Paper 7 - Direct Taxation

Section A

(Question No. 1 is compulsory and any four from Question No. 2 to 6)

Question 1

(a) Answer the following sub-divisions briefly in the light of the provisions of the Income-tax Act, 1961: (1×8)

(i) State the manner of determination of residential status of a Company.

(ii) State the taxability or otherwise, of interest received from the Central/State Government, in the hands of a non-resident.

(iii) State the provisions relating to exemption of income of mutual funds, as contained in Section 10(23D) of the Income tax Act, 1961.

(iv) State the taxability or otherwise, of salary, perquisite, allowance, received as gift by an employee from the employer.

(v) State the taxability or otherwise of income from house property, which is used by the assessee for the purposes of his own business.

(vi) State, whether an assessee can claim depreciation under section 32, on capital expenditure incurred on construction of any structure in a building, which is taken on lease, for the purposes of business or profession.

(vii) State, whether an assessee can claim deduction of expenditure incurred on scientific research, carried on by him.

(viii) State the circumstance, when interest is levied under Section 234A of the Income Tax Act, 1961. Also, state the rate at which interest is payable.

(b) Choose the correct alternative: (1×5)

(i) Remuneration received in respect of services rendered on a foreign ship is exempt in the case of:

(a) A resident.
(b) A non-resident, who is not a citizen of India.
(c) Resident, but not ordinarily resident.
(d) A citizen of India.

(ii) Rent or revenue derived from land, is treated as an agricultural income, if:
(a) It is derived from land.
(b) It is derived from land situated in India.
(c) It is derived from land situated in India, used for agricultural purposes.
(d) It is derived from land situated in India, used for agricultural and business purposes.

(iii) Deduction under section 80C of the Income Tax Act, 1961 can be claimed for fixed deposit made in any scheduled bank, if the minimum period of deposit is:
(a) 5 years.
(b) 8 years.
(c) 10 years.
(d) 12 years

(iv) The maximum exemption in respect of transport allowance granted to an employee to meet his expenditure for the purpose of commuting between the place of his residence and the place of his duty shall be:
(a) ₹600 per month.
(b) ₹700 per month.
(c) ₹800 per month
(d) ₹900 per month.

(v) The gross annual value of a house property, whose Municipal Value is ₹30,000, Actual Rent is ₹32,000, Fair Rent is ₹36,000 and Standard Rent is ₹40,000, shall be:
(a) ₹36,000.
(b) ₹35,000.
(c) ₹30,000
(d) ₹40,000

Question 2

(a) Compute the total income of Mr. Mukul for the A.Y. 2014-15 from the following information, relating to his income for the financial year 2013-14:

(i) He received salary of ₹30,000 per month including conveyance allowance @ ₹3,000 per month for official purposes.

(ii) He deposited ₹3,000 per month in his account under a pension scheme notified by the Central Government.

(iii) He paid a sum of ₹72,000 during the year as interest on loan taken in June, 2009 from bank for higher studies of his son.

(iv) He paid health insurance premium for himself and for his family members ₹10,200 in cash and ₹10,800 by credit card.

(v) He invested ₹48,000 in notified bonds issued by NABARD in January 2014.

(vi) Equity shares having fair market price of ₹1,20,000 (on the date of exercise of option) were allotted to him by the company at a concessional price of ₹24,000 on 04.06.2013, which were sold by him for ₹2,16,000 on 02.03.2014.

(b) Mr. Umesh did not file his return of income for the Assessment Year 2013-14 and a notice under section 142(1) of the Income Tax Act, 1961 was issued by the assessing Officer in November, 2013. The return of income was filed in December, 2013. He wants to file a revised return in January, 2014. Explain, whether it is possible to file a revised return?

(c) Explain whether it is mandatory for an assessee to claim depreciation under Section 32 of the Income Tax Act, 1961?

[8+3+2]

Question 3

(a) State with reasons, based on the provisions of the Act, as to chargeability of the following receipts to tax in the Assessment Year 2014-15:

1. **Rent of ₹1 Lakh charged from the tenants occupying houses (constructed on the land situated in India and used for agricultural purposes). The houses were used for residential purposes.**

2. **In addition to salary, Minister of Minority Welfare received an amount of ₹2,000 per month as an entertainment allowance.**

3. **Rent of ₹55,000, due for the period 01.04.2010 to 31.08.2010, was received on 23.12.2013, because of a court order. The property was sold out by the owner on 08.04.2013.**

4. **Growth Ltd. follows mercantile system of accounting. During the financial year 2013-14 it has negotiated with its bankers and converted an interest amount of ₹5 Lakhs into term loan which includes ₹ 2 Lakhs pertaining to the financial year 2013-14. Can the interest of ₹2 Lakhs pertaining to the Assessment Year 2013-14, be allowed as business expenditure?**

(b) Mr. Vighnesh received the following gifts during the P.Y. 2013-14, from his friend Mr. Mukesh:

(i) Cash gift of ₹60,000 on his birthday, 31st August, 2013.

(ii) 50 shares of Theta Ltd., the fair market value of which was ₹1,20,000 on the date of transfer i.e. 01.11.2013. The gift was received on the occasion of Diwali. Mr. Mukesh had originally purchased the shares on 13.06.2013, at a cost of ₹70,000.

Further on 05.01.2013, Mr. Vighnesh purchased land from his brother's relative for ₹10,00,000. On 7th March, 2014, the assessee sold 50 shares of Theta ltd. for ₹1.5 Lakhs.

Compute the Gross Total Income of Mr. Vighnesh, comprising of incomes chargeable under the heads "Income from Other source" and "Capital Gains" for A.Y. 2014-15.

[8+5]

Question 4

(a) Sterling LLP reports the following details for the financial year 2013-14:
Net Profit as per Profit and Loss account ₹54,00,000.

The following items are reflected in the Profit and Loss Account:

Credits	₹ In lakhs
Dividend from Indian companies	1
Net profit from an undertaking eligible for 100% deduction under section 80-IA	20
Profit on sale of vacant site	7
"Debits: Working partner's salary	12
Interest on capital to partners @ 12%	15
Provision for income tax	14
Commission (tax was deducted in financial year 2012-13 and remitted before the 'due date' for filing the return of income)	5.20
Depreciation	12

Other information –

(i) Depreciation allowable under section 32 of the Income-tax Act, 1961 is ₹ 8 lacs.

(ii) Long-term capital gain on sale of vacant site (computed) ₹ 5 lacs.

(iii) Working partner's salary and interest on capital to partners are authorized payment but subject to limits of section 40(b).

Calculate:

(i) Total income and regular income tax payable (as per normal provisions) for the Assessment Year 2014-15.

(ii) Adjusted total income and alternate minimum tax payable for the Assessment Year 2014-15.

(b) Distinguish between the nature of penalty leviable under Section 271AA and Section 271B of the Income Tax Act, 1961.

[10+3]

Question 5

(a) Discuss the liability for tax deduction at source in the following cases for the A.Y. 2014-15:

(i) An Indian company pays gross salary including allowances and monetary perquisites amounting to ₹5,60,000 to its Finance Manager. Besides, the company provides non-monetary perquisites to him in the same period whose value is estimated at ₹ 2,40,000.

(ii) Indira, an individual whose total sales in business during the year ending 31.03.2014 was ₹80 Lakhs, paid ₹6.5 Lakhs by cheque on 12.02.2014 to a contractor (an individual), for construction of his business premises, in full and final settlement. No amount was credited earlier to the account of the contractor in the books of Indira.

(iii) A television company pays ₹1,50,000 to a cameraman for shooting of a documentary film.

(iv) M/s. Joy Ltd. paid to Mr. Juneja ₹1,80,000 for compulsory acquisition of his house as per law of the State Government.

(b) Neeta Jain, engaged in various types of activities, gives the following types of particulars for her income for the previous year 2013-14:

(i) Profit of business of consumer and house hold products: ₹1,00,000.
(ii) Loss of business of readymade garments: ₹20,000.
(iii) Brought forward loss of catering business which was closed in A.Y. 2013-14: ₹30,000.
(iv) Short-term loss on sale of securities and shares: ₹30,000.
(v) Profit of speculative transactions entered into during the year: ₹25,000.
(vi) Loss of speculative transactions of A.Y. 2009-10, not set off till A.Y. 2013-14: ₹30,000.

Compute the total income of Ms. Neeta Jain for the A.Y. 2014-15.

[8+5]

Question 6

(a) State whether the following assessees have to file return of income and if so, the due date of filing return for the Assessment Year 2014-15:

(i) A registered trade union having income from let out property of ₹1,90,000.

(ii) A public trust hospital having an aggregate annual receipt of ₹110 Lakhs and availing exemption under Section 10(23C)(via) with total income of ₹1,65,000, before giving effect to such exemption.

(iii) A charitable trust registered under Section 12AA of the Income tax Act, 1961, having total income of ₹2,10,000.

(b) Flora Ltd. provides you with the following extracts from its Balance Sheet for the financial year ending on 31.03.2014:

Particulars	Amount (₹)	
	Unit X	Unit Y
Fixed Assets	75,00,000	1,70,00,000
Debtors	75,00,000	56,00,000
Liabilities	21,00,000	38,00,000
Stock-in-trade	37,50,000	19,00,000
Reserves		1,11,00,000
Share Premium		12,50,000

The paid up capital of Flora Ltd. amounted to ₹250 Lakhs.

The company acquired Unit Y on 01.04.2011. They made certain capital additions in the form of fixed assets for ₹19 Lakhs, during the year 2011-12. The members of the company have authorized the Board in their meeting held on 25.02.2013 to dispose off the Unit 'Y'. The company decides to sell the unit 'Y', by way of slump sale for ₹170 Lakhs as consideration.

The buyer agreed with the vendor-company to give time for putting through the sale, but not later than 31.07.2014, subject to a discount of 2% on agreed sale consideration. However, this

discount is not applicable, if the sale is completed after 31.03.2014. The written down value of the fixed assets of Unit Y under section 43(6) is ₹112 Lakhs.

Discuss the impact of the date of sale on the taxation of capital gains in the hands of Flora Ltd.

[6+7]

Section B

Question 7

(a) State the provisions of the Wealth Tax Act, 1957 relating to the assets transferred under revocable transfers. Also, explain the term 'revocable transfers'.

(b) State the provisions of the Wealth Tax Act, 1957 relating to conversion by an individual of his self-acquired property into joint family property.

[3+2]

Question 8 [OPTION- I]

Vineet is an individual, who is resident and ordinarily resident in India. The values of his assets and liabilities as per Schedule III of the Wealth Tax Act, 1957, as on 31.03.2014, are as follows:

Particulars	Amount(₹)
Guest House in Hong Kong	10,00,000
Jewellery gifted to his wife	15,00,000
Value of interest in the assets of a firm as a partner	8,00,000
Cash in hand	3,00,000
He took a loan for building the residential house in Mumbai	75,000
Commercial complex at Delhi having 20 offices which were let out for the whole of the previous year.	30,00,000
Residential house in Mumbai, which is let-out for 320 days in that previous year	10,00,000

Compute the net wealth and the wealth tax liability of Mr. Vineet for the A.Y. 2014-15. (5)

OR

Question 8 [OPTION- II]

(a) State the provisions relating to valuation of jewellery under the Wealth Tax Act, 1957.

(b) Mr. Maheshwar is aged 35 years. His father has settled a property in trust giving whole life interest therein to Maheshwar. The income from the property for the years 2010-11 to 2013-14 was ₹35,000, ₹40,500, ₹41,000 and ₹43,000 respectively. The expenses incurred each year were ₹1,500, ₹8,500, ₹250 and ₹9,000 respectively.

Calculate the value of life interest of Mr. Maheshwar in the property so settled on the valuation date March 31, 2014 on the assumption that the value of house as per Schedule III is ₹20 lakh. [Multiplier at the age of 35 is 10.804].

[2+3]

Section C

Question 9

(a) Discuss the concept of "Permanent Establishment", in the context of Double Taxation Avoidance Agreements.

(b) State the factors to be considered in determining whether a country is a tax haven or not.

(2+3)

Question 10 (OPTION-I)

(a) International Ltd. - a US Company has a subsidiary Native Ltd. in India. International Ltd. sells mobile phones to Native Ltd. for resale in India. International Ltd. also sells mobile phones to Country Ltd. - another mobile phone reseller in India. The sales quantity and price fixed by International Ltd. are as follows:

Buyer	Sale Price (₹/ unit)	Sale Quantity (mobile phones)
Native Ltd.	12,000	48,000
Country Ltd.	11,000	

The warranty in case of sale of mobile phones by Native Ltd. is handled by itself, whereas for sale of mobile phones by Country Ltd., International Ltd. is responsible for warranty for 6 months. Both International Ltd. and Native Ltd. extended warranty at a standard rate of ₹500 per annum.

In respect of the given transactions:

(i) Compute the Arm's Length Price for Native Ltd. for the given transactions.

(ii) Compute the additions required to be made in the total income of Native Ltd.

(iii) Also state whether the provisions of Section 10AA and Chapter- VIA, are applicable on the recomputed total income of Native Ltd.

(b) Techno King India Ltd., is a financial BPO arm of Techno King Inc., Germany. It bills Techno King Inc., at $ 20,00,000 per month for its services. Techno King India Ltd., also provides the same services to SG Ltd., South Africa and bills it at $ 18,00,000 per month. The man-hours spent on each work form the basis of billing. The direct cost of services per hour for Techno King India Ltd., works out to $500 and the indirect cost of services per hour for Techno King India Ltd., works out to $2000 per hour. In a month of 30 days Techno King India Ltd. works at 2 shifts per day, consisting of 7 hours work for Techno King Inc., Germany and 6 hours work for SG Ltd. respectively. Determine, whether the transactions are done at Arm's Length.

(c) Clear View Glasses Ltd., India exports semi finished glasses to its parent company Clear View Glasses Inc., USA. The exports are made at $ 200 per glass to the US Company (Freight and Insurance costs $75 is incurred separately). The cost per glass works out to $125 on import. Clear View Glasses Inc., USA polishes the glasses and markets the same @ $ 500 per glass. The polishing and marketing process cost @ $100 per glass. Compute the Arm's Length Price (ALP), for the said transaction.

(d) Luxury Life, India exports bath furniture only to its holding company, Luxury Life, Canada. The sale price per furniture is CAD 2,500. The direct and indirect costs amount to CAD 1,750. The furniture industry in India, of the comparable companies, has earned total export revenue of CAD 3,750 million. The industry average of total expenses of comparable companies works out to 85%. Compute the arm's length price of Luxury Life India.

(e) Discuss whether adjustment is required in the context of transfer pricing provisions, where the transfer price adopted for an international transaction for sale of goods by an Indian company during the financial year 2012-13 is ₹100 Lakhs, whilst the Arm's Length Price determined using the most appropriate method are ₹96 Lakhs and ₹ 112 Lakhs. Assume that the rate of permissible variation prescribed by the Central Government is 2% of the transfer price for this class of the international transaction.

(4+4+4+4+4)

OR

<u>Question 10 (OPTION-II)</u>

(a) The Income Tax Act, 1961 provides for taxation of a certain income earned by Nilesh. The Double Taxation Avoidance Agreement, which applies to Nilesh, excludes the income earned by Nilesh from the purview of tax. Is Nilesh liable to pay tax on the income earned by him? Discuss.

(b) Ms. Lakshmi, a resident Indian, furnishes the details for the Assessment Year 2014-15 :

Particulars	Amount (₹)
Income from profession	1,94,000
Share of income from a partnership in country X (tax paid in Country X for this income in equivalent ₹ 8,000)	40,000
Commission income from a concern in country Y (tax paid in country Y @ 20%, converted in equivalent Indian Rupees	30,000
Interest on scheduled banks [other than savings account]	20,000

(c) A foreign company WorldBiz Inc. carries on business in India through a branch office located in India. It submits the following information for the year ended 31.03.2014.

	Particulars	₹ Lakhs
(a)	Royalties received in pursuance of an agreement entered into on 30-06-2003 with an Indian concern	200
	Expenditure to earn the above income (i) Depreciation as per Income Tax Act on assets in branch in India	10
	(ii) Depreciation as per Income Tax Act on assets located in head office in U.S.A. which assets are partially used for Indian operations	9
	(iii) Salaries & other expenses of staff in India	120
	(iv) Payment to Singapore office for use of their data in India	6
	(v) Reimbursement of actual expenses incurred by Head office for the Indian Branch	12

	(vi) Paid to Head Office for apportionment of Certain head office expenditure	**15**
(b)	**Interest received from Indian concerns for moneys lent in foreign currency** **Collection charges for the interest**	**50** **5**
(c)	**Commission income received in India** **Expenses to earn the commission income**	**90** **11**

Compute the total income and tax liability for the Assessment Year 2014-15.

(d) Define "Specified Domestic Transaction", in the context of provisions relating to transfer pricing.

(4+4+7+5)