

Paper 11- Indirect Taxation

Answer to MTP_Intermediate_Syllabus 2012_Dec 2015_Set 1

The following table lists the learning objectives and the verbs that appear in the syllabus learning aims and examination questions:

	Learning objectives	Verbs used	Definition
LEVEL B	KNOWLEDGE What you are expected to know	List	Make a list of
		State	Express, fully or clearly, the details/facts
		Define	Give the exact meaning of
	COMPREHENSION What you are expected to understand	Describe	Communicate the key features of
		Distinguish	Highlight the differences between
		Explain	Make clear or intelligible/ state the meaning or purpose of
		Identify	Recognize, establish or select after consideration
		Illustrate	Use an example to describe or explain something
	APPLICATION How you are expected to apply your knowledge	Apply	Put to practical use
		Calculate	Ascertain or reckon mathematically
		Demonstrate	Prove with certainty or exhibit by practical means
		Prepare	Make or get ready for use
		Reconcile	Make or prove consistent/ compatible
		Solve	Find an answer to
		Tabulate	Arrange in a table
	ANALYSIS How you are expected to analyse the detail of what you have learned	Analyse	Examine in detail the structure of
		Categorise	Place into a defined class or division
		Compare and contrast	Show the similarities and/or differences between
Construct		Build up or compile	
Prioritise		Place in order of priority or sequence for action	
Produce		Create or bring into existence	

Paper 11- Indirect Taxation

Time Allowed : 3 Hours

Full Marks : 100

The figures in the margin on the right side indicate full marks.

All questions are compulsory. In question No. 1, all sub-questions are compulsory. In question Numbers 2 to 8, student may answer any two of the three sub-questions (a), (b) and (c).

Wherever necessary, you may make suitable assumptions and state them clearly in your answer.

Working notes should form part of the answer.

1. Answer the following questions with suitable reasons: [1×20=20]
- (a) When one can pay duty under protest in Excise?
 - (b) What kind of duty is to be performed by DGFT regarding SCOMET Items?
 - (c) Whether Cenvat Credit is available on CST sale?
 - (d) State the periodicity of issue of C form?
 - (e) A non-executive director of a company is receiving sitting fees and commission of ₹ three lakhs from a private limited company. Is service tax payable? Under which head? Who is liable to pay service tax?
 - (f) Which entry in Seventh Schedule to Constitution of India is relevant for purpose of imposition of service tax?
 - (g) CESTAT (Tribunal) has passed an order on issue relating to classification of goods. An assessee is aggrieved with the order. Where he should file appeal?
 - (h) Is currency 'goods' for purpose of Customs Act?
 - (i) There is difference of opinion about interpretation of a provision in Foreign Trade Policy among following authorities:
 - (i) Principal Chief Commissioner of Customs
 - (ii) Director General of Foreign Trade
 - (iii) Revenue Secretary, Ministry of Finance
 - (iv) Chairman, Central Board of Excise and Customs (CBE&C).Whose interpretation will be held as final and binding?
 - (j) If the difference between actual transaction value and the average of arms length price determined by most appropriate method is below specified limit, the actual transaction value is accepted for income tax purposes without any adjustment. What is the limit?
 - (k) Name the variants of VAT.
 - (l) State the name of any two methods for computing Arm's Length Price in case of international taxation.
 - (m) State the elements which should be considered while calculating the value of export goods under computed value method.
 - (n) Mention the quantum of drawback for re-exporting of duty paid imported goods without use.
 - (o) State the taxability of service tax for municipal functions performed by a Government Authority.
 - (p) Whether business directories are included in the term, 'print media' for levy of service tax.
 - (q) A hotel garden was let out to a political party for 2 days for a meeting. Charges received ₹ 30,000 (excluding service tax). The hotel charges 10% service charges which are later distributed as tips to employees. Compute the service tax payable thereon.
 - (r) Manpower supply services by an individual to a company is ₹ 1,00,000. Compute the service tax liability by applying reverse charge mechanism.
 - (s) State the purpose of the Central Excise Tariff Act.

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- (f) State the manner to compute the assessable value if whole or part of excisable goods are not sold by the assessee but are used for consumption by him or in his behalf in production/ manufacture of other goods.**

Answer of 1:

- (a) Sometimes it happens that the classification of goods done by excise authorities, assessable value determined by the excise authorities in adjudication proceedings, etc. are not agreeable or acceptable to the assessee. In such cases, the assessee can file an appeal and in the meanwhile he can pay duty under protest.
- (b) Export of Special Chemicals, Organisms, Materials, Equipment and Technologies (SCOMET) is either prohibited or restricted. These cover nuclear material, nuclear reactors, equipment for nuclear explosive devices, rocket systems, toxic chemicals, micro- organisms, chemicals for weapons, viruses, etc. Application for license for exporting these items is to be made to DGFT (Director General of Foreign Trade). Application will be considered by Exim Facilitation Committee (EFC).
- (c) No. Credit of Central Sales Tax (CST) paid on inputs and capital goods purchased from other States will not be available.
- (d) The purchasing dealer is required to issue C form to selling dealer on quarterly basis. One C form should contain all sales in the quarter.
- (e) Service tax is payable under 'Other Taxable Services' @ 12.36%. The company which is receiving the service of director is liable to pay service tax under reverse charge mechanism [RCM].
- (f) Entry 97 i.e. Residual Powers in List I of Seventh Schedule, which reads as follows - 'Any other matter not included in List II or List III including any tax not mentioned in list II or list III'.
- (g) He should file appeal before Supreme Court.
- (h) Yes - Currency has been specifically included in definition of 'goods' under Section 2(22) of Customs Act.
- (i) Interpretation of Director General of Foreign Trade (DGFT) will be final and binding.
- (j) If the difference between the price of actual transaction and average of the arm's length price determined is within the range of three percent (plus or minus), the transaction price shall be accepted without any adjustment [The limit was five per cent (plus or minus) up to 1-4-2013].
- (k) Generally three variants of VAT are available, e.g. — (1) consumption variant, (2) gross product variant and (3) income variant.
- (l) Arm's Length Price can be computed by any one of the following method:
- comparable uncontrolled price method;
 - resale price method;
 - cost plus method;
 - profit split method;
 - transaction net margin method;
 - such other method; as may be prescribed by the CBDT.

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- (m) The elements which should be considered while calculating the value of export goods under computed value method are as follows:
- Cost of production, manufacture or processing of export goods;
 - Charges, if any, for the design or brand;
 - An amount towards profit.
- (n) The quantum of drawback for re-exporting of duty paid imported goods without use is 98% of import duty.
- (o) The municipal functions performed by a Government Authority are exempted from levy of service tax under Article 243W of the Constitution.
- (p) Business directories are not included in the term, 'print media'. So these are eligible for levy of service tax.
- (q) Hotel garden was let out to a political party is a matter of renting of immovable property. The taxable amount will be [₹ 30,000 + 10% of ₹ 30,000 = ₹ 33,000]. The service tax will be — 12.36% of ₹ 33,000 or ₹ 4,079.
- (r) The total service tax liability is ₹ 12,360 (12.36% of ₹ 1,00,000) in providing manpower supply services by an individual to a company. The amount of service tax payable by the service provider is ₹ 3,090 (25% of 12,360) and the amount of service tax payable by the service receiver is ₹ 9,270 (75% of 12,360).
- (s) The purpose of the Central Excise Tariff Act is — it lists various goods with rate of duty applicable thereon in the form of tariff headings/ entries. It provides principles of classification goods.
- (t) If whole or part of excisable goods are not sold by the assessee but are used for consumption by him or in his behalf in production/ manufacture of other goods, the assessable value will be 110% of cost of production or manufacture of such goods. Cost of production shall be computed as per Cost Accounting Standard – 4 issued by the Institute of Cost Accountants of India.

2. Answer any two:

[2×2=4]

- (a) Write any two disadvantages of indirect tax. 2
- (b) List the characteristics of Indirect Taxes. 2
- (c) If there is a matter in Concurrent List and both Centre and State make a law on that matter, which law will prevail? 2

Answer of 2(a):

The following are the disadvantages of indirect tax:

1. Indirect taxes do not depend on paying capacity. Since this tax is uniform, the tax payable on commodity is same, whether it is purchased by a poor man or a rich person. Hence, the indirect taxes are termed as 'regressive'.
2. Tax on goods and services increases its prices, which reduces demand of goods and services. Lesser demand means lower growth of industrialization.

Answer of 2(b):

The following are the characteristics of Indirect Taxes:

- (1) Meaning: Indirect Tax is a tax where incidence and impact fall on two different person.
- (2) Nature of tax: Indirect Taxes are regressive in nature.
- (3) Taxable Event: Purchase / Sale / Manufacture of goods and provision of services.

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- (4) Levy & Collection: Indirect taxes are levied & collected from the consumer but paid / deposited to the Exchequer by the Assessee / Dealer.
- (5) Shifting of Burden: Tax burden is shifted on the subsequent / ultimate user.
- (6) Collection: Indirect Taxes are collected at the time of sale or purchases or rendering of services.

Answer of 2(c):

The law made by parliament shall prevail over the law made by the state legislature and the latter will be valid only to the extent to which it is not repugnant to the former.

3. Answer any two:

[8×2=16]

(a)(i) Star Ltd. sold farm equipments to the agriculturists on ex-factory basis, upon payments made before dispatch of the goods. Star Ltd. at the request of their customers, arrange for payment of freight and transit insurance and for the dispatch of the goods to the destination. The Department's view is that since freight and transit insurance has been paid by Star Ltd., and since they have also arranged for the transport of goods, there is no ex-factory delivery of goods, and the cost of insurance and freight has to be included to the price for purposes of determination of value and excise duty should be payable on such basis. Discuss whether the contention of the Department is correct in law. 4

(ii) Keen Ltd. purchased certain inputs which were directly consigned to the job worker's premises for manufacture of intermediate goods. State the conditions subject to which Keen Ltd. will be entitled to take credit of the duty paid on such inputs. 2

(iii) A Ltd., a manufacturer of excisable goods, has applied for provisional assessment under Rule 7 of Central Excise Rules, 2002 and paid duty on provisional basis. The Assistant Commissioner issued a show-cause notice before finalisation of provisional assessment on the ground of misclassification of goods. With the help of decided case law discuss the validity of show-cause notice. 2

(b)(i) Koel Ltd. is engaged in the manufacture of machines. It has supplied one machine to M/s. A & Co. with the following details. Determine the total amount of central excise duty and cess payable thereon.

Price of machine excluding taxes and duties — ₹ 8,50,000

Installation and erection expenses — ₹ 30,000

Packaging charges — ₹ 12,500

Design and engineering charges — ₹ 4,000

Cost of material supplied free of charge by buyer — ₹ 10,000

Pre-delivery inspection charges — ₹ 1,000

Other necessary information is as under:

Cash Discount @ 20% on price is allowed as per terms of contract because buyer made full payment in advance.

Bought out accessories worth ₹ 8,000 supplied with Machine. Central Excise Duty is 12%, Education Cess 2% and Secondary and Higher Education Cess is 1%. 6

(ii) State the applicability of the concept of 'deemed manufacture' for the goods covered under Maximum Retail Price (MRP). 2

(c)(i) Priya Industries started its production activities on 15th March, 2015. In the month of March, 2015, 1,000 units of raw material were purchased at ₹ 150 per unit, paying excise duty @ 8%. 800 units of raw material were consumed in manufacturing process and finished output was sold for ₹ 1,40,000 (excluding excise duty @ 8%). For simplification, you may ignore the conversion cost and assume the rates of excise duty to be inclusive of education cess. Pass the Journal entries in the books of the assessee. 6

(ii) A manufacturer purchased certain inputs from X. The assessable value was ₹ 20,000 and

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the Central Excise duty was calculated at ₹ 3,296 making a total amount of invoice at ₹ 23,296. However, buyer-manufacturer paid only ₹ 20,800 to X in full settlement of this bill. How much CENVAT credit can be availed by manufacturer and why? 2

Answer of 3(a)(i):

Transaction Value will be assessable value where the goods are sold by the assessee, for delivery, at the time and place of removal, the assessee and the buyer of the goods are not related and the price is the sole consideration for the sale.

Factory is a place of Removal u/s 4(3) of Central Excise Act. Hence, transaction value for sale at factory, i.e. the place of removal can be taken as assessable value.

The delivery of the goods at the customers' destination and the payment of freight and transit insurance are made by the Company only on request by the customers. Therefore, the insurance and freight have no relevance in this matter. Escorts JCB Ltd. 146 ELT 31 (SC).

The Company is not liable to pay excise duty on the basis of the price inclusive of freight and insurance. Therefore, contention of the Department is invalid in law.

Answer of 3(a)(ii):

Keen Ltd. will be entitled to take Cenvat credit of the duties paid on inputs/taxes paid on input services used in manufacture of intermediate products by the jobs worker, if the -

- Job worker is availing the benefit of exemption notification no. 214/86, where Keen Ltd. undertakes to pay duty liability on job work done by job worker.
- The said intermediate goods are received by Keen Ltd. for use in or in relation to manufacture of final product.

Answer of 3(a)(iii):

The Supreme Court in Siddhartha Tubes Ltd. v. CCEx. [2012] 276 ELT A131 (SC) (also in CCEx. v. ITC Ltd. [2006] 203 ELT 532 (SC) has held that show-cause notice under section 11A of the Central Excise Act can be issued for recovery if duty of excise is not levied or short levied. Before finalisation of provisional assessment, the question of non levy or short levy cannot arise.

Moreover, the time-limit under section 11A for service of show-cause notice in case of provisional assessment, starts from the date of adjustment of duty after final assessment.

Thus, before finalization of provisional assessment, show cause notice so issued is not valid.

Answer of 3(b)(i):

Computation of Assessable Value of the Machine u/s 4 of Central Excise Act, 1944

Particulars	Amount (₹)	Reasons
Price of Machine	8,50,000	Assumed to be an all-inclusive price.
Less: Installation and erection expenses	(30,000)	Since installation is post-removal expense, it should be excluded from Assessable Value (AV).
Add: Value of materials supplied by buyer	10,000	Such free materials shall be considered as an additional consideration from buyer to manufacturer, and included as per Rule 6 of Central Excise (Valuation) Rules.
Assessable Value	8,30,000	
Less: Excise Duty at 12%	99,600	
Less: Education Cess at 2%	1,992	
Less: SHEC @ 1%	996	

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Total Duty Payable	1,02,588	
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Working Notes: Adjustments are not made for the following items based on the reasoning given therein -

1. Packing Charges are specifically included in AV u/s 4.
2. Design and Development Expenses are incurred in relation to manufacture, and hence includible in AV.
3. Pre-Delivery Inspect on Charges are assumed to be incurred as per the contract before removal from factory, and hence includible in Assessable Value.
4. Bought out items are considered as trading activity, and hence excluded from Assessable value u/s 4.
5. Assumed that the Price mentioned above is final price after deducting discounts. Further assumed that the discounts are given as part of the normal practice of trade, and hence eligible for deduction. Hence, no adjustment is required.

Answer of 3(b)(ii):

The following processes in respect of goods mentioned in Third Schedule to the Central Excise Act, 1944 is considered Deemed Manufacture -

1. Packing or repacking in a Unit Container,
2. Labelling or Re-labelling of containers including declaration or alteration of retail sale price on the container,
3. Adoption of any other treatment on the goods to render the product marketable to consumer.

Answer of 3(c)(i):

Journal entries in the books of M/s. Priya Industries:

	Particulars		Debit	Credit
On the date of purchase	Purchases A/c Dr. CENVAT Credit Receivable A/c Dr. To Sundry Creditors A/c [Purchase of 1,000 units of raw material & CENVAT credit receivable on it]		1,50,000 12,000	1,62,000
At the time of sale	Sundry Debtors A/c Dr. To Sales A/c To Excise Duty A/c [Sale of goods & excise duty payable on it]		1,51,200	1,40,000 11,200
On payment of duty	Excise Duty A/c Dr. To CENVAT Credit Receivable A/c [Excise duty paid out of CENVAT credit available]		11,200	11,200

Answer of 3(c)(ii):

As per Rule 3(1) of the CENVAT Credit Rules, 2004, a manufacturer of final products is allowed to take credit of excise duty paid on any input or capital goods received in the factory of manufacturer of final product. Thus, in case of inputs or capital goods, the eligibility of availing CENVAT credit does not depend upon making the payment for such inputs or capital goods to the supplier. Therefore, the manufacturer can avail full CENVAT credit of ₹ 3,296 provided X does not claim the refund of the excess excise duty paid by him. The same has been clarified vide Circular No. 877/15/2008-CX., dated 17-11-2008.

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4. Answer any two:

[6×2=12]

(a) Alo & Company Ltd. have imported a machine from U.K. From the following particulars furnished by them, arrive at the assessable value for the purpose of customs duty payable:

(i) F.O.B. cost of the machine	10,000 U.K. Pounds
(ii) Freight (air)	3,000 U.K. Pounds
(iii) Engineering and design charges paid to a firm in U.K.	500 U.K. Pounds
(iv) License fee relating to imported goods payable by the buyer as a condition of sale	20% of F.O.B. cost
(v) Materials and components supplied by the buyer free of cost valued	₹ 20,000
(vi) Insurance paid to the insurer in India	₹ 5,000
(vii) Buying commission paid by the buyer to his agent in U.K.	100 U.K. Pounds
Other particulars:	
(i) Inter-bank exchange rate as arrived by the authorized dealer	₹ 72.50 per U.K. Pound
(ii) CBEC had notified for purpose of Section 14 of the Customs Act, 1962, exchange rate of	₹ 70.25 per U.K. Pound
(iii) Import r paid demurrage charges for delay in clearing the machine from the Airport	₹ 5,000

(Make suitable assumptions wherever required and show workings with explanations)

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(b)(i) Pen Power Ltd. is registered under 'Project Import Regulations, 1986' for import of power equipments at concessional rate to implement a project for setting -up of a power plant. It imported a gas turbine and generator under the Project Import Regulations, 1986, but before these could reach the project site these were lost/destroyed in the sea within India.

The department denied project import concession under the Heading 9801 and demanded full duty, as the goods were not used in the project. Discuss with decided case law, whether the demand made by the department is tenable in law. 4

(ii) State the eligible projects which will come under the purview of Project Import. 2

(c)(i) A person makes an unauthorized import of goods liable to confiscation. After adjudication, Assistant Commissioner provides an option to the importer to pay fine in lieu of confiscation. It is proposed to impose a fine (in lieu of confiscation) equal to 50% of margin of profit. From the following particulars calculate the maximum amount of fine that can be imposed: Assessable value - ₹ 40,000, Total duty payable - ₹ 20,000, Market value - ₹ 1,00,000. Also calculate the amount of fine and the total payment to be made by the importer to clear the consignment. 4

(ii) Define 'Prohibited Goods' in the context of Customs Act. 2

Answer of 4(a):

Computation of assessable value

FOB cost of the machine	£ 10,000.00
Exchange rate notified by CBEC	₹ 70.25

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FoB price in Indian ₹	7,02,500.00
Add: License fee relating to imported goods payable by the buyer as a condition of sale @ 20% of FoB Price [Includible in Value]	1,40,500.00
Add: Development work [Development work other than in India is includible] [£ 500X ₹ 70.25 = ₹ 35,125]	35,125.00
Add: Materials and components supplied by the assessee-buyer (free of charge) [Includible]	20,000.00
Add: Buying commission paid to agent abroad [Not includible]	NIL
Add: Cost of transport as follows —	
1. Normal cost: Actual is £ 3,000; but in case of import by air, it can't exceed 20% of FoB i.e. 20% of £ 10,000 = FoB i.e. 20% of £ 10,000 = 2,000 £ X ₹ 70.25 2,000 × ₹ 70.25	1,40,500.00
2. Demurrage: As per Rule 10(2), cost of transport includes the ship demurrage charges on chartered vessels. In this case, the import is by air. Hence, the demurrage charges cannot be included.	Not included
Add: Insurance [It is assumed to be for import upto airport, hence, includible.]	5,000.00
CIF	10,43,625.00
Add: Loading, unloading and handling charges @ 1% of CIF	10,436.25
Assessable Value	10,54,061.25

Answer of 4(b)(i):

The facts of this case are similar to that in Commissioner v. Lanco Kondapalli Power Pvt. Ltd - 2011 (268) E.L.T. A76 (S.C.), wherein it was held that when -

- ◆ goods are not used elsewhere in India for any purpose than that of the project, or
- ◆ goods are destroyed,

in such conditions, there is no additional liability for differential duty.

Therefore, since the goods were meant for the project and were not used for any purpose other than the project, the concession could not be withdrawn.

The department's demand is, therefore, not tenable in law.

Answer of 4(b)(ii):

The following eligible projects which will come under the purview of Project Import:

- (i). industrial plant;
- (ii). irrigation project;
- (iii). power project ;
- (iv). mining project;
- (v). project for the exploration for oil or other minerals, and
- (vi). such other projects as the Central Government may, having regard to the economic development of the country notify in the Official Gazette in this behalf.

Answer of 4(c)(i):

The answer is as follows -

- Maximum Fine Maximum Fine = Market price of the goods confiscated - Import duty chargeable thereon = ₹ 1,00,000 - ₹ 20,000 = ₹ 80,000.
- Margin of profit = Market Value -Cost of imported goods = ₹ 1,00,000 - ₹ 40,000 (assessable

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value, being cost upto landing; of goods in India) - ₹ 20,000 Import Duty (duty is payable even if redemption fine is imposed) = ₹ 40,000.

- Redemption fine: 50% of margin of profit = 50% of ₹ 40,000 = ₹ 20,000. (This is within the maximum fine that may be imposed).
- Total sum payable to clear the goods = Duty + Redemption fine = ₹ 20,000 + ₹ 20,000 = ₹ 40,000.

Answer of 4(c)(ii):

As per section 2(33) of the Customs Act, "Prohibited goods" means any goods –

- Whose import or export is subject to any prohibition under this Act or any other law for the time being in force,
- But does not include any such goods in respect of which the conditions of permission of import or export have been complied with.

5. Answer any two:

[4×2=8]

- (a) State the principles of imposition of restrictions on Foreign Trade Policy by Directorate General of Foreign Trade. 4
- (b)(i) A regular exporter of goods intends to apply for Advance Authorization for annual requirements. What is the maximum value for which he is entitled to get Annual Advance Authorisation? 2
- (ii) When an exporter can apply for Special Brand Rate of duty drawback? 2
- (c) Write short notes on 'Niryat Bandhu' and E-BRC (Bank Realisation Certificate) in the context of EXIM policy. 2+2

Answer of 5(a):

Directorate General of Foreign Trade (DGFT) may, through a notification, adopt and enforce any measure necessary for: -

- A. Protection of public morals;
- B. Protection of human, animal or plant life or health;
- C. Protection of patents, trademarks and copyrights, and the prevention of deceptive practices;
- D. Prevention of use of prison labour;
- E. Protection of national treasures of artistic, historic or archaeological value;
- F. Conservation of exhaustible natural resources;
- G. Protection of trade of fissionable material or material from which they are derived;
- H. Prevention of traffic in arms, ammunition and
- I. Implements of war.

Answer of 5(b)(i):

Annual Advance Authorisation will be granted upto 300% of FOB value of physical exports in preceding financial year and / or FOB value of deemed exports in preceding year or ₹ one crore whichever is higher.

Answer of 5(b)(ii):

The conditions of eligibility to apply for Special Brand Rate of duty drawback are:

1. The All Industry Rate fixed should be less than 80% of the duties paid by him;
2. Rate should not be less than 1% of FOB value of product except when amount of drawback per shipment is more than ₹ 500.

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3. Export value is not less than the value of imported material used in them – i.e., there should not be 'negative value addition'.

Answer of 5(c):

Niryat Bandhu

A novel 'Niryat Bandhu' scheme for mentoring first generation entrepreneurs has been conceptualised. The Officer (Niryat Bandhu) would primarily mentor interested individuals in the arena of international business. Such hand-holding by officers of DGFT would help the new exporters/importers by leveraging the knowledge base of officers and by providing timely and appropriate guidance.

E-BRC

Bank Realization Certificates (BRCs), evidencing receipt of export proceeds would be transmitted electronically from the respective banks to the DGFT. This will bring down transaction cost to the exporters as they will not be required to obtain physical copies of BRCs from the banks and then submit such physical copy to DGFT.

6. Answer any two:

[10×2=20]

(a)(i) Mr. R provided repair and maintenance services of equipments belonging to Z Ltd., which are used in manufacture of oxygen. The repair and maintenance work was carried out at factory of Z Ltd. using electricity belonging to Z Ltd. The charges for services are fixed at ₹ 1,00,000, while value of electricity used is estimated at ₹ 10,000. The Department argued that the value of electricity is consideration in kind and is liable to service tax in hands of Mr. R. Decide. 4

(ii) A builder constructed 25 flats in a residential apartment, out of which 23 were booked before start of construction. The price thereof was to be received in instalments during the period of construction. The flats were priced at ₹ 45 lakhs per flat (exclusive of taxes) (the price of land apportioned as ₹ 15 lakhs per flat was included in the said sum). Construction was started and completed in the same year. After issuance but before receipt of completion certificate, the balance two flats were sold at a price of ₹ 55 lakhs per flat (exclusive of taxes). Determine taxable value under service tax law and service tax thereon assuming that builder has opted for abatement available under law. 6

(b) Compute taxable value of services provided from the following sums received by a bank (all sums exclusive of service tax, if any) -

- (1) Interest on loan : ₹ 550 lakhs ;
- (2) Interest on Overdraft facility : ₹ 100 lakh (including ₹ 15 lakhs for discounting of bills);
- (3) Commission on sale of foreign currency to banks : ₹ 60 lakh ;
- (4) Commission on sale of foreign currency to authorized dealers : ₹ 30 lakh ;
- (5) Processing fees in relation to loans, etc. provided to customers : ₹ 25 lakh ;
- (6) Commission and Processing charges on issuance of bank drafts, etc.: ₹ 400 lakhs (Value of bank drafts issued was ₹ 100 crores);
- (7) Services in relation to issuance of Commercial Papers : ₹ 30 lakh ;
- (8) Margin earned on trading in currency swaps : ₹ 50 lakh ;
- (9) Interest at exorbitant rates on credit card dues : ₹ 25 lakh ;
- (10) Gross amount of currency exchanged (INR to foreign or vice-versa) : ₹ 5000 lakhs. The RBI reference rate was not available. The Bank has not exercised option to pay service tax at prescribed rates under composition scheme. 10

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(c)(i) Z Ltd. of Delhi has appointed Paras Inc. of US as an agent for marketing of goods manufactured by Z Ltd. Z Ltd. has paid a commission of ₹ 15,00,000 to Paras Inc. for the services rendered for the half year ending 31-03-2015. Discuss service tax liability of the service rendered by Paras Inc. of US. 3

(ii) Rekha Ltd., a unit in SEZ, received services from various service providers in relation to authorized operations in SEZ during the month August, 2014. At the time of making payment, service provider asks it to pay tax, however, it argues that service tax is not applicable on taxable services provided to it. The following details are furnished for the month August, 2014:

1. Value of Taxable services used exclusively for authorised operations within SEZ : ₹ 5,00,000
2. Value of Taxable Services used by SEZ units and DTA (Domestic Tariff Area) units : ₹ 8,00,000
3. Value of Taxable services used wholly for DTA units : ₹ 3,00,000
4. Export Turnover of SEZ Unit: ₹ 1,00,00,000
5. Turnover of DTA Unit: ₹ 60,00,000
6. Service Tax Rate : 12.36%

Compute the amount payable as service tax by M/s. Rekha Ltd. along with incentives available to it by way of exemption/refund/CENVAT Credit for the month assuming that all conditions are complied with. 4

(iii) Mr. Khan a famous cricketer furnishes you with the following information of the various receipts for the quarter ended 31-03-2015. Calculate his service tax liability if all the amounts are exclusive of service tax. Ignore small service provider exemption.

- (1) Receipts from Sports Authority of India for participation in recognised sport: ₹ 50 lakh;
- (2) Receipts from franchisee of Indian Premier league (not a recognised sports body): ₹ 75 lakh;
- (3) Receipts from acting as brand ambassador for corporate client: ₹ 20 lakh ;
- (4) Khel Ratna award received from Government of India : ₹ 10 lakh;
- (5) Receipts of sports training academy to coach young players: ₹ 15 lakh. 3

Answer of 6(a)(i):

On similar facts, it was held in *Inox Air Products Ltd. v. CCEC* [2012] 24 taxmann.com 114 (Bom.) that electricity supplied free of cost by customer for use by service provider in provision of operating and maintenance services cannot be regarded as a consideration in kind received by assessee and, hence, it is not includible in taxable value of services provided. This is so because such electricity doesn't result in any benefit accruing to assessee. In fact, such electricity is consumed in manufacture of final product of Z Ltd. viz. Oxygen. Hence, the value of services, in this case, is ₹ 1,00,000.

Answer of 6(a)(ii):

Construction service u/s 66E(b) of Finance Act, 1994 covers construction of a residential apartment intended for sale to a buyer "wholly or partly" except where entire consideration is received after issuance of completion certificate by competent authority. Hence, sale of two flats after issuance of completion certificate, is not a declared service u/s 66E(b). In fact, it is a sale of immovable property and not a service.

Total sum charged on 23 flats (including value of land) (value of land is to be included in total amount as per the abatement Notification No. 26/2012-ST) = ₹ 45 lakhs X 23 flats = ₹ 1,035 Lakhs.

Answer to MTP_Intermediate_Syllabus 2012_Dec 2015_Set 1

Taxable Value = ₹ 1,035 lakhs X 25% = ₹ 258.75 Lakhs (abatment of 75% will be available, as flat is residential, price is below ₹ 1 crore & area is assumed to be below 2,000 sq. ft.)

Service Tax @ 12.36% on ₹ 258.75 Lakhs = ₹ 31.98 Lakhs approx.

Answer of 6(b):

Computation of taxable value

- (1) Interest on loan: ₹ 550 lakhs - Covered under negative list u/s 66D(n) - Not taxable ;
- (2) Interest on Overdraft: ₹ 100 lakh (including ₹ 15 lakhs for discounting of bills) - Covered under negative list u/s 66D(n) - Not taxable (OD facility & discounting is in nature of loan)
- (3) Commission on sale of foreign currency to banks : ₹ 60 lakh - Covered under negative list u/s 66D(n) - Not taxable ;
- (4) Commission on sale of foreign currency to authorized dealers : ₹ 30 lakh - Covered under negative list u/s 66D(n) - Not taxable ;
- (5) Processing fees in relation to loans, etc. provided to customers : ₹ 25 lakh - Not covered under negative list, as only interest/discount are excluded - Taxable ;
- (6) Commission and Processing charges on issuance of bank drafts, etc.: ₹ 400 lakhs (Value of bank drafts issued was ₹ 100 crores) - Commission is taxable (Value of bank drafts is transaction in money and not a service) - ₹ 400 lakhs taxable ;
- (7) Services in relation to issuance of Commercial Papers : ₹ 30 lakh - Taxable ;
- (8) Margin earned on trading in currency swaps : ₹ 50 lakh - Not taxable, as currency swaps are 'derivatives' viz. Securities and, therefore, goods and trading in goods is covered in negative list u/s 66D(e) ;
- (9) Interest at exorbitant rates on credit card dues : ₹ 25 lakh - As per Department Guidance Note, such interest is not covered by negative list, as credit card facility is not extending of deposit/loan and such interest is also not excludible in view of Rule 6(2), as it is not interest for delayed payment of goods/services - However, as per judicial view, even if exorbitant, it is in nature of interest and covered by negative list u/s 66D(n) - Not taxable
- (10) Gross amount of currency exchanged (INR to foreign or vice-versa): ₹ 5000 lakhs. The RBI reference rate was not available. The Bank has not exercised option to pay service tax at prescribed rates under composition scheme - Since option under Rule 6(7B) is not exercised; hence, value is to be determined as per Rule 2B of Service Tax Valuation Rules, 2006. Value, where RBI rate is not available, is 1% of gross amount of INR = 1% of ₹ 5000 lakhs = ₹ 50 lakhs. (Sale and purchase of foreign currency to/from general public is taxable).

Taxable Value = 25 + 400 + 30 + 50 = ₹ 505 lakhs,

Answer of 6(c)(i):

Here Paras Inc. provides services as an intermediary. "Intermediary" means a broker, an agent or any other person, by whatever name called, who arranges or facilitates a supply of goods, between two or more persons, but does not include a person supplies the goods on his account. As per the provision of Rule 9 of POP Rules, 2012 the place of provision of intermediary services shall be the location of the service provider. Here Paras Inc. (service provider) is situated in non taxable territory, the place of provision of service shall be US. Hence, the commission received by Paras Inc. from Z Ltd. shall not be taxable in India.

Answer of 6(c)(ii):

The relevant computations as per Notification No. 12/2013-ST, dated 01-07-2013 are shown below -

Sl. No.	Particulars	Value	Service Tax payable @ 12.36%	Refund, if any
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Answer to MTP_Intermediate_Syllabus 2012_Dec 2015_Set 1

(i)	Taxable services used exclusively for authorised operations within SEZ	5,00,000	Fully Exempt; Option not to pay service tax	No need to claim refund, as tax not paid
(ii)	Services used by both SEZ and DTA units -Proportionate Refund = Service Tax × SEZ Turnover ₹ 100 lakhs ÷ Total Turnover of all the units to which service relates ₹ 160 lakhs	8,00,000	98,880	61,800
(iii)	Services used wholly for DTA - No refund/exemption	3,00,000	37,080	-
Total			1,35,960	61,800
Amount available as CENVAT Credit to the DTA units [Service Tax payable - Refund] (Proportionate amount of service tax that have not been refunded after applying the formula shall be available to the DTA Units of the entity as CENVAT Credit.)				74,160

Answer of 6(c)(iii):

Computation of value of taxable service and service tax liability of Mr. Khan (amount in ₹):

(1) Receipts from Sports Authority of India for participation in recognised sports	Exempt
(2) Receipts from franchisee of Indian Premier League (not a recognised sports body)	75,00,000
(3) Receipts from acting as brand ambassador for corporate client	20,00,000
(4) Khel Ratna award received from Government of India is not a consideration for service and hence the same shall not be liable for service tax	Not taxable
(5) Receipts of sports training academy to coach young players	Exempt
Value of taxable services	95,00,000
Service tax payable @ 12.36%	11,74,200

7. Answer any two:

[6×2=12]

(a)(i) State various purposes for which goods can be purchased at concessional rate under Central Sales Tax Act, by issuing C form. 2

(ii) Compute Vat payable on works contract when the dealer does not intend to pay Vat under any composition scheme – Contract Price (excluding Vat) – ₹ 1,00,000. Input materials used in contract including Vat @ 14.5% - ₹ 11,450, Cost of labour in execution of the works contract – ₹ 25,000. Cost of other services in the execution of works contract – ₹ 10,000, Consumables used in the works contract – ₹ 5,000, Plant and machinery purchased including Vat @ 4% - ₹ 26,000, Vat rate on output – 14.5%. Assume that 100% input tax credit on capital goods is available. 4

(b) Mr. X, a dealer located in the State of Maharashtra, dealing in machinery used is rolling mills furnishes following information for the financial year 2014 - 15.

1. Total inter-state Sales during the financial year (CST not shown separately) – ₹ 2,29,50,000
2. Trade Commission for which credit notes have been issued separately – ₹ 5,78,125
3. Freight and Transportation charges charged separately in invoice – ₹ 4,00,000
4. Freight charges included in value but not shown separately – ₹ 2,00,000
5. Insurance for transport of machinery upto destination – ₹ 75,000
6. Installation and commissioning charges levied separately in invoice – ₹ 1,00,000
7. The buyers have issued C form in respect of machinery bought by them from Mr. X.

Answer to MTP_Intermediate_Syllabus 2012_Dec 2015_Set 1

Compute the tax liability under CST Act.

6

(c)(i) A dealer claims that he has sent some goods out of State on stock transfer basis. What evidence he is required to produce before sales tax officer to prove the stock transfer? If he is unable to produce that evidence, what are the consequences? 1+2

(ii) State the dealers who are not eligible to opt for composition scheme under Vat regime? 3

Answer of 7(a)(i):

As per section 8(3) of CST Act, goods — (I) intended for resale, (II) for use in manufacture or processing for sale (III) for use in telecommunications network (IV) for use in mining (V) for use in power generation/distribution, or (VI) containers and packing materials are only eligible for concessional rate of CST.

Answer of 7(a)(ii):

Vat can be paid after deducting value of services and consumables. Thus, deduction of ₹ 40,000 is available [₹ 25,000 + ₹ 10,000 + ₹ 5,000]. Hence, Vat is payable on ₹ 60,000 (₹ 1,00,000 – ₹ 40,000) @ 14.5%. Thus, Vat payable on the contract is ₹ 8,700. Input tax credit available – (1) On input material – ₹ 1,450 [(11,450 x 14.5)/114.5] (2) On plant and machinery – ₹ 1,000 [(26,000 x 4)/104]. Thus, total Vat credit available = ₹ 2,450. Hence, net Vat payable by cash = ₹ 8,700 – ₹ 2,450 = ₹ 6,250.

Answer of 7(b):

	₹	₹
Gross Sales Turnover (including CST)		2,29,50,000
Less:		
(i) Trade Commission	5,78,125	
(ii) Freight charged separately	4,00,000	
(iii) Installation and Commissioning	1,00,000	10,78,125
Aggregate Sale Price for CST		2,18,71,875
Less: CST payable - (2,18,71,875 x 2)/102		4,28,860
Turnover for year 2014-15		2,14,43,015

Answer of 7(c)(i):

The dealer has to produce F form which is to be issued by the branch or depot which has received the goods despatched by dealer. If the dealer is unable to produce F form, the sale will be treated as sale within the State of dealer and will be liable to State Vat at applicable rate. Interest will also become payable for delayed payment.

Answer of 7(c)(ii):

Small dealers having gross turnover exceeding ₹5 lakhs but upto ₹50 lakhs have option of composition scheme. They will have to pay a small percentage of gross turnover.

They will not be entitled to any input tax credit. Following dealers are not eligible for composition scheme -

- I. Dealers who make inter-state purchases
- II. Dealers who make inter-state sales
- III. Dealers who import the goods and then sale in India
- IV. Dealers who stock transfer goods outside the State
- V. Dealers who export the goods
- VI. Dealers who want to show Vat in their Invoice.
- VII. Dealers whose turnover exceeds ₹50 lakhs.

Answer to MTP_Intermediate_Syllabus 2012_Dec 2015_Set 1

- 8. Answer any two:** **[4×2=8]**
- (a) Describe the application of Resale Price Method (RPM) in the context of Arm's Length Price.** **4**
- (b) State the procedure to calculate Income Tax on the basis of Arm's Length Basis.** **4**
- (c) State the meaning of 'safe harbour'. Also state the implications of it in the context of international transfer pricing.** **2+2**

Answer of 8(a):

Resale Price Method (RPM) method is ideally suited to measure the value of the services performed by a buyer or seller of goods who generally acts as a distributor and does not add a significant value to goods sold. It is applicable even with differences in products, as long as the functions performed are similar. However, it is less useful where goods are further processed or in nature of raw material.

RPM is applied in a backward process. From the sale price to an unrelated third party, appropriate adjustments to the gross margin are made by comparing the transaction to other, third party transactions. The applications of this method are as follows:

- (1) This method can be applied when there are no comparable uncontrolled sales and an applicable resale price is available within a reasonable time before or after the controlled sale.
- (2) Where the reseller does not add substantial value to the goods through physical modification. Limited enhancements such as packaging, repackaging, labeling or minor assembly ordinarily do not generally affect the use of RPM. Hence, RPM may not be applicable if the reseller performs value added functions.
- (3) RPM is more accurate where it is realized within a short time of the reseller's purchase of goods.
- (4) RPM is ordinarily used when the controlled reseller does not use intangible property to add substantial value to the products.
- (5) RPM is applied when the reseller does not alter the physical characteristics of the product.
- (6) Where the reseller has the exclusive right to resell the goods, the gross margin would be affected by factors like size of market, existence of substitute goods, and level of activity undertaken by the reseller.

Answer of 8(b):

To avoid such 'tax arbitrage' it has been provided that income arising from an international transaction shall be computed having regard to arm's length price (ALP) - section 92(1) of Income-tax Act.

The provisions apply only when transactions are between two entities which are 'associated enterprises'.

Sections 92 to 92F of Income-tax Act provide a statutory framework for computation of reasonable, fair and equitable profit and tax in India so that the profits chargeable to tax in India do not get diverted elsewhere by altering the prices charged and paid in intra-group transactions. Any income arising from an international transaction shall be computed having regard to arm's length price (ALP).

The provisions are contained in Chapter X of Income-tax Act, which is a title 'Special Provisions relating to avoidance of tax'.

Answer to MTP_Intermediate_Syllabus 2012_Dec 2015_Set 1

Thus, the provisions are to ensure that there is no avoidance of taxes through tax arbitrage.

Answer of 8(c):

Many transactions are coming within purview of section 92C of Income Tax Act. This raises lot of disputes. Hence, section 92CB of Income Tax Act empowers CBDT to formulate safe harbour rules.

'Safe Harbour' means circumstances in which income tax authorities shall accept the transfer price declared by assessee, without going into details of Arm's Length Price (ALP).

Assessee can opt to exercise Safe Harbour Rules by submitting form No. 3CEFA to assessing officer. If assessing officer does not take any action within two months from end of the month in which the option was filed, the Safe Harbour action will be considered to have been accepted.

The option will remain valid for five years. However, once the option is accepted, it cannot be changed and if assessee declares less margin in a particular year, the income will be calculated on basis of safe harbour rates or margins only [This is rather risky, as assessee binds himself for five years].

The transfer price will be accepted in following situations, as specified in rule 10TD of Income Tax Rules.