
- (b) *What is meant by EASIEST scheme? Enlist the benefits of EASIEST scheme to an assessee under the service tax provisions.* (4 Marks)
- (c) *Seth Traders, a registered dealer of Bihar having stock of goods worth ₹ 60,000 purchased from West Bengal wishes to opt for composite scheme. Advise the dealer whether it is possible?* (4 Marks)

Answer

- (a) (i) Section 10(5) exempts the leave travel concession received by an employee from his employer for himself and his family which includes, *inter alia*, his spouse and children, in connection with proceeding on leave to any place in India. The exemption is not available to more than two surviving children of an individual. However, this restriction shall not apply in case of multiple births on the second occasion (i.e., after the first child).

In the present case, Mr. Rajesh can avail exemption for all his three children since the son's age is more than the age of his twin daughters. The holiday being in India and the journey being performed by air (economy class), the entire reimbursement of ₹ 58,000 towards leave travel concession met by the employer is fully exempt under section 10(5).

However, if the twins' age is more than the age of the son, Mr. Rajesh cannot avail exemption for all his three children. The exemption in respect of leave travel concession under section 10(5) can be availed in respect of only two children.

The taxable leave travel concession, in this case, will be ₹ 5,000, being one-third of ₹ 15,000.

The leave travel concession exempt under section 10(5), in such a case, would be ₹ 53,000 (₹ 58,000 - ₹ 5,000)

- (ii) As per section 10(10B), exemption available to Mr. Gobind in respect of retrenchment compensation, in this case, will be the least of the following limits:

Compensation actually received = ₹ 10,00,000

Statutory limit = ₹ 5,00,000

Amount calculated in accordance with the provisions of section 25F of the Industrial Disputes Act, 1947

$$\frac{15}{26} \times \frac{(20,000 \times 3) + (5,000 \times 3)}{3} \times 30 \text{ years}^1 = ₹ 4,32,692$$

Therefore, ₹ 4,32,692, being the least of the above limits, would be exempt under section 10(10B).

The taxable retrenchment compensation will be :

Retrenchment compensation received ₹ 10,00,000

Less: Exemption under section 10(10B) ₹ 4,32,692

Taxable Retrenchment Compensation ₹ 5,67,308

- (b) EASIEST stands for Electronic Accounting System in Excise and Service Tax. This scheme makes tax payment easy and is available with 28 banks.

The benefits of EASIEST scheme to an assessee under the service tax provisions are as follows:-

- (i) Only one copy of the challan is to be filled instead of four copies as required earlier.
 - (ii) EASIEST facilitates online verification of the status of tax payment using Challan Identification Number.
- (c) As per the principles laid down in the White Paper, a dealer desirous of availing the benefits of VAT Composition Scheme should not have stock of the goods purchased from outside the State. Therefore, if the dealer wishes to avail the benefit of the scheme, he must ensure that he does not possess stock of such goods as on the date of exercise of option.

¹ 30 years refer to the completed years of service. The remaining 4 months are not considered, since only part of a year in excess of 6 months has to be considered in such computation.

Hence, it is not possible for Seth Traders, a registered dealer of Bihar, to opt for the composition scheme as it has a stock of goods worth ₹ 60,000 purchased from West Bengal (State other than the State of Bihar) on the day it wishes to opt for the composition scheme.

Question 4

- (a) From the following information of Mr. Mohit for the financial year 2012-13, you are required to compute his total income for the financial year 2012-13 and ascertain the amount of losses which will be carried forward to next year.

		₹
(i)	He owns two houses:	
	House No. 1 – Income after all statutory deductions	80,000
	House No. 2 – Current year loss	(38,000)
(ii)	He has three proprietary business concerns:	
	(a) Textile Business:	
	(i) Discontinued from 30 th September 2012 – Current year's loss	40,000
	(ii) Brought forward loss of A.Y. 2009-10	95,000
	(b) (i) Chemical Business – since discontinued	Nil
	(ii) Bad debts allowed in earlier years recovered during the year	35,000
	(iii) Brought forwarded business loss of A.Y. 2011-12	50,000
	(c) Leather Business – Profit for the current year	1,00,000
	(d) Share of profit in a firm in which he is partner since 2001	16,550
(iii)	(a) Short term capital gain	60,000
	(b) Long term capital loss	35,000
(iv)	Contribution to LIC towards premium	10,000

(8 Marks)

- (b) State with reasons whether the following statements are correct or incorrect under the service tax provisions:
- Mr. P provides the service in March, 2012. He receives the payment by cheque on 30-3-2012 and the cheque is cleared on 15-4-2012. The point of taxation of this service will be 30-3-2012 and the rate of service tax will be 10%.
 - Postal services for registered post are liable to service tax.
 - M/s SR Brothers having office in Jammu, provide the services to M/s QR Ltd. in Patna. These services are not liable to service tax.

(4) Jaipur Branch of ABC Ltd. provides services to Baroda Branch of ABC Ltd. These services are not liable to service tax. (4 Marks)

(c) Discuss the provisions of VAT for 'stock transfer'. (4 Marks)

Answer

(a) **Computation of total income of Mr. Mohit for the A.Y. 2013-14**

Particulars	₹	₹
1. Income from house property		
House No.1	80,000	
House No.2	(-) <u>38,000</u>	42,000
2. Profits and gains of business or profession		
Profit from leather business	1,00,000	
Less: Current year loss of textile business	(-) <u>40,000</u>	
	60,000	
Bad debts (allowed as deduction in earlier year) recovered during the year is taxable under section 41(4)	<u>35,000</u>	
	95,000	
Less: Brought forward business loss of textile business for A.Y.2009-10 set off against the business income of current year	<u>95,000</u>	Nil
3. Capital Gains		
Short-term capital gains		<u>60,000</u>
Gross Total Income		1,02,000
Less: Deduction under Chapter VI-A		
Under section 80C – LIC premium paid		<u>10,000</u>
Total Income		<u>92,000</u>

Losses to be carried forward to A.Y. 2014-15

Particulars	₹
Business loss of discontinued chemical business of A.Y. 2011-12 to be carried forward under section 72	50,000
Long term capital loss of A.Y. 2013-14 to be carried forward under section 74 (Note 2)	35,000

Notes:

- (1) Share of profit from firm of ₹ 16,550 is exempt under section 10(2A) in the hands of the partner, Mr. Mohit.
- (2) Long-term capital loss cannot be set-off against short-term capital gains. Therefore, it has to be carried forward to the next year to be set-off against long-term capital gains of that year. It can be carried forward for a maximum of 8 assessment years.

Note: The above solution has been worked out on the basis of the following assumptions:

- (1) The current year loss of ₹ 38,000 is respect of House No. 2 is the computed loss after deduction of municipal tax, interest and 30% of Net Annual Value.
- (2) Life insurance premium paid is fully allowable as deduction under section 80C on the assumption that the same is within the limit of 10% or 20% of actual capital sum assured, as the case may be (20% if the policy is issued before 1.04.2012 and 10% if the policy is issued on or after 1.04.2012).

- (b) 1. **The statement is not correct.** Service tax rate was increased from 10% to 12% with effect from April 1, 2012. It has been assumed that the invoice for the service has been issued post change in effective rate of tax [on or after 01.04.2012]. Since the cheque received on 30.03.2012 (before change in effective rate, viz. 01.04.2012) has been credited in bank on 15.04.2012 (after 4 working days from 01.04.2012), date of payment shall be the date of credit in the bank account, viz. 15.04.2012.

In case a taxable service has been provided before the change in effective rate of tax, and the invoice for the same has been issued and the payment received after the change in effective rate of tax, the point of taxation will be:

(a) date of payment (15.04.2012)

or

(b) date of issuing of invoice (post change in effective rate of tax)

whichever is earlier (not 30.3.2012).

Moreover, the rate of service tax would be the new rate i.e. 12% and not 10%.

Note: In case it is assumed that the invoice has been issued on 30.03.2012, the above statement would be correct. However, in case it is assumed that the invoice has been issued on any date before 01.04.2012 but not on 30.03.2012, above statement would be incorrect. .

- (2) **The statement is not correct.** Postal services relating to registered post are not liable to service tax because such services are included in the negative list of services.

- (3) **The statement is not correct.** Though M/s SR Brothers have office in Jammu (non-taxable territory), the services provided by them to M/s QR Ltd. in Patna would be liable to service tax as service tax is levied on all taxable services provided in the taxable territory (Patna).
- (4) **The statement is correct.** Services provided by the Jaipur Branch of ABC Ltd. to its Baroda Branch are not liable to service tax. Since both the branches of ABC Ltd. are located in the taxable territory, they cannot be treated as establishments of distinct persons and services provided to oneself are not taxable.
- (c) Inter-State transfers do not involve sale and, therefore they are not subjected to sales-tax. The same position continues under VAT.

However, the tax paid on:

- (i) inputs used in the manufacture of finished goods which are stock transferred; or
- (ii) purchases of goods which are stock transferred

will be available as input tax credit after retention of 2% of such tax by the State Governments.

Question 5

- (a) Mr. A is an employee of Larsen Limited and has substantial interest in the company. His salary is ₹ 25,000 p.m. Mrs. A also is working in that company at a salary of ₹ 10,000 p.m. without any professional qualification.

Mr. A also receives ₹ 30,000 as income from securities. Mrs. A owns a house property which she has let out. Rent received from such house property is ₹ 12,000 p.m.

Mr. & Mrs. A have three minor children - two twin daughters and one son. Income of the twin daughters is ₹ 2,000 p.a. and that of his son is ₹ 1,200 p.a. Compute the income of Mr. and Mrs. A. (8 Marks)

- (b) ABC & Co. is a partnership firm engaged in the business of recruitment and supply of labourers. The firm, which had rendered taxable services to the tune of ₹ 30 lacs in the financial year 2011-12, furnishes the following details pertaining to the half year ended on 30-9-2012: (4 Marks)

Sl. No.	Particulars	₹
1.	Amounts collected from companies for pre-recruitment screening.	3,00,000
2.	Amount collected from companies for recruitment of	
	- Permanent staff	1,80,000
	- Temporary staff	4,50,000
3.	Advances received from prospective employers for conducting campus interviews in colleges.	80,000

Wherever applicable, service tax has been charged separately and received from clients.

Compute the value of taxable services rendered and the service tax payable by the assessee for the relevant half year. The rate of service tax is 12%, education cess is 2% and higher education cess is 1%.

- (c) Manufacturer A sold product X to B of Delhi @ ₹1,000 per unit. He has charged CST @ 4% on the said product and paid ₹ 60 as freight. B of Delhi sold goods to C of Delhi @ ₹ 1,250 per unit and charged VAT @ 12.5% C of Delhi sold goods to D, a consumer @ ₹ 1,500 per unit and charged VAT @ 12.5%.

Compute VAT Liability of B & C.

(4 Marks)

Answer

- (a) **Computation of Total Income of Mr. A and Mrs. A for the A.Y. 2013-14**

Particulars	Mr. A (₹)	Mrs. A (₹)
Income from Salaries		
Salary income of Mr. A (₹ 25,000 × 12)	3,00,000	
Salary income of Mrs. A (₹ 10,000 × 12) (See Note 1)	1,20,000	
Income from House Property		-
Rent received (₹ 12,000×12)	1,44,000	
Less: Deduction under section 24@30%	<u>43,200</u>	1,00,800
Income from other sources		
Income from securities	30,000	
Income before including income of minor children under section 64(1A) (See Note 2)	4,50,000	1,00,800
Income of twin daughters ₹ 4,000 (₹ 2,000 per child x 2)		-
Less: Exempt u/s 10(32) (₹ 1,500 x 2)	<u>₹ 3,000</u>	1,000
Income of the minor son ₹ 1,200		
Less: Exempt u/s 10(32)	<u>₹ 1,200</u>	-
Total Income	4,51,000	1,00,800

Notes:

- (1) As per section 64(1), in case the spouse of the individual receives any amount by way of income from any concern in which the individual has substantial interest, then, such income shall be included in the total income of the individual. The only

exception is in a case where the spouse possesses any technical or professional qualifications and the income earned is solely attributable to the application of her technical or professional knowledge and experience, in which case, the clubbing provisions would not apply.

In this case, the salary of ₹ 10,000 p.m. received by Mrs. A from the company has to be included in the total income of Mr. A, as Mrs. A does not possess any technical or professional qualification for earning such income and Mr. A has substantial interest in the company.

- (2) As per section 64(1A), the income of a minor child is to be included in the total income of the parent whose total income (excluding the income of minor child to be so clubbed) is greater. Further, as per section 10(32), income of a minor child which is includible in the income of the parent shall be exempt to the extent of ₹ 1,500 per child.

Therefore, the income of minor children shall be included in the income of Mr. A, since Mr. A's income of ₹ 4,50,000 (before including the income of the minor child) is greater than Mrs. A's income of ₹ 1,00,800.

Note - The solution has been worked out on the basis of the following assumptions:

- (1) It has been assumed that the income earned by the minor children is not on account of any activity involving application of any skill or talent.
- (2) Rent received has been assumed as gross annual value in the absence of standard rent, municipal value and fair market value.
- (3) Income of each twin daughter has been taken as ₹ 2,000 p.a.

Alternatively, the question can also be interpreted to mean that the cumulative income of the twin daughters is ₹ 2,000 p.a., in which case the income to be clubbed under section 64(1A) would be Nil, since the entire income would be exempt under section 10(32). Consequently, the total income of Mr. A in such a case would be ₹ 4,50,000.

- (b) **Computation of value of taxable services and service tax payable by ABC & Co. for the half year ended 30-9-2012:**

Particulars	Amount (₹)
Amounts collected from companies for pre-recruitment screening	3,00,000
Amounts collected from companies for recruitment of-	
- Permanent staff	1,80,000
- Temporary staff	4,50,000
Advances received from prospective employers for conducting campus	

interviews in colleges [Point of taxation in case of receipt of an advance is the date of receipt of each such advance]	<u>80,000</u>
Value of taxable service	<u>10,10,000</u>
Service tax @ 12% = ₹ 10,10,000 × $\frac{12}{100}$	1,21,200
Education cess @ 2% = ₹ 1,21,200 × $\frac{2}{100}$	2,424
Secondary and higher education cess @ 1% = ₹ 1,21,200 × $\frac{1}{100}$	<u>1,212</u>
Service tax payable	<u>1,24,836</u>

Note: Since the value of taxable services rendered by ABC & Co. exceeds ₹ 10 lakh in the financial year 2011-12, it shall not be eligible for the small service provider's exemption in the financial year 2012-13.

(c) Computation of VAT liability of B & C:

Particulars	Turnover under VAT (₹)	Output VAT (%)	Input VAT credit (₹)	Net VAT liability (₹)
Sale of goods by B to C [B's liability]	1,250	$= 1,250 \times \frac{12.5}{100}$ $= 156.25$	Nil [CST paid on purchases is not Vatable]	156.25
Sale of goods by C to D [C's liability]	1,500	$= 1,500 \times \frac{12.5}{100}$ $= 187.50$	156.25	31.25

Question 6

- (a) Ms. Neelima had purchased 500 equity shares in A Ltd. at a cost of ₹ 30 per share (brokerage 1%) in February, 1979.

She got 50 bonus shares in September, 1980.

She again got 550 bonus shares by virtue of her holding on March, 1985. Fair market value of the shares of A Ltd. on April, 1981 is ₹ 50.

In January, 2013, she transferred all her shares @ ₹ 240 per share (brokerage 2%).

Compute the capital gains taxable in the hands of Ms. Neelima for the Assessment Year 2013-14, assuming:

- (a) A Ltd. is an unlisted company and securities transaction tax was not applicable at the time of sale.
- (b) A Ltd. is a listed company and the shares are sold in a recognised stock exchange and securities transaction tax was paid at the time of sale.

Cost inflation index.

F.Y. 1981-82	100	
F.Y. 1984-85	125	
F.Y. 2012-13	852	(8 Marks)

- (b) Mr. Rajesh, a proprietor of Z enterprise, provides taxable services. He received the following amount during the financial year 2012-13:

- (i) ₹1,25,000 as advance while signing a contract.
- (ii) ₹6,00,000 by pay order during process of providing service.
- (iii) ₹5,25,000 by credit card after completion of service as on 31st December, 2012.

Compute the value of taxable service and amount of service tax payable by him. Assume service tax has been charged separately. Z enterprise is not eligible for small service provider's exemption in the financial year 2012-13.

The rate of service tax is 12%, education cess is 2% and higher education cess is 1%.

(4 Marks)

- (c). Distinguish between Gross Product Variant and Consumption Variant of VAT. (4 Marks)

Answer

- (a) (a) In case A Ltd. is an unlisted company and STT was not applicable at the time of sale

Computation of capital gains of Ms. Neelima for the A.Y. 2013-14

Particulars	₹
500 equity shares	
Sale proceeds (500 × ₹ 240)	1,20,000
Less : Brokerage paid (2% of ₹ 1,20,000)	2,400
Net sale consideration	1,17,600
Less : Indexed cost of acquisition [₹ 50 × 500 × 852/100]	2,13,000
Long term capital loss (A)	95,400

50 Bonus shares (Allotted in September, 1980)	
Sale proceeds (50 × ₹ 240)	12,000
Less : Brokerage paid (2% of ₹ 12,000)	240
Net sale consideration	11,760
Less : Indexed cost of acquisition [₹ 50 × 50 × 852/100] [See Note below]	21,300
Long term capital loss (B)	9,540
550 Bonus shares (Allotted in March, 1985)	
Sale proceeds (550 × ₹ 240)	1,32,000
Less: Brokerage paid (2% of ₹ 1,32,000)	2,640
Net sale consideration	1,29,360
Less: Cost of acquisition	NIL
Long term capital gain (C)	1,29,360
∴ Taxable long term capital gains (A+B+C)	24,420
Note: In case of bonus shares allotted before 1.4.1981, the fair market value as on 1.4.1981 is taken as the cost of acquisition. In case of bonus shares allotted after 1.4.1981, the cost of acquisition will be Nil.	

Alternative presentation:**Computation of capital gains of Ms. Neelima for the A.Y. 2013-14**

Particulars	₹	₹
Sale proceeds of original and bonus shares (1100 × ₹ 240)		2,64,000
Less : Brokerage paid (2% of ₹ 2,64,000)		5,280
Net sale consideration		2,58,720
Less : Indexed cost of acquisition of original shares [₹ 50 × 500 × 852/100]	2,13,000	
Indexed cost of acquisition of bonus shares allotted in September, 1980 [₹ 50 × 50 × 852/100]	21,300	
Cost of acquisition of bonus shares allotted in March 1985	Nil	
		2,34,300
Taxable long term capital gains		24,420
Note: In case of bonus shares allotted before 1.4.1981, the fair market value as on 1.4.1981 is taken as the cost of acquisition. In case of bonus shares allotted after 1.4.1981, the cost of acquisition will be Nil.		

- (b) In case A Ltd. is a listed company and the shares are sold in a recognized stock exchange and STT was paid at the time of sale.

Section 10(38) exempts long-term capital gains arising from, *inter alia*, sale of equity shares of a company if such transaction is chargeable to securities transaction tax. In this case, since STT has been paid at the time of sale, the entire long-term capital gains arising from sale of equity shares of A Ltd. would be exempt under section 10(38).

- (b) **Computation of taxable service of Mr. Rajesh for financial year 2012-13:**

Particulars	₹
Advance received while signing a contract [Note 2]	1,25,000
Amount received while providing service by pay order [Note 3]	6,00,000
Amount received on completion of service through credit card [Note 4]	<u>5,25,000</u>
Value of taxable service	<u>12,50,000</u>

Calculation of service tax liability

Particulars	₹
Service tax @ 12% on ₹12,50,000	1,50,000
Add: (i) Education cess @ 2% on service tax	3,000
Add: (ii) Secondary and higher education cess @ 1% on service tax	<u>1,500</u>
Total service tax payable	<u>1,54,500</u>

Notes:

- Where the provision for service is for a consideration in money, the value of taxable service is the gross amount charged for such service.
 - Gross amount charged for the taxable service includes amount received before the provision of such service.
 - Money *inter alia* means pay order.
 - Gross amount charged *inter alia* includes payment by credit card.
- (c) **Gross product variant:** The gross product variant allows deductions for taxes on all purchases of raw materials and components, but no deduction is allowed for taxes on capital inputs. In other words, taxes on capital goods such as plant and machinery are not deductible from the tax base in the year of purchase and tax on the depreciated part of the plant and machinery is not deductible in the subsequent years.

Consumption variant: Consumption variant of VAT allows for deduction on all business purchases including capital assets. Thus, gross investment is deductible in calculating

value added. It neither distinguishes between capital and current expenditures nor specifies the life of assets or depreciation allowances for different assets.

Question 7

- (a) Answer any **two** of the following three sub-divisions:
- (i) Briefly discuss the provisions relating to payment of advance tax in case of capital gains and casual income.
 - (ii) Explain the provision regarding the taxability of limited liability partnership under the Income-tax Act, 1961.
 - (iii) State the head of income in the following cases under which the receipt is to be assessed and comment.
 - (A) A uses his property for his own business. Can he claim depreciation?
 - (B) B lets out his property to X. X sublets it. How is sub-letting to be assessed in the hands of X?
 - (C) C has built a house on a leasehold land. He has let out the property and claims the rent as income from house property and deducted expenses on repairs, security charges, insurance and collection charges totaling to 40% of receipts.
- (2 x 4 = 8 Marks)
- (b) How is the value of the service under service tax provisions determined where such value is not ascertainable? (4 Marks)
- (c) What are the procedural requirements under VAT Act for claiming set off of input tax on capital goods? (4 Marks)

Answer

(a) (i) Payment of advance tax in case of capital gains and casual income

- (1) Advance tax is payable by an assessee on his/its total income, which includes capital gains and casual income like income from lotteries, crossword puzzles etc.
- (2) Since it is not possible for the assessee to estimate his capital gains, income from lotteries, etc., it has been provided that if any such income arises after the due date for any installment, then, the entire amount of tax payable (after considering tax deducted at source) on such capital gains or casual income should be paid in the remaining installments of advance tax which are due.
- (3) Where no such installment is due, the entire tax should be paid by 31st March of the relevant financial year.
- (4) If the entire tax liability is so paid, no interest liability under section 234C would arise for deferment of advance tax,

Note: In case of casual income (winnings from lotteries, crossword puzzles, card games, gambling, betting, races including horse races etc.), the entire tax liability is fully

deductible at source@30% under section 194B and 194BB. Therefore, advance tax liability would arise only in respect of the education cess and secondary and higher education cess element of such tax, if the same, along with tax liability in respect of other income, if any, is ₹10,000 or more.

(ii) Taxability of limited liability partnerships (LLPs) under the Income-tax Act, 1961

- (i) The taxation scheme of LLPs in the Income-tax Act, 1961 is on the same lines as applicable for general partnerships, i.e. tax liability would be attracted in the hands of the LLP and tax exemption would be available to the partners. Therefore, the same tax treatment would be applicable for both general partnerships and LLPs.
- (ii) The rate of income-tax applicable to LLPs is the same as the rate applicable for firms i.e. 30% of total income.
- (iii) The provisions of section 40(b) requiring payment of remuneration only to working partner in accordance with the terms of the partnership deed for a period commencing on or after the date of the partnership deed, would apply to LLPs as well. Further, disallowance of interest in excess of 12% per annum and salary exceeding the prescribed limits would also be applicable in the case of LLPs.
- (iv) However, whereas a partnership firm can opt for presumptive taxation scheme under section 44AD, an LLP cannot opt for such scheme.

(iii) (A) Yes, Mr. A can claim depreciation, since the property is an asset used for business purposes. Section 22, which is the charging section for "Income from house property" specifically excludes from its scope, property which an assessee, as an owner, occupies for the purpose of any business or profession carried on by him.

(B) In the hands of Mr. B, income from letting out of property to Mr. X is chargeable under the head "Income from house property", since Mr. B is the owner of the property.

However, since Mr. X is not the owner of the house property, the income from sub-letting will not be chargeable under the head "Income from house property". It will be assessed as "Income from other sources" in the hands of Mr. X.

In the alternative, it would be assessed as "Profits and gains of business or profession", if X is engaged in the business of sub-letting.

(C) Income from letting out of a house built on leasehold land is taxable under the head "Income from house property" in the hands of Mr. C. Ownership of land is not a pre-requisite for charge of income under the head "Income from house property".

The annual letting value (higher of municipal value and fair rent, but restricted to standard rent) or actual rent, whichever is higher, would be the gross annual value of the house property. The municipal taxes paid by Mr. C during the year is to be deducted from gross annual value to arrive at the net annual value.

Deduction of 30% of net annual value is allowable under section 24 to arrive at the income chargeable under the head "Income from house property". No other deduction is allowable in respect of repairs, insurance, security and collection charges.

Note – Interest on loan borrowed for construction of house is deductible under section 24(b) from Net Annual Value to arrive at the Income from house property, in addition to the statutory deduction of 30%,

- (b) The value of the service, where such value is not ascertainable, shall be determined under service tax provisions in the following manner:-

(i) Value of similar services

The value of taxable service shall be equivalent to the gross amount charged by the service provider to provide similar service to any other person subject to fulfillment of the conditions below:

1. Such service is in the ordinary course of trade.
2. The gross amount charged is the sole consideration.

(ii) When value of similar services cannot be ascertained

Where the value of similar services cannot be determined in the manner discussed above, the service provider shall determine the equivalent money value of such consideration. However, such value shall, in no case be less than the cost of provision of such taxable service.

- (c) The dealer will have to bifurcate their purchase into capital goods eligible for set off and capital goods not so eligible (being items covered in the negative list). The purchase of capital goods must be supported with a tax invoice. The set off must be claimed as per the applicable provisions in respect of installments and after obtaining prior permission, if required under the applicable State VAT law. Set off on capital goods should not exceed the tax paid by the vendor on the same in the Government Treasury.