

DIRECT TAXATION

Full Marks: 100

Time Allowed: 3 hours

This paper contains 4 questions. All questions are compulsory, subject to instruction provided against each question. All workings must form part of your answer. Assumptions, if any, must be clearly indicated.

Question No.1: Answer all the sub-questions. [Total = 20 marks]

- (a) Ms. Anisha an Indian national, left India for employment purpose on 31.08.2013 and came back on a holiday on 07.04.2014. Determine her residential status for the previous year 2013-14. [1 mark]
- (b) Mr. John, an American national, received Rs.3,00,000 (in INR equivalent) from a business in South Africa, having its set-up/registered office in India. Is there any tax liability? [1 mark]
- (c) Cost of Telecom License Fees Rs.140 lacs, for a period of 7 years. After 4 years, the licence was transferred at Rs.90 lacs. Is there any taxable income? [2 marks]
- (d) A Pvt. Ltd. Co. incurred an expense of Rs.30 lacs for conducting an in-house research and development of bio-technology in the business of manufacture or production. State the amount of deduction available for tax purposes. [1 mark]
- (e) Cost of cultivation of sugarcane Rs.5 lacs; Market value of sugarcane when transferred to factory Rs.9 lacs. Sale of sugar Rs.23 lacs; Employee Benefit Expenses Rs.3 lacs. Determine the business income and taxable income. [2 marks]
- (f) An assessee submitted return of income after the due date. He now wants to revise the return. Discuss the possibility of revision. [1 mark]
- (g) Can incomplete, unsigned or unverified return lead to best judgement assessment? [1 mark]
- (h) An assessee- businessman lives in a rented accommodation, paying a rent of Rs.10,000 per month. His gross total income of Rs.7,00,000 includes long term capital gains of Rs.2,00,000 and is eligible to claim deduction under Chapter VIA amounting to Rs.90,000 before considering this provision. What can be the maximum deduction claimed by the assessee? [2 marks]
- (i) You have spent Rs.1,35,000 for medical treatment on specified disease on any of your dependent family member (aged 65 years). You have also recovered Rs.65,000 from Insurance Company. State the deduction available under Chapter VIA. [1 mark]
- (j) Due date for filling return of income 31.7.14. Actual date of submission of return 19.08.2014. Tax on Total Income Rs.96,000. Advance Tax paid Rs.48,000, TDS Rs.17,000. What is the interest payable u/s 234A? [1 mark]
- (k) For the purpose of wealth tax valuation, a building is considered having a Net Maintainable Rent (NMR) of Rs.45,00,000. The building is on a freehold land and having 12% as excess of unbuilt area over specified area. Ascertain value of the building. [2 marks]
- (l) State the features of Cost Plus Method used for computing Arm's Length Price. [2 marks]
- (m) What is the basis for selection of 'Comparable Companies' in a Transfer Pricing Study? [1 mark]
- (n) Define an 'Associated Enterprise' under the context of applicable rules on Transfer Pricing. [2 marks]

Paper 7- Direct Taxation_Syl2012_Set 2_PTP

Question No.2: Answer any four questions [4 × 13 marks = 52 marks] [This section represents Income Tax Act only]

2(a)(i) Mr. X owns a House Property in Gurgaon. Gross Municipal Value Rs.10 lacs. The property is used partly as self-occupied for 7 months, vacant for one month and let-out for residential purpose for 4 months during the previous year 2013-14 @ Rs.95,000 per month. Municipal Tax paid @ 15%. Compute Income from House Property. Would your answer differ if the property was located in Delhi? [6 marks]

2(a)(ii) Mr. Hari (aged 82 years) transferred a House Property (by a gift will) on the occasion of their 50th wedding anniversary. The Municipal Value of the property is Rs.30 lacs. His wife in turn has partially let out the property at a monthly rent of Rs.60,000 for a period of 3 months during the previous year 2013-14. Income earned by Mr. Hari out of Interest on Fixed Deposits Rs.3,10,000; Interest on Savings Bank Account Deposits Rs.80,000 and Dividend from Indian Companies Rs.1,50,000. What is the Total Income of Mr. Hari and Mrs. Hari for the previous year 2013-14 ? [7 marks]

2(b) (i) X Ltd. purchased an asset for Rs.3 lacs during 2011-12 which was exclusively used for scientific research purpose, which was sold in 2013-14 for Rs.50,000. Another asset was purchased for Rs.5 lacs on 11.07.2013, having a rate of depreciation @ 10% p.a. The same was also sold on 10.12.13 for Rs.4,50,000. Discuss the tax liability, if any, which may arise of these transactions? [4 marks]

2(b)(ii) Furnished the Profit & Loss Account for the newly commenced business in India, owned by Mr. B (non-resident Indian) for the year ended 31.03.2014 : [9 marks]

| | |
|---|---------------------|
| (I) Revenue from Operations in India | Rs.50,00,000 |
| (II) Other Income | |
| ❖ Interest from Investment in Fixed Deposits Rs.3,50,000 | |
| ❖ Dividend from Shares in Indian Companies Rs.1,95,000 | Rs.5,45,000 |
| (III) Total Revenue (I + II) | Rs.55,45,000 |
| (IV) Expenses | |
| Cost of Materials Consumed | Rs.23,00,000 |
| Changes in Inventory | (Rs.1,20,000) |
| Employee Benefit expenses | Rs.15,76,000 |
| Finance Costs | Rs.2,10,000 |
| Depreciation | Rs.1,90,000 |
| Other Expenses | Rs.3,97,000 |
| Total Expenses | Rs.46,53,000 |
| (V) Profit before exceptional and extraordinary items and tax | Rs.8,92,000 |
| (VI) Exceptional items | NIL |
| (VII) Profit before extraordinary items and tax (V - VI) | Rs.8,92,000 |
| (VIII) Extra ordinary items | NIL |
| (IX) Profit before tax (VII - VIII) | Rs. 8,92,000 |

Paper 7- Direct Taxation_Syl2012_Set 2_PTP

From the analysis of records, it was identified that:

- (1) Value of Closing Stock was shown at Market Value, while the cost price is Rs.1,05,000;
 - (2) Revenue from Operations is inclusive of Service Tax amounting to Rs.4,82,000;
 - (3) Employee Benefit Expenses includes salaries paid to an employee (resident and ordinarily resident for the previous year 2013-14) outside India Rs.90,000 without TDS;
 - (4) Finance cost includes Rs.90,000 recovered/charged by Mr. B from the business towards interest cost on own capital contribution. However, the bank rate of interest on such capital could have been Rs.70,000
 - (5) Other expenses includes Advertisement expenses paid Rs.20,000 for advertisement published in souvenir of a political party;
 - (6) Employee Benefit expenses also includes Rs.1,20,000 paid to his brother as salary for working as the Manager of his business. Based on his brother's educational qualification and work experience the salary could have been Rs.1,50,000.
- Compute Income from Business for the assessment year 2014-15.

2(c)(i) Ms. Karima (aged 47 years), a resident Indian, is physically challenged (56% disability) purchased jewellery worth Rs.5,00,000 during 1997-98. During the year 2006-07 she purchased further jewellery worth Rs.8,00,000. All the jewellery were sold by her during October 2013 for Rs.32,00,000 and thereafter in January 2014 purchased her second house property for Rs.29,00,000 to be used for residential purposes. Analyse the tax-impact, if any. [7 marks]

2(c)(ii) Non-Agricultural Income (other than capital gains and income from house property) Rs.1,50,000, Income from Capital Gains Rs.6,50,000. Deductions eligible under Chapter VIA Rs.1,90,000. Municipal Value of House Property in Delhi Rs.40,00,000 (used as self-occupied for residential purpose). Municipal Tax paid @ 15%. Interest on Loan taken for construction of House Property Rs.1,63,000, 40% of such interest stands due as on 31.03.2014. Ascertain the Tax Liability if the Assessee is a Senior Citizen (age 78 years) for the previous year 2013-14. [6 marks]

2(d)(i) Ms. Nandana (aged 46 years), an employee of Happy Ltd. furnishes information relating to her Income for the financial year 2013-14, where she joined during the year and served for five months:

Basic Pay Rs.50,000 pm; Dearness Allowance Rs. 35,000 pm (60% forming part of salary for retirement benefits); Accommodation provided by employer in a city having population more than 30 lacs; Cost of furnishings in that accommodation Rs.4 lacs. She is also provided with a 18 H.P. Motor car including chauffeur for which expenses are borne by employer. Ms. Nandana was also sent for an Executive Program on Strategic Management, for which the course fee of Rs.90,000 was paid by the employer. Employer's makes an equal contribution with employee @ 20% to RPF and Interest credited to RPF @ 9% amounting to Rs.9,000. In LIC - on a Single Premium Policy for self, paid Rs.90,000 (on a Policy Value of Rs.4,00,000) . Compute Total Income of Ms. Nandana for the assessment year 2014-15. [9 marks]

Paper 7- Direct Taxation_Syl2012_Set 2_PTP

2(d)(ii) Mr. Sameul retired on 31.01.2014 after 33 years of service from a Central Government Department. He received Rs.32 lacs as Gratuity, Leave Salary encashment Rs.13 lacs. He is entitled to a pension of Rs.30,000 per month from February 2014. In March, 2014, he commutes 60% of his pension and receives Rs.12,00,000. Compute Income from Salary of Mr. Samuel for the assessment year 2014-15. [4 marks]

2(e)(i) Total Income of MPX Associates (a partnership ship) for the financial year 2013-14 is Rs.2,00,000 after claiming deductions under Chapter VIA of Rs.14,00,000. Compute the Alternate Minimum Tax Payable for the previous year 2013-14. [3 marks]

2(e)(ii) Book Profit of a partnership firm is Rs.20,50,000. Salary paid to partners Rs.6,00,000. What is the eligible salary payable to partners for the previous year 2013-14? [3 marks]

2(e)(iii) State the features of the Reverse Mortgage Scheme. [3 marks]

2(e)(iv) Mr. B is providing professional services to Unpleasant Ltd. for which he was paid Rs.10,000 (in October 2013) and Rs.19,000 (in January 2014). An amount of Rs. 3,000 is payable for February 2014. Justify the applicability of TDS on these transactions [4 marks]

Question No.3: Answer any one question [1 × 8 marks = 8 marks] [This question represents Wealth Tax Act only]

3 (a) Compute Total Taxable Wealth based on Residential Status (RoR, RnoR, NR) of an Assessee on the valuation date 31.03.2014:

- (i) Residential building located in India, municipal value Rs.90,00,000. Loan taken against hypothecation of this building for purchase of a residential building in USA Rs.65,00,000;
- (ii) Residential building located in USA having a value of Rs.80,00,000 (in INR equivalent). Loan taken against hypothecation of this building Rs.15,00,000 to procure Motor Car in India.
- (iii) Motor Car valued at Rs.20,00,000 which is located in India.
- (iv) Another Residential House Property was transferred to spouse (as gift on birthday) value Rs.35,00,000. [8 marks]

3(b) Compute Taxable Wealth of Mr. Rangaswamy for the Assessment Year 2014-15:

- (i) A residential house valued at Rs. 25,00,000, meant exclusively for residential purposes and which is allotted to an employee who is in whole-time employment, having a gross annual salary of less than Rs. 10,00,000. Loan taken for purchase of this property Rs.17,00,000;
- (ii) A commercial house valued at Rs. 19,00,000 let out for 320 days during the Previous Year. Loan taken for construction of this property is Rs.16,00,000.
- (iii) A firm house valued at Rs.37,00,000 situated at an aerial distance of 23 kms from the jurisdiction of a municipal board.
- (iv) Motor cars held by him for running them on hire amounting to Rs.39,00,000. Loan against Motor Cars Rs.29,00,000.
- (v) Asset of Rs.12,00,000 transferred to son's wife.
- (vi) Any unused urban land held by the assessee for industrial purposes for a period of 2 years from the date of its acquisition by him valued at Rs.19,00,000. [8 marks]

Paper 7- Direct Taxation_Syl2012_Set 2_PTP

Question No.4: Answer any two questions [2 x 10 marks = 20 marks] [On International Taxation Chapters only]

4(a) What is the need for Arm's Length Pricing? State the difficulties in applying arm's length principle. [4+6]

4(b) Jackle, Korea and CD Ltd, an Indian Company are associated enterprises. CD Ltd manufactures Cel Phones and sells them to Jackle, Korea & Fox, a Company based at Nepal. During the year CD Ltd supplied 2,90,000 Cellular Phones to Jackle Korea at a price of Rs. 4,000 per unit and 45,000 units to Fox at a price of Rs. 6,800 per unit. The transactions of CD Ltd with Jackle and Fox are comparable subject to the following considerations -

- (i) Sales to Jackle are on FOB basis, sales to Fox are CIF basis. The freight and insurance paid by Jackle for each unit is Rs. 1,200.
- (ii) Sales to Fox are under a free warranty for Two Years whereas sales to Jackle are without any such warranty. The estimated cost of executing such warranty is Rs. 700.
- (iii) Since Jackle's order was huge in volume, quantity discount of Rs. 300 per unit was offered to it.

Compute the Arm's Length Price and the amount of increase in the Total Income of CD Ltd, if any, due to such Arm's Length Price. [10 marks]

4(c) Branco Inc., a French Company, holds 54% of Equity in the Indian Company Chirag Technologies Ltd (CTL). CTL is engaged in development of software and maintenance of the same for customers across the globe. Its clientele includes Branco Inc. During the year, CTL had spent 3,500 Man Hours for developing and maintaining software for Branco Inc, with each hour being billed at Rs. 1,800. Costs incurred by CTL for executing work for Branco Inc. amount to Rs. 26,00,000.

CTL had also undertaken developing software for Harsha Industries Ltd for which CTL had billed at Rs. 3,200 per Man Hour. The persons working for Harsha Industries Ltd and Branco were part of the same team and were of matching credentials and caliber. CTL had made a Gross Profit of 58% on the Harsha Industries work.

CTL's transactions with Branco Inc. are comparable to the transactions with Harsha Industries, subject to the following differences:

- (i) Branco gives technical know-how support to CTL which can be valued at 12% of the Normal Gross Profit. Harsha Industries does not provide any such support.
- (ii) Since the work for Branco involved huge number of man hours, a quantity discount of 15% of Normal Gross Profits was given.
- (iii) CTL had offered 90 Days credit to Branco the cost of which is measured at 3% of the Normal Billing Rate, No such discount was offered to Harsha Industries Ltd.

Compute ALP and the amount of increase in Total Income of Chirag Technologies Ltd. [10 marks]