

Suggested Answer_Syl12_June2015_Paper_7

INTERMEDIATE EXAMINATION

GROUP I

(SYLLABUS 2012)

SUGGESTED ANSWERS TO QUESTIONS

JUNE 2015

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 assumptions and state the same clearly in the answers.

Working notes should form part of the answers.

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

Section A

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

1. (a) Fill up the blanks: 1x10=10
- (i) A company incorporated outside India is said to be resident in India, if control and management is _____ situated in India.
 - (ii) A foreign company is liable to surcharge at 5%, if the total income exceeds ` _____.
 - (iii) A Zero coupon bond is a long-term capital asset, if it is held for more than _____ months before transfer.
 - (iv) If statement of deduction of tax at source is not filed within due date, the deductor is liable to a fee of ` _____ per day of default or the amount of tax deductible, whichever is less.
 - (v) Maximum amount of exemption under section 10(10C) of the Income-tax Act in respect of compensation received for voluntary retirement is ` _____.
 - (vi) A manufacturing company investing more than ` _____ in new plant and machinery in previous year 2014-15 is entitled to investment allowance @ 15%.
 - (vii) An assessee can contest an order of the Income-tax Appellate Tribunal on any substantial question of law by filing appeal to the jurisdictional High Court within _____ days from the date of receipt of the said order.
 - (viii) Royalty payable by Government to a non-resident is liable to be taxed at _____% on gross amount of royalty.
 - (ix) A farm house located beyond _____ km from any municipal area is not chargeable to wealth tax.
 - (x) The value of an asset transferred by Mr. X to Mr. Y under a revocable transfer deed is includible in the net wealth of _____.

Suggested Answer_Syl12_June2015_Paper_7

- (b) Choose the most appropriate alternative: 1x5=5
- (i) Subject to fulfillment of other conditions, remuneration received by a foreign national as an employee of a foreign enterprise for services rendered by him during his stay in India is exempted from income tax, if his stay in India does not exceed a period of
- (A) 30 days
 - (B) 60 days
 - (C) 90 days
 - (D) 120 days
- (ii) Long-term capital gain on off-market sale of shares of a listed company without availing of indexation benefit is taxed at
- (A) 5%
 - (B) 10%
 - (C) 15%
 - (D) 20%
- (iii) If dividend declared by an Indian company on or after 1st October, 2014 amounts to ₹ 50,00,000, then dividend distribution tax (without considering surcharge and education cess) is
- (A) ₹ 5,00,000
 - (B) ₹ 6,25,000
 - (C) ₹ 7,50,000
 - (D) ₹ 8,82,353
- (iv) Deduction under section 80 JJAA in respect of employment of new workmen can be claimed by company for an amount equal to
- (A) 15% of additional wages to new workmen
 - (B) 20% of additional wages to new workmen
 - (C) 25% of additional wages to new workmen
 - (D) 30% of additional wages to new workmen
- (v) A return of income for Assessment Year 2014-15 filed within the due date specified in Section 139(1) can be revised by the assessee at any time before expiry of
- (A) 31st March, 2015
 - (B) 31st March, 2016
 - (C) 31st December, 2014
 - (D) 31st December, 2015
- (c) Attempt all the questions below: 1x5=5
- (i) At what rate of interest on debentures of an Indian public limited company subscribed in foreign exchange by a non-resident Indian taxed?
- (ii) What is the period for which an advance pricing agreement shall remain valid?
- (iii) What is the rate of tax applicable to income of a non-resident sportsman who is a foreign national by way of participation in any sport in India?
- (iv) P. Ltd., a foreign company gave loan to Q. Limited, an Indian company. When shall P. Ltd. be deemed to the associated enterprise of Q. Ltd.?
- (v) What is 'uncontrolled transaction'?

Suggested Answer_Syl12_June2015_Paper_7

Answer:

1. (a) (i) Wholly
(ii) `10 crores
(iii) 12 months
(iv) 200
(v) `5 lacs
(vi) `25 crores
(vii) 120
(viii) 25
(ix) 25
(x) Mr. X
- (b) (i) (C) 60 days
(ii) (B) 10%
(iii) (D) `8,82,353
(iv) (D) 30% of additional wages to new workmen
(v) (B) 31st March, 2016
- (c) (i) 20%
(ii) Five consecutive previous years.
(iii) 20%
(iv) If loan obtained by Q. Limited from P. Limited constitutes at least 51% of the book value of the assets of Q. Limited, then P. Limited and Q. Limited shall be said to be associated enterprises.
(v) Uncontrolled transaction means transaction between unrelated enterprises, whether resident or non-resident.
2. (a) **Can Mr. Ajit who has long-term capital gain from sale of vacant site in India buy a residential house outside India to claim exemption under section 54F? Assume that he has no residential property in India. 3**
- (b) **Vijay, a resident individual aged 59, is running a wholesale business in fertilizers, whose turnover for the year ended 31.03.2015 is `70 lacs. Is he liable to pay advance tax, if he maintains books of accounts and gets his accounts audited under section 44AB of the Income-tax Act, 1961 (business income is `5.2 lacs)? Will your answer be different if he opts for presumptive taxation? He has no other income. 3**
- (c) **Name any four businesses which are eligible for deduction under section 35AD of the Income-tax Act, 1961. 4**
- (d) **How is the unrealized rent dealt with in annual value determination of a house property under the Income-tax Act, 1961? What are the conditions to be satisfied in this regard? 3**

Answer:

2. (a) Exemption u/s 54F
- When the assessee has no residential house property or has not more than one residential house property, he is eligible to claim exemption under section 54F.
 - When a long-term capital asset other than a residential house is transferred, the exemption by way of investment in residential house could be obtained by deploying the net consideration.

Suggested Answer_Syl12_June2015_Paper_7

- The exemption is subject to the condition that the assessee has within a period of one year before or two years after the date of transfer of long-term capital asset acquires a residential house or three years after transfer constructs a new residential house in India for the purpose of availing the exemption under section 54F.
- A person transferring a long-term capital asset in India cannot acquire a residential house outside India and be eligible for exemption under section 54F.
- Thus the person cannot claim exemption in respect of long-term capital gain on sale of vacant site in India by acquiring a residential house outside India.

(b) Liability to pay advance tax

Where the assessed tax payable by an individual who is not a senior citizen, exceeds ` 10,000, he is liable to pay advance tax.

In the first situation, since the tax payable on total income exceeds ` 10,000 he is liable to pay advance tax.

Where he opts for presumptive tax, the obligation to pay advance tax will not arise at all.

(c) Eligible businesses u/s 35AD

The following businesses are specified business as per section 35AD(8):

- Setting up and operating a cold chain facility
- Setting up and operating a warehouse facility for storage of agricultural produce.
- Laying and operating a cross country natural gas or crude or petroleum oil pipe line network for distribution, including storage facilities being an integral part of such network.
- Building and operating, anywhere in India, a hotel of two star or above category as classified by the Central Government.
- Building and operating, anywhere in India, a hospital with at least one hundred beds for patients.
- Developing and building a housing project under a scheme for slum redevelopment or rehabilitation framed by the Central Government or State Government, as the case may be and notified in this behalf.
- Developing and building a housing project under a scheme for affordable housing framed by the Central Government or State Government, as the case may be and notified in this behalf.
- Production of fertilizers in India.
- Setting up and operating an inland container depot or a container freight station notified or approved under the Customs Act, 1962.
- Bee-keeping and production of honey and beeswax.

Suggested Answer_Syl12_June2015_Paper_7

- Setting up and operating a warehouse facility for storage of sugar.
- Laying and operating a slurry pipeline for the transportation of iron ore;
- Setting and operating a semi-conductor wafer fabrication manufacturing unit notified by the Board in accordance with such guidelines as may be prescribed.

(d) Unrealised rent

The amount of unrealized rent is not to be includible while determining the annual value of a property.

However, the following conditions are to be satisfied for excluding the unrealized rent.

- (i) The tenancy must be bona fide.
- (ii) The defaulting tenant has vacated or steps have been taken to compel him to vacate the property.
- (iii) The defaulting tenant is not in the occupation of any other property of the assessee; and
- (iv) The assessee has taken all steps to institute legal proceedings for the recovery of unpaid rent or satisfies the Assessing Officer that the legal proceedings would be useless.

3. (a) Sarath Ltd., engaged in manufacturing activity, acquired new plant for ` 30 crores in August 2014 which was put to use from 15.09.2014. Compute depreciation, additional depreciation under section 32(1)(ia) and investment allowance under section 32AC of the Income-tax Act, 1961 for the plant. Quantify the written down value of asset as it would be on 31.03.2015. 4

(b) Vivitha Pipes Ltd., set up a new unit for extension of its manufacturing activity. It incurred `45 lakhs towards preliminary expenses. The cost of the project is ` 600 lakhs and the amount of capital employed is ` 700 lakhs. Determine the amount eligible for amortization under section 35D and the period of amortization. 6

(c) When does advance money received for transfer of capital asset become chargeable to tax? Under what head of income is it chargeable? 3

Answer:

3. (a)

Particulars		` in lakhs
Normal depreciation at 15% on ` 30 crores	A	450
Additional depreciation at 20% on ` 30 crores	B	600
Investment allowance under section 32AC at 15% on ` 30 crores	C	450
Closing WDV = `30 crores – Depreciation – Additional depreciation [i.e. `30 crores - A – B] = ` (30 crores – 4.50 crores – 6 crores)		1,950

Note: Investment allowance under section 32AC will not reduce the block value of assets.

Suggested Answer_Syl12_June2015_Paper_7

(b) Amortization of preliminary expenses

Preliminary expenses are eligible for amortization in 5 equal annual installments.

In the case of company, 5% of the cost of the project or the capital employed shall be considered for computing the amount eligible for amortization.

5% of the cost of the project = ₹600 lakhs × 5% = ₹30 lakhs

5% of the capital employed = ₹700 lakhs × 5% = ₹35 lakhs

Actual preliminary expenditure incurred = ₹45 lakhs.

The assessee hence is eligible to amortise ₹35 lakhs under section 35AD.

Amount eligible for amortization for 5 years = ₹7 lakhs for each year.

(c) As per section 56(2)(ix) any sum of money received as advance in the course of transfer of capital asset is chargeable.

(i) If such sum is forfeited; and

(ii) The negotiations did not result in transfer of such capital asset.

Thus the advance amount forfeited will be taxed as income from other sources.

4. (a) Mr. Ashwin finance manager in Beta Ltd. gives you the following information:

(i) A rent-free accommodation is provided by the employer at Bangalore by taking the accommodation on lease basis whose rent was ₹20,000 per month.

(ii) He is provided with a motor car (cubic capacity of engine more than 1.6 liters) both for official and personal use. The expenses on running and maintenance are met by the employee.

Assume annual salary for the purpose of perquisite valuation as ₹6,00,000.

You are requested to compute the perquisite value in the hands of Mr. Ashwin. 4

(b) When are the books of account of a person engaged in notified profession liable for audit under section 44AB? What is the penalty is leviable for failure to get the accounts audited? 2

(c) State the conditions to be satisfied when a sole proprietary concern is succeeded by a company, to avail tax exemption in respect of capital gains. 4

(d) Mr. Bharat, an engineering graduate, born and brought up in India, got employment in USA in August 2014. By what date he should leave India, in order to become a non-resident? By that, what tax advantage he will get? 3

Answer:

Suggested Answer_Syl12_June2015_Paper_7

4. (a) Computation of Perquisite value in the hands of Mr. Ashwin

Particulars	`	`
Rent-free accommodation:		
Rent paid by the employer at ` 20,000 per month × 12	2,40,000	
15% of salary i.e., 15% of ` 6,00,000	90,000	
-Whichever is less is taken as the value of perquisite		
Perquisite value of rent-free accommodation (A)		90,000
Perquisite value of motor car:		
Cubic capacity of engine more than 1.6 litres and the expenses are met by the employee, hence the perquisite value ` 900 per month. (` 900 × 12) (B)		10,888
Total perquisite value in the hands of Mr. Ashwin (A) + (B)		1,00,800

(b) Every person carrying on profession shall, if his gross receipts in profession exceed ` 25 lakhs in any previous year must get his accounts audited under section 44AB.

For failure to get the accounts audited the penalty leviable is 0.5% of the gross receipt or ` 1,50,000 – whichever is less (section 271B).

(c) Conversion of sole proprietary concern into a company
Where a sole proprietary concern is succeeded by the company the capital gain on transfer of any capital asset or intangible asset will be tax-free.

The following conditions are to be satisfied in this regard:

- (i) All the assets and liabilities of the sole proprietary concern relating to the business immediately before the succession become the assets and liabilities of the company;
- (ii) The shareholding of the sole proprietor in the company is not less than 50% of the total voting power in the company and
- (iii) The continues to remain so for a period of 5 years from the date of succession; and
- (iv) The sole proprietor does not receive any consideration or benefit, directly or indirectly, in any form or manner, otherwise than by way of allotment of shares in the company.

(d) **Planning for residential status**

A person who leaves India for employment if remains for less than 182 days during the financial year of leaving, he will be a non-resident.

Mr. Bharat must leave India before 29th September, 2014 to be non-resident for the financial year 2014-15.

When he plans his departure in such a way that he becomes non-resident, his income accruing or arising outside India will not be subjected to tax in India. His income accruing or arising in India alone will be liable to tax in India.

Suggested Answer_Syl12_June2015_Paper_7

5. (a) Mr. Dhoni sold a residential building at Cochin for ₹65 lakhs in December 2014. The stamp valuation authority determined the value at ₹80 lakhs which was not contested by Mr. Dhoni. The property was acquired in April, 2004 for ₹6 lakhs. He acquired a residential flat at Ranchi for ₹55 lakhs and an other residential house at Cuttack for ₹25 lakhs before March, 2015. Compute the capital gain of Mr. Dhoni for the assessment year 2015-16.

Note:

Financial Year	Cost inflation index
2004-05	480
2014-15	1,024

You are required to plan in such a way that the incidence of tax is the least. 5

- (b) Explain the provisions relating to carry forward and set off of losses by closely held companies. 3

- (c) Mohit Sharma gives you the following information for the year ended 31.03.2015:

Owns 3 goods carriages throughout the financial year 2014-15

Retail trade turnover ₹36,00,000.

Has eligible brought forward depreciation of the assessment year 2012-13 ₹60,000 relating to retail trade.

Deposited ₹80,000 in PPF account and ₹90,000 in tax saver deposit.

Assume that he wants to offer income by opting for sections 44AD and 44AE.

Compute his total income for the assessment year 2015-16. 5

Answer:

5. (a)

Computation of capital gain of Mr. Dhoni for the assessment year 2015-16

Particulars	₹
Sale consideration of residential building at Cochin	65,00,000
Stamp valuation authority has determined the value at ₹80 lakhs.	
The higher of the two is to be adopted as deemed sale consideration u/s 50C	80,00,000
Less: Indexed cost of acquisition	
₹6,00,000 × 1024 ÷ 480	12,80,000
Capital gains before exemption	67,20,000
Less: Exemption U/s. 54	
In respect of residential property acquired at Ranchi	55,00,000
Taxable long-term capital gain	12,20,000

Note: From the assessment year 2015-16 onwards, the exemption under section 54 is limited to one residential house in India. Out of the two residential properties acquired by him, he can opt for exemption under section 54 in respect of one property only. The higher of the values has been adopted for maximizing the benefit to the assessee.

- (b) Losses of closely-held companies

Section 79 deals with carry forward and set off of business loss in the case of a company in which public are not substantially interested.

Where on the last day of the previous year in which the loss is sought to be carried forward and set off, the shares of the company carrying not less than 51% of the voting

Suggested Answer_Syl12_June2015_Paper_7

power must continue to be held by the persons who held 51% of the total voting power on the last day in which the loss was incurred.

This restriction will not apply if the change in shareholding takes place due to death of a shareholder or transfer of shares is by way of gift by a shareholder to his relative.

Also, it is not applicable where there is a change in shareholding of an Indian company which is a subsidiary of a foreign company as a result of amalgamation or demerger of a foreign company, provided 51% of the shareholders of the amalgamating or demerged foreign company continue to be shareholders of the amalgamated or the resulting foreign company.

(c)

Computation of total income of Mr. Mohit Sharma for the Assessment Year 2015-16

Particulars	`	`
Income U/s. 44AD from retail trade @ 8% on ` 36,00,000		2,88,000
Income U/s. 44AE in respect of plying of goods carriages ` (7,500 × 3 × 12)		2,70,000
Business income prior to set off		5,58,000
Less: Brought depreciation not eligible for set off as the b/f depreciation is deemed to be current year depreciation and has been deducted while computing income under section 44AD		---
Gross Total Income		5,58,000
Less: Deduction u/s. 80C		
In respect of PPF contribution	80,000	
In respect of Tax saver deposit	90,000	
Maximum amount deductible		1,50,000
Total Income		4,08,000

6. (a) **Vimala Pharma Ltd. informs that it has net profit of ` 60 lakhs for the year ended 31st March, 2015. It gives you the following further information:**
- (i) **Depreciation as per books ` 3,50,000.**
 - (ii) **Bad debts written off in the books ` 5,00,000, which includes ` 1 lakh due from one customer who has disputed the liability to pay but continues to have business relationship with the company.**
 - (iii) **Proposed dividend debited to Profit and Loss Account ` 6 lakhs.**
 - (iv) **One machinery which has become useless has been written off in P&L Account, the amount debited being ` 90,000.**
 - (v) **Provident Fund collections from employees for the year ` 1,50,000 and company's own contribution of ` 1,10,000 for the year have not been remitted. These amounts are shown as Sundry Liability in the books. Assume it will be remitted after 31st December, 2015.**
 - (vi) **Income from agricultural lands surrounding the factory ` 50,000 credited to Profit and Loss Account.**
 - (vii) **Bank term loan for purchase of machinery waived ` 2 lakhs is credited to capital reserve account.**
 - (viii) **The opening WDV of plant and machinery was ` 15,90,000. One machinery for ` 4,10,000 was acquired on 01.06.2014 and was put to use immediately.**
 - (ix) **Provisions for taxation debited in the Profit and Loss Account amounts to ` 15 lakhs.**

You are requested to compute the income of the company under the head 'Profits and gains of business or profession' for the assessment year 2015-16.

9

Suggested Answer_Syl12_June2015_Paper_7

(b) State whether TDS/TCS provisions are attracted in the following cases:

4

- (i) A newspaper paid ` 2,00,000 to ex-cricketer of New Zealand for writing series of articles during World Cup Cricket matches.
- (ii) Mr. X purchased jewellery from a showroom for ` 5,50,000 on 10.10.2014 by cheque.
- (iii) When Mr. Y purchased fly ash from a factory to use the fly ash for manufacture of bricks.
- (iv) A partnership firm having a turnover of ` 40 lakhs during the financial year 2013-14 made contract payment of ` 35,000 to an individual for a single bill.

Answer:

6. (a)

Computation of business income of Vimala Pharma Ltd for the assessment year 2015-16

Particulars		`	`
Net Profit as per profit and loss account			60,00,000
Add:			
Depreciation debited to P&L A/c			3,50,000
Bad debts write off is deductible if it is written off in the books. Even if the customer has relationship with the assessee the write off is deductible without any attendant conditions. TRF Ltd. v. CIT 323 ITR 397			Nil
Proposed dividend debited to P&L Account			6,00,000
Machinery discarded debited to P&L account – disallowed			90,000
Provident fund collections and deductions out of salary not remitted to be treated as income			2,60,000
Provision for taxation debited to P&L account			15,00,000
			88,00,000
Less:			
Agricultural income credited to P&L Account		50,000	
Bank term loan waiver is not liable to tax as section 41(1) will not apply			Nil
Depreciation on plant and machinery			
Opening WDV	15,90,000		
Add: New additions	4,10,000		
	20,00,000		
Depreciation @ 15% on ` 20 lakhs		3,00,000	
			3,50,000
Income from Business			84,50,000

(b) Liability to TDS/TCS

- (i) As per section 194E tax is deductible at source at 20% on the payment made to non-resident foreign citizen sportsman.
- (ii) When jewellery is purchased in cash the tax collection at source will apply. In this case as the purchase was made by means of cheque, TCS provisions will not apply.
- (iii) When goods purchased are meant for manufacturing it is not liable for tax collection at source. Only when it is for the purpose of trade, TCS provisions will apply.
- (iv) Tax is deductible at source in respect of each contract when it exceeds ` 30,000. [Clause (i)(k) of the Explanation to section 194C will be applicable to partnership firms.]

Suggested Answer_Syl12_June2015_Paper_7

Section B

(Wealth Tax Act)

[Answer any one question]

7. (a) A property self occupied for 6 months was let out on a monthly rent of ₹ 10,000 from 01.10.2014. The municipal tax on the property amounts to ₹ 20,000 per annum. The tenant has deposited ₹ 2 lakhs. The municipal annual value for the property is ₹ 1,40,000. Compute the capitalized value of the property. The property has been constructed utilising the permissible extent (200 sq. ft.) of total available land of area 3,000 sq. ft.

4

- (b) How is the interest of a partner in the assets owned by the firm computed and charged to wealth tax?

4

Answer:

7. (a) The property let out for less than 300 days for residential purpose is an asset liable for wealth tax. The valuation of the property is given below:

Particulars	₹
Actual rent received for 6 months	60,000
Add: 15% of the amount of deposit of ₹ 2 lakhs for 6 months.	15,000
Rental value for 6 months	75,000
Annual rent	1,50,000
Municipal value	1,40,000
Note: Higher of annual rent or the municipal value to be adopted. Since the annual value is more, the same is adopted.	
Gross maintainable rent = annual rent i.e.,	1,50,000
Less: Municipal tax (annual)	20,000
Net maintainable rent	1,30,000
Capitalized value ₹ 1,30,000 × 12.5	16,25,000

- (b) Valuation of interest of partner in a firm

The value of interest of a partner in a firm is to be determined in the manner laid down as follows-

- If the assets belong to the business of the Firm/AOP then value the same as per Rule 14.
- If the assets are not the assets of the business then value the same as per Schedule III. Under Schedule III, Part E, Rule 16 the net wealth of the Firm shall be determined as if Firm is an assessee.

Thereafter that portion of wealth as is equal to the amount of capital of the partners shall be allocated.

The residual net wealth of the Firm shall be allocated among the partners in accordance with the agreement of partnership for distribution of assets in the event of dissolution and in the absence of such an agreement in the proportion in which the partners are entitled to share the profits.

The total sum so allocated to a partner shall be taken as the value of the interest.

No exemption under section 5 shall be allowed to a firm but partners are entitled for proportionate exemption in their individual assessment.

Suggested Answer_Syl12_June2015_Paper_7

8. (a) State whether the following are assets under the Wealth Tax Act: 4
- (i) Farm house situated in a village 20 kms from the municipal limits in Delhi, where the corporate office is located.
 - (ii) Guest house located 30 kms from the municipal limits.
 - (iii) Vacant land held as stock in trade for the past 7 years.
 - (iv) Lands meant for industrial use acquired 18 months before the valuation date.
- (b) Mr. Vasudevan transferred a vacant site in an urban area to Miss Jothi on 01.01.2015, who subsequently got married to his son Vaibhav on 01.03.2015. In whose hands will this vacant urban land be treated as an asset as on 31.03.2015? 4

Answer:

8. (a) (i) Farm house beyond 25 kms. from the municipal limits is not an asset. However, in this case it is situated within 25 kms. Hence, it is an asset.
- (ii) Guest house is an asset liable for wealth tax regardless of the distance from the municipal limits.
- (iii) Vacant land held as stock in trade is not liable for wealth tax for a period of 10 years from the date of its acquisition. Hence, it is not an asset.
- (iv) Land meant for industrial use is not an asset for a period of 2 years from the date of its acquisition. Since, it was acquired 18 months before the valuation date it is not an asset.

(b) Clubbing of wealth

In computing the total wealth of an individual, any asset transferred by him to his son's wife shall be clubbed in his hands.

In the given situation, as on the date of transfer of the urban land, Miss Jothi was not married to the Vasudevan's son Vaibhav.

Therefore, the vacant urban land cannot be treated as an asset in the hands of Vasudevan, as on 31.03.2015.

It will be treated as the asset of Jothi, as on 31.03.2015.

Section C
[International Taxation, DTTA, etc.]
Answer any two questions.

9. (a) Explain binding nature of advance pricing agreement. 3
- (b) Is it possible to apply advance pricing agreement entered into in a previous year to international transactions entered into in preceding previous years as well? 3
- (c) Ayush is a musician who derived income of ` 1,25,000 during the previous year 2014-15 from a concert performed in a country with which India has no double taxation avoidance agreement. Tax of ` 31,250 was deducted at source in the said country. His income from profession in India during the previous year 2014-15 amounted to ` 3,00,000. Compute tax payable by Ayush for Assessment Year 2015-16. 4

Suggested Answer_Syl12_June2015_Paper_7

Answer:

9. (a) Binding nature of APA
As per section 92Cc(4) the advance pricing agreement entered into shall be binding –
- (i) On the person in whose case, and in respect of the transaction in relation to which, the agreement has been entered into, and
 - (ii) On the principal commissioner or and the income-tax authorities subordinate to him, in respect of the said person and the said transaction.

However, the agreement shall not be binding if there is a change in law or facts having bearing on the agreement so entered.

- (b) Applicability of ALP to earlier year
As per section 92CC (9A) inserted by the finance (no. 2) act, 2014 advance pricing agreement may provide for determining the arm's length price or specify the manner in which arm's length price shall be determined in relation to international transaction entered into by the person during maximum four previous years preceding the first of the previous years for which such agreement is entered into and the arm's length price shall be determined in accordance with the said agreement.

- (c) Computation of tax payable by Ayush for Assessment year 2015-16

Particulars	Amount (₹)
Income in the foreign country	1,25,000
Income in India	3,00,000
Total income	4,25,000
Tax on total income $(4,25,000 - 2,50,000) \times 10\%$	17,500
Less: Rebate u/s 87 A	2,000
	15,500
EC & SHEC at 3%	465
Total	15,965
Average Rate of tax in India $(15,965/4,25,000 \times 100)$	3.756%
Average Rate of tax in Foreign Country $(31,250/1,25,000 \times 100)$	25%
Doubly taxed income	1,25,000
Less: Amount of relief u/s 91 $(1,25,000 \times 3.756\%)$ (lower of a & b)	4,695
Tax payable $(15,965 - 4,695)$	11,270

10. (a) **What are the consequences (other than penalty) of adjustment made by the Assessing Officer to arm's length price in international transactions entered into by the assessee resulting in increase in taxable income?** **3**
- (b) **A person resident in India seeks to remit certain amount liable to tax in India to a company incorporated in a notified jurisdictional area. At what rate should the tax be deducted a source from such payment?** **3**
- (c) **P. Ltd., an Indian company, sold steel rods to its holding company, Q. Ltd., USA at US Dollar 200 (FOB) per MT during previous year 2014-15. P. Ltd. also sold identical product to an independent company in USA, R. Ltd. at US Dollar 400 (CIF) per MT. Insurance and freight amounts to ₹200 per MT. Determine whether the transaction between P. Ltd. and Q.**

Suggested Answer_Syl12_June2015_Paper_7

Ltd. satisfies the arm's length test.

4

Answer:

10. (a) Consequences of adjustments made to ALP

In case the Assessing Officer makes adjustment to arm's length price in an international transaction which results in taxable income of the assessee, the following consequences shall follow:

- (i) No deduction under section 10A/ 10B/ 10AA or under Chapter VI-A shall be allowed from the income so increased.
- (ii) As a consequence, the total income of the assessee will go up by the amount of adjustment so made.
- (iii) No corresponding adjustment would be made to the total income of the other associated enterprise (in respect of payment made by the assessee from which tax has been deducted or is deductible at source) on account of increase in the total income of the assessee on the basis of the arm's length price so recomputed.

(b) TDS from interest paid to an entity in NJA

As per section 94 a(5), notwithstanding anything contained in any other provision of the income-tax Act, where a person makes any payment of any sum on which tax is deductible at source, the tax shall be deducted at the highest of the following rates:

- (i) At the rate or rates in force;
- (ii) At the rate specified in the relevant provision of the income-tax Act, 1961;
- (iii) At the rate of 30%.

(c) As P. Ltd. holds more than 26% shares in Q. Ltd., P. Ltd. and Q. Ltd are deemed to be associated enterprises.

As P. Ltd., supplied similar product to R. Ltd., an unrelated entity in USA, the transaction between P. Ltd. and R. Ltd. is comparable uncontrolled transaction for determining arm's length price. Comparable uncontrolled price (CUP) method for determining ALP is applicable.

	US Dollar
Price per MT of steel rods to R Ltd.	400
Less; Cost of insurance and freight	200
Arm's length price	200

Since the price charged from Q. Ltd. is equal to ALP, the transaction between P. Ltd. and Q. Ltd. satisfies the arm's length test.

11. (a) When shall a transaction entered into with an unrelated person shall be deemed to be an international transaction with an associated enterprise? 4

(b) Explain the purposes for which the Central Government enters into double taxation avoidance agreement with any foreign country as per section 90 of the Income-tax Act, 1961. 4

(c) What is residuary method of determination of arm's length price as per Rule 10AB of the Income-tax Rules? 2

Answer:

Suggested Answer_Syl12_June2015_Paper_7

11. (a) International transactions with an AE

As per section 92B as amended by the finance (No.2) Act, 2014 a transaction entered into by an enterprise with a person other than an associated enterprises (i.e., "other person" shall be deemed to be an international transaction entered into between two associated enterprises in the following cases:

- (i) There exists a prior agreement in relation to the relevant transaction between the other person and the associated enterprise or,
- (ii) Where the terms of the relevant transaction are determined in substance between such other person and the associated enterprise and
- (iii) Either the enterprise or the associated enterprise or both of them are non-residents.

It is immaterial whether such other person is a non-resident.

(b) Purposes for which the Central Government can enter into DTAA

Under Section 90(1) the purposes for which the Central Government can enter into double taxation avoidance agreement with foreign country are:

- (i) Granting of double taxation relief, i.e., relief in respect of income on which income-tax has been paid in India and also in the foreign country or granting of relief in respect of income-tax chargeable under the income-tax Act and under the corresponding law in that country to promote mutual economic relations, trade and investment.
- (ii) For avoidance of double taxation of income under the income-tax Act and under the corresponding law in force in that country or specified territory.
- (iii) For exchange of information for the prevention of evasion or avoidance of Income tax chargeable under the income-tax Act or under the corresponding Law in force in that country or specified territory or investigating of cases of such evasion or Avoidance.
- (iv) For recovery of income-tax under the income-tax Act and under the corresponding law in force in that country or specified territory as the case may be.

(c) Residuary method of determination of ALP

As per Rule 10AB, for the purpose of section 92C(1)(f), the residuary or other method for determination of the arm's length price in relation to an international transaction or specified domestic transaction shall be any method which takes into account the price which has been charged or paid, or would have been charged or paid, for the same or similar uncontrolled transaction, with or between non-associated enterprises, under similar circumstances, considering all material facts.