

INTERMEDIATE EXAMINATION GROUP II (SYLLABUS 2012)

SUGGESTED ANSWERS TO QUESTIONS DECEMBER 2015

Paper-11: INDIRECT TAXATION

Time Allowed : 3 Hours

Full Marks : 100

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

All questions are compulsory. In question No. 1, all sub-questions are compulsory.

In Question Nos. 2 to 8, student may answer any two of the three sub-questions (a), (b) and (c).

1. Answer the following questions with suitable reasons: 1×20=20

- (a) State the provision in Constitution of India which empowers State Government to levy sales tax (State Vat) on sale of goods within State.
- (b) A manufacturer manufactured goods on 24-02-2015, when excise duty was 12%, education cess was 2% and secondary and higher education payable was 1% of basic excise duty. He cleared goods from his factory on 06-03-2015, when excise duty rate was 12.50% and education cess was exempt. Advise the manufacturer the rate at which he should pay excise duty and education cess.
- (c) Who is senior in grade between Principal Commissioner and Chief Commissioner of Central Excise?
- (d) An assessee did not pay excise duty due to ignorance. During audit, the mistake was pointed out. Assessee paid the excise duty along with interest on his own. What is the maximum penalty that can be imposed on assessee?
- (e) An assessee has head office in Mumbai and factories at Rajkot and Pune. He is receiving various input services at Mumbai. He wants to transfer the credit of service tax paid on the input services to his factories, as he cannot utilize the credit at Mumbai office. Advise him.
- (f) An importer imported goods from out of India, and cleared on payment of customs duty. He claims that now they are not 'imported goods'. Is his claim correct?
- (g) Who is responsible to file Import Manifest in case of import of goods by sea?
- (h) What is 'relevant date' for issuing show cause notice demanding customs duty, if duty was not levied or not charged?
- (i) Which authority can make amendments/changes in Foreign Trade Policy?
- (j) A unit in Domestic Tariff Area (DTA) is making supplies to EOU unit. The unit paid excise duty while clearing goods and claimed refund of excise duty. His refund claim was rejected by department stating that he should have cleared without payment of excise duty to EOU. Is the contention of department correct?
- (k) When is e-payment of service tax is mandatory?
- (l) A show cause notice for payment of service tax of ` 4 lakhs plus penalty of ` 4 lakhs was issued to assessee. The demand was confirmed by Assistant Commissioner, but was dropped by Commissioner (Appeals). Department is of the view that order of

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Commissioner (Appeals) is not proper. Advise department on action that can be initiated by them.

- (m) Service provider A is providing exempted services. Service provider B is providing services in negative list. State distinction in respect of availment of Cenvat Credit of input services received by A and B.
- (n) A foreign exchange dealer purchased US dollars 1,000 from a tourist on dated 02-03-2015 at the rate of ₹ 64.70 per US dollars. The RBI reference rate that day was 1 USD= ₹ 66.40. Calculate value of service on which service tax is payable.
- (o) An air travel agent collected following amounts from his customer—Air fare—₹ 5,000. His service charges—₹ 400. Total—₹ 5,400. His bill is dated 14-04-2015. Calculate service tax payable by him.
- (p) What restrictions in respect of sales tax that can be imposed on declared goods?
- (q) Vat acts as self policing mechanism. Justify this statement.
- (r) An importer imported goods for resale. He paid following duties— Basic customs duty, Countervailing duty, Special CVD, Anti dumping duty and education cess. Is he eligible to get any refund if he resales the goods in India? If so, of which duty?
- (s) What is the maximum period for which Advance Pricing Agreement can be executed?
- (t) Comment—Presently, General Anti Avoidance Rules (GAAR) are applicable only when transaction exceeds ₹ 100 crores in a financial year.

Answer:

1. (a) Entry 54 of List II of seventh schedule to Constitution of India empowers State Government to levy sales tax (Vat) on sale within the State.
- (b) The manufacturer should pay excise duty @ 12.50%. Education cess is not payable.
- (c) Chief Commissioner is senior in grade.
- (d) No penalty can be imposed on assessee as matter stands closed, as per section 11A(1)(b)(ii) of Central Excise Act.
- (e) Assessee should register his Mumbai office as Input Service Distributor. He can then transfer the Cenvat credit to his factories by issuing monthly invoice on basis of turnover of his two factories.
- (f) His claim is correct. As per section 2(25) of Customs Act, 'imported goods' does not include goods which have been cleared for home consumption.
- (g) Master of vessel is responsible for filing Import Manifest in case of import of goods by sea. He is 'person in charge'.
- (h) If customs duty was not levied or charged, date of order of clearance of goods from customs is the 'relevant date'.
- (i) Government of India, Ministry of Commerce and Industry.
- (j) Contention of department is correct. As per Foreign Trade Policy, in such cases, refund is not permissible.
- (k) E-payment of service tax is mandatory for all service providers, irrespective of the quantum of service tax.
- (l) Normally, department can file appeal before CESTAT against order of Commissioner (Appeals). However, if the service tax involved is less than ₹ five lakhs, department cannot file appeal before CESTAT against order of Commissioner (Appeals), as per litigation policy of Government of India.
- (m) There is no distinction. Neither A nor B can avail Cenvat credit of input services.
- (n) Value of service = $(66.40 - 64.70) = 1.70 \times 1,000 = ₹ 1,700$ [rule 2B of Service Tax (Determination of Value) Rules, 2006]
- (o) Service tax payable is 12.36% of ₹ 400 i.e. ₹ 49.44.
- (p) Maximum rate at which sales tax can be imposed on declared goods by State Government is 5%.
- (q) A buyer gets input tax credit only if the seller issues proper Vat invoice. Hence, buyer insists that he will purchase goods from seller only if he issue proper Vat invoice. This increases tax compliance as buyer acts as police for seller.

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- (r) He is entitled to get refund of special CVD of 4% paid by him at the time of imports.
- (s) Maximum period for which Advance Pricing Agreement can be executed is five years.
- (t) At present, **General Anti Avoidance Rules (GAAR)** is not applicable to any transaction.

2. Answer any two of the three sub-questions (a), (b) and (c). 2×2=4
- (a) Explain significance of 'taxable event' with reference to tax liability. 2
 - (b) Name any two transactions which are 'deemed sale of goods' under constitutional provisions, on which service tax is also payable. 2
 - (c) State distinction between duty and cess. 2

Answer:

2. (a) 'Taxable event' is that on happening of which the charge of tax is fixed. It is that event, which on its occurrence creates or attracts the liability to tax. Such liability does not accrue at any earlier or later point of time.
- (b) Works contract, service of food in restaurant, hire purchase and leasing.
- (c) Distinction between cess and duty is that cess is a charge levied and collected for specified purposes, while duty (excise duty or customs duty) is for general revenue of Government. Duty is for general revenue purposes, while cess is for a definite purpose. Cess may be on production of goods or on export of goods.

3. Answer any two of the three sub-questions (a), (b) and (c). 8×2=16

- (a) (i) Enumerate items which have been specifically excluded from definition of 'input' in Cenvat Credit Rules i.e., inputs not eligible for availment of Cenvat Credit. 4
 - (ii) A LTU (large tax payer unit) can send intermediate goods from one registered unit to another without payment of excise duty. However, in certain circumstances, the LTU can clear goods to another registered unit only after payment of excise duty. What are those circumstances? 2
 - (iii) What are the products on which excise duty is payable under compounding levy scheme? Is the scheme mandatory or at the option of the manufacturer? 2
- (b) (i) Explain provisions relating to 'garnishee proceedings' in Central Excise for recovery of Excise duty. 3
- (ii) HMT Ltd. sold a special purpose machine. The details of contract are as follows:
- (1) Basic price—` 20,00,000
 - (2) Packing Charges charged extra—` 20,000
 - (3) Erection and commissioning charges for erection at the place of customer's factory —` 1,50,000.
 - (4) Separate Charges for designing the machinery—` 70,000.
 - (5) Insurance Charges for despatch of machinery from factory of HMT to the place of customer —` 20,000.
 - (6) Outward freight of machinery from-place of removal to customer's factory—` 30,000 extra
 - (7) State VAT—charged extra—` 2,00,000
 - (8) Cash discount @ 2% was allowable on basic price if customer paid total amount before despatch of goods. The customer had made full advance payment.

Excise duty rate is 12.5% which was charged extra.

Calculate Assessable Value of the machine and excise duty payable. Ignore Education cess and Secondary and Higher Education cess. 5

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- (c) (i) An assessee had manufactured certain goods and recorded them in his Daily Stock Account (DSA). Some inputs were lying in his store room and some inputs were on the shop floor. There were heavy floods due to which the inputs as well as final products in store room were damaged beyond repairs. Advise assessee the course of action to be taken in each case in respect of excise duty and Cenvat Credit. Note that the assessee has applied for compensation from insurance company and has obtained compensation. 4
- (ii) JG International Ltd. furnished the following information for the month of October 2015:
- (1) Input Goods A — Invoice dated 12-07-2014—Excise duty paid— ` 3,00,000.
 - (2) Input Goods B — Invoice dated 10-04-2015—Excise duty paid— ` 1,00,000.
 - (3) Input Goods C — Original invoice not available but Xerox copy duly certified by excise officer available—Excise duty paid— ` 4,40,000.
 - (4) Input Service X — Invoice dated 12-10-2015—Service tax paid— ` 22,300.
 - (5) Machinery falling under chapter heading 84 — Invoice dated 12-07-2014—Excise duty paid— ` 4,00,000.
 - (6) Invoice of Goods Transport Agency (GTA) for bringing raw materials to the factory was dated 15-08-2015. Service tax paid by JG International Ltd. ` 40,000 under reverse charge on 20-10-2015. However, payment was made to the Goods Transport Agency on 13-11-2015.

Determine the Cenvat Credit that can be availed by assessee during the month of October 2015. 4

Answer:

3. (a) (i) Following items have been excluded from definition of input in Cenvat Credit Rules.
- (A) light diesel oil, high speed diesel oil or motor spirit, commonly known as petrol;
 - (B) any goods used for - (a) construction or execution of works contract of a building or a civil structure or a part thereof; or (b) laying of foundation or making of structures for support of capital goods, - - except for the provision of service portion in the execution of a works contract or construction service as listed under clause (b) of section 66E of the Act
 - (C) capital goods except when used as parts or components in the manufacture of a final product.
 - (D) motor vehicles
 - (E) any goods, such as food items, goods used in a guesthouse, residential colony, club or a recreation facility and clinical establishment, when such goods are used primarily for personal use or consumption of any employee; and
 - (F) any goods which have no relationship whatsoever with the manufacture of a final product.
- (ii) If the registered unit is EOU/STP/EHTP unit, it is required to clear goods only on payment of excise duty. Similarly, if the recipient unit is enjoying exemption available in Himachal Pradesh, Uttaranchal, Sikkim, J&K, Kutch or North Eastern States, goods must be cleared only on payment of excise duty.
- (iii) The scheme is applicable to stainless steel pattas/pattis and Aluminium circles. The scheme is at the option of manufacturer. He can pay excise duty under normal scheme.
- (b) (i) Garnishee proceedings means Recovery from any other person who is required to pay any amount to the defaulter.

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'Garnishee order' means order to attach money or goods belonging to debtor in the hands of a third person. It is an order to garnishee requiring him not to pay or deliver the money or property of debtor to him but to pay it to Court/Authority.

It is possible that the some other person is liable to pay some amount to the defaulter - e.g. creditor. It is also possible that the defaulter may be having some amounts in Banks or Post Office or some insurance amount may be due to him or it may be held by such Bank/Post Office/Insurance company (even if not due). In such cases, the Central Excise Officer can issue notice to such creditor, bank, post office or insurance company to deposit such amount directly with Central excise, instead of paying it to the defaulter.

Once such notice is issued, such creditor, Bank, Post Office or Insurance company shall deposit the amount directly with the department. Such deposit with department has to be made even if as per the procedure, some pass book, insurance policy, deposit receipt or endorsement is required to be produced to Bank/Post Office/Insurance Company by the defaulter.

If such creditor, Bank, Post Office or Insurance Company, to whom notice has been issued, fails to pay such amount, such person himself will be considered as defaulter and recovery can be made from him as per provisions of Central Excise Act.

- (ii) Excise duty is not payable on the following - (i) erection and commissioning charges (ii) Insurance for dispatch of final product (iii) outward freight after place of removal (iv) State Vat.

Cash discount - Rs 40,000 [2% of ` 20,00,000]. This is allowable as deduction.

Packing charges are not allowed as deduction from the assessable value.

Thus, aggregate sale price in respect of which Vat and excise duty payable is

(A) Basic price - 20,00,000

(B) Add - Design charges - 70,000

(C) Add - Packing charges - ` 20,000

(D) Less - Cash discount allowable as deduction - ` 40,000.

Hence, assessable value = A+B+C-D = 20,50,000

Excise duty @ 12.5% = ` 2,56,250

- (c) (i) Assessee should inform department about loss as soon as possible. In respect of final products destroyed in store room, he should apply for remission of excise duty under rule 21 of Central Excise Rules.

Rule 3(5C) of Cenvat Credit Rules provides that if duty on final products is remitted under rule 21 of Central Excise, Cenvat credit of duty paid on inputs and input services used in manufacture or such goods shall be reversed. Thus, proportionate reversal of Cenvat credit is required.

In respect of inputs lost in store room, he is required to reverse the Cenvat credit as the inputs cannot be said to be used in manufacture.

In respect of inputs lost which were on shop floor, these are used in the manufacturing process and hence any reversal of Cenvat credit is not required.

- (ii) (i) Cenvat credit is not eligible as invoice date is beyond one year
(ii) Cenvat credit of ` 1,00,000 on input goods available
(iii) Cenvat credit is not available on basis of Xerox copy of invoice.
(iv) Cenvat credit of input service of ` 22,300 is available
(v) Time limit of one year for taking Cenvat credit is not applicable in respect of

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capital goods. Hence, Cenvat credit of 50% of excise duty i.e. 2,00,000 [50% of ` 4,00,000] is available.

(vi) Cenvat credit of GTA input service of ` 40,000 available, even if payment of bill amount is not made to service provider.

Thus, total Cenvat credit available as follows -1,00,000 + 22,300 + 2,00,000 + 40,000 = 3,62,300.

Alternative Answer :

- (I) Cenvat credit is not eligible as invoice date is beyond six months
 - (II) Cenvat credit of ` 1,00,000 on input goods not available
 - (III) Cenvat credit is not available on basis of Xerox copy of invoice.
 - (IV) Cenvat credit of input service of ` 22,300 is available
 - (V) Time limit of six months for taking Cenvat credit is not applicable in respect of capital goods. Hence, Cenvat credit of 50% of excise duty i.e. 2,00,000 [50% of ` 4,00,000] is available.
 - (VI) Cenvat credit of GTA input service of ` 40,000 available, even if payment of bill amount is not made to service provider.
- Thus, total Cenvat credit available as follows - 22,300 + 2,00,000 + 40,000 = 2,62,300.

4. Answer any two of the three sub-questions (a), (b) and (c). 6×2=12

(a) Calculate (A) the Assessable Value of equipment imported from USA and (B) basic customs duty payable, on basis of following details—

- (i) FOB Value of Equipment — 10,000 US dollars.
- (ii) Air freight paid — 3,500 US dollars.
- (iii) Insurance for transit of machine— not ascertainable.
- (iv) Cost of design work of the machine done in India— ` 45,000.
- (v) Commission paid to Indian Local Agents — ` 40,000.
- (vi) Cost of transport of goods from port to godown of importer in India— ` 15,000
- (vii) Exchange rate is 1 US dollar as notified by CBE&C= ` 65.80. RBI reference rate- ` 65.70. Exchange rate at which actually payment was made to bank— ` 65.60.
- (viii) Customs duty rate- 10%. Excise duty on similar product if manufactured in India— 12.50%. 5+1=6

(b) (i) An importer imported shoes which are covered under MRP valuation provisions under Central Excise. Abatement available is 30%. The MRP printed on the shoe is ` 1,000. The assessable value of the product for purposes of levy of customs duty is ` 600. Customs duty rate is 10% and excise duty rate is 12.5%. Ignore education cess.

Calculate (A) CVD payable under Section 3(1) of the Customs Tariff Act (B) special additional duty (SAD) payable under Section 3(5) of the Customs Tariff Act (C) Basic custom duty payable. 1+1+1=3

(ii) What are 'stores' under Customs Act? State provisions relating to payment of customs duty on stores. 3

(c) (i) Mrs. Jaya Pradnya, an Indian resident, had gone to Germany for business purposes. She brought following goods while returning to India after one week:

- (a) Her personal effects like wearing cloths etc. of ` 56,000
- (b) Two litre of liquor— value ` 6,000
- (c) New mobile of ` 38,400
- (d) One laptop — ` 75,900

Calculate the customs duty payable by her. 4

(ii) What is 'Preferential Rates of Customs Duty'? 2

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Answer:

4. (a)

FOB Value of equipment	10,000 US Dollars
Air freight restricted to 20% of FOB value	2,000 US Dollars
Insurance @ 1.125% of FOB value	112.50 US Dollars
Total value	12,112.50 US Dollars
Value in Indian Rupees @ Rs 65.80	₹ 7,97,002.50
Add - Local Agent's Commission	₹ 40,000
CIF Value in Rupees	₹ 8,37,002.50
Add Landing charges @ 1 %	₹ 8370.03
Assessable value for customs purposes	₹ 8,45,372.53
Basic customs duty @10%	₹ 84,537.25

- (b) (i) (A) Since the product is covered under MRP valuation provisions, excise duty is payable on ₹ 700 [after abatement of 30%]. Thus, CVD payable is 12.5% of ₹ 700 i.e. ₹ 87.50.
(B) If product is covered under MRP valuation provisions, SAD is exempt. Hence, SAD is not payable.
(C) Basis Customs duty payable is 10% of ₹ 600 i.e. ₹ 60.
- (ii) Section 2(38) of Customs Act define 'Stores' as goods for use in a vessel or aircraft and includes fuel and spare parts and other articles of equipment, whether or not they are required for immediate fitting.

The ships/aircrafts coming from abroad require spares and consumables for their ships and hence special provisions have been made.

Stores manufactured or produced in India may be exported without payment of export duty, as stores on any foreign going vessel with permission of Customs Officer, who will determine the requirement based on size of vessel or aircraft, length of journey etc.

Since the supply is treated as 'export' it will be eligible for duty drawback.

- (c) (i) (a) There is no duty on personal effects.
(b) One laptop can be imported without payment of customs duty. Hence, no customs duty is payable on laptop.
(c) Liquor is not allowed as personal effects. However, liquor upto 2 liter can be accommodated in General Free Allowance (GFA).
(d) Total dutiable goods imported are ₹ 44,400. [6,000 + 38,400].

General Free Allowance of ₹ 45,000 is available.
Hence, no customs duty is payable by Mrs. Jaya Pradnya.

- (ii) Some countries have been declared as 'preferential areas'. These are - Mauritius, Seychelles and Tonga. Goods manufactured and produced in these countries are eligible for preferential rate of duty under section 4 of Customs Tariff Act. Customs Tariff Act provides two columns - one for 'Standard rate' and other for 'Preferential Area'.

5. Answer any two of the three sub-questions (a), (b) and (c). 4x2=8
(a) An SEZ unit does not have sufficient orders for exporting goods. The SEZ unit has been

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able to get some orders from Domestic Tariff Area for supply of his products.
Advise him about duty payable, export obligation and procedure. 4

(b) Who is 'status holder' under Foreign Trade Policy? What are various grades of status holders in FTP. State relaxation available to status holder in respect of opening export warehouse in India. 4

(c) State objective and salient features of Merchandise Exports from India Scheme (MEIS). 4

Answer:

5. (a) There are no restrictions on DTA sale. However, the units must achieve positive NFE (Net Foreign Exchange) within five years of commercial production.

Thus, SEZ unit can supply goods to DTA, subject to condition that he must achieve positive NFE. The supply is treated as 'import' by DTA unit and normal customs duty is payable. If the DTA unit makes payment to SEZ unit in foreign exchange, the supply to DTA unit will be considered for discharge of his export obligation. Otherwise, such supply will not be treated for fulfillment of export obligation.

Since the supply from SEZ is practically import by DTA unit, the Indian buyer intending to procure goods from SEZ unit will have to file 'Bill of Entry for Home Consumption'.

- (b) Status Holders are business leaders who have excelled in international trade and have successfully contributed to country's foreign trade. They are expected to contribute towards India's exports and provide guidance and hand-holding to new entrepreneurs.

All exporters of goods, services and technology having an import-export code (IEC) number shall be eligible for recognition as a status holder. Status recognition depends upon export performance. An applicant shall be categorized as status holder upon achieving export performance during current and previous two financial years, as indicated below. The export performance will be counted on the basis of FOB value of export earnings in free foreign exchange.

For deemed export, FOB value of exports in Indian Rupees shall be converted in US \$ at the exchange rate notified by CBEC, as applicable on 1st April of each Financial Year.

For granting status, export performance is necessary in at least two out of three years.

- One Star Export House - US \$ 3 million
- Two Star Export House - US \$ 25 million
- Three Star Export House - US \$ 100 million
- Four Star Export House - US \$ 500 million
- Five Star Export House - US \$ 2000 million

Two Star Export Houses and above are permitted to establish export warehouses in India.

- (c) Objective of MEIS scheme is to offset infrastructural inefficiencies and associated costs involved in export of goods/products, which are produced/manufactured in India, especially those having high export intensity, employment potential and thereby enhancing India's export competitiveness.

An exporter gets MEIS scrips based on his export performance.

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The duty credit scrips can be used for following - (a) Payment of customs duties for import of inputs as well as capital goods, as per Department of Revenue (DOR) notification except items listed in Appendix 3 A of **ANF 2015-2020** (b) Payment of excise duty on domestic procurement of inputs or goods, including capital goods as per customs notifications (c) Payment of service tax on procurement of services as per service tax notification. List of products and list of markets eligible under **MEIS** scheme is given in Handbook of Procedures.

The rates of rewards of various products ITC(HS) code wise are also given. The 8scheme is not applicable to all products and exports to all countries. The scheme is limited to specified products and countries. Even, the value of scrip is not uniform to all specified countries. The countries have been classified in three groups A, B and C. The value of scrip depends upon the product exported and country to which the goods are exported. The value of MEIS scrip normally varies between 2% to 5% of FOB value of exports. In majority of cases, the duty scrip available is 5% of FOB value of exports.

6. Answer any two of the three sub-questions (a), (b) and (c). 10×2=20

- (a) (i) An assessee received an input service on 15-06-2015. Value of service was ` 1,00,000 on which service tax of ` 14,000 was charged by service provider (without education cess). He issued invoice dated 14-07-2015. The assessee received the original invoice dated 14-07-2015 of service provider in respect of the input service on 27-08-2015. The bill was passed by finance department of 03-09-2015. 90% of amount of bill was paid to service provider was made by assessee on 15-12-2015 in full and final settlement of bill of service provider.

Advise actions to be taken by assessee in respect of Cenvat Credit. 4

- (ii) An air conditioned restaurant made bill dated 15-03-2015 as follows— Food charges— ` 2000. Service charges— ` 200. Vat was charged separately in invoice at appropriate rate. Calculate service tax payable. 3

- (iii) ABC Ltd., a firm of architects, were awarded contract for design of office premises in Abu Dhabi. The contract was awarded by Mumbai based firm JKM Exporters Ltd. for their office in Abu Dhabi. Discuss liability of service tax. 3

- (b) (i) Jhanak Services Ltd. were liable to make payment of service tax of ` 2,00,000 for the month of November 2014. However, the service tax was deposited on 18-12-2015 on his own, without department taking any action. Jhanak Services Ltd. has shown the amount as payable in his return filed on 22-04-2015. The value taxable services provided by them during the preceding financial year was ` 65 lakhs.

(1) Compute the amount of interest payable by Jhanak Services Ltd.

(2) Calculate penalty payable.

(3) What action could have been initiated by department against Jhanak Services Ltd.? 3+1+1=5

- (ii) What is 'declared service'? What was the purpose in making provision of 'declared services'? Name any four activities which are 'declared services'. 2+1+2=5

- (c) (i) (A) State salient features of definition of 'works contract' in Service Tax Law. (exact reproduction of definition is not required.)

(B) If a contractor charges ` 10 lakhs for constructing a factory building using his

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own material, how much service tax is payable by him? The construction was completed during January 2015 to May 2015.

(C) State whether following are works contracts:

- (1) Taking out Xerox copy.
- (2) Housekeeping contract using consumables (cleaning contract) 2+2+2=6

(ii) State whether following transactions are subject to service tax, giving brief reasons:

- (A) Sale of foreign currency by one bank to another
- (B) Services provided to Reserves Bank of India
- (C) Service of construction of office building provided to Indian railways
- (D) Giving construction machinery on hire without operator

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Answer:

6. (a) (i) Assessee can take Cenvat credit of ` 14,000 on 27-8-2015. He is required to make payment within three months from date of invoice i.e. before 14-10-2015. Since he did not make such payment, he is required to pay 'amount' of ` 14,000, i.e. reverse the Cenvat credit. Later when he makes 90% payment in full and final settlement of the invoice of service provider, he can take 90% of Service tax as Cenvat credit i.e. ` 12,600 on 15-12-2015.
- (ii) Service tax is payable on 40% of ` 2,200 i.e. on ` 880. Service tax @ 12% of ` 880 is ` **105.60**. Education cess @ 2% - ` **2.11** and Secondary and Higher Education Cess - ` **1.06**.
- (iii) As per rule 8 of Place of Provision of Service Rules (POPS Rules), the place of provision of Service is India as both service provider and service receiver are in India. As per rule 5 of POPS Rules, the place would have been Dubai as immovable property is located outside India. However, as per rule 14 of POPS Rules, later rule prevails over earlier rule and hence rule 8 would prevail over rule 5 of POPS Rules. Hence, place of service would be India. Thus, service tax will be payable by ABC Ltd.
- (b) (i) (A) Due date of payment was 6-12-2014.
The interest payable under section 75 of Finance Act, 1994 will be as follows – (a) if delay upto 6 months - 18% p.a. (b) if delay more than six months and upto one year - 18% p.a. for first six months and 24% p.a. for delay beyond six months (c) if delay more than one year – 18% p.a. for first six months and 24% p.a. for next 6 months and 30% p.a. for any delay beyond one year.
Hence, interest payable is as follows
From 7-12-2014 to 6-6-2015 - for 6 months @ 18% - $(2,00,000 \times 18 \times 6)/(12 \times 100) = ` 18,000$
From 7-6-2015 to 6-12-2015 - for 6 months @ 24% - $(2,00,000 \times 24 \times 6)/(12 \times 100) = ` 24,000$
From 7-12-2015 to 18-12-2015 - for 12 days @ 30% - $(2,00,000 \times 30 \times 12)/(365 \times 100) = ` 1,972.60$
Hence, total interest payable = ` 43,972.60.
(B) No penalty is payable as assessee paid service tax with interest on his own as per section 73(3) of Finance Act, 1994.
(C) Department could have started recovery proceedings in any of the modes specified in section 87 of Finance Act, 1994, without issue of any show cause notice. [section 73(1B) of Finance Act, 1994]
- (ii) The definition of 'service' as per section 65B(44) of Finance Act, 1994 states that it includes 'declared service'.

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"Declared service" means any activity carried out by a person for another person for consideration and declared as such under section 66E of Finance Act, 1994 - section 65B(22) of Finance Act, 1994.

Section 66E of Finance Act, 1994 (introduced w.e.f. 1-7-2012) states as follows -

The following shall constitute declared services, namely:—

- (a) renting of immovable property;
- (b) construction of a complex, building, civil structure or a part thereof, including a complex or building intended for sale to a buyer, wholly or partly, except where the entire consideration is received after issuance of completion-certificate by the competent authority.
- (c) temporary transfer or permitting the use or enjoyment of any intellectual property right;
- (d) development, design, programming, customisation, adaptation, upgradation, enhancement, implementation of information technology software;
- (e) agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act;
- (f) transfer of goods by way of hiring, leasing, licensing or in any such manner without transfer of right to use such goods;
- (g) activities in relation to delivery of goods on hire purchase or any system of payment by installments;
- (h) service portion in the execution of a works contract;
- (i) service portion in an activity wherein goods, being food or any other article of human consumption or any drink (whether or not intoxicating) is supplied in any manner as a part of the activity'.

Though the definition uses the words 'declared service', actually it covers some 'deemed services'. These have been specifically included in the definition of 'declared services' as many of these are partly covered either under 'sale of goods' or 'deemed sale of goods' which are subject to State Vat/Central Sales Tax (CST). Hence, to avoid disputes, deeming provision has been made to clarify that service portion of such transactions can be taxed.

- (c) (i) (A) For purpose of service tax, the term 'works contract' has been defined as follows -

"Works contract" means a contract wherein transfer of property in goods involved in the execution of such contract is leviable to tax as sale of goods and such contract is for the purpose of carrying out construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, alteration of any movable or immovable property or for carrying out any other similar activity or a part thereof in relation to such property - section 65B(54) of Finance Act, 1994.
- (B) The value of service is ` 4 lakhs. Service tax @ 12% of ` 4 lakhs = 48,000. Education cess payable @ 2% - ` 960. Secondary and Higher Education Cess - ` 480.
- (C) Xerox is a works contract. Simple cleaning contract using consumables is not works contract as property in goods involved is not passed on to buyer.
- (ii) (a) Sale of foreign currency by one bank to another is not taxable as in Clause (n)(ii) of Negative List of services as per section 66D of Finance Act, 1994.
- (b) Services provided by RBI are exempt but services provided to RBI are not exempt.
- (c) Construction service of 'original works' provided to railways are exempt vide Sr. No. 14(a) of Notification No. 25/2012-ST dated 20-6-2012.
- (d) The activity is 'transfer of right to use goods'. Hence, State Vat is payable and not service tax.

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7. Answer any two of the three sub-questions (a), (b) and (c). 6x2=12
- (a) (i) State reasons why VAT is termed as 'consumption based tax'. 3
(ii) State distinction between zero rated sale and exempt sale. State one transaction which is zero rated and one transaction which is exempt sale. 3
- (b) JK Traders, a dealer submits from Gujarat the following information. Compute the Net VAT liability from the following information (figures in Rupees):
Value of import of raw material (including 10% import duty) ` 2,20,000.
Raw material was purchased from Gujarat, (including excise duty @ 12%). VAT paid @ 4% on the above purchase was ` 4,48,000.
Raw material was purchased from Karnataka (including CST @ 2%)— 1,70,000
Transportation and manufacturing expenses— 94,000
JK Traders sold entire manufactured products at a profit of 10% on the cost of production. VAT rate on such sale is 4%. 6
- (c) (i) State whether following are 'goods': 2
(1) Electricity
(2) Lottery ticket
(3) Packaged software
(4) Share certificate
- (ii) A dealer in Haryana sold goods to a buyer in Delhi at ` 1,00,000, excluding sales tax. VAT rate in Haryana is 5%. Calculate Central Sales tax payable if —
(1) Buyer in Delhi issued C form
(2) Buyer in Delhi issued H form
(3) Buyer in Delhi issued I form
(4) Buyer in Delhi did not issue any form 2
- (iii) State purpose of composition scheme in VAT laws. 2

Answer:

7. (a) (i) Vat is termed as consumption based tax and tax is received by Government only when goods or services are finally consumed. Till goods are finally consumed, input tax credit is available to the buyer. Input tax credit is passed on from one to another, Thus, effectively, Government does not get any tax at that stage. Government gets tax revenue only when goods are finally consumed as the final consumer cannot pass on that credit to another person.

- (ii) Distinction between 'zero rated sale' and 'exempt sale' is that in case of 'zero rated sale', credit is available on tax paid on inputs, while in case of exempt goods, credit of tax paid on inputs is not available.

Certain sales are 'zero rated' i.e. tax is not payable on final product in certain specified circumstances. In such cases, credit will be available on the inputs i.e. credit will not have to be reversed. For example, exports are zero rated.

Sale of certain goods like newspaper, national flag, un-processed produces in unorganised sector are exempt from sales tax. Vat is not payable on such sale. However, input tax credit is not available.

- (b) Input tax credit available to JK Traders is as follows
(a) Imported raw material - Nil
(b) Raw material purchased from Gujarat - 4,48,000
(c) Raw material purchased from Karnataka - No credit is available.
Thus, total input credit available is ` 4,48,000.
In respect of purchases from Gujarat, Vat is ` 4,48,000.

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Hence, net purchase price (including excise duty but excluding Vat) is $(100 \times 4,48,000)/4$ i.e. ₹ 1,12,00,000 [check that 4% of 1,12,00,000 is ₹ 4,48,000].

Total cost of production is as follows -

- (a) Imported raw material - 2,20,000 (including import duty as its credit is not available)
- (b) Raw material purchased from Gujarat - 1,12,00,000
- (c) Raw material purchased from Karnataka - 1,70,000
- (d) transportation and manufacturing expenses - 94,000.

Total net cost of production ₹ 1,16,84,000 (a + b + c + d)

Profit @ 10% of cost of production – ₹ 11,68,400.

Hence, selling price is ₹ 1,28,52,400.

Vat payable @ 4% of selling price is ₹ 5,14,096.

Input Tax Credit available is ₹ 4,48,000

Hence, Vat payable by cash is ₹ 66,096 [5,14,096-4,48,000]

Tutorial note: If trader pays special CVD on the imported goods, that amount will be eligible as input tax credit.

(c) (i) (A) Yes (B) No (C) Yes (D) No.

(ii) (A) 2,000 (B) No tax (C) No tax (D) ₹ 5,000.

(iii) Vat requires heavy compliance cost due to detailed accounting and paper work involved. Small dealers do not have sufficient knowledge and expertise to comply with the requirements relating to records and accounts.

Hence, for them, a simplified composition scheme has been provided. It is optional.

8. Answer any two of the three sub-questions (a), (b) and (c). 4×2=8

(a) Explain provisions of Resale Price Method of computing Arm's Length Price. 4

(b) A company providing software development service to its group company outside India found that it is required to submit huge amount of data and information to income tax department to justify the arm's length price. The company wants a simplified method. The company seeks your advice. Advise the company. 4

(c) (i) Dynamic Products Pvt. Ltd. is manufacturer and exporter of electrical machinery. It filed income tax return for A.Y. 2015-16 declaring profit as ₹ 112 lakhs. The company had sold 200 pieces of electrical machinery to its associated enterprise outside India in Germany @ 280 Euro per piece. 80 pieces of similar machinery were sold to an unrelated buyer in Germany @ 350 Euro per piece. Exchange rate of Euro was one Euro = ₹ 80. Compute the taxable income of Dynamic Products Pvt. Ltd. stating the method you will apply. 2

(ii) A foreign parent company sold its product to its Indian subsidiary at 2,000 dollars per piece. The foreign company had sold similar product to unrelated buyer in India at 2,200 dollars per piece. Exchange rate is 1 dollar = ₹ 62. Compute Arm's Length Price. 2

Suggested Answer_Syl12_Dec2015_Paper 11

Answer:

8. (a) Resale price method (RSP) is applied to determine arm's length price when property purchased or service obtained from one associated enterprise is resold to an unrelated enterprise.

Under this method, the price at which property purchased or services obtained by the enterprise from an associated enterprise is resold or are provided to an unrelated enterprise, is identified. The resale price is reduced by the amount of a normal gross profit margin accruing to the enterprise or to an unrelated enterprise from the purchase and resale of the same or similar property or from obtaining and providing the same or similar services, in a comparable uncontrolled transaction, or a number of such transactions.

The price is further reduced by the expenses incurred by the enterprise in connection with the purchase of property or obtaining of services. The price is adjusted to take into account the functional and other differences, including differences in accounting practices, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of gross profit margin in the open market. The adjusted price arrived at is taken to be an arm's length price (ALP).

- (b) Provisions are contained in 'Safe Harbour Rules'.

'Safe Harbour' means circumstances in which income tax authorities shall accept the transfer price declared by assessee, without going into details of Arm's Length Price (ALP).

Assessee can opt to exercise Safe Harbour Rules by submitting form No. 3CEFA to assessing officer.

The option will remain valid for five years. However, once the option is accepted, it cannot be changed and if assessee declares less margin in a particular year, the income will be calculated on basis of safe harbor rates or margins only.

In case of software development service or information technology enabled service, if operating profit margin declared in international transaction in relation to operating expenses is not less than 20% if transactions are upto ` 500 crores in the previous year or not less than 22% if value of such transactions exceed ` 500 crores during the previous year.

- (c) (i) The 'Comparable uncontrolled price method' is most appropriate. In this method, the price charged or paid for property transferred or services provided in a comparable uncontrolled transaction, (i.e., a transaction between enterprises other than associated enterprises whether resident or non-resident) or a number of such transactions, is identified.

In this case, the uncontrolled price is 350 Euro. Hence, difference of 70 euro per piece is required to be added in the profit. Thus, profit to be increased = 70 euro x 200 Nos. x 80 ` = 11,20,000

Thus, the taxable income of AMF Electronics Ltd. is ` 112 + 11.2 = ` 123.2 lakhs.

- (ii) The price of USD 2,000 is accepted as if the price is taken as USD 2,200, profit of Indian subsidiary will be lower. Thus, income tax payable by him would be lower. Hence, arm's length price - 2,000 x 62 = ` 1,24,000.