

FINAL EXAMINATION GROUP III (SYLLABUS 2012)

SUGGESTED ANSWERS TO QUESTIONS DECEMBER 2015

Paper- 16 : TAX MANAGEMENT AND PRACTICE

Time Allowed : 3 Hours

Full Marks : 100

*The figures in the margin on the right side indicate full marks.
Wherever required, the candidate may make suitable assumptions and state them clearly in the answer.*

Working notes should form part of the relevant answer.

**All questions in Income Tax relate to the Assessment Year 2015-16,
unless stated otherwise**

SECTION A

Tax Management

Answer any five questions from this Section.

1. (a) The following is the balance sheet of VV Ltd. as on 31.03.2015, on which date the Fertilizer Division was transferred by way of slump sale for a consideration of ₹ 300 lakhs:

Liabilities	₹ in lakhs	Assets	₹ in lakhs
Paid up capital	1,000	Fixed Assets:	
Reserves	700	Cement Division	300
Liabilities:		Fertilizer Division	500
Cement Division	400	Steel Division	1,000
Fertilizer Division	500	Other Assets:	
Steel Division	600	Cement Division	200
		Fertilizer Division	400
		Steel Division	800
	3,200		3,200

Additional information:

- (i) Fixed Assets of Fertilizer Division include land, which was acquired for ₹ 40 lakhs in 2007 and re-valued at ₹ 100 lakhs on 31.03.2015, just before slump sale.

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(ii) Other Fixed Assets of Fertilizer Division represent their Written Down Values as per books. The written down value under Section 43(6) of the Income Tax Act is ₹ 320 lakhs.

(iii) Other Assets of Fertilizer Division reflected at ₹ 400 lakhs represent book value of non-depreciable assets.

(iv) The Fertilizer Division is operational from 1st January, 2012.

Compute the Capital Gain chargeable to income tax on the slump sale of Fertilizer Division, for the Assessment Year 2015-16. Also suggest a possible reinvestment for availing exemption from the resultant Capital Gains. 7

(b) Fig Ltd. is engaged in manufacture of both excisable and non-excisable goods in its factory from 01.11.2014 which was occupied by it as tenant. The following particulars are pertaining to the period from November 1, 2014 to March 31, 2015:

Sl. No.	Particulars	₹ in lakhs
(i)	Clearances of branded goods of another company	70
(ii)	Export sales to Bhutan	60
(iii)	Export sales to UK and Russia	120
(iv)	Clearance of goods (duty paid based on annual capacity of production under Section 3A of the Central Excise Act, 1944)	50
(v)	Clearance of goods subject to valuation based on retail sale price under Section 4A of the Central Excise Act, 1944 (said goods are eligible for 30% abatement)	300
(vi)	Job-work under Notification No. 214/86-CE	80

During the period from 01.04.2014 to 31.10.2014, the previous tenant of the building which is presently occupied by Fig Ltd. had cleared excisable goods of the aggregate value of ₹ 105 lakhs.

Your advice is sought as to whether Fig Ltd. could claim the benefit of exemption in terms of Notification No. 8/2003-CE dated 01.03.2003 for the Financial Year 2015-16.

Advice suitably, showing the necessary computation and working notes/explanations. 7

Answer:

1. (a) Computation of net worth of Fertilizer Division

Particulars	₹ in lakhs
Book value of non-depreciable assets	
Land	40
Other assets	400
Written down value of depreciable assets U/s. 43(6)	320
Aggregate value of assets	760
Less: Value of liabilities of Fertilizer Division	500
Net worth of Fertilizer Division	260

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Computation of capital gain on slump sale of Fertilizer Division

Particulars	₹ in lakhs
Sale consideration from slump sale of Fertilizer Division	300
Less: Net worth of the Fertilizer Division	<u>260</u>
Long-term capital gain on slump sale of Fertilizer Division	<u>40</u>

Note : Since the fertilizer division is operational from January, 2012 and is transferred in March, 2015, by way of slump sale, the capital gain is chargeable to tax as long-term capital gain. It is eligible for concessional rate of tax at 20.6%.

The assessee can invest the long-term capital gain (upto ₹50 lakhs) in REC / NHAI Capital Gain bonds to avail tax exemption [Section 54EC], within six months from the date of transfer.

1. (b) Computation of value of clearances for home consumption in the financial year 2014-15.

Sl. No.	Particulars	Working Note	₹ in Lakh
(i)	Clearances of branded goods	1	Nil
(ii)	Export sales to Bhutan	1	60
(iii)	Export sales to UK and Russia	1	Nil
(iv)	Clearance of goods (duty paid) based on annual capacity of production under section 3A of the Central Excise Act, 1944		50
(v)	Clearance of goods subject to valuation based on retail sale price under section 4A of the Central Excise Act, 1944.	2	210
(vi)	Job work under Notification No. 214/86 – CE	1	Nil
(vii)	Clearance of previous tenant of the building occupied by Fig Ltd.	3	105
	Total		425

Working Notes:

- In order to claim the benefit of exemption under Notification No. 8/2003 – CE in a financial year, the total turnover should not exceed ₹ 400 lakhs in the immediately preceding financial year.
For computing the turnover of ₹ 400 lakhs the Notification No. 8/2003 seeks exclusion of the following:
 - Clearances bearing the brand name or trade name of another person are to be excluded.
 - Export turnover is excluded. However, export to Bhutan and Nepal are not excluded and they are treated as “clearance for home consumption”. It is assumed that the goods exported to Bhutan are excisable goods.
 - Clearances under specified job work notification are excluded and Notification No. 214/86 – CE dated 25.03.1986 is one of the specified notifications.
- In the case of goods subject to valuation under section 4A of the Central Excise Act, 1944, the value for the purpose of SSI exemption would mean the retail price less abatement. Hence, the value of such clearances would be ₹ 300 lakhs × 70% = ₹ 210 lakhs.

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3. For the purpose of computing the turnover of ₹ 400 lakhs, all the clearances made by different manufacturers from the same factory are to be clubbed together. The clearances worth ₹ 105 lakhs of previous tenant of the building occupied by Fig Ltd. hence is added.

Advice:

Since the value of clearances for home consumption exceeds ₹ 400 lakhs in the financial year 2014-15, Fig Ltd is not eligible to claim the benefit of exemption under Notification No. 8/2003 – CE dated 01.03.2003 in the financial year 2015-16.

2. (a) VKS Hotels (P) Ltd. located in Nilgiri District of Tamil Nadu State, was established in April, 2012. Nilgiri District is a specified district having 'World Heritage Site' status and is eligible for deduction under section 80-ID of the Income Tax Act, 1961. It furnishes you the following information for the year ended 31.03.2015:

- (i) Net Profit as per Profit and Loss Account ₹ 20 lakhs.
- (ii) Depreciation debited in the books ₹ 70 lakhs.
- (iii) Amount received towards Dharmadha by separately mentioning in the sales bills ₹ 7,00,000. This has not been credited to Profit and Loss Account.
- (iv) ₹ 10 lakhs was paid towards use of trademark for 10 years in April, 2014. This has been debited to Profit and Loss Account.
- (v) Provision for gratuity based on actuarial valuation debited to Profit and Loss Account ₹8 lakhs.
- (vi) Dividend received from subsidiary Indian company credited to Profit and Loss Account ₹ 2,00,000.
- (vii) Depreciation as per Income Tax Rules ₹ 60 lakhs.
- (viii) ₹ 5,00,000 was paid towards feasibility study for examining proposals for commencing a textile business and the project was abandoned.

Compute the total income of VKS Hotels (P) Ltd. for the Assessment Year 2015-16. Ignore MAT provisions. 7

- (b) State the place of provision of service in the following cases: 7

- (i) RR Agency of Cochin is appointed as commission agent by a foreign company for sale of its goods to Indian customers. RR Agency is eligible for a fixed percentage of commission from the foreign company.
- (ii) PQR Hardwares, Bangalore imported second hand computers from its customers located in Singapore for repairs. After necessary repairs, the computers were re-exported to South Africa without being put to use in India.
- (iii) Vivi Airlines, an airlines company located in Chennai hired aircraft from a foreign airlines company located in Colombo, Sri Lanka, for a period of 15 days. The aircraft was used in Colombo-Kuala Lumpur sector.

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Answer:

2. (a) Computation of total income of Raghu Hotels (P) Ltd for the Asst. year 2015-16

Particulars		₹
Net Profit as per Profit and Loss Account		20,00,000
Add:		
Depreciation debited to Profit and Loss Account		70,00,000
Amount paid towards use of trademark is a revenue expenditure since the assessee has not purchased trademark on outright basis		Nil
Provision for gratuity debited to Profit and Loss Account not allowable – Sec. 40A(7)		8,00,000
Expenditure towards feasibility of study for new business not allowable business [since this is unrelated to existing business - CIT v. Priya Village Roadshows Ltd 332 ITR 594]		5,00,000
		1,03,00,000
Less: Amount received from Dharmada not liable to tax - <i>Bijili Cotton Mills (P) Ltd.</i> 's case Supreme Court	7,00,000	
Dividend received from subsidiary company - Exempt U/s.10(34)	2,00,000	
Depreciation as per Income-tax Rules	60,00,000	69,00,000
Gross Total Income		34,00,000
Less: Deduction U/s. 80-ID @ 100% of the profits		34,00,000
Total Income		NIL

2. (b)

- (i) The commission agent is covered under rule 9(c) of Place of Provision of Services Rules, 2012 w.e.f. 01.10.2014. Accordingly, the place of provision of services provided or agreed to provided by RR Agency as commission agent of goods to foreign company will be the location of the service provider.

Hence the POP of services will be Cochin.

- (ii) As per second proviso to **rule 4(a)** of the Place of Provision of Services Rules, 2012, when the goods are temporarily imported into India for repairs and are re-exported after the repairs without being put to use in the taxable territory, the place of provision of service shall be the location of the service receiver.

Accordingly, the place of provision of service is the location of service receiver i.e Singapore.

- (iii) Under rule **9(d)** of the Place of Provision of Services Rules, 2012, the place of provision of service consisting of hiring of all means of transport other than (a) aircrafts; and (b) vessels except yachts up to a period of one month, is the location of service provider (w.e.f. 01.10.2014).

Services of hiring of aircraft and vessel (except yachts), irrespective of the period of hire will be the location of the service receiver.

In this case, the service receiver is Vivi Airlines which has taken aircrafts on hire from foreign airlines and the place of service will be Chennai (location of service recipient) in accordance with rule 3 of POPS rules.

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3. (a) A partnership firm consisting of three partners Weeks, Worrell and Walcott is engaged in the business of automobile trade. Its turnover for the Financial Year 2014-15 was ₹95 lakhs and its Net Profit as per Books of Account is ₹ 5,20,000.

The partnership deed of the firm authorizes interest on capital at 15% on partners' capital contribution of ₹ 5 lakhs each. The deed authorizes monthly working partner salary of ₹10,000 to all the partners.

The firm has brought forward business loss relating to Assessment Year 2012-13 of ₹ 4,00,000 and unabsorbed depreciation of the Assessment Year 2014-15 of ₹ 1,00,000.

The partners have omitted to get the accounts audited under Section 44AB before the due date specified in Section 139(1) i.e. 31.10.2015. They seek your advise as to (i) whether they can declare presumptive income under Section 44AD; or (ii) admit income as per Books of Account which could attract penalty under Section 271B of the Income Tax Act, 1961.

You are requested to answer based on the cost-benefit analysis of filing the return of income, based on book results vis-a-vis the presumptive income under Section 44AD of the Income Tax Act, 1961. You have to consider the benefit likely to accrue in future also, assuming the rate of tax in future also. 7

- (b) An input service distributor has a total of 4 units viz. P, Q, R and S which are operational in the current year ended 31.03.2015. It has a common input service credit of ₹ 15,000 pertaining to more than one unit. The details of the turnover in the previous year and current year are given below:

Unit	Turnover in ₹	
	Previous year	Current year
P (Manufacturing excisable goods)	16,00,000	17,00,000
Q (Providing taxable and exempted service)	12,00,000	13,00,000
R (Manufacturing excisable and exempt goods)	13,00,000	20,00,000
S (Providing exclusively exempted service)	9,00,000	12,00,000

The common input service relates to units P and Q. How will the CENVAT credit be distributed? 7

Answer:

3. (a) The question is specific that only based on the cost-benefit analysis, the advice has to be given. A comparative chart would show the relevant position.

Particulars	Presumptive income U/s.44AD	As per regular books of account
Net Profit as per Profit and Loss Account		5,20,000
Presumptive income U/s. 44AD @8% of ₹ 95 lakhs	7,60,000	
Less: unabsorbed depreciation treated as current depreciation	(Not eligible)	(1,00,000)
	7,60,000	4,20,000
Less: Interest on Capital on ₹ 15 lakhs @ 12%	(1,80,000)	(1,80,000)

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Book Profit	5,80,000	2,40,000
Less: Working partners salary		
(a) Actually paid (10,000 × 3 × 12) = 3,60,000		
(b) Allowed U/s 40(b)		
– 90% of ₹ 3 lakh or ₹ 1.50 which is more	2,70,000	
– 60% of ₹ 2,80,000	<u>1,68,000</u>	
	4,38,000	2,16,000
	3,60,000	2,16,000
Less: Brought forward business loss	2,20,000	24,000
	2,20,000	24,000
Tax thereon @ 30.9%	Nil	Nil
Add: Penalty U/s 271B @ 0.5% of the turnover		47,500
Total Tax Liability	Nil	47,500

The assessee by opting regular provisions will have 'nil' tax liability. But, the assessee-firm will have to pay penalty of ₹ 47,500. However, it can carry forward the brought forward business loss of ₹ 3,76,000 for set off in future assessment years. This benefit of carry forward will result in tax saving of ₹ 1,16,184. Thus resulting in effective net tax assets of ₹ 68,684 (i.e. ₹ 1,16,184 - ₹ 47,500).

The assessee by opting section 44AD provision will lose the benefit of set off of brought forward depreciation of ₹ 1,00,000.

The assessee hence is advised to opt for regular provisions instead of presumptive provision contained in section 44AD.

3. (b) As per the amended rule 7(d) of the CENVAT Credit Rules, 2004 distribution of input service credit to all the units shall be in the ratio of their turnover of the **previous year. This distribution is irrespective of whether such common input services were used in all the units or in some of the units. [CBEC Circular No. 178/4/2014-ST dt. 11.07.14]**

The distribution of credit will be as under:

- (i) Distribution to 'P'
 $= ₹ 15,000 \times ₹ 16,00,000 / ₹ 50,00,000$
 $= ₹ 4,800$
- (ii) Distribution to 'Q'
 $= ₹ 15,000 \times ₹ 12,00,000 / ₹ 50,00,000$
 $= ₹ 3,600$
- (iii) Distribution to 'R'
 $= ₹ 15,000 \times ₹ 13,00,000 / ₹ 50,00,000$
 $= ₹ 3,900$
- (vi) Distribution to 'S'
 $= ₹ 15,000 \times ₹ 9,00,000 / ₹ 50,00,000$
 $= ₹ 2,700$

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4. (a) M/s Techno Ltd. furnishes the following information pertaining to the previous year 2014-2015.

Description	₹ in lakhs		
	Plant and Machinery	Factory Building	Intangible Assets (Patents)
Rate of depreciation	15%	10%	25%
Opening Written Down Value as on 1st April, 2014	14.50	25.00	15.00
Date of purchase/Acquisition 15th June, 2014—Plant and Machinery 29th September, 2014—Patent	12.00	Nil	5.00
Date of purchase/Acquisition 15th December 2014—Plant and Machinery 14th February 2015—Buildings	4.00	18.00	Nil
One out of the two patents sold on 29th March, 2015			3.00

Additional information:

One of the machineries purchased on 15th June, 2014 (original cost ₹ 1.50 lakhs) was destroyed by fire on 15th February, 2015 and the assessee received a compensation of ₹ 0.50 lakhs from the insurance company. Building acquired on 14th February, 2015 includes cost of land of ₹ 3 00 lakhs.

Calculate the eligible depreciation claim by M/s Techno Ltd. for the Assessment Year 2015-2016. (ignore additional depreciation). 7

- (b) Akash Ltd., started manufacturing excisable goods in September, 2014. Small scales exemption in terms of Notification No. 8/2003 as amended has been availed for the Financial Year 2014-2015. The following details are provided by Akash Ltd.:

Particulars	₹
1800 MT of inputs purchase @ ₹ 10,000 per MT (inclusive of central excise duty @ 12.36%)	1,80,00,000
Capital goods purchased on 20th October, 2013 (inclusive of excise duty at 12.36%)	50,00,000
Finished goods sold (excluding excise duty @ 12.36%) (At uniform transaction value exclusive of excise duty throughout the year)	3,00,00,000

There is neither any processing loss nor any inventory of input and output.

Compute the amount of excise duty payable in cash, if any, during the year 2014-2015. Show your working and notes with suitable assumption as may be required. 7

Answer:

4. (a) Computation of eligible depreciation for the Assessment year 2015-2016. (₹ In Lakhs)

Description	Plant And Machinery	Building	Intangible Assets (Patents)
Permissible rate of depreciation	15%	10%	25%
Depreciated Value of the block on 1st April 2014	14.50	25.00	15.00
Add: Actual Cost of Assets Purchased / Acquired during the previous year 2014-2015 15th June 2014 - Plant And Machineries & 29th September 2014 - Patent	12.00	Nil	5.00
Add: Actual Cost Of Assets Purchased / Acquired			

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During the Previous year 2014-2015			
1 st December 2014 - Plant and Machinery	4.00	15.00	Nil
14 th February 2015 - Building		(Note-1)	
Less : Money received as compensation from the insurance company in respect of assets destroyed by fire	(0.50)	Nil	(3.00)
Total	30.00	40.00	17.00
Depreciation allowable:			
Assets used for less than 180 Days during 2014-15. (depreciation rate is 50% of normal rate)			
Plants Machinery-(15%*50%* ₹ 4.00Lakhs)= ₹ 0.30 Lakhs	0.30		-
Buildings - (10%*50%* ₹ 15.00 Lakhs)= ₹ 0.75 Lakhs		0.75	
Assets Used for 180 Days and more during - previous year 2014-15 (Depreciation rate is 100% of normal rate)			
Plant & Machinery - (15%* ₹ 26.00 lakhs) = ₹ 3.90 Lakhs	3.90		
Buildings - (10%* ₹ 25.00 Lakhs) = ₹ 2.50 Lakhs		2.50	
Patent - (25%* ₹ 17 lakhs = ₹ 4.25 Lakhs)			4.25
Depreciation-Total: ₹ 11.70 Lakhs	4.20	3.25	4.25
Written Down Value on March 31,2015	25.80	36.75	12.75

Note: addition made to Building during previous year includes land of ₹ 3.00 lakhs on which depreciation is not allowable: Hence the addition to building taken as ₹ 15.00 lakhs (₹ 18 lakhs -cost of land ₹ 3 lakhs)

4. (b) Computation of central excise duty payable in cash by M/S AKASH Ltd.

Particulars	Amount in ₹	
Finished goods sold during the year		3,00,00,000
Less: Exemption of ₹150 Lakhs under Notification No. 8/2003 CE Dated 01-03-2003.		1,50,00,000
Dutiable clearances		1,50,00,000
Excise duty payable @ 12.36% (₹1,50,00,000 X 12.36%)		18,54,000
Less: CENVAT Credit available on inputs (Note 2)		
Proportion of inputs consumed in dutiable clearances = ₹ 1,50,00,000/ ₹3,00,00,000 = 50%		
(A) Excise duty paid on such inputs = ₹ 1,80,00,000 X (12.36/112.36 X 50%)	9,90,032	
(B) CENVAT credit available on capital goods (Note 3) (50,00,000X12.36/112.36)	5,50,018	15,40,050
Excise Duty Payable in cash		3,13,950

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Notes and Assumptions forming part of computation are as follows:

- (1) Since there is neither any processing loss nor inventory of inputs and output, it implies that all goods manufactured have been sold and entire quantity of inputs has been used in manufacturing these goods.
- (2) In respect of units availing SSI exemption no CENVAT Credit is available on inputs consumed in exempted clearances of ₹ 150 Lakhs (Notification No. 8/2003 CE Dated 01.03.2003).
- (3) In respect of units availing SSI Exemption, CENVAT credit on capital goods can be availed but Utilized only after clearance of ₹ 150 Lakhs [Notification No.8/2003/CE Dated 01.03.2003]. Further, entire credit on capital goods can be taken in the same financial year by such units [Third Proviso to rule 4(2)(a) of the CENVAT Credit Rules, 2004].

5. (a) G Ltd. furnishes following data in respect of certain items procured in the month of May, 2014:

Items	Excise duty paid in ₹
Raw Material	1,52,000
Capital Goods used for generation of electricity for captive use within the factory	4,00,000
Motor Sprit	40,000
Inputs used for construction of building	2,00,000
Dairy and bakery products consumed by the employees	20,000
Paints used for painting machinery	15,000

The aggregate value of clearance of the company for preceding financial year is ₹ 450 lakhs.

The company seeks your advice on the amount of CENVAT Credit available to it, from the above data. Advise them suitably. 7

- (b) Explain whether tax has to be deducted at source, as per the provisions of the Income Tax Act, 1961 under the following situations, each being independent of the other. If yes, the rate of tax and the amount of TDS should be stated (Provisions of DTAA may be ignored):
- (i) Rent of ₹ 2,00,000 paid by Govindaya Tubes LLP to Mr. Naresh, who has been living in Singapore for the last 12 years and has never visited India during such period. The building is used for training purposes. 3
 - (ii) Mrs. Sarawathi purchased a house property for ₹ 48 lakhs on 12.01.2015 from Mrs. Lakshmi, a resident. The value adopted by the stamp valuation authority was ₹ 55 lakhs. 2
 - (iii) Divya & Co., a partnership firm, has paid lorry freight of ₹ 3 lakhs on 12.03.2015 to Mr. Govinda, a lorry fleet owner having 11 Lorries and having PAN. 2

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Answer:

5. (a) Computation of CENVAT Credit Available for the month of May 2014.

Since the assessee is not eligible for SSI Exemption as its value of clearances during preceding year exceeds ₹ 400 lakhs, the credit of capital goods is eligible only up to 50% in the first year that is 2014-2015 and balance in the next year(s).

Items	Eligibility As	Reason	In ₹
Raw Material	Input	Used In the Factory and in relation to manufacture of dutiable product.	1,52,000
Capital Goods used for generation of electricity for captive use within the factory	Capital goods	Specifically eligible and include as capital goods under rule 2(a) of CENVAT Credit Rules. It is eligible even if such capital goods used outside the Factory. (50% of ₹ 4 lakhs)	2,00,000
Motor Sprit	Not Eligible	Specifically excluded from 'Input' (rule 2(k)(A))	Nil
Inputs used for construction of Building	Not Eligible	Specifically excluded from 'input' as used in the construction of Building (Rule 2(K)(B))	Nil
Dairy And Bakery Products Consumed by the employees	Not Eligible	Specifically excluded from 'Input' as used Primarily for personal use of employees. Rule 2(k)(E)	Nil
Paints Used For Painting Of Machinery used in Manufacturing	Input	Used in the Factory and indirectly related to manufacture	15,000
Total			3,67,000

5. (b)

- (i) In this case, from the details given, it is clear that the landlord is a non-resident. This is a payment made to a non-resident. The provisions of section 195 will apply and not sec. 194-I.

Since the house property is situated in India, the rent is taxable in India. Tax has to be deducted at source at 30% plus education cess 2% and Secondary and Higher education cess 1% i.e. totally 30.9%.

TDS amount will therefore be 30.9% on ₹ 2 lacs = ₹ 61,800.

- (ii) As per the provisions of section 194-IA, where a transferee of an immovable property other than rural agricultural land for a value exceeding ₹ 50 lacs from a resident, has to deduct tax at source @ 1% on the purchase consideration. The value determined by the stamp valuation authority is not relevant.
Since the consideration is less than ₹ 50 lacs, there is no obligation to deduct tax at source.
- (iii) As per the provision of sec. 194C(6), no deduction shall be made from any sum credited or paid or likely to be credited or paid during the previous year to the account of a contractor during the course of business of plying, hiring or leasing goods carriages, on furnishing of his Permanent Account Number, to the person paying or crediting such sum.

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The person responsible for paying and crediting any sum to the person referred to in section 194C(6) shall furnish, to the prescribed income-tax authority or the person authorized by it, such particulars, in such form and within such time as may be prescribed. [Sec. 194C(7)]

Hence, the payee has not required to deduct tax.

6. (a) **BG Ltd., an Indian company located at Kolkata, imported into India certain commodities in December, 2014 from a country which is covered by a Notification issued under Section 9A of the Customs Tariff Act, 1975. The relevant particulars relating to import are as follows:**

CIF value of the consignment—US \$ 25,000

Quantity imported—500 kgs.

Exchange rate applicable—US \$ 1 = ₹ 50

Basic Customs Duty (BCD)—20%

Education Cess and Secondary & Higher Education Cess may be adopted, where applicable.

As per the Notification, the anti-dumping duty leviable will be equal to the difference between the cost of the commodity calculated @ US \$ 70 per kg. and the landed value of the commodity as imported.

Calculate the liability on account of normal duties, cess and anti-dumping duty. Assume that only BCD and Education Cess and Secondary & Higher Education Cess are payable.

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- (b) **Rishikesh Fertilizers Ltd., seeks your opinion on the deductibility of the following items debited to the Profit and Loss Account, while computing its business income:**

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- (i) ₹ 50,000 paid as secret commission to a Government department official, an unidentified person. The payment has been approved by the Board as a normal trade practice.
- (ii) ₹ 2 lakhs incurred towards issue of convertible debentures, the debentures being convertible into equity shares after one year from the date of issue.
- (iii) ₹ 1 lakh paid to a local gang for rescuing an executive director who was kidnapped.

Answer:

6. (a) **BG Ltd. Computation of customs duty**

Particulars	₹
CIF value of the consignment (US \$ 25,000 x ₹ 50)	12,50,000
Add: Landing charges at 1%	12,500
Assessable value	12,62,500
Add: BCD @ 20%	2,52,500
Add: Education & SAH Education Cess @ 3% on BCD	7,575
Landed value/cost of the goods (A)	15,22,575
Cost of commodity for the purpose of anti-dumping	17,50,000

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Notification (B) (500 kg x US \$70 per kg x ₹ 50 per dollar)	
Anti-dumping duty (B-A)	2,27,425

Notes:

1. For the purpose of anti-dumping duty Notification, "landed value" means assessable value as determined under the Customs Act, 1962 and includes all duties of customs except duties levied under section 3, 8B, 9 and 9A of the Customs Tariff Act, 1975.
2. No Education Cess & SAH Edu is imposable on anti-dumping duty.

6. (b)

- (i) Any expenditure incurred in contravention of any law, for the time being in force, is not deductible u/s 37 of the Income-tax Act, 1961, even though it is incurred wholly and exclusively for the purposes of business.

Secret commission paid to a Government official is covered by the above and hence is not deductible. It is not relevant that it is a trade practice or has been approved by the Board. This is not secret commission to some general public, but to a Govt. official, which is not ethical.

Further, since no tax would be deducted at source (as the payee is not identified), the provisions of section 40(a)(ia) will also be attracted. Disallowance will arise on this count also.

Some of the earlier decisions rendered on the issue holding that secret commission might be allowable, will not hold good after the introduction of section 40(a)(ia).

- (ii) Expenses relating to issue of convertible debentures is in respect of a loan and cannot be equated to expenses incurred for issue of share capital. It is a deductible expenditure.

It is immaterial that the debentures are convertible into equity shares after one year. Hence ₹ 2 lacs can be allowed as deduction.

In the case of **CIT vs Secure Meters 321ITR 611 (SC)** the Supreme Court has clearly held that expenditure on issue of debentures, whether partly or fully convertible, is a deductible expenditure.

- (iii) Ransom money paid to for rescuing the executive director, who was kidnapped, cannot be said to be an expenditure incurred in contravention of any law, for the time being in force and not deductible u/s 37 of the Income-tax Act, 1961.

Therefore the said payment can be claimed as deduction, being a payment made wholly and exclusively in connection with the business. Without the executive director, the functioning of the company will be affected and hence expenditure incurred to rescue him will be deductible.

Similar view was taken in **CIT vs- Khem Chand Moti Lai Jain, Tobacco Products (P) Limited 340 ITR99 (P&H)**.

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SECTION B Tax Practice

Answer Question No. 9 which is compulsory and any one from the rest in this Section.

7. (a) Poorni Cars Ltd., is engaged in manufacture of cars in the State of Tamil Nadu. Being a prestigious unit, certain VAT concessions were conferred by the High Power Committee (HPC) of the State Government, consequent to which only 60% of the VAT collected was remitted during the year to the State Government. According to the Central Excise Department, the VAT retained by the assessee and not remitted to the State Government, amounting to ₹ 40 lakhs during the year ended 31.03.2015, would form part of the "Transaction value", since the HPC had not stated anything about the retained VAT amount against any scheme of capital subsidy. The entitlement certificate also did not give any indication of deferment of tax or capital subsidy.

Is the contention of the Department tenable in law?

7

- (b) Mr. Gavaskar, an Engineering graduate who worked abroad for the past 20 years in software industry, returned to India recently. He inherited one residential house at Fort, Mumbai which was acquired by his father in 1950's. The fair market value of the property as on 01.04.1981 is ₹ 5 lakhs. The property, if sold now, would fetch a price of ₹ 3 crores. He desires to start a company for manufacture of fertilizer at Rajkot. He wants to have a tax-free use of entire sale proceeds in the venture contemplated by him.

Cost inflation index for the FY 2014-15 is 1024.

Advise Mr. Gavaskar suitably within the four corners of law.

8

Answer:

7. (a) As per section 4(3)(d) of the Central Excise Act, transaction value "means the price actually paid or payable for the goods, when sold, and includes in addition to the amount charged as price, any amount that the buyer is liable to pay to, or on behalf of, the assessee, by reason of, or in connection with the sale, whether payable at the time of the sale or at any other time, including, but not limited to, any amount charged for, or to make provision for, advertising or publicity, marketing and selling organization expenses, storage, outward handling, servicing, warranty, commission or any other matter; but does not include the amount of duty of excise, sales tax and other taxes, if any, actually paid or actually payable on such goods."

In the given situation, since the VAT collected was not remitted to the Govt., the issue is whether it is to be included in the transaction value. The VAT has been actually paid by the customers, but not remitted to the State Govt.

Similar issue came up before the Supreme Court in the case of **CCE vs. Maruti Suzuki Ltd.** 2014 (307) ELT 625 (SC).

The Supreme Court agreed with the Revenue that there was no mention in the decision of the HPC about adjustment of this amount of sales tax concession against any scheme or any capital subsidy. The entitlement certificate also did not give any indication of deferment of tax or capital subsidy.

The Apex Court held that since assessee retained 50% of the sales tax collected from customers which was neither actually paid to nor actually payable to the Government, transaction value under section 4(3)(d) of the Central Excise Act, 1944, would include the amount of sales tax.

The **contention of the Department is hence tenable** in law.

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7. (b) Advice for Mr. Gavaskar for avoiding LTCG tax

Mr. Gavaskar when transfers the residential house, he would become liable for long-term capital gains. The indexation benefit for the financial year 2014-15 would at the most increase the indexed cost of acquisition to 51.20 lakhs ($\text{₹ } 5 \text{ lakhs} \times 1024/100$). The long-term capital gain would be around ₹ 2.50 crores.

Since he wants to deploy the entire sale proceeds in the new venture proposed by him, he cannot deploy the capital gain or sale proceeds in section 54EC bonds. Even such deployment is limited to ₹ 50 lakhs and therefore use of section 54 or section 54EC is ruled out.

Mr. Gavaskar must comply with the provisions of section 54GB which provides exemption in respect of capital gain arising on transfer of residential property. The following conditions are to be satisfied for availing the benefit:

- (i) The assessee must deploy the net consideration for subscription of equity shares of an eligible company.
- (ii) The eligible company within one year from the date of subscription in equity shares by the assessee must utilize this amount for purchase of new asset.
- (iii) The eligible company means the company incorporated in India during the period from the first day of April of the previous year relevant to the assessment year in which the capital gain arises to the due date of furnishing of return under section 139(1) by the assessee.
- (iv) The eligible company must be engaged in the business of manufacture of an article or thing.
- (v) Mr. Gavaskar must hold more than 50% of share capital or more than 50% of voting right after the subscription in shares.
- (vi) The company must be a small or medium enterprise as per MSME Act, 2006.
- (vii) The new asset means new plant and machinery and does not include office appliances including computers or computer software or any vehicle.
- (viii) The recipient company must use the amount obtained by way of subscription by issue of shares towards acquisition of new assets. To the extent it is not utilized for the purchase of new asset before the due date specified under section 139 it shall be deposited in such bank or institution specified by the Central Government in the official gazette. The proof of such deposit shall accompany the return filed.
- (ix) Mr. Gavaskar must not transfer equity shares of the company and similarly the company must not transfer the new asset acquired by it for a period of 5 years from the date of their acquisition. In the event of transfer, the capital gain not charged earlier shall be deemed to be the capital gain of the previous year in the hands of Mr. Gavaskar or the company, as the case may be.
- (x) Only individual and HUF assessee could avail this benefit of establishing an MSME enterprise in the form of corporate entity and avail tax exemption from capital gains on transfer of residential house property. Mr. Gavsakar being an individual, can avail this benefit.

8. (a) M/s. Dolphin Consultants (DC) in Mumbai has entered into a contract in April, 2014 with Tungabhadra Steels Ltd. (TSL) in Karnataka for conducting technical survey in relation to setting up of steel plants in various locations, all over India. As per terms of the contract,

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DC is to receive consultancy fees and reimbursement of expenses actually incurred on travelling and accommodation for carrying out the survey. The parties also separately agreed that DC would pay the clearing charges for goods imported by TSL through Mumbai port. For this purpose, TSL declared DC as their agent.

Discuss on what principles the value of taxable service will be computed by DC. 8

- (b) Mr. Singh's income tax assessment for the Assessment Year 2006-07 was made by the Assessing Officer on 30th November, 2008 after making certain disallowance under Section 40A(3). Mr. Singh preferred an appeal to the Commissioner (Appeals) contesting the disallowance and the Commissioner (Appeals) passed the order of appeal on 31st December, 2011. The Assessing Officer gave the appeal effect by passing an order on 1st February, 2012. Thereafter, Mr. Singh noticed that the Assessing Officer did not consider brought forward loss of Assessment Year 2005-06, though such loss was assessed by the Assessing Officer and duly claimed by Mr. Singh in the return of income for the Assessment Year 2006-07. Mr. Singh filed an application under Section 154 of the Income Tax Act on 1st January, 2015. The Assessing Officer rejected the application on the ground that such application was time-barred.

Explain with reasons, the correctness or otherwise of the contention of the Assessing Officer. 7

Answer:

8. (a) From the given facts it is seen that the consultancy fees charged by the DC would be taxed under service tax. The issue is whether and to what extent the reimbursements claimed by DC would be included in the taxable value of service. Section 67 of the Finance Act, 1994, the governing section for service tax valuation, provides inter alia that service tax would be payable on the gross amount charged, and where the consideration is not ascertainable, valuation will be on the basis of the Service Tax (Determination of Value) Rules, 2006 ("Rules"). Rule 5(1) of the Rules states that value would include all costs and expenses incurred by the service provider and reimbursed by the service receiver. Rule 5(2) states that where such expenses are incurred by the service provider as a 'pure agent' of the service recipient, it shall be excluded from value. This would include situations where the service provider incurs an expenditure on behalf of the service recipient as an agent of the latter, and where the service provider does not use or hold any title to the goods or services so procured. It follows that the expenditure as pure agent should be on something that has no relationship with the service being provided. These conditions are prescribed in Rule 5(2).

In the instant case, reimbursement claimed in respect of travelling and accommodation expenses cannot be said to be incurred by DC as a pure agent of TSL since the prescribed conditions are not fulfilled. Hence as per the law as it stands, such reimbursements shall be included in the value of taxable service.

However, the judiciary have been holding divergent views on this issue. The more recent decisions lean more in the assessee's favour. Particular reference may be made to the decision of the Delhi High Court in **Intercontinental Consultants & Technocrats (P) Ltd. Vs UOI (2013) 38 STT 75**, where it was held that such reimbursement can never be considered for levy of service tax since the same is not covered in section 67 of the Act. Accordingly, Rule 5(1) of the Valuation Rules was held to be ultra vires as it travelled beyond the scope of section 67 of the Act. However, the applicability of such decisions is open to question. The High Court was of the firm view that service tax is payable for 'such service', reimbursable expenses are not charges for 'such service' and hence not includible in value.

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It may also be mentioned that in the Finance Bill, 2015, section 67 has been amended by introducing an Explanation that consideration for service shall include reimbursement of expenses. To nullify the said judgment of Delhi High Court Sec.67 has been amended to provide that consideration for a taxable service shall include all reimbursable expenditure or cost incurred and charged by the service provider.

Explanation given under section 67. It provides that

“(a) ‘consideration’ inter-alia includes-

- (i) any amount that is payable for the taxable services provided or to be provided;
- (ii) any reimbursable expenditure or cost incurred by the service provider and charged, in the course of providing or agreeing to provide a taxable service, except in such circumstances, and subject to such conditions, as may be prescribed....”

Given the above, ‘Consideration’ now will specifically cover reimbursements in the service tax net.

This will however be applicable only the date of enactment of the Finance Bill, 2015 (date from which the amendment takes effect) and not to the expenses reimbursed prior to that date.

As regards reimbursement of clearing charges, it is seen that DC has incurred this as pure agent of TSL and the required conditions have been fulfilled. Hence this reimbursement shall not be included in taxable value.

8. (b) As per section 154 of the Income-tax Act, 1961, an order of rectification of any mistake apparent from the record can be passed by the Assessing Officer before expiry of 4 years from the end of the financial year in which the order sought to be rectified was passed by him. The mistake should be one apparent from records and also, a time limit is prescribed in this regard.

Non-consideration of brought forward loss relating to earlier year duly assessed by the Assessing Officer and claimed in the return of income in subsequent year is a mistake apparent from the record.

The issue for consideration in the instant case is whether the time limit for 4 years under section 154 would apply from the end of the financial year 2008-09 in which the assessment order was passed or from the end of the financial year 2011-12 in which the order giving appeal effect was passed by the Assessing Officer.

Once an appeal against the order passed by the Assessing Officer is preferred and is decided by the appellate authority, the order of the Assessing Officer merges with the order of the appellate authority. After such merger, the original order of the Assessing Officer ceases to exist and the order of the appellate authority prevails. Thus the period of limitation of 4 years for the purpose of section 154 has to be counted from the financial year 2011-12 in this case and the same would expire on 31st March, 2016. Since the assessee has filed the application for rectification on 1st January, 2015. Therefore, the application for rectification cannot be rejected on the ground of expiry of period of limitation.

Since both the requirements of section 154 stand fulfilled, the rejection of the rectification application by the APO is not proper.

Above view finds its support from the decisions in **Hind Wire Industries vs. CIT (1995) 212 ITR (SC)** and **CIT vs. Tony Electronics Limited (2010) 320 ITR 378 (Del)**.

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9. Sanvitha Manufacturing Industries Ltd. reports a net profit of ₹ 15 lakhs for the year ended 31.03.2015 after debit/credit of the following items:

A. Items debited to Profit and Loss Account:	₹
(i) Provision for income tax	5,00,000
(ii) Expenditure towards amalgamation of Cochin Industries P Ltd., Cochin in December 2014.	8,00,000
(iii) Fees for technical services paid to foreign company without deduction of tax at source and no TDS was remitted till the date specified in Section 139(1).	1,00,000
(iv) Provision for Bad and Doubtful Debts	6,00,000
(v) Depreciation	40,00,000
(vi) Cash payments for purchase of raw materials in excess of ₹ 20,000. Aggregate of such payments	7,00,000
(vii) Bank term loan interest (actually paid during the year and up to the 'due date' for filing the return specified in section 139(1) ₹ 3,00,000)	8,00,000
(viii) Rent paid for a branch premises owned by one of the directors who has 22% stake in the company. (25% of the expenditure is excessive to the prevailing market rent).	12,00,000
B. Items credited to Profit and Loss Account:	
(i) Revaluation reserve in respect of fixed assets	7,50,000
(ii) Agricultural income—net	3,50,000
(iii) Deferred tax liability	4,00,000

Additional Information:

- (i) Depreciation debited to Profit and Loss Account given above includes ₹ 10,00,000 in respect of assets revalued.
- (ii) The following amounts are brought forward as on 01.04.2014, relating to the Assessment Year 2014-15:

Particulars	As per Books of Account ₹	As per Income Tax assessment ₹
Business Loss	22,00,000	Nil
Unabsorbed Depreciation	17,00,000	35,00,000

You are required to compute for the Assessment Year 2015-16,—

- (i) Income liable to tax under Section 115JB of the Income Tax Act, 1961; and
 (ii) Total income chargeable to income tax, as per normal provisions.

Answer:

9. Sanvitha Manufacturing Industries Ltd.

Computation of income to tax under section 115JB for the A.Y. 2015-16

Particulars	₹
Net Profit as per Profit and Loss Account	15,00,000

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Add	Provision for income-tax		5,00,000
	Expenditure towards amalgamation of Cochin Industries (P) Ltd, Cochin in December 2014 - need not be added back for computing income liable to tax U/s. 115JB		Nil
	Fees for technical services paid to foreign company without deduction of tax at source - though liable for disallowance U/s. 40(a)(i), no adjustment is required U/s. 115JB.		Nil
	Provision for bad and doubtful debts - tantamount to provision for diminution in value of asset i.e. sundry debtor - hence added		6,00,000
	Depreciation debited to P&L account - added		40,00,000
	Cash payment for purchase of raw materials exceeding ₹20,000. Aggregate payments ₹7,00,000 - does not require any adjustment U/S.115JB		Nil
	Bank term loan interest whether paid or not has no significance while computing income liable to tax U/s.115JB		Nil
	Rent paid to branch premises to a person having substantial interest is liable for disallowance U/s. 40A(2)(b) but has no impact while computing income U/s. 115JB.		Nil
			66,00,000
Less	Amount withdrawn from revaluation reserve credited to P&L account	7,50,000	
	Agricultural income exempt U/s.10	3,50,000	
	Deferred tax liability credited to P&L account	4,00,000	
			15,00,000
			51,00,000
Less	Depreciation excluding depreciation in respect of assets revalued (₹40 lakhs minus ₹10 lakhs)	30,00,000	
	Brought forward business loss or unabsorbed depreciation as per books of account - whichever is less is deductible	17,00,000	
			47,00,000
	Income liable to tax U/s.115 JB		4,00,000

Sanvitha Manufacturing Industries Ltd

Computation of total income for the A.Y.2015-16

Particulars		₹
Net Profit as per Profit and Loss Account		15,00,000
Add	Provision for income-tax	5,00,000
	Expenditure towards amalgamation of Cochin Industries (P) Ltd, Cochin in December 2014 - the expenditure is deductible in 5 equal annual instalments. 4/5 th of the expenditure is added back [Section 35DD].	6,40,000
	Fees for technical services paid to foreign company without deduction	1,00,000

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	of tax at source -liable for disallowance U/s.40(a)(i).		
	Provision for bad and doubtful debts -disallowed		6,00,000
	Depreciation debited to P&L account - added back		40,00,000
	Cash payment for purchase of raw materials exceeding ₹20,000. Aggregate payments ₹7,00,000- disallowed U/s.40A(3)		7,00,000
	Bank term loan interest actually paid is only allowable. Unremitted portion of term loan interest added back		5,00,000
	Rent paid to branch premises to a person having substantial interest: Liable for disallowance U/s. 40A(2)(b)		3,00,000
			88,40,000
Less	Amount withdrawn from revaluation reserve credited to P&L account	7,50,000	
	Agricultural income exempt U/s.10	3,50,000	
	Deferred tax liability credited to P&L account	4,00,000	
			15,00,000
			73,40,000
Less	Depreciation excluding depreciation in respect of assets revalued (₹40 lakhs minus ₹10 lakhs)	30,00,000	
	Unabsorbed depreciation brought forward from earlier years	35,00,000	
			65,00,000
	Total Income		8,40,000