

Paper-7 – Direct Taxation

PTP_ Intermediate_Syllabus 2012_Dec2015_Set 3

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

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

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Time Allowed: 3 hours

Full Marks:

100

All the questions relate to the assessment year 2015-16, unless stated otherwise.

Working notes should form part of the answers.

Answer all questions.

Question No 1. Answer all the questions [2 x 10 = 20]

- (i) Mr. Pratap is an employee of ABC Ltd. getting a salary of ₹ 40,000 per month which is 'due' on the last day of the month but is paid on the 7th of next month. He is paid the salary of April, 2015 and May, 2015 in advance in March, 2015. What will be his gross income for the assessment year 2015-2016? [2]
- (ii) Star Ltd. imported machinery from Germany on 27.8.14 at a cost of ₹ 60 crores. Customs Duty paid @ 20%. Government granted subsidy of ₹ 35 crores. The entire logistics was supported by Nexgen Courier Ltd., an Indian Company. Total Service charges paid to them ₹ 30 lacs (Pre-acquisition cost) including service tax of ₹ 3,70,800. Compute Actual Cost, if assessee, avail CENVAT credit. [2]
- (iii) An individual practicing as a chartered engineer is in receipt of fees from a company, which had retained him for purposes of valuation of properties. The total fee agreed upon between the parties was ₹50,000. The engineer was paid the following amounts by the company:
30.01.2015 - ₹12,000 (advance of fees)
20.03.2015 - ₹20,000 (towards completion of work)
15.04.2015 - ₹18,000 (balance of fees on completion of work). Discuss the obligation for tax deduction at source. [2]
- (iv) X Ltd lets out its property to Y. Y sub-lets it. How is the sub-letting receipt will assessed in the hands of Y? [2]
- (v) Anirudh is a Regional Sales Manager of A Ltd. He is paid salary plus commission based on volume of sales effected by him. Anirudh claimed that the expenses incurred by him for earning the commission should be allowed as deduction. Discuss the validity of his claim. [2]
- (vi) Mr. Ravi, an IAS Officer, was posted to USA by the Government of India on 11.07.2014 for a period of 3 years. He was paid salary of ₹ 3 Lakhs for the period 01.04.2014 to 01.07.2014 and of ₹12 Lakhs for period upto 31.03.2015. He left India for USA in the night of 10.07.2014 and did not come even for a day until 31.03.2015. Examine the taxability of the above Income. [2]
- (vii) Explain the concept of marginal Relief? [2]
- (viii) What are the advantages while computing arm's length price Transactional Net Margin Method? [2]
- (ix) What are the methods in computation of arm's length pricing in relation to International Transaction/specified Domestic Transactions? [1]

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- (x) What are the modes of transfer of Intangible Assets under Internal transactions? [2]
- (xi) People Housing Ltd is engaged in the business of constructing residential and commercial properties. One of the building properties was included in the closing stock in Balance Sheet. The said building was let out for a monthly rent as suitable buyers could not be found. All other buildings had been sold by the company. State with reasons whether the income by way of rent from the unsold property is assessable as income from business or income from house property. [1]

Question 2. Answer any four questions [4 × 15 = 60]

- (a)(i) The following is the income of Shri Sudhir Kumar for the previous year 2014 – 15:

	₹
A. Profits from business in Iran received in India.	5,00,000
B. Income from house property in Iran received in India.	1,20,000
C. Income from house property in Sri Lanka deposited in a bank there.	1,80,000
D. Profits of business established in Sri Lanka deposited in a bank there, this business is controlled in India (out of ₹2,00,000 a sum of ₹1,00,000 is remitted in India).	2,00,000
E. Income from profession in India but received in England	2,40,000
F. Profits earned from business in Kanpur.	1,60,000
G. Income from agriculture in England, it is all spent on the education of children in London.	2,70,000

From the above particulars ascertain the taxable income of Shri Sudhir Kumar for the previous year 2014-15, if Shri (i) a resident and ordinarily resident, (ii) not ordinarily resident, and (iii) a non-resident. [5]

- (ii) Value of unfurnished accommodation (computed) ₹ 70,000. Cost of furniture provided by the employer ₹1,00,000. Hire charges of furniture (other than those owned by employer) provided in the accommodation ₹1,500 p.m. Amount recovered from employee ₹ 1,000 p.m. Compute taxable value of perquisite. [3]
- (iii) XYZ Ltd incurred expenditure amounting to ₹3,00,000 in connection with the issue of rights shares and ₹2,00,000 in connection with the issues of Bonus shares during the year ending 31.3.2015. The company seeks your opinion in the matter of eligibility for deduction of the expenditure incurred from its business profits for the assessment year 2015-16. [2]
- (iv) Prayag Power Projects is a power generating unit. On 1.4.2012, it purchased a plant of ₹ 60,00,000, eligible for depreciation @15% on SLM. Compute balancing charge or terminal depreciation assuming the plant is sold on 21.4.2014 for : (a) ₹ 10,50,000 (b) ₹ 35,00,000 (c) ₹ 48,00,000 (d) ₹65,00,000. (Ignore the provision of additional Depreciation) [5]

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(b)(i) For the previous year 2014–15, the business income of Shyam Ltd. before allowing expenditure on family planning is ₹2,00,000. The company had incurred the following expenditure on family planning amongst its employees during the previous year 2014-15:

- (1) Revenue expenses on family planning ₹1,10,000.
- (2) Capital expenditure on family planning ₹6,00,000.

Compute the deduction available for expenditure on family planning to the company assuming the company has income from other sources amounting to ₹20,000.

What will be your answer if the revenue expenditure on family planning is ₹2,15,000 instead of ₹ 1,10,000. **[5]**

(ii) HUM Bros., an HUF, started an undertaking in "Special Economic Zone" during the Previous Year 2009-2010. From the following particulars relating to the Previous Year 2014-2015, compute the Total Income for the Assessment Year 2015-2016:

	₹ (in lakh)
(i) Total Turnover	60
(ii) Export Sales	50
(iii) Business Profits	30
(iv) Receipt of convertible foreign exchange in India up to 30th September 2015	32
(v) Convertible foreign exchange kept outside India with the permission of RBI for importing a new machinery	8
(vi) Receipt of convertible foreign exchange in December 2015	6
(vii) Convertible foreign exchange received for reimbursement for freight, insurance attributable to export	4

[3]

(iii) Sweet Ltd. grows sugarcane to manufacture sugar. The data for the financial year 2014-15 is as follows :

Cost of cultivation of sugarcane	₹ 9,00,000
Market value of sugarcane when transferred to factory	₹ 15,00,000
Other manufacturing cost	₹ 9,00,000
Sales of sugar	₹ 37,50,000
Salary of Managing Director who looks after all operations of the Company	₹ 4,50,000

Determine its Business Income and Agricultural Income. **[3]**

(iv) Shri Shyam Temple Trust (Regd.) derived ₹ 7,00,000 income from the property held under charitable trust during the Previous Year 2014-2015. About 40% of the income has been received by the end of the financial year. The trust could spend ₹60,000 for charitable purposes during the year 2014-2015 and 40% receipts, received by the year end in 2014-2015, are being planned to be applied for charitable purposes during the Previous Year 2015-2016. Compute its income for the said two years if the amount planned to be spent during Previous Year 2015-2016 for charitable purposes is ₹ 1,00,000. **[4]**

(c)(i) Compute the capital gain in the following cases:

- (1) (a) P commenced a business on 15.04.1991. The said business is sold by P on 18.04.2014 and he received ₹12,00,000 towards goodwill.
- (b) What will be your answer in the above case, if P had acquired the goodwill for this business for a consideration of ₹2,00,000.

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- (2) R has been living in a rented accommodation since May 1994 and he is paying a rent of ₹500 per month. The landlord got the house vacated from R on 16.07.2014 and paid a sum of ₹5,00,000 for vacating the house.
- (3) S is a Chartered Accountant practicing in Delhi since January 1983. He transfers the practice to another Chartered Accountant Y on 15.07.2014 and charges ₹5,00,000 towards goodwill.
- (4) R purchased tenancy right on 01.04.1979 for ₹1,60,000. The same was sold by him on 14.08.2014 for ₹20,00,000. Fair market value of tenancy right as on 01.04.1981 was ₹2,50,000. **[5]**

(ii) The written down value of a block of asset as on 1.4.2014 was ₹8,00,000. An asset of the same block was acquired during the year for ₹3,00,000. Thereafter, all the assets of the block are sold for ₹12,00,000. Compute the depreciation for the assessment year 2015-16 and also indicate if there is any short-term capital gain/loss. **[2]**

(iii) Mr. Shahil purchased a piece of land on 4.1.1978 for ₹50,000. This land was sold by him on 2.9.2014 for ₹14,00,000. The market value of the land as on 1.4.1981 was ₹1,20,000. Expenses on transfer were 2% of the sale price. Compute the capital gain for the assessment year 2015-16. **[2]**

(iv) A has 2 motor cars which are used by him exclusively for his personal purposes. The cost of the cars was ₹1,50,000 and ₹1,80,000. The first car was transferred by him on 5.1.2015 to a firm in which he is a partner as his capital contribution. The market value of the car as on 5.1.2015 is ₹1,00,000, but it was recorded in the books of account of the firm at ₹2,00,000. Compute the capital gain if any, chargeable for the assessment year 2015-16. **[2]**

(v) Mr. Rahul, has computed his Gross Total Income for the assessment year 2015-16 which amounted to ₹4,70,000. It includes ₹3,70,000 on account of long-term capital gain. He has deposited ₹1,20,000 in a PPF during the previous year. Compute the tax payable by Mr. Rahul, a resident in India assuming that he is less than 60 years of age. **[4]**

(d)(i) From the following details, compute the Gross Total Income of Mr. A for the assessment year 2015-16:

	₹
1. Taxable income from salary	80,000
2. Income from house property House 'A' (let out)	(-) 95,000
House 'B' (Self – occupied , interest on borrowed money)	(-) 9,000
3. Short-term capital gain	12,000
4. Loss from long- term assets	25,000
5. Interest on securities (gross)	10,000

[4]

(ii) Chakarvarti is a Cost Accountant drawing following salary and allowances:

- Basic pay 20,000 p.m.
- Dearness allowance 1,000 p.m.
- City Compensatory allowance 100 p.m.
- House Rent allowance 750 p.m.
- Reimbursement of cost of travel and course fee to attend a seminar at Ooty 5,500
- Bonus at 20% of salary including Dearness allowance is also received. He is given a motor car (below 1.6 ltr.) and is entitled to use it for both office and private purposes. His employer also pays ₹400 p.a. on a Personal Accident Insurance Policy

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consistent with its policy of insuring all its employees. Deductions have been made from his salary as follows:

- Contribution to a recognized provident fund ₹ 1,000 p.m. and contribution to an approved superannuation fund ₹ 400 p.m.

There are matching contributions for both by the employer.

- Chakarvarti was in receipt of the following from a partnership firm where he was sharing one-third of the profits:
 - ₹ 45,000 as share of profits.
 - ₹ 30,000 as salary from the firm.
 - ₹ 20,000 as commission there from.
- He was a member of an association of persons from where he was paid ₹ 50,000 as share of profits. The association is chargeable to tax at the maximum marginal rate of tax.
- He donated ₹ 25,000 to National Foundation for Communal Harmony.
- Chakarvarti's minor son earned ₹35,000 by way of interest on public deposit in a company.
- Chakarvarti received ₹ 700 as interest in savings bank account in a (non-nationalised) scheduled bank. He pays ₹ 3,200 p.a. as life insurance premium.
- Chakarvarti is living in his own house. Annual value as fixed by Municipal Corporation is ₹ 7,200, while half year's tax is ₹ 900. He pays ₹ 100 as insurance on this property besides ₹ 3,600 as interest on ₹30,000 on mortgage, of this property. The borrowing was partly (₹ 20,000) for acquiring the house and the balance (₹10,000) for purchasing a home air-conditioner for the house.
- Chakarvarti received a gift valuing ₹ 4,900 on the occasion of the silver jubilee of the company. It is stated that a uniform amount was paid to each employee on this occasion.

Compute the assessee's total income for the assessment year 2015 – 16. **[7]**

- (iii) The estimated Gross Total Income of Mr. Jay is ₹8,45,000 which includes ₹1,00,000 on account of LTCG earned on 16.09.2014. Compute the Advance Tax Payable by Mr. Jay, assuming ₹11,000 has been deducted at source during the financial year 2014-15. **[4]**

- (e)(i) Mr. Khan, has accumulated profits of ₹3,00,000 excluding capitalized profits i.e. bonus shares of ₹1,00,000 issued in the past. The company distributed assets of ₹2,50,000 to the shareholder. Compute the amount taxable as dividend if the market value of the asset on the date of the distribution is:

- A. ₹2,00,000
- B. ₹3,50,000
- C. ₹4,50,000

[3]

- (ii) Sudhir was the Karta of HUF. He died leaving behind his major son Ganesh, his widow, his grandmother and brother's wife. Can the HUF retain its status as such or the surviving persons become co-owners? **[3]**

- (iii) If an assessment is remanded back to Assessing Officer, can he introduce new sources of income for assessment? **[3]**

- (iv) Can assessee follow different method of accounting for different businesses? **[3]**

- (v) An assessee filed a return of income on 31.8.2015 in respect of Assessment Year 2015-16 disclosing an income of ₹5 lakhs from business. It was not accompanied by proof of payment of tax due on self-assessment. Discuss the validity of such a return. **[3]**

Question No 3. Answer any two questions [2 × 10 = 20]

(a) "Mingle Engineering Ltd", a Korean Non Resident Company, had entered into an agreement for designing, fabricating, hook-up and commissioning of a platform in Bombay High with "Crude Oil India Ltd" an Indian Company. The agreement entered into was in two parts, one for the value to be charged for fabrication of structure in Korea for ₹20 Crores (having element of Profit in it of ₹ 2 Crores) and other for the Installation and Commissioning of the structure in Bombay High for ₹15 Crores (having element of Profit in it of ₹1.5 Crores). The Korean Company will also be setting up an Office in India for the activity of installation and commissioning of the platform which is likely to be completed in 9 months.

On these facts, you are required to answer -

(A) Whether the office of Mingle Engineering Ltd. to be opened in India be considered as its "Permanent Establishment"/ "Business Connection"?

(B) The amount of profits, if any, of the Non-Resident Company subject to tax in India.

(C) The Income subject to Tax in India, when the ALP of the fabrications of structure is determined at ₹ 19 Crores. **[10]**

(b)(i) Mobeaux LLP of Poland and Vamsi Ltd of India are Associated Enterprises. Vamsi imports 1000 compressors for Air Conditioners from Mobeaux at ₹ 7,500 per unit and these are sold to Winland Cooling Solutions Ltd at ₹11,000 per unit Vamsi had also imported similar products from De-Heat Ltd and sold outside at a Gross Profit of 20% on Sales.

Mobeaux offered a Quantity Discount of ₹ 1,500 per unit. De-Heat could offer only ₹ 500 per unit as Quantity Discount. The Freight and Customs Duty paid for imports from Poland had cost Vamsi ₹ 1,200 a piece. In respect of purchase from De-Heat, Vamsi had to pay ₹ 200 only as Freight Charges.

Determine the Arm's Length Price and the amount of increase in Total Income of Vamsi Ltd. **[5]**

(ii) EF Limited, an Indian Company, is engaged in manufacturing electronic components. 74% of the Shares of the Company are held by EF Inc. incorporated in USA. EF Limited has borrowed funds from EF Inc. at LIBOR plus 150 points. The LIBOR prevalent at the time of borrowing is 4% for US \$. The Borrowings allowed under the External Commercial Borrowings Guidelines issued under FEMA are LIBOR plus 200 basis points. Discuss whether the Borrowing made by EF Ltd is at Arm's Length. **[5]**

(c)(i) VKS International Ltd, the Assessee, has sold goods on 12.01.2015 to L Ltd. located in a Notified Jurisdictional Area (NJA), for ₹ 10.5 Crores. The sale price of identical goods sold to an unfamiliar customer in New York during the year was ₹ 11.5 Crores. While the second sale was on CIF basis, the sale to L Ltd was on F.O.B. basis. Ocean Freight and Insurance amount to ₹ 20 Lakhs.

India has a Double Taxation Avoidance Agreement with the USA. The Assessee has a policy of providing After-Sales Support Services to the tune of ₹ 14 Lakhs to all customers except L Ltd. The ALP worked out as per Cost Plus Method for identical goods is ₹ 12.10 Crores.

You are required to compute the ALP for the Sales made to L Ltd, and the amount of consequent increase, if any, in profits of the Assessee-Company. **[5]**

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(ii) Speedy Motors Ltd, an Indian Company, declared Income of ₹20 Crores computed in accordance with Chapter IV-D but before making any adjustments in respect of the following transactions for the year ended on 31.03.2015:

(A) Royalty of \$ 50,00,000 was paid to Fista Ltd for use of technical know—how in the manufacturing of van. However, Fista Ltd had provided the same know-how to another Indian Company for \$ 45,00,000. The manufacture of Van by Speedy Motors Ltd is wholly dependent on the use of technical know-how, in respect of which Fista Ltd has exclusive rights.

(B) Loan of Euro 5 Crores with interest @ 10% p.a. advanced by Hughes Ltd, a French Company, was outstanding on 31.03.2015. The Total Book Value of assets of Speedy Motors Ltd on the date was ₹ 500 Crores. Hughes Ltd had also advanced similar loan to another Indian Company @ 8% p.a. Total Interest paid for the year was EURO 0.5 Crore.

(C) 7,000 Vans sold to Hitech Ltd which holds 41% Shares in Speedy Motors Ltd at a price which is less by \$ 100 each van than the price charged from Bento Ltd.

Briefly explain the provisions of the Act affecting all these transactions and compute Taxable Income of Speedy Motors Ltd for A.Y.2015-2016 assuming that the value of 1\$ and of 1 EURO was ₹ 42 and ₹ 67, respectively, throughout the year. **[5]**