

Suggested Answer_Syl12_Dec2016_Paper 16

FINAL EXAMINATION

GROUP III

(SYLLABUS 2012)

SUGGESTED ANSWERS TO QUESTIONS

DECEMBER 2016

Paper- 16: TAX MANAGEMENT AND PRACTICE

Time Allowed: 3 Hours

Full Marks: 100

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

Wherever required, the candidate may make suitable assumptions and state them clearly in the answers.

Working notes should form part of the relevant answer.

All sub- divisions of a question should be answered continuously.

All questions in Income Tax relate to the Assessment year 2016 – 17, unless stated otherwise.

Answer Question No. 1 which is compulsory and answer any five from the rest.

1. (a) Choose the most appropriate alternative: 1×10 = 10
- (i) Which of the following income is not to be treated as income of a charitable trust from properties held under trust?
- (A) Income from units of mutual funds specified in section 10(23D)
(B) Capital gain on sale of immovable property
(C) Agricultural income
(D) Interest on fixed deposit with banks
- (ii) Advance tax is not payable during a financial year, if the amount of income tax as reduced by the amount of tax deducted or collected at source is less than
- (A) ₹ 10,000
(B) ₹ 7,500
(C) ₹ 5,000
(D) ₹ 2,500
- (iii) The rate of surcharge applicable to a domestic company having a total income of ₹ 7.50 crores is
- (A) 5%
(B) 7%
(C) 10%
(D) 12%
- (iv) CENVAT credit is to be reversed if value of input service and service tax payable is not paid
- (A) Within 2 months of the date of invoice.
(B) Within 3 months of the date of invoice.
(C) Within 4 months of the date of invoice.

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- (D) Within 6 months of the date of invoice.
- (v) Input which is not eligible for CENVAT credit is
- (A) Light diesel oil.
 - (B) Goods used for generation of electricity for captive consumption.
 - (C) Accessories cleared along with the final product, the value of which is included in the value of the final product.
 - (D) Stores consumed for manufacture of the final product.
- (vi) The threshold limit of consideration eligible for exemption from service tax in respect of performance in folk or classical art forms of music/ dance/ theatre is
- (A) ₹ 1,00,000
 - (B) ₹ 1,50,000
 - (C) ₹ 2,00,000
 - (D) ₹ 5,00,000
- (vii) When Service is rendered by a person located in non-taxable territory to a person in taxable territory then the person liable to pay service tax would be
- (A) none
 - (B) service provider
 - (C) service receiver
 - (D) both equally
- (viii) Time limit for return of capital goods from a job worker to the manufacturer for the purpose of availing CENVAT credit is
- (A) 6 months
 - (B) 1 year
 - (C) 18 months
 - (D) 2 years
- (ix) When Mr. A incurred medical expenditure for his father (age 70) of ₹25,000 and paid by cheque health insurance premium of ₹10,000 on father's policy, the quantum of deduction eligible under section 80D would be
- (A) ₹30,000
 - (B) ₹25,000
 - (C) ₹ 10,000
 - (D) ₹ 15,000
- (x) When a partnership firm consisting of four partners with equal share has brought forward business loss of ₹10 lakhs and one of the partners retired on 01.04.2016, the amount of business loss eligible for carry forward would be
- (A) ₹ 10 lakhs
 - (B) Nil
 - (C) ₹ 2.50 lakhs
 - (D) ₹ 7.50 lakhs
- (b) Fill up the blanks: 1 × 10 = 10
- (i) Service provided by a guest house for lodging purpose is not liable to service tax, if the declared tariff of a unit of accommodation is less than ₹ _____.
 - (ii) Central excise registration is granted within _____ working days of the receipt of a duly completed application form.
 - (iii) Interest on compensation for acquisition of a property is chargeable to income tax in the year of _____ (accrual/ receipt).
 - (iv) Maximum penalty under section 271B of the Income-tax Act for failure to furnish tax audit report within due date prescribed in section 44AB is ₹ _____.
 - (v) Deduction under section 80G of the Income-tax Act is allowed at _____.

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- _____ % of the amount of donation made to Swachh Bharat Kosh.
- (vi) When a new industrial undertaking is set up in the State of West Bengal on or after 01.04.2015, the rate of additional depreciation applicable for the plant and machinery installed therein would be _____.
- (vii) The turnover limit prescribed under section 92BA for the specified domestic transaction is ₹ _____.
- (viii) When the quarterly statement of TDS is filed belatedly, the fee for default in furnishing the statement shall be ₹ _____ per day.
- (ix) The rate of service tax applicable in respect of a charitable institution conducting yoga classes would be _____.
- (x) Transport allowance granted to an employee, who is physically fit to meet his expenses for commuting between the place of residence and place of work is exempted under section 10(14) of the Income-tax Act to the extent of ₹ _____ per month.

Answer: 1 (a)

- (i) C. Agricultural Income
 (ii) A. ₹ 10,000
 (iii) B. 7%
 (iv) B. within 3 months of the date of invoice
 (v) A. Light Diesel Oil
 (vi) B. ₹ 1,50,000
 (vii) C. Service receiver
 (viii) D. 2 years
 (ix) A. ₹ 30,000
 (x) D. ₹ 7.50 lakhs

Answer: 1 (b)

- (i) 1,000
 (ii) Two
 (iii) Receipt
 (iv) 1,50,000
 (v) 100
 (vi) 35%
 (vii) 20 crores
 (viii) 200
 (ix) Nil
 (x) 1,600

2. (a) SA Associates, a partnership firm consisting of two partners, Sukanya and Ananya is engaged in the business of trading in leather goods in Kolkata.

The summarized Profit & Loss Account of the firm for the year ended 31st March, 2016 is given below:

| Particulars | ₹ | Particulars | ₹ |
|---------------------------------------|------------------|-------------|------------------|
| Cost of goods sold and other expenses | 89,95,000 | Sales | 95,50,000 |
| Depreciation | 50,000 | | |
| Net profit c/d | 5,05,000 | | |
| | 95,50,000 | | 95,50,000 |

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| | | | |
|---|----------|----------------|----------|
| Interest on capital to Sukanya (at 15%) | 1,50,000 | Net profit b/d | 5,05,000 |
| Partner's Remuneration: | | | |
| Sukanya | 1,44,000 | | |
| Ananya | 1,20,000 | | |
| Share of profit: | | | |
| Sukanya | 45,500 | | |
| Ananya | 45,500 | | |
| | 5,05,000 | | 5,05,000 |

Additional Information:

- (i) Cost of goods sold includes cash purchase of ₹2,00,000 from a supplier on a single day.
- (ii) Interest on partners' capital and remuneration to partners are duly authorised by the partnership deed.

The firm opts to pay tax on presumptive basis under section 44AD of the Income-tax Act:

- (i) Compute the income of the firm under the head "profits and gains from business or profession" for Assessment Year 2016-17.
- (ii) If the firm does not wish to opt for presumptive scheme under section 44AD, what is the additional compliance burden for the firm? 8

- (b) Mr. Subramani purchased 1000 equity shares in VKS Private Ltd. at a cost of ₹50 per share on 01.12.2012. VKS Private Ltd. has two divisions viz. textile division and paints division. Paints division was transferred on 1st October, 2015 by VKS Private Ltd. to RR Private Ltd. in a scheme of demerger which satisfies all the conditions laid down in section 2(19AA) of the Income-tax Act. Under the demerger scheme Mr. Subramani received 750 shares in RR Private Ltd.

Mr. Subramani sold 500 shares of VKS Private Ltd. and 600 shares of RR Private Ltd. at ₹200 per share and ₹300 per share respectively on 28.03.2016.

Net book value of assets transferred by VKS Private Ltd. to RR Private Ltd. was ₹25 lakhs. Paid-up capital and general reserve of VKS Private Ltd. immediately before demerger were ₹60 lakhs and ₹40 lakhs respectively.

Compute capital gain arising from above transactions in the hands Mr. Subramani for Assessment Year 2016-17 indicating briefly the reasons to support your answer.

Cost inflation index-Financial Year 2012-13: 852; financial year 2015-16: 1081. 8

Answer 2: (a) (i)

Computation of Income of SA Associates under the head "Profits & Gains from business or Profession" for Assessment Year 2016-17

| | ₹ | ₹ |
|--|----------|----------|
| Profit calculated at 8% of Sales under section 44AD (₹ 95,50,000 × 8/100) | | 7,64,000 |
| Less: Interest on Partners Capital (₹ 1,50,000 × 12/15) | | 1,20,000 |
| Book Profit | | 6,44,000 |
| Less: Partners' Remuneration under section 40(b) | | |
| 90% of ₹3,00,000 | 2,70,000 | |
| 60% of 3,44,000 | 2,06,400 | |
| | 4,76,400 | |
| Partners' remuneration paid | 2,64,000 | |
| Deduction restricted to | | 2,64,000 |

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| | | |
|-------------------------|--|----------|
| Taxable Business Income | | 3,80,000 |
|-------------------------|--|----------|

Note: In case profit is computed on presumptive basis under section 44AD, deductions under section 30 to 38 are deemed to have been allowed.

Hence, there cannot be any disallowance under section 40A (3) in respect of cash payment of ₹ 2,00,000 made on a single day.

- (ii) If the firm does not opt for presumptive taxation scheme under section 44AD, additional compliances are as follows:
- (a) The firm has to maintain books of accounts compulsorily under section 44AA.
 - (b) The accounts of the firm are required to be compulsorily audited under section 44AB.

Answer 2: (b)

Computation of capital gains in the hands of Mr. Subramani for Assessment Year 2016-17

| Particulars | ₹ | ₹ |
|--|----------|----------|
| Consideration for sale of 600 shares of RR Private Ltd (600 × ₹300) | 1,80,000 | |
| Less: Indexed cost of acquisition ₹ 7,500 × 1081/852 (Note 2) | 9,516 | |
| Long-term capital gain on sale of shares of RR Private Ltd | | 1,70,484 |
| Consideration for sale of 500 shares of VKS Private Ltd (500 × 200) | 1,00,000 | |
| Less: Indexed cost of acquisition ₹18,750 × 1,081/852 (Note 3) | 23,790 | |
| Long-term capital gain | | 76,210 |
| Total long-term capital gain | | 2,46,694 |

Notes:

1. As per section 47(vii), capital gain tax liability does not arise in case of any transfer or issue of shares by the resulting company, in a scheme of demerger to the shareholders of the demerged company if the transfer or issue is made in consideration of demerger of the undertaking. Therefore, tax liability does not arise to Mr. Subramani on receipt of 750 shares in RR Private Ltd. in consideration of demerger of paints divisions of VKS Private Ltd.
2. As per section 49 (2C), the cost of acquisition of shares of resulting company shall be the amount which bears to the cost of acquisition of shares held by the assessee in the demerged company the same proportion as the net book value of the assets transferred in a demerger bears to the net worth of the demerged company immediately before demerger.
Net worth means aggregate of paid up capital and general reserves as appearing in the books of account of demerged company immediately before the demerger Therefore, cost of acquisition of each share of RR Private Ltd is-
 $\text{₹}50 \times \text{₹}25 \text{ lakhs} / (\text{₹}60 \text{ lakhs} + \text{₹}40 \text{ lakhs}) = \text{₹}12.50$
Cost of acquisition of 600 shares of RR Private Ltd = ₹ 12.50 × 600 = ₹ 7,500
3. As per section 2(42A), the period of holding of shares of demerged company is to be considered for computing the period of holding of shares of resulting company. Since the shares of VKS Private Ltd were acquired on 01-12-2012, the period of holding of shares of RR Private Ltd is more than 36 months. Hence, capital gain on sale of shares of RR Ltd. is long-term capital gain.
4. As per section 49(2D), the cost of acquisition of the original shares held by the shareholders of the demerged company shall be deemed to have been reduced by the amount as arrived at under section 49(2C).
Therefore, cost of acquisition of each share of VKS Private Ltd. = ₹50 - ₹ 12.50 = ₹37.50
Cost of acquisition of 500 shares of VKS Ltd. = 500 × ₹ 37.50 = ₹18,750

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3. (a) Statement of Profit & Loss of SRK Ltd., a company resident in India for the year ended 31.03.2016 shows a net profit of ₹25,00,000 after debit/ credit of the following items:

(i) Items debited to Statement of Profit & Loss:

| Particulars | ₹ |
|--|----------|
| Provision for permanent diminution in valuation of Investments | 85,000 |
| Provision for gratuity made on the basis of actuarial valuation | 1,50,000 |
| Interest on term loan due to a bank (not paid before due date for filing return of income for Assessment Year 2016-17) | 1,65,000 |
| Penalty for violation of provisions of Foreign Exchange Management Act | 1,00,000 |
| Provision for loss of subsidiary company, MNO Ltd. | 1,50,000 |

(ii) Items credited to Statement of Profit & Loss:

| Particulars | ₹ |
|--|----------|
| Share in income of one association of persons as member | 1,10,000 |
| Income from units of mutual funds specified in section 10(23D) | 80,000 |
| Long-term capital gain | 3,00,000 |

Additional information:

- (i) Balance of Statement of Profit & Loss shown in the Balance Sheet at the asset side as at 31.03.2015 was ₹15,00,000 which includes unabsorbed depreciation of ₹ 5,00,000.
- (ii) Long-term capital gain has been invested in bonds of National Highway Authority of India.
- (iii) The Association of Persons of which the company is a member has paid tax at maximum marginal rate.

Compute minimum alternate tax under section 115JB of the Income-tax Act for Assessment Year 2016-17 indicating brief reason for treatment of each item. 8

- (b) Good Health Trust is registered under section 12AA of the Income-tax Act and engaged in providing training in yoga and promoting yoga. During previous year 2015-16 details of gross receipts of the trust are as follows:

| Particulars | ₹ |
|--|-----------|
| Receipts by way of fees for training in yoga and delegate fees for seminar on yoga | 25,00,000 |
| Interest on investments | 5,50,000 |
| | 30,50,000 |

- (i) State with reasons whether the trust can retain its character of a charitable trust in Assessment Year 2016-17.
- (ii) Assuming that the trust is formed to run a gymnasium centre and its gross receipts comprise of training fees ₹3,80,000, voluntary contribution ₹7,20,000 and interest on investments ₹9,00,000, will it lose the character of charitable trust? 8

Answer: 3 (a)

Computation of Book Profit of SRK Ltd. and Minimum Alternate Tax for Assessment Year 2016 – 2017

| Particulars | ₹ | ₹ |
|--|---|-----------|
| Net profit as per Statement of Profit & Loss | | 25,00,000 |
| Add: Provision for permanent diminution in value of investment | | |

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| | | |
|---|----------|-----------|
| not allowed | 85,000 | |
| Provision for loss of subsidiary company not allowed | 1,50,000 | |
| | | 2,35,000 |
| | | 27,35,000 |
| Less: Share in income of association of persons | 1,10,000 | |
| Income from units of mutual funds specified in section 10(23D) | 80,000 | |
| Business loss or unabsorbed depreciation, as per books whichever is lower | 5,00,000 | |
| | | 6,90,000 |
| Book Profit under section 115JB | | 20,45,000 |
| Minimum alternative tax at 18.5% | | 3,78,325 |
| Education cess at 3% | | 11,350 |
| | | 3,89,675 |

Notes:

1. Provision for gratuity made on the basis of actuarial valuation is not a provision for unascertained liability. Hence, it is not to be added back.
2. Interest on term loan due to bank not paid on or before due date of filing return of income is disallowed under section 43B in computation of business income. But the same is not disallowed in computation of book profit under section 115JB even if it is not paid on or before due date of filing return of income.
3. Penalty for infraction of any law is disallowed under normal provision, but the same is not disallowed for computation of book profit under section 115JB.
4. Long-term capital gain is a part of book profit under section 115JB. Exemption under section 54EC is not available for investment in National Highway Authority for computation of book profit under section 115JB.
5. Since AOP has paid tax at maximum marginal rate, share of the assessee company in income of AOP is to be reduced in computation of book profit.

Answer: 3 (b)

- (i) The definition of "charitable purpose" as per section 2(15) of the Income-tax Act has two parts viz. specific category like relief of the poor, education, medical relief, preservation of environment (including watersheds, forest and wildlife) and preservation of monuments or places or objects of artistic or historic importance and general category viz. advancement of any other object of general public utility.

The Finance Act, 2015 has amended section 2(15) with effect from Assessment Year 2016-17 to include "yoga" in the specific category. It means that with effect from Assessment Year 2016-17 any institution which undertakes activities like holding programmes on yoga or publishing books on yoga or other programmes as part of its activities, such activities shall not be considered as advancement of any other object of general public utility.

The definition of "charitable purpose" under section 2(15) has been further amended to provide that the advancement of any other object of general public utility shall not be a charitable purpose, if it involves the carrying on any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business, for a cess or fee or any other consideration, irrespective of nature of use or application or retention, of income from such activity,

- (1) such activity is undertaken in the course of carrying out of such advancement of any other object of general public utility; and
- (2) the aggregate receipt from such activity or activities, during the previous year does not

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exceed 20% of the total receipts, of the trust or institution undertaking such activity or activities, for the previous year.

Yoga being under the specific category in the definition of "charitable purpose", the restriction applicable to institution engaged in advancement of general public utility shall not be applicable to Good Health Trust, even though its receipts of ₹ 25 lakhs by way of fees for training in yoga and delegate fee for seminar on yoga exceeds 20% of total receipts of ₹ 30.50 lakhs. Therefore, the trust can retain its character of a charitable trust in Assessment Year 2016-17 and is entitled to exemption under section 11.

(ii) Running a gymnasium center is, however, not falling in the specific category. It is advancement of any other object of general public utility.

But it can be seen that its receipts by way of training fee (i.e. fee for commercial activity) is ₹3.80 lakhs and it constitutes 19% of total receipts of ₹20 lakhs. Since receipt from commercial activity has not exceeded 20% of total receipts of the trust, it will not lose the character of charitable trust and it is entitled to exemption under section 11 in Assessment Year 2016-17.

4. (a) Parikhshit holds 17% shares in Tintin Private Ltd. He gifted 12% shares to his wife, Prerana on their marriage anniversary on 01.12.2015. Prerana obtained a loan of ₹10 lakhs at 10% interest p.a. from Tintin Private Ltd. on 28.02.2016, when the accumulated profit of the company was ₹ 7.50 lakhs.

Examine the tax implication of the above transactions for Assessment Year 2016-17. 6

(b) Anil, employed with a company furnished the following particulars of his investments and payments during the previous year 2015-16:

| Particulars | ₹ |
|---|----------|
| Contribution to Public Provident Fund | 80,000 |
| Five year term deposit with a nationalized bank | 1,00,000 |
| Life Insurance premium (on a policy with sum assured ₹1,20,000 taken on 1st June, 2015 on his own life) | 15,000 |
| Contribution at the rate of 15% of his salary to the National Pension Scheme of the Central Government. The employer made matching contribution | 1,80,000 |

Compute the deduction that can be claimed by Anil under Chapter VI-A of the Income-tax Act for Assessment Year 2016-17. 6

(c) The business premises of Bijli Private Ltd. were searched under section 132 of the Income-tax Act on 01.08.2015, when assessment proceedings under section 143(3) for Assessment Year 2013-14 and Assessment Year 2014-15 and reassessment proceeding under section 147 for Assessment Year 2011-12 were pending before the Assessing Officer.

(i) State the assessment years for which notice under section 153A can be issued for making post-search assessment.

(ii) Also state the fate of the pending assessments and reassessment. 4

Answer: 4 (a)

Property received from relative without consideration is not chargeable to tax under section 56(2) in the hands of the recipient. Relative includes spouse. Therefore, gift of shares by Parikhshit to his wife, Prerana is not taxable in the hands of Prerana.

Under section 2(22)(e), any payment by a closely-held company by way of loan or advance to its shareholder, being a person who is the beneficial owner of shares, holding not less than 10%

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of the voting power, is deemed as dividend to the extent to which the company possesses accumulated profits.

Accordingly, in this case, ₹7,50,000 (i.e., loan to the extent of accumulated profits of Tintin Private Ltd.) would be deemed as dividend in the hands of Prerana, who holds 12% equity shares in Tintin Private Ltd., under section 2(22)(e).

Thereafter, the clubbing provisions under section 64(1)(iv) would be attracted, as per which, income as arises, directly or indirectly, from asset transferred to spouse, otherwise than for adequate consideration, would be included in the hands of the transferor.

If the assets so transferred are shares in a company, the loan taken from the company is deemed as dividend income of the shareholder under section 2(22)(e) to the extent to which the company possesses accumulated profits. Thus, on account of this deeming provision, such loan is treated as income arising from the shares. [CIT v. Vimalan (A.) (1975) 98 ITR 529 (Mad.)]

Accordingly, as per section 64(1)(iv), such income arising in the hands of the shareholder, Prerana, by virtue of section 2(22)(e) (i.e., deemed dividend of ₹7,50,000) would be included in the total income of Parikhshit, who had transferred the said shares to Prerana without consideration.

Answer: 4 (b)

Computation of deduction available to Anil under Chapter VI-A for Assessment Year 2016-17

| Particulars | ₹ | ₹ |
|---|----------|-----------------|
| <u>Deduction under section 80C</u> | | |
| Contribution to Public Provident Fund | 80,000 | |
| Five year term deposit with bank | 1,00,000 | |
| Life Insurance Premium (Deduction restricted to 10% of sum assured i. e. ₹12,000) | 12,000 | |
| | 1,92,000 | |
| Deduction restricted to | | 1,50,000 |
| <u>Deduction under section 80CCD(1)</u> | | |
| Own contribution to National Pension Scheme of Central Government | 1,80,000 | |
| Less: Deduction admissible under section 80CCD(1B) | 50,000 | |
| | 1,30,000 | |
| Deduction restricted to 10% of salary (1,80,000 × 10/15) | | 1,20,000 |
| | | 2,70,000 |
| Aggregate deduction under section 80C and 80CCD (1) restricted to ₹ 1,50,000 under section 80CCE | | 1,50,000 |
| Deduction under section 80CCD (1B) in respect of own contribution to National Pension Scheme of Central Government | | 50,000 |
| Deduction for employer's contribution to National Pension Scheme of Central Government under section 80CCD(2) restricted to 10% of salary | | 1,20,000 |
| Total deduction under Chapter VI-A | | 3,20,000 |

Note: Deduction under section 80CCD (1B) is not subject to overall limit of ₹1,50,000 under section 80CCE. Hence, it is beneficial for Anil to claim deduction under section 80CCD (1B) first in respect of own contribution to National Pension Scheme. Thereafter, the remaining amount of ₹1,30,000 should be claimed under section 80CCD(1) subject to a maximum of 10% of salary.

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Answer: 4 (c)

- (i) Where a search has been conducted under section 132 of the Income-tax Act, the Assessing Officer shall serve a notice under section 153A to the person whose premises has been searched requiring him to furnish return of income in respect of each of the assessment years falling within six assessment years immediately preceding the assessment year relevant to the previous year in which such search is conducted.
In the given case, search was conducted on 01-08-2015 previous year 2015-16 relevant to assessment year 2016-17. Therefore, the Assessing Officer can issue notice for six assessment years' viz. 2010-11, 2011-12, 2012-13, 2013-14, 2014-15 and 2015-16.
- (ii) Any assessment or reassessment relating to any assessment year falling within the period of six assessment years pending on the date of initiation of search under section 132 shall abate.
Accordingly, assessment under section 143(3) for Assessment Year 2013-14 and Assessment Year 2014-15 and reassessment for Assessment Year 2011-12 shall stand abated.

5. (a) **Mr. Srinivasan is owner of residential building at Chennai, in respect of which the following details are furnished to you:**

(i) **Basement of the building is leased to Mr. Shantanam, who is a retail trader. Half of the basement is used by Mr. Shantanam as godown for storing his goods and the other half is used as his office..**

(ii) **Ground floor of the building is let out to Mr. Rathi who uses the same as a guest house.**

(iii) **First floor is occupied by Mr. Srinivasan for his residential purpose.**

(iv) **Second floor is let out to Ms. Sumangala who uses the same as her residence.**

For each floor of the building separate rent agreement/ lease deeds have been executed.

Examine the liability of Mr. Srinivasan to service tax in respect of the building. Also state whether principle of bundled service shall apply. **8**

(b) **MNO Ltd. imports a machine by air. CIF price of the machine is 5,000 US \$. Freight paid and insurance cost are 1,000 US \$ and 1,500 US \$. The bank realizes the payment from the importer at the exchange rate of ₹61 per US \$. The rate of exchange notified by the Central Board of Excise and Customs is ₹60 per US \$, while the exchange rate notified by RBI is ₹ 62 per US \$.**

MNO Ltd. spends ₹50,000 in India for carrying out certain development activities with respect to the imported machine.

Basic customs duty is 10%, excise duty leviable on similar goods in India is 12.5% and education cess is 3% on duty. Additional duty of customs leviable under section 3(5) of the Customs Tariff Act is exempt.

Compute the amount of total customs duty payable by MNO Ltd. **8**

Answer: 5 (a)

- (i) **Basement:** As per section 65B (41) of the Finance Act, 1994, renting includes letting, leasing, licensing or other similar arrangements in respect of immovable property.
Hence, leasing out of the basement of the building to Mr. Shantanam is not covered under negative list under section 66D (m) of the Finance Act, 1994, as Mr. Shantanam uses the basement for commercial purpose.
Therefore, it would be liable to tax as declared service.
- (ii) **Ground floor:** Ground floor has been let out to Mr. Rathi who uses the same as guest house i.e. commercial purpose. Renting of ground floor is not covered under negative list of services. Hence it would be liable to service tax as declared service.

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- (iii) First floor: As the first floor is used by Mr. Srinivasan himself, it is not a service. Therefore, it is not liable to service tax.
- (iv) Second floor: Renting of second floor to Ms. Sumangala, who uses the same for her residence, is covered in the negative list of services.
Thus, it is not chargeable to service tax

As Mr. Srinivasan has let out different floors of his residential building to different tenants and separate rent agreement/lease deeds have been executed for each floor of such building, principle of bundled service will not apply.

Answer: 5 (b)

Computation of customs duty payable by MNO Ltd.

| Particulars | Amount ₹ |
|---|---------------|
| CIF Value | 5,000 US \$ |
| Less: Freight | 1,000 US \$ |
| Less: Insurance | 1,500 US \$ |
| FOB value | 2,500 US \$ |
| Add: Freight (20% of FOB value) – Note 1 | 500 US \$ |
| Add: Insurance (actual) | 1,500 US \$ |
| CIF | 4,500 US \$ |
| Add: 1% for landing charge | 45 US \$ |
| Value in US \$ | 4,545 US \$ |
| Exchange rate as per CBEC | ₹60 per US \$ |
| Assessable value (₹60 × 4,545 US \$) | ₹2,72,700 |
| Basic customs duty @ 10% | ₹27,270 |
| | ₹2,99,970 |
| Additional duty of customs as per section 3(1) of the Customs Tariff Act (CVD): 12.5% of ₹ 2,99,970 | ₹37,496 |
| Education cess at 3% on (₹ 27,270 + ₹ 37,496) | ₹1,943 |
| Total customs duty payable (₹ 27,270 + ₹ 37,496 + ₹ 1,943) | ₹66,709 |

Note:

1. As the goods are imported by air, the freight is restricted to 20% of FOB value as per rule 10(2) of the Customs (Determination of Value of Imported Goods) Rules 2007]
 2. Although there is no information regarding landing charges, they are charged @1% of CIF value [Rule 10(2) of the Customs (Determination of Value of Imported Goods) Rules, 2007]
 3. Rate of exchange determined by CBEC is considered in view of Explanation to section 14 of the Customs Act, 1962.
 4. As per Rule 10(1)(b)(iv) of the Customs (Determination of Value of Imported Goods) Rules, 2007 value of development work undertaken elsewhere than in India is includible in the value of imported goods.
 5. Since excise duty rate on similar goods is 12.5%, CVD will be levied @ 12.5%.
- 6. (a) PQR Manufacturing Private Ltd. manufactures a product 'A' for captive consumption in the factory of the company. Following details are provided to you in respect of manufacture of the product 'A'.**

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| Particulars | ₹ |
|--|----------|
| Cost of direct materials consumed (including excise duty ₹12,500 for which CENVAT credit is available) | 1,12,500 |
| Direct labour cost | 85,400 |
| Consumption of stores and spares | 12,600 |
| Quality control cost | 3,000 |
| Research & Development cost | 2,500 |
| Administrative cost: Production overhead | 4,500 |
| Others | 2,000 |
| Selling and distribution cost | 28,000 |
| Scrap value realized | 3,200 |

Determine the value of product 'A' for the purpose of excise duty under rule 8 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000. 8

- (b) In an appeal filed by Rishi Private Ltd., CESTAT passed an order holding that the activity carried on by the company attracts service tax liability. The company is willing to contest the order of the CESTAT.

Advise the company as to whether it can file appeal to the jurisdictional High Court on the question of levy of service tax on the activity carried on by the company. 4

- (c) Determine the place of provision of services and their taxability in the following cases: 2×2= 4

(i) Vinod, a consulting engineer provides his professional services to a company incorporated in UK in respect of an immovable property located in Cairo.

(ii) XYZ Ltd. has been engaged by Oil & Gas Ltd. to provide specific services connected with exploration of oil and gas by virtue of a single agreement for a composite consideration in respect of specific sites in Tripura, Assam and Gujarat. The proportion of services provided by XYZ Ltd. in the above States is 25%, 65% and 10%. XYZ Ltd. does not have centralized registration.

Answer: 6 (a)

Cost of production of goods produced for captive consumption is to be determined as per " Cost Accounting Standard (CAS)-4: Cost of Production for Captive Consumption' issued by the Institute of Cost Accountants of India as per CBEC circular no. 692/8/2003 dated 13- 02 -2003.

Computation of cost of production as per CAS-4 and value of the excisable goods

| Particulars | ₹ |
|---|----------|
| Cost of direct materials (₹1,12,500 - excise duty ₹12,500) Note 1) | 1,00,000 |
| Direct labour cost | 85,400 |
| Consumption of stores and spares | 12,600 |
| Quality control cost | 3,000 |
| Research & Development cost | 2,500 |
| Administrative cost relating to Production (Note 2) | 4,500 |
| | 2,08,000 |
| Less: Scrap value realized | 3,200 |

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| | |
|---|----------|
| Cost of production as per CAS- 4 | 2,04,800 |
| Value of excisable goods ($\text{₹}2,04,000 \times 110\%$) (Note 3) | 2,25,280 |

Notes

1. As CENVAT credit is available on central excise duty paid on direct materials, the same has been deducted from cost of direct materials as per CAS-4
2. Administrative overhead in relation to activity, which is not a manufacturing activity is excluded in determining cost of production as per CAS-4
3. Selling and distribution cost is not to be considered for computation of cost of production as they are not in relation to production activity.
4. As per rule 8 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, the value of the excisable goods used for captive consumption is 110% of cost of production of such goods.

Answer: 6 (b)

Section 83 of the Finance Act, 1994 provides that the provisions of section 35G and section 35L of the Central Excise, 1944 shall be applicable to service tax.

As per section 35G (1) of the Central Excise Act, 1944 an appeal shall lie to the High Court from every order passed in appeal by the CESTAT (other than an order relating, among other things, to the determination of any question having a relation to the rate of duty of excise or to the value of goods for the purposes of assessment), if the High Court is satisfied that the case involves a substantial question of law.

Section 35L(1) of the Central Excise Act, 1944 provides that an appeal shall lie to the Supreme Court from any order passed by CESTAT relating, among other things, to the determination of any question having relation to the rate of duty of excise or to the value of goods for purposes of assessment.

Thus on a combined reading of section 35G(1) and section 35L(1), it can be inferred that an appeal against an order of CESTAT relating to the determination of any question having a relation to the rate of duty of excise / service tax or to the value of goods/services for purposes of assessment shall not lie to the High Court. Appeal against such orders will lie to the Supreme Court.

Further, as per section 35L(2), the determination of any question having a relation to the rate of service tax shall include the determination of taxability for the purposes of assessment.

Hence, in the given case Rishi Private Ltd. should be advised to file appeal to the Supreme Court under section 35L of the Central Excise Act, 1944, which alone has exclusive jurisdiction to decide the said question.

Answer: 6 (c)

- (i) In this case, consulting engineer's services provided by Vinod are in respect of an immovable property located in Cairo. Place of provision of service is Cairo, which is a non-taxable territory.
Hence, no service tax is chargeable. (Rule 5 of PoPS Rules)
- (ii) In the given case, all the locations fall within the taxable territory. However, PoPS Rules shall

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still apply as these rules are also useful for those service providers who operate from multiple locations within India having centralized registration for the purpose of determining the precise taxable jurisdiction applicable to their operations.

Where any immovable property related services referred to in rule 5 of PoPS Rules is provided at more than one location, including a location in the taxable territory where the greatest proportion of the service is provided (rule 7 of the PoPS Rules).

Hence, in the given case, XYZ Ltd is liable to service tax and the place of provision of services is Assam as greatest proportion of services is provided in Assam.

7. (a) (i) CI Ltd entered into a contract with a foreign supplier for import of certain goods at US \$ 500 CIF per MT. Under the contract, the consignment was to be shipped in July 2015. However, time for shipment was extended mutually to 15.09.2015. Goods were actually shipped on 10.09.2015 at the price prevailing on the date of contract. The international market price of the goods had increased drastically after expiry of the original shipment period. The Revenue contended that the contract price could not be accepted as transaction value in terms of Rule 3 of the Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 and therefore, customs duty should be imposed on increased price.
Decide the correctness of the contention of the Revenue by a decided case law. 4
- (ii) Can penalty be imposed under rule 15(1) of the CENVAT Credit Rules, 2004 on the directors of the company for wrong CENVAT credit availed by company? 4
- (b) M/s. India Bakers manufactures biscuits named as "India nuts". Biscuits are notified under section 4A of the Central Excise Act, 1944 with an abatement of 30%. The following information has been furnished by M/s. India Bakers with regard to clearances of packs of 'India Nuts'.
- (i) 5,000 packs having MRP of ₹100 per pack were sold in retail packages, but the buyer is charged for 4500 packs only at ₹90 per pack. (Further 100 packs were given free as quantity discount).
- (ii) 200 packs were given as samples, without any MRP on the pack.
- (iii) 1,000 packs manufactured on job work basis for Mumbai Bakers, another bakery company, which were cleared after putting MRP of ₹100 each. Each such pack is sold by Mumbai Bakers at ₹80 to individual customers. Cost of raw material supplied by Mumbai Bakers is ₹30,000, job charges including profit of M/s. India Bakers is ₹15,000, transportation charges of raw material to M/s. India Bakers and biscuits to Mumbai Bakers is ₹5,000.
- (iv) 200 packs of biscuits having MRP ₹100 each were packed in a single package for protection and safety during transportation and cleared at ₹12,500. 1000 of such packages were cleared.

Determine the central excise duty payable, if rate of duty is 12.5%.

Note: Turnover of M/s. India Bakers in the previous financial year is ₹ 440 lakh. 8

Answer: 7 (a)

- (i) In the instant case, it can be observed that since the contract entered into for supply of goods at US \$ 500 CIF per MT could not be performed on time, the extension of time for shipment was agreed upon by both parties to the contract.

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The goods had volatile fluctuations in its price in the international market. But the supplier did not increase the price of the goods even after the increase in its price in the international market.

Further, there is no evidence that the supplier and the importer were in collusion. Extension of time for shipment was mutually agreed upon.

Therefore, contention of the Revenue to levy customs duty on increased price is not correct.

The above view is supported by the decision of the Supreme Court in the case of CCus vs Aggarwal Industries Ltd. 2011(272) ELT 641 (SC)

- (ii) The words "any person" used in rule 15(1) of the CENVAT Credit Rules, 2004 clearly indicate that the person who has availed CENVAT credit wrongly shall only be liable to penalty. Therefore, if wrong CENVAT credit is taken by a company, penalty under Rule 15(1) can be imposed on the company. Penalty cannot be imposed on directors of such company.

Answer: 7 (b)

Computation of assessable value

| | ₹ | ₹ |
|---|-------------|-------------|
| Retail sale price of 5,000 packs (5,000 × ₹ 100) | 5,00,000 | |
| Less : Abatement @ 30% | 1,50,000 | |
| Assessable value (A) | | 3,50,000 |
| Retail sale price of 200 packs given as free samples (200 × ₹ 100) | 20,000 | |
| Less: Abatement @ 30% | 6,000 | |
| Assessable Value (B) | | 14,000 |
| Retail sale price of 1000 packs manufactured on job work basis (1000 × ₹ 100) | 1,00,000 | |
| Less: Abatement @ 30% | 30,000 | |
| Assessable Value (C) | | 70,000 |
| Retail sale price of 1000 packages containing 200 packs each packed for safety in transportation (200 × ₹ 100 × 1000) | 2,00,00,000 | |
| Less Abatement @ 30% | 60,00,000 | |
| Assessable Value (D) | | 1,40,00,000 |
| Total assessable value (A)+(B)+(C)+(D) | | 1,44,34,000 |
| Excise duty @ 12.5% of ₹ 1,44,34,000 | | 18,04,250 |

Notes:

- (i) Section 4A of the Central Excise Act, 1944 overrides section 4 and therefore the assessable value will be the retail price declared on the package less abatement irrespective of the quantity discounts offered.
- (ii) Free samples have to be valued by taking into consideration the deemed value under section 4A of the Act.
- (iii) The assessable value will be retail sale price less abatement as per section 4A and not the value as determined under rule 10A of the Central Excise Valuation (Determination

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of Price of Excisable Goods) Rules, 2000.

- (iv) Outer packaging is not wholesale package since it is meant for protection / safety during transportation. Such packaging does not require details like name / address, cost, month, year etc. The valuation hence will be on the basis of section 4A i.e. resale price less abatement.
- (v) Since the turnover in the previous financial year was more than ₹400 lakhs, Indian Bakers is not entitled to SSI exemption available under notification no. 8/2003 dated 01.03.2003 in the current year.

8. (a) (i) **What you understand by advance authorization scheme of duty exemption? Explain basic conditions of such authorization.** 4
- (ii) **A merchant exporter has annually exported goods whose FOB value ranged between \$ 5 million and \$ 10 million for the last 3 years. What is his status? What privileges is he eligible for?** 4
- (b) **Ms. Renu Kochar aged 28 years is a practicing cost accountant and a resident and citizen in India. Her income from profession in India for the previous year 2015-16 is ₹7,40,000 (Computed). During the year she visited Hong Kong to advise her clients located there and gross fee earned from clients in Hong Kong is ₹3,50,000. Tax paid on gross amount of fees in Hong Kong amounted to ₹87,500. Staff and overhead attributable to income derived in Hong Kong is ₹50,000. India does not have any double taxation avoidance agreement with Hong Kong.**
- She paid life insurance premium for self ₹1,10,000. She also paid ₹32,000 through credit card mediclaim insurance premium for her mother aged 61 years.**
- Determine the tax payable by Ms. Renu for Assessment Year 2016-17.** 8

Answer: 8 (a)

- (i) In the advance authorization scheme the importer is permitted to import goods which are used for export without payment of customs duty.

Advance authorization is valid for 12 months from the date of issue of such authorization.

The period for fulfillment of export obligation under advance authorization is 18 months from the date of issue of authorization or as notified by DGFT.

Export proceeds must be realized in free convertible foreign currency except otherwise specified.

- (ii) Based on the export performance during current and previous 2 financial years, business entities are given star grading such as one star export house, two star export house and upto five star export house based on the FOB value of export.

The merchant exporter having export turnover exceeding \$ 3 million and upto \$ 25 million is eligible for grading as one star export house. The privileges are -

- (a) Authorisation and custom clearances for both imports and exports on self declaration basis.
- (b) Fixation of input output norms on priority i.e. within 60 days.

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- (c) Exemption from compulsory negotiation of documents through banks. The remittance receipts however would continue to be received through banking channels.
- (d) Exemption from furnishing of bank guarantee in schemes under FTP.
- (e) They are entitled to export freely exportable items on free of cost basis for export promotion subject to an annual limit of ₹10 lakhs or 2% of average annual export realization during preceding three licensing years, whichever is higher.

Answer: 8 (b)

Computation of tax payable by Ms. Renu Kochar for Assessment Year 2016-17

| Particulars | ₹ | ₹ |
|---|----------|-----------|
| Income from profession in India | | 7,40,000 |
| Gross Income from profession in Hong Kong | 3,50,000 | |
| Less: Staff and overhead cost | 50,000 | |
| | | 3,00,000 |
| Gross Total Income | | 10,40,000 |
| Less: Deduction under section 80-C for life insurance premium | 1,10,000 | |
| Deduction under section 80-D for mediclaim insurance premium for mother who is a senior citizen (actual premium or ₹ 30,000, whichever is less) | 30,000 | 1,40,000 |
| Total Income | | 9,00,000 |
| Tax on above | | 1,05,000 |
| Education cess (3%) | | 3,150 |
| Total tax | | 1,08,150 |
| Rate of tax in India (1,08,150/9,00,000 × 100%) | | 12.02% |
| Rate of tax in Hong Kong (87,500 / 3,50,000 × 100%) | | 25% |
| Amount of income doubly taxed | | 3,00,000 |
| Amount of double taxation relief under section 91 (₹3,00,000 x 12.02%) (Note) | | 36,060 |
| Net tax payable (₹1,08,150 – ₹36,060) | | 72,090 |
| Note: Amount of double tax relief under section 91 is calculated by applying lower of Indian tax rate and rate of tax in Hong Kong on the doubly taxed income i.e. ₹ 3,00,000 | | |