INTERMEDIATE EXAMINATION

GROUP I

(SYLLABUS 2012)

SUGGESTED ANSWERS TO QUESTIONS

JUNE 2017

Paper-7: DIRECT TAXATION

Time Allowed : 3 Hours **Full Marks : 100**

The figures in the margin on the right side indicate full marks.
Wherever required, the candidate may make suitable assumption(s) and
State the same clearly in the answer.

Working notes should form part of the relevant answer.

All question relate to the Income – tax Act, 1961

All the questions relate to the Assessment Year 2017-18, unless otherwise stated.

Section A

Answer *Question No. 1*, which is compulsory and *any four* from *Question Nos. 2 to 6*.

1. (a) Fill up the blanks: **1×10=10**

(i) The maximum amount deductible under section 80GG in respect of house rent paid by a self-employed individual is ₹ _____________ per month.

(ii) The loss from activity of owning and maintaining race horses can be carried forward for ___________assessment years, immediately succeeding the assessment year for which loss was first computed.

(iii) In order to qualify as long-term capital assets, shares of a private limited company should be held for more than ___________months immediately before transfer.

(iv) In case of under-reporting of income, the assessee is liable to penalty under section 270A for an amount equal to_____________% of tax payable on under-reported income.

(v) The amount of standard deduction available in respect family pension received by the legal heir of the deceased is 33 1/3% of such pension or ₹ ___________, whichever is less.

(vi) When a trader opts for presumptive income determination u/s 44AD, advance tax is payable on or before _____________of the previous year.

(vii) Irrespective of the period of holding of asset, profit arising to a block of depreciable asset from transfer of such asset is always taxed as _____________capital gain.

(viii) The due date for filing return of income for Assessment Year 2017-18 of a company, which is required to obtain a report under section 92E in respect of specified domestic transactions is_____________.

(ix) Amount received by a member of a HUF as his share from the income of the HUF is _________(included/not included) in his total income.

(x) Mr. X gifted ₹1 lakh to his wife, Mrs. X who invested such sum in a business. The business suffered a loss of ₹20,000. Such loss ______(can/cannot) be set off against eligible income of Mr. X.

(b) Choose the most appropriate alternative: 1×5=5

(i) Rate of surcharge applicable to a foreign company having total income of ₹8 crore is:
a. Nil
b. 2%
c. 5%
d. 10%

(ii) Income Computation and Disclosure Standards are to be applied in computation of income under the head:
a. Capital Gain only
b. Profits and Gains of business or profession only
c. Income from other sources only
d. Both "Profits and Gains from business or profession" and "income from other sources"

(iii) New plant and machinery acquired and put to use by an assessee engaged in transmission of power is eligible for additional depreciation at _________of actual cost.
a. 10%
b. 12.5%
c. 15%
d. 20%

(iv) Maximum amount of exemption available in respect of amount received under voluntary retirement scheme is:
a. ₹ 2,00,000
b. ₹ 3,00,000
c. ₹ 4,00,000
d. ₹ 5,00,000

(v) An individual can claim deduction from his gross total income in respect of expenditure for the medical treatment of a dependent being a person with disability up to maximum limit of
a. ₹50,000
b. ₹1,00,000
c. ₹75,000
d. ₹1,25,000

(c) Match the following: 1×5=5

(i) Contribution of ₹8,000 in cash by a company to a political party	(a) Allowed as deduction in computing business income
(ii) Commodity Transaction Tax	(b) Income from other sources
(iii) Forfeiture of advance received for transfer of capital asset	(c) Not eligible for deduction under section 80 GGB
(iv) Interest from Sukanya Samridhi Account	(d) Allowed only on payment basis
(v) Amount payable to the Indian Railway for use of railways asset	(e) Not included in total income

Answer: 1

(a) (i) 5,000

(ii) 4

(iii) 24

(iv) 50%. (If it is assumed that under-reporting is due to misreporting, then 200%)

(v) 15,000

(vi) 15th March

(vii) Short – term

(viii) 30-11-2017

(ix) Not included

(x) Can

Answer: 1 (b)

(i) B. 2%

(ii) D. Both "Profits and gains of business or profession" and "Income from other sources)

(iii) D. 20% of cost

(iv) D. ₹ 5,00,000

(v) C. ₹ 75,000

Answer: 1 (c)

(i) Contribution of ₹ 8,000 in cash by a company to a political party	(c) Not eligible for deduction under section 80 GGB
(ii) Commodity Transaction Tax	(a) Allowed as deduction in computing business income
(iii) Forfeiture of advance received for transfer of capital asset	(b) Income from other sources
(iv) Interest from Sukanya Samridhi Account	(e) Not included in total income
(v) Amount payable to the Indian Railway for use of railways asset	(d) Allowed only on payment basis

2. (a) Mr. Rao had a house property in Hyderabad. The house was let out to Mr. Reddy from August 2011 to September 2012. Mr. Rao was unable to realize three months' rent amounting to ₹ 30,000 from Mr. Reddy. The said unrealised rent was reduced in computing income from house property for Assessment Year 2013-14.

Mr. Rao had let out the property to the State Government from October 2012 to December 2015. In October 2014, he increased the rent from ₹ 20,000 per month to ₹ 30,000 per month, but the State Government had disputed the increase in rent.

The house remained vacant for January 2016. He sold the house in February 2016. Mr. Rao recovered unrealised rent to the extent of ₹ 20,000 from Mr. Reddy in December 2016. He also received arrear rent amounting to ₹ 1,50,000 from the State Government in January 2017 after settlement of dispute regarding increase in rent.

State with reason, whether recovery of unrealised rent and arrear rent be taxable in Assessment Year 2017-18. If so, under what head of income and what is the amount chargeable to tax? 6

(b) Avishek works in VKS Limited on a basic salary of ₹ 50,000 per month. He is also entitled to dearness allowance of 20% of basic salary. Dearness allowance is included in salary for retirement benefit. He is also entitled to house rent allowance of ₹ 20,000 per month.
The company enhanced his basic salary by ₹ 5,000 per month with effect from 1st January, 2017.
Avishek was staying with his friend without paying rent till 31st October, 2016. He has taken a flat on rent at ₹ 14,000 per month at Erode with effect from 1st November, 2016.

Compute taxable house rent allowance for the Assessment Year 2017-18.

(c) State the maximum amount of exemption that can be claimed in respect of the following allowances/receipts: 1×5=5

(i) Transport allowance granted to an employee who is blind.
(ii) Hostel expenditure allowance for children of employee.
(iii) Gratuity received by an employee covered under the Payment of Gratuity Act, 1972.
(iv) Retrenchment compensation received by a workman.
(v) Amount received by an employee at the time of closure of account under National Pension Scheme.

Answer: 2 (a)

As per section 25A (1), the amount of unrealised rent subsequently realized from a tenant or the amount of arrears of rent received from tenant, as the case may be, by an assessee shall be deemed to be the income from house property in the financial year in which such rent is realized shall be taxed under the head "income from house property", whether the assessee is the owner of the house property or not in that financial year.
As per section 25A (2), standard deduction @ 30% of the unrealised rent and arrears of rent shall be allowed.
Hence, unrealised rent of ₹ 20,000 and arrear of rent of ₹ 1,50,000 shall be taxable in Assessment Year under the head "Income from house property" in the hands of Mr. Rao.

Computation of income of Mr. Rao under the head "Income from house property" for the Assessment Year 2017-18

Particulars	₹
Unrealised Rent	20,000
Arrear Rent	1,50,000
	1,70,000
Less Standard deduction at 30%	51,000
Taxable income from house property	1,19,000

Answer: 2 (b)

Particulars	₹	₹
House Rent Allowance Received (₹ 20,000 × 12)		2,40,000
Less: Amount exempted under section 10(13A)		
Least of the following: (i) Allowance actually Received	2,40,000	

(ii) Rent paid over 10% of salary (Note) (iii) 40% of salary: ₹ 3,18,000 x 40%	38,200 1,27,200	
		38,200
Taxable House rent Allowance		2,01,800

Note

	₹	₹
Rent paid from 01-11-2016 to 31-03-2017 (₹ 14,000 × 5)		70,000
Salary and DA from 01-11-2016 to 31-12-2016		
(₹ 50,000 + ₹ 10,000) × 2	1,20,000	
Salary and DA from 01-01-2017 to 31-03-2017(₹ 55,000 + ₹11,000) × 3	1,98,000	
	3,18,000	
10% of Basic salary and DA from 01-11-2016 to 31-03-2017		31,800
Excess of rent paid over 10% of salary		38,200

Answer: 2 (c)

Allowance/receipt	Maximum amount of exemption
(i) Transport allowance granted to an employee who is blind	₹ 3,200 per month
(ii) Hostel expenditure allowance for children	₹ 300 p. m per child upto maximum of two children
(iii) Gratuity received by an employee covered under the Payment of Gratuity Act	₹ 10,00,000
(iv) Retrenchment compensation received by a workman	₹ 5,00,000
(v) Amount received by an employee at the time of closure of account under National Pension Scheme	40% of total amount payable.

3. (a) Following is the Profit and Loss Account of Mr. Ghosh for the year ended 31.03.2017:

	Particulars	**₹**		**Particulars**	**₹**
To	**Interest**	**1,20,000**	**By**	**Gross Profit**	**9,25,000**
To	**Salary & Bonus**	**2,70,000**	**By**	**Dividend from Indian companies**	**30,000**
To	**Rent**	**60,000**			
To	**Medical expenses:** **Self** **Staff**	 **15,000** **10,000**	**By**	**Agricultural income (From land in Malaysia)**	**45,000**
To	**Administration expenses**	**70,000**	**By**	**Public Provident Fund interest**	**50,000**
To	**Depreciation**	**85,000**			
To	**Donation**	**20,000**			
To	**Net Profit**	**4,00,000**			
		10,50,000			**10,50,000**

Additional information:

(i) Salary & Bonus includes, payment to son of ₹ 1,30,000. Excess payment under section 40A(2)(a) is ₹ 35,000.

(ii) Depreciation allowable under Income-tax Rules, 1962 is ₹ 49,000.

(iii) Donation includes (a) ₹ 12,000 paid to Prime Minister's Relief Fund, and (b) ₹ 8,000 to a charitable trust registered U/S.12AA and recognized under section 80G. Both were through account payee cheques.

You are required to compute the total income of Mr. Ghosh for the Assessment Year 2017-18. **10**

(b) State with brief reason, whether the following are eligible for deduction while computing income under the head "Profits and gains of business or profession": **1×5=5**

(i) Cash paid to agriculturist ₹ 30,000 for buying sugarcane by a sugar mill.

(ii) Brokerage paid to Ramesh (a resident) ₹ 12,000 by a company without deduction of tax at source.

(iii) Interest on capital paid by a firm to its partners @15% per annum, in accordance with the partnership deed.

(iv) Freight paid to carrier in cash ₹ 43,000.

(v) Payment of ₹ 33,000 to supplier of raw material by use of credit card.

Answer 3(a)

Computation of total income of Mr. Ghosh for the Assessment year – 2017 – 2018

Particulars	₹	₹
Income From Business **(Working Note 1)**		3,81,000
Income from Other Sources:		
Dividend from Indian Companies – exempt under section 10(34)	Nil	
Agricultural income from land in Malaysia	45,000	
Interest from PPF - exempt U/s.10	Nil	
Income chargeable under this head		45,000
Gross Total Income		4,26,000
Less : Deduction under section 80 G		
Donation to PM Relief Fund @ 100%	12,000	
Donation to Charitable Trust ₹8,000 @ 50%	4,000	
		16,000
	Total Income	4,10,000

Working Note 1: Computation of income from Business

Particulars	₹	₹
Net Profit as per Profit and Loss Account		4,00,000
Add:		
Medical expenses to staff- allowed		-
Medical expenses to self- disallowed		15,000
Depreciation debited to P&L account (considered separately)		85,000
Donation debited to P & L account (not an expenditure for business)		20,000
Excess salary paid to son – disallowed under section 40A(2)		35,000
		5,55,000
Less:		

Dividend from Indian Companies	30,000	
Agricultural income from land in Malaysia	45,000	
Interest on PPF a/c	50,000	
Depreciation as per Income-tax rules	49,000	
		1,74,000
Income from Business		3,81,000

Answer 3(b):

(i)	Deductible: Cash paid for agricultural produce to the cultivator, grower or producer is not liable for disallowance under section 40A(3) even if it is paid in contravention of that provision i.e above ₹ 20,000.
(ii)	Deductible: When brokerage paid exceeds ₹ 15,000 the liability to deduct tax at source under section 194H would arise. Since, it is less than the said limit, it is eligible for deduction as TDS requirement is not attracted.
(iii)	Deductible up to 12% and the balance 3% is liable for disallowance. Section 40(b) enables allowance of interest on capital when the interest payment exceeds 12%.
(iv)	Not Deductible: As the payment to carrier towards freight is more than ₹35,000 in cash, such cash payment is liable for disallowance under section 40A(3).
(v)	Deductible: As payment is made by means of credit card, disallowance under section 40A(3) is not called for irrespective of the amount.

4. (a) Answer the following questions with brief reasons/working:

(i) Mr. Rao having 30% shareholding in Jain(P) Ltd., received dividend of ₹ 12 lakhs in December, 2016. Mr. Raghu having 20% shareholding in the same company received ₹ 8 lakhs by way of dividend at the same time.-How will the dividend income be treated in the hands of Mr. Rao and Mr. Raghu respectively? The company has paid DDT u/s 115/O.

(ii) Mr. Raj took life insurance policy in the name of his wife for ₹ 5 lakhs with annual premium of ₹ 45,000 on 01.06.2016. On the same date, he also took another policy in the name of his son (age 15) with severe disability (as referred to in section 80U) for ₹ 2,00,000 with annual premium of ₹ 40,000. Determine the quantum of life insurance premiums eligible for deduction under section 80C. 3+2=5

(b) Ms. Padmaja furnishes you the following information for the year ended 31.03.2017:

(i) Acquired a vacant site for ₹ 5,20,000 in June, 2016 and the valuation for stamp duty purpose was ₹ 5,60,000.

(ii) Sold a let out residential building for ₹ 10,50,000 to John (non-relative) when stamp duty value was ₹ 13,60,000. Indexed cost of the. asset (computed) ₹ 11,10,000.

(iii) Won ₹ 35,000 in a crossword puzzle contest.

(iv) Income from business (computed) ₹ 9,20,000.

(v) Paid ₹ 90,000 towards tuition fee for part-time MBA course pursued by her.

(vi) Paid by cheque ₹ 26,000 towards health insurance premium by her parents (who are senior citizen) and ₹ 7,500 by cash towards preventive health check-up for herself.

(vii) Paid ₹ 40,000 in notified National Pensions Systemss Trust.

Compute the total income of Ms. Padmaja for the Assessment Year 2017-18. 5

(c) Mr. Arvind entered into an agreement for sale of vacant land to Mr. Bimal on 01.07.2016 and received ₹ 1,00,000 by cash. The agreement got cancelled as Mr. Bimal could not mobilize money to buy the land. Mr. Arvind hence forfeited the advance money in January, 2017. Discuss the tax consequence of the transaction in the hands of Mr. Arvind as regards acceptance of advance in cash and its forfeiture subsequently. 5

Answer: 4 (a)

(i) Where the total income of an assessee, being an individual or HUF or a firm, resident in India includes any income by way of dividend and such dividend exceeds ₹ 10 lakhs, it is chargeable to tax at the rate of 10% (plus surcharge and education cess). [sec.115BBDA]

Hence, such dividend income is liable to tax in the hands of Mr. Rao even though the company has paid DDT under section 115-O. The dividend income is not exempt under section 10(34).

Since the dividend income of Mr.Raghu is less than ₹ 10 lakhs it is not covered by section 115 BBDA. Hence it is exempt under section 10(34).

(ii) Where the life insurance policy is issued after. 01.04.2013 the quantum of premium exceeding 10% of the capital sum assured is not eligible for deduction under section 80C.

However, where the policy covers a person with disability or with severe disability the quantum is limited to 15% of the capital sum assured instead of 10%.

Thus the premium paid on wife's policy is deductible.

The premium paid on son (with severe disability) is eligible for deduction to the extent of 15% only i.e. ₹ 30,000 only.

Hence the total amount deductible would be ₹ 45,000 + ₹ 30,000 = ₹ 75,000.

(b) **Computation of Total income of Ms. Padmaja for the Asst. Year 2017 – 2018**

	₹	₹
Income from Business (computed)		9,20,000
Income from Other Sources:		
(i) Crossword puzzle contest	35,000	
(ii) Difference in price of acquisition of vacant site being below ₹50,000 there is no tax implication	Nil	
		35,000
Income from Long Term Capital Gain:		
Sale of residential building to John for consideration less than stamp duty value attracts section 50C. Hence, stamp duty value shall be deemed to be the full value of consideration.		
Deemed sale consideration	13,60,000	
Less: Indexed cost of acquisition	11,10,000	

			2,50,000
Gross Total Income			12,05,000
Less : Deduction under section 80C			
For Part-time education not eligible for deduction		Nil	
Deduction Under section 80CCC			
Contribution to Notified Pension Scheme		40,000	
Deduction Under section 80D			
Medical Insurance premium	26,000		
Preventive Health Check up paid in cash is also allowed	5,000		
		31,000	
			71,000
Total income			11,34,000

(c)

Mr. Arvind received ₹ 1,00,000 as advance for sale of vacant land. This amount was forfeited subsequently. Where any sum of money is received as advance in the course of negotiations for transfer of a capital asset and if such amount is forfeited, it is taxable under the head 'Income other sources'.
It is not to be reduced from the cost of acquisition or fair market value or the written down value of the asset.
The receipt of advance in cash exceeding ₹ 20,000 is in contravention of section 269SS of the Act.
Hence the recipient i.e. Mr. Arvind is liable for penalty equal to the amount of advance under section 271D of the Act.

5. (a) Balaji, engaged in manufacturing activity, furnishes you the following details:

	Furniture & Fittings	Plant & Machinery
Opening WDV (01.04.2016)	**15,000**	**2,50,000**
Acquired and used (01.07.2016)	**25,000**	**3,10,000 (Includes excise duty eligible for CENVAT credit of ₹10,000)**
Acquired and used (01.01.2017)	**10,000**	**1,50,000**
Sold on 20.09.2016	**20,000**	**75,000**
Sold on 12.03.2017	**—**	**2,40,000**

Compute eligible depreciation for the Assessment Year 2017-18 (ignore additional depreciation). 5

(b) State with brief reason the "due date" for filing return of income in the following cases: 5

(i) Dr. Anand Hair Clinic (P) Ltd. having aggregate annual receipt of ₹110 lakhs and income from business of ₹ 6,20,000 (compute).

(ii) Timber Traders, a partnership firm, having business loss of ₹ 2,30,000 and total turnover of ₹ 56,27,000. It is not opting for the presumptive provisions of section 44AD of the Act.

(iii) Mr. Sridhar doing proprietary business, with annual turnover exceeding ₹ 200 lakhs and income from business (computed) of ₹ 7,40,000.

(iv) A Charitable trust registered under section 12AA, having total income of ₹ 2,40,000 before giving effect to the provisions of sections 11 and 12 of the Act.

(v) Mr. Malik doing trade in automobile spare parts, with turnover below ₹ 50 lakhs and having a windmill for generation of power, which is eligible for deduction under section 80-IA of the Act.

(c) Ms. Sanvitha sold a residential building for ₹ 52 lakhs to Ms.Vivitha on 01.06.2016. The stamp duty valuation for the purpose of registration was ₹ 60 lakhs. Ms. Sanvitha paid brokerage @ 1% of the sale consideration.
The property was originally acquired for ₹ 4.97 lakhs in July, 2005. Further construction was made in the financial year 2012-13 for ₹ 8,52,000.
Ms. Sanvitha deposited ₹ 30 lakhs in capital gain bonds of Rural Electrification Company in October, 2016. She has non-speculation business loss of ₹ 3,48,000 (computed) for the financial year 2016-17.
You are requested compute her total income for the assessment year 2017-18. 5
Cost inflation index:
Financial Year 2005-06 = 497
2012-13 = 852
2016-17=1125

Answer: 5 (a)

	Furniture & Fittings	Plant& Machinery
Opening WDV	15,000	2,50,000
Add: Additions upto 02.10.16	25,000	3,00,000
Additions after **02.10.16**	10,000	1,50,000
	50,000	7,00,000
Less: Sold during the year	20,000	3,15,000
Block value before depreciation claim	30,000	3,85,000
Depreciation (@ 10% on ₹10,000) × ½	500	
Depreciation (@ 15% on ₹1,50,000) × ½		11,250
Depreciation on 10% on ₹20,000	2,000	
Depreciation on 15% on ₹2,35000		35,250
Total Depreciation	2,500	46,500
Closing WDV after Depreciation	27,500	3,38,500

Note: If is also possible to take the view that under the block concept position as at year end alone is relevant and that sales can be first set off against assets acquired /used for less then 180 days. In such case the entire blocks will be eligible for depreciation @ 10% and 15% respectively. In such case depreciation on furniture is 10% of 30,000 = ₹ 3,000. Depreciation on plant & machinery is 15% of 3,85,000 = ₹ 57,750.

Answer: 5 (b)

(i)	In the case of a company, whose accounts are liable to audited under any other law (i.e. Companies Act, 2013), the return of income has to be filed on or before 30.09.2017.
(ii)	The accounts are to be audited under section 44AB of the Act since the assessee

	firm has not opted for presumptive provisions contained in section 44AD. Thus the return has to be filed on or before 30.09.2017.
(iii)	As the annual turnover has exceeded ₹200 lakhs, the accounts are to be audited under section 44AB of the Act and the 'due date' for filing the return would be 30.09.2017
(iv)	The total income before giving effect to the provisions of section 11 and section 12 of the Act, is below the maximum limit not chargeable to tax i.e. below ₹2,50,000. Hence the 'due date' is 31st July, 2017.
(v)	As the assessee wants to claim deduction under section 80-IA of the Act, the 'due date' for filing the return of income would be 30.09.2017.

Answer: 5 (c)

Computation of total income of Ms. Sanvitha for A. Y. 2017 – 18

		₹	₹
Profits and gains of business or profession - computed			(3,48,000)
Capital Gains:			
Sale consideration is below the stamp duty value, hence stamp duty value to be adopted as deemed sale consideration		60,00,000	
Less : Brokerage @ 1% of 52 lakhs		52,000	
		59,48,000	
Less: Indexed cost of acquisition			
F.Y 2005-06 : 497000 × 1125/497	11,25,000		
F.Y.2012-13: 852000 × 1125/852	11,25,000		
		22,50,000	
		36,98,000	
Less: Exemption under section 54EC for investment in REC bonds		30,00,000	
Long –term capital gain			6,98,000
Total Income			3,50,000

Note: Business loss can be set off against long-term capital gain.

6. (a) State with reasons, the amount of tax to be deducted at source under section 194C from the following amounts payable: 2×2=4

(i) Amount payable to Samir against four different contract viz. contract 1 ₹ 30,000, contract 2 ₹ 25,000, contract 3 ₹ 26,000 and contract 4 ₹ 20,000.

(ii) Amount ₹ 2,50,000 payable to Sriram, a contractor for plying goods carriage. Sriram submitted declaration that he owns eight goods carriages and he furnished his permanent account number to the payer.

(b) Laxman Memorial Trust, which operates a hospital, is registered as a charitable trust under section 12AA. Following details have been furnished by the trust in respect of the previous year 2016-17:

	Particulars	₹
(i)	**Income from operation of hospital**	**16,50,000**
(ii)	**Voluntary non-corpus contribution (including anonymous contribution of 2,00,000)**	**5,00,000**

(iii)	Amount applied for the purposes of the hospital	12,50,000

Compute the total income of the trust and the tax payable by it for the assessment year 2017-18. **6**

(c) The Principal Commissioner of Income-tax or Commissioner of income-tax has the power under section 263 to revise any order passed by the Assessing Officer, if such order is erroneous in so far as it is prejudicial to the interest of the Revenue. In this context, answer the following:

(i) When is an order passed by the Assessing Officer deemed to be erroneous in so far as it is prejudicial to the interest of the Revenue?

(ii) What is the time limit for passing such order of revision? **5**

Answer 6 (a)

(i) As per section 194C, tax is not required to be deducted at source from amount credited or paid to a contractor, if such amount does not exceed ₹ 30,000. However, if the aggregate of the amounts credited or paid during the financial year exceeds ₹ 1,00,000, the payer has to deduct tax at source.
Here, the aggregate of amounts payable exceeded ₹ 1,00,000, tax is to be deducted at source under section 194C. The tax to be deducted is 1% of ₹ 1,01,000 i.e ₹ 1,010.

(ii) Where a contractor for plying of goods carriages furnishes PAN and a declaration that he has not owned more than ten goods carriages at any time during the financial year, the payer is not required to deduct tax at source.
Here, Sriram, the contractor has furnished PAN and a declaration that he owns only eight goods carriages, the payer is not required to deduct tax at source under section 194C.

Answer 6 (b)

Computation of taxable income of Laxman Memorial trust and tax payable for Assessment year 2017 – 2018

Particulars	₹	₹
Income from operation of hospital		16,50,000
Voluntary contribution other than anonymous contribution		3,00,000
		19,50,000
Less: 15% of ₹ 19,50,000 allowed to be set apart		2,92,500
Amount available for application for charitable purpose Less: Amount applied for the purpose of hospital		16,57,500 12,50,000
		4,07,5000
Add: Anonymous donation (₹ 2,00,000 - ₹ 1,00,000 exempt under section 115BBC)		1,00,000
Total Income		5,07,500
Tax on anonymous donation of ₹ 1,00,000 @ 30%		30,000
Tax on other income of ₹ 4,07,500 at normal rates: Upto ₹ 2,50,000	Nil	
On balance of ₹1,57,500@ 10%	15,750	
		15,750
		45,750
Education cess @ 3%		1,373

Total Tax payable		47,123
Rounded off u/s 288B		47,120

Answer 6 (c)

(i) As per Explanation 2 to section 263, for the purpose of the section, an order passed by the Assessing Officer shall be deemed to be erroneous in do far as it is prejudicial to the interest of the revenue, if the Principal Commissioner or Commissioner is of the opinion that-

(a) the order is passed without making enquiries or verification which should have been made;
(b) the order is passed allowing any relief without enquiring into the claim;
(c) the order has not been made in accordance with any order, direction or instruction issued by the CBDT under section 119
(d) the order has not been passed in accordance with any decision which is prejudicial to the assessee, rendered by the jurisdictional High Court or Supreme Court in the case of the assessee or any other person.

(ii) Time limit for passing the order of revision under section 263 is two years from the end of the financial year in which the order sought to be revised was passed.

Section B
(International Taxation and Transfer Pricing)

Answer Question No. 7, which is compulsory, and any one Question Nos. 8 and 9.

7. State, without indicating reasons, whether the following statement are true or false. 1×5=5

(a) In case there is no Double Taxation Avoidance Agreement, the relief on foreign income is known as unilateral relief.
(b) Monetary limit for specified domestic transaction is ₹ 25 crore.
(c) Where there is a Double Taxation Avoidance Agreement between India and foreign country, person resident in the foreign country is entitled to double taxation relief, provided tax residency certificate is obtained by that person.
(d) Rate of tax as per Income-tax Act on income by way of royalty received by a non-resident from an Indian company in pursuance of an agreement entered into on 1st April, 2010 is 15%.
(e) Salary received by an individual, who is a non-resident, from his overseas employer for services rendered in India is liable to tax in India.

Answer 7:

(a) True
(b) False
(c) True
(d) False
(e) True

8. (a) State the difficulties in applying the arm's length principle in the context of transfer pricing. 5

(b) State with brief reason, whether the following lead to emergence of 'associated enterprises' relationship: 1×5=5

(i) A Co. Ltd. (USA) having 29% equity shares in B Co. Ltd. of Mumbai and 26% equity shares in Mega Co. Inc. of Singapore.

(ii) Axe Co. Ltd. of Kolkata availed ₹ 3 crores loan based on the guarantee of Max Co. Ltd. of UK. The total borrowing of Axe Co. Ltd. was ₹ 40 crores, excluding this loan.

(iii) New Stream Ltd., UK, appointed one executive director in Wonder Ltd. of Cochin. New Stream Ltd. has 15% stake in Wonder Ltd.

(iv) White Garments Ltd of Mumbai used the secret formula of Bashir Inc. of Singapore for which it paid ₹ 5 crores. The secret formula is the basis for the manufacturing activities of White Garments Ltd.

(v) BB Ltd. purchased raw materials from Chennai Ltd. of Colombo for ₹ 60 crore, out of its total purchase of ₹ 80 crores.

(c) Soft Ltd. of Chennai supplied shoes to its holding company Rock Ltd. of US. It supplied ₹ 10000 pairs at ₹ 1,500 per pair. It sold the same quality shoes at ₹ 1,800 per pair to unrelated parties. It allowed credit period of 3 months to Rock Ltd., as against 1 month allowed to unrelated parties. The interest burden on Soft Ltd. was quantified @ ₹ 10 lakhs due to extra credit time allowed to Rock Ltd.

Rock Ltd. supplied leather to Soft Ltd. at concessional rate which resulted in lower cost of production by ₹ 50 per pair.

Compute the amount of income that would be impacted by the transactions between the parties, in the context of transfer pricing provisions. 5

Answer 8:

(a) Although the arm's length principle has international consensus, the following difficulties are experienced in applying such principle in a number of situations:

1. Difficulty in identifying transactions between independent parties which can be considered as exact comparable with controlled transactions
2. In multi-national organizations, the group first identifies the goal and then creates the associated enterprises and finally the transactions are entered into. These procedures do not apply to independent enterprises. Thus, there may be transactions within a multi-national group which may not be between independent enterprises.
3. The reductionist approach of splitting a multi-national group into various components before evaluating transfer pricing mean that benefits of economics of scale or integration between the parties, is not appropriately allocated between the multinational group.
4. Application of arm's length imposes compliance burden on enterprises, as they require the multi-national group to search for comparable transactions, robust documentation, etc. that they would otherwise not do.
5. Arm's length principle involves a lot of cost to the group.

(b)

(i) Any person or enterprise holds directly or indirectly shares carrying not less than 26% of the voting power in each of such enterprises lead to associated enterprise relationship among them.

(ii) When one enterprise guarantees not less than 10% of the total borrowings of the other enterprise they become associated enterprises. In this case the borrowing including the loan based on guarantee would be ₹ 43 crores and whereas the guaranteed loan is only ₹ 3 crores which is less than 10% and hence they are not associated enterprises.

(iii) Though the shareholding is below 26% yet when one or more executive directors or executive members of the governing board of one enterprise is appointed by another enterprise the relationship of associated enterprises emerges into existence.

(iv) When one enterprise is wholly dependent on the use of secret formula or process of which the other enterprises is the owner or in respect of which the other enterprise has exclusive rights, they become associated enterprises. Since White Garments Ltd is dependent on the secret formula of Bashir Inc. they become associated enterprises.

(v) When 90% or more raw materials required for manufacture by one enterprise is supplied by another enterprise, the relationship of associated enterprise comes into existence. In this case, the purchase from Chennai Ltd is ₹60 crores out **of** the total purchase of ₹80 crores and hence the relationship of AE does not come into existence.

(c) Computation of income to be adjusted due to transactions with associated enterprise

Particulars	₹
Sale to unrelated party (per pair)	1 ,800
Less: Sale to related party (per pair)	1,500
	300
For 10000 pairs	30,00,000
Add: Extra expenditure by way of interest due to supply to related party.	10,00,000
	40,00,000
Less: Saving in cost due to supply of raw material by related party 10000 x 50	5,00,000
Addition to be made to the total income of Soft Ltd	35,00,000

9. (a) Government of India can enter into Double Taxation Avoidance Agreement with Government of any other country. What does such agreement normally provide for? 5

(b) Answer the following briefly: 1×5=5

(i) When will the requirement from maintenance of information and documents required under section 92D not apply in respect of international transaction or specified domestic transaction?

(ii) State the prescribed form in which the report of international transaction is to be obtained from a Chartered Accountant.

(iii) For how many years should the information and documents related to international transaction to be maintained?

(iv) State the quantum of penalty leviable for failure to furnish the report of international transactions as per section 92E.

(v) How is the expenditure incurred from any transaction with a person located in notified jurisdiction area (NJA) is dealt with under the Income-tax Act?

(c) Write short notes on: 5

Advance Pricing Agreement

Answer 9:

(a) A double taxation avoidance agreement provides for the following:

1. Granting of relief in respect of income which is taxed both in India and that

country.

2. Granting of relief in respect of income tax chargeable in India and under the corresponding law in force in that country for promoting mutual economic relations, trade and investment.
3. Type of income which shall be charged to tax in either country so that there is avoidance of double taxation of same income under the Indian law and the corresponding law in force in that country.
4. Exchange of information for the prevention or avoidance of income tax in India or in that country or investigation of cases of such evasion or avoidance.
5. For recovery of income tax under Indian law and under the corresponding law in force in that country

(b)

(i) Maintenance of documents or information is not required in respect of international transaction if the aggregate value in relation to international transaction does not exceed ₹ 1 crore.

(ii) Every person who has entered into an international transaction shall obtain a report in Form No.3CEB from a chartered accountant and furnish the same before 30th November of the assessment year.

(iii) As per rule 10E(5) the information and documents relating to international transactions are to be maintained for a period of 8 years from the end of the relevant assessment year.

(iv) The quantum of penalty leviable for failure to furnish the report of international transaction as per section 92E would be ₹ 1,00,000 (section 271BA).

(v) No expenditure or allowance from any transaction with a person located in a notified jurisdictional area shall be allowed unless the assessee maintains such other documents and furnishes such other information as may be required.

(c) Advance Pricing agreement is an agreement between a taxpayer and Revenue on the transfer price methodology for a set of international transactions over a period of time.

The CBDT with the approval of the Central Government may enter into APA with any person determining the arm's length price or specifying the manner in which the ALP is to be determined in relation to an international transaction to be entered into by that person.

It is binding on the assessee and the revenue consisting of the Principal Commissioner or Commissioner and the income-tax authorities subordinate to them.

Such agreement shall be valid for a period not exceeding 5 consecutive previous years as may be specified in the agreement.

The APA shall not be binding if there is a change in law or facts which may have a bearing on the agreement so enter into.

The agreement shall be declared void ab initio if it was obtained by the person by fraud or misrepresentation of facts.