



## FINAL CA – May 2018

### DIRECT TAXATION

Test Code – F29

Branch: MULTIPLE Date: 14.01.2018

(50 Marks)

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*Note: All questions are compulsory.*

#### Question 1 (4 marks)

The following remedies are available to Mr. D under the Income-tax Act, 1961:

1. **File an appeal before the Commissioner (Appeals):** D can file an appeal under section 246A, against the order of assessment under section 143(3), to the Commissioner (Appeals). An appeal can be filed by an assessee even against inclusion in assessment, of such income erroneously included by him in the return of income. **(1 ½ mark)**
2. **File a revision petition:** in the alternative, D can file a revision petition under section 264 with the Commissioner of Income-tax seeking exemption of interest from Relief Bonds, not claimed in the return of income and not allowed in the order of assessment. **(1 ½ mark)**
3. **File an application for rectification:** The other course of action D could take is to file an application under section 154 with the Assessing Officer, seeking rectification of the order of assessment made. The consistent judicial view is that exemption not claimed by the assessee and not allowed by the Assessing Officer, though the material relating thereto was in the return of income, constitutes a mistake apparent from the record. **(1 mark)**

#### Question 2 (6 marks) (3 marks each)

##### **Rectification of assessment order under section 154 due to subsequent change of law on retrospective basis.**

If the assessment order is plainly and obviously inconsistent with the specific and clear provision as amended retrospectively, indisputably there is a mistake apparent from record. In the light of the retrospective amendment, the assessment order had to be revised.

If there is a retrospective amendment in law disallowing an expense / taxing a receipt and in assessment order the expenses has been allowed / receipt has been held as non – taxable, then there is a mistake apparent from record in the order of A.O.

In view of this, the Assessing Officer can, under section 154, rectify the order of assessment, in the light of the later amendment of the law with retrospective effect.

If there is a retrospective amendment in law, the same can be given effect to by passing & rectification order under section 155. However, the period of limitation of four years shall apply.

##### **Rectification of assessment order under section 154 on account of subsequent judgement of Supreme Court**

CBDT Circular: A mistake arising as a result of subsequent interpretation of law by the Supreme Court would constitute a “mistake apparent from records” and rectification under section 154 is possible.

Where an assessee moves an application under section 154 pointing out that in light of a letter Supreme Court judgement, a mistake has occurred in any of the completed assessments, then rectification under section 154 shall be made provided that the rectification application is made within the prescribed period of four years.

The Income-tax authority can disallow a deduction under section 154 on the basis of a letter Supreme Court judgement. But in this case, the rectification order must be passed within the prescribed period of four years.

**Question 3 (10 marks)**

As per section 50B, any profits or gains arising from the slump sale of the undertaking effected in the previous year shall be chargeable to income-tax as capital gains and shall be deemed to be the income of the previous year in which the transfer took place. If the assessee owned undertaking transferred under slump sale for more than 36 months before the date of transfer, then the capital gain shall be deemed to be **long-term capital gains. (1 mark)**

Indexation benefit is not available in case of slump sale.

**Ascertainment of tax liability of Alpha Ltd. From slump sale of Unit – 2 (3 marks)**

Particulars	₹
Slump sale consideration	3,00,00,000
Less: Cost of acquisition (net worth) [See working Note below]	1,00,00,000
Long – term capital gain (as Unit – 2 is held for more than 36 months)	2,00,00,000
<b>Calculation of tax liability</b>	
Income tax @20% on long term capital gain under section 112	40,00,000
Surcharge @7%, since total income exceeds ` 1 crore but does not exceed ` 10 crore	2,80,000
	42,80,000
Education cess @ 2% and Secondary and higher education cess @ 1%	1,28,000
<b>Total tax liability</b>	<b>44,08,400</b>

**Working Note: Net Worth of Unit – 2 (2 mark)**

WDV of block of assets	75,00,000
Debtors	68,00,000
Inventories	22,00,000
	1,65,00,000
Less: Liabilities	65,00,000
<b>Net Worth</b>	<b>1,00,00,000</b>

**ii. Tax Advice (4 marks)**

(a) Transfer of any capital asset by a holding company to its 100% Indian subsidiary company is exempt from tax under section 47. Therefore, if it is possible for Alpha Ltd., it should try to acquire the entire shareholding of Beta Ltd and make Beta Ltd its wholly owned subsidiary. Thereafter, upon slump sale, the resultant capital gain shall not attract tax liability.

However, in such case also, Alpha Ltd. Should not transfer any shares in Beta Ltd. for 8 years from the date of slump sale.

(b) Alternatively, if acquisition of 15% shares is not feasible, Alpha Ltd. may think about demerger plan of Unit 2 to get the exemption from tax by virtue of section 47.

**Question 4 (16 marks)**

**Computation of Total Income of BM Private Ltd. For the A.Y. 2018-19**

	<b>Particulars</b>	<b>Amount</b>	
I	<b>Income from house property [Rental income from commercial property]</b> Net Annual Value	2,50,000	
	<b>Less:</b> Deduction under section 24 30% of Net Annual Value	75,000	1,75,000 (2 marks)
II	<b>Profits and gains of business and profession</b> Profits from manufacturing business <b>[See Working Note below]</b>	77,50,000	
	<b>Less:</b> Set off of losses from trading in derivatives in a recognized stock exchange [allowed to be set –off against profits from the business of manufacturing as per section 70(1) since it is not speculative in nature.	2,50,000	75,00,000
III	<b>Capital Gains</b> Sale consideration	50,00,000	
	<b>Less:</b> Indexed Cost of Acquisition [` 40,00,000 x 272/220]	4945,455	
	<b>Long term capital gains</b>		54,545 (2 marks)
	<b>Income from other sources</b> Rent received from vacant land	1,20,000	
	Interest received on income –tax-refund	1,00,000	
	Excess of issue price of shares over the fair market value of shares is taxable as per section 56(2)(viib) in the case of BM Pvt. Ltd. Not being a company in which public are substantially interested [ ` 40 )i.e, ` 100 – 60] x 1,00,000 shares]	40,00,000	42,00,000 (2 marks)
	<b>Gross Total Income</b>		1,19,49,545
	<b>Less: Deduction under Chapter VI A</b>		
	<b>Deduction under section 80G</b>		
	Donation to Swachh Baharat Kosh [qualifies for 100% deduction – assuming that the same has not been spent in pursuance of corporate social responsibility under section 135 (5) of the companies Act, 2013]	1,00,000	
	Deduction under section 80GGB		
	Contribution to Political Party [ Not allowable as deduction since the contribution is made in cash]	Nil	1,00,000 (1 mark)
	<b>Total Income</b>		<b>1,18,49,545 (1 mark)</b>

**Working Note:**

**Computation of profits and gains from the business of manufacturing (8 marks)**

<b>Particulars</b>	<b>Amount ( ` )</b>	
Profits and Gains from Business and Profession Net Profit as per profit and loss account		90,00,000
Add : Item debited but to be considered separately		
(i)Donation paid to Swachh Bharat Kosh, considered	1,00,000	

separately [Not an expenditure incurred wholly and exclusively for the manufacturing business. Hence, not allowable under section, 37]		
(ii) Contribution to political party [Not an expenditure incurred wholly and exclusively for the manufacturing business. Hence nor allowable under section 37]	2,00,000	
(iii) Payment to transport contractor [As per section 194C (6), no tax is required to be deducted at source since the payment is to a transport contractor not having more than 10 goods carriages at any time during the process year and he has given a declaration to that effect along with his PAN. Hence, disallowance under section 40(a)(ia) for non – deduction of tax at source is not attracted. Also, since payment is made by account payee cheque, no disallowance under section 40A(3) is attracted].	---	
(iv) Bonus to employee [Since the payment is made after due date is filing of return of income, disallowance under section 43B is attracted]	2,00,000	
(v) Provision for income –tax (including interest of ` 50,000 thereon) (Net allowable as deduction. Disallowance under section 40(a)(ii) is attracted.	3,00,000	
(vi) Loss from trading in futures and options (derivatives) in stock in a recognized stock exchange) (Since loss from trading in futures and options in stock is not related of the business of manufacturing, the same is not incurred wholly and exclusively for this business and hence, is not allowable as deduction under section 37, while computing profits from the business of manufacturing]. However, such loss can be set off under section 70.	2,50,000	
		10,50,000
		10,50,000
<b>OTHER ADJUSTMENTS</b> Add: Cash Payment for the purchase of raw material deemed as income [Since the provisions for outstanding bill for purchase of raw material has been allowed as deduction during the P.Y. 2014-15, cash payment in excess of ` 10,000 against such bill in the P.Y. 2017-18 would be deemed as income of P.Y 2017-18 as per section 40A[(3A)]		50,000
		1,01,00,000
Less : Expenditure to be allowed Depreciation [difference between the normal depreciation of ` 17.75 lakhs as per Income tax- Act, 1961 [See Note below] and depreciation charged to the statement of profit and loss of ` 12 lakhs]	5,75,500	
Note – Printers and scanners form an integral part of the computer system and they cannot be used without the computer. Hence, they are part of the computer system, they would be eligible for depreciation at the higher rate		

of 60% applicable to computers including computer software. However, EPABX is not a computer and is, hence, not entitled to higher depreciation @ 60 %		
Particulars	₹	
Depreciation computed as per Income tax Act, 1961	20,00,000	
Less: Depreciation @ 60 % wrongly provided in respect of EPABX = 60% of ₹ 5,00,000		
	17,00,000	
Add :Depreciation @ 15% on EPABX = 15% of ₹ 5,00,000	75,000	
Correct Depreciation as per Income tax act, 1961	17,75,000	
Less : Additional depreciation on new plant and machinery Since plant and machinery was purchased only on 15.10.2017, it was put to use for less than 180 days during the year. Hence additional depreciation is to be restricted to 10% (i.e., 50 % of 20%) of ₹ 20 lakhs	2,00,000	
<b>Less : Audit Fees relating to P.Y. 2016-17</b> [₹ 30,000, being 30% of audit fees of ₹ 1,00,000 provided for in the books of account of P.Y. 2016-17 would have been disallowed due to non- deduction and deposit of tax at source. Since tax has been deducted in September, 2017 and paid on 6.10.2017, the amount of ₹ 30,000 is deductible while computing business income of P.Y. 2017-18	30,000	
<b>Less : Contribution to University</b> [Contribution to a University approved and notified under section 35(1) (ii) would qualify for weighted deduction @150%. Since ₹ 1,50,000 has already been debited to the statement of profit and loss, the balance ₹ 75,000 has to be deducted while computing business income]	75,000	8,80,000
<b>Less</b> :Items credited to the statement of profit and loss, but not includible in business income.		
<b>(I)</b> Rent received from vacant land (Chargeable to tax under the head "Income from other Sources")	1,20,000	
<b>(II)</b> Rent received from commercial property owned by the company (Chargeable to tax under the head "Income from house property")	2,50,000	
<b>(III)</b> Interest received on income land (Chargeable to tax under the head "Capital Gains")	1,00,000	
<b>(IV)</b> Profit on sale of unused land (Chargeable to tax under the head "Capital Gains").	10,00,000	14,70,000
<b>Profits and Gains from the business of manufacturing</b>		<b>77,50,000</b>

**Question 5 (10 marks) (2 marks for each point)**

	Particulars	Tax treatment in the hands of	
		KDS Realty Trust (REIT)	Unit Holders
1.	Rental income of ₹ 3crores of REIT from directly owned real estate assets	<p>Any income of a business trust, being a REIT, by way of renting or leasing or letting out any real estate asset owned directly by such business trust is exempt in its hands as per section 10(23FCA). Consequently, the rental income is exempt in the hands of the REIT.</p> <p>As per section 194LBA, REIT has to deduct tax@10% in case of distribution of such rental income component to a resident unit holder and at rates in force in case of distribution to a non-resident unit holder.</p>	<p>The distributed income or any part thereof, received by a unit holder from the REIT. Which is in the nature of income by way of renting or leasing or letting out any real estate asset owned directly by such REIT is deemed of the unit holder as per section 115UA(3), therefore, such income is taxable in their hands. The component of rental income received from REIT in the hands of each unit holder would be determined in the proportion of 3/11 by virtue of section 115UA (1).</p>
2.	Short-term capital gains of ₹ 1.5crore on sale of listed shares of Brahma Ltd.	<p>As per section 115UA(2), the total income of a business trust shall be chargeable to tax at the maximum marginal rate, subject to the provisions of sections 111A and 112.</p> <p>Accordingly, KDS Realty Trust is liable to tax@15% under section 111A in respect of short-term capital gains on sale of listed shares of special purpose vehicle i.e., Brahma Ltd.</p> <p>No tax is deductible at source on the short-term capital gain component of income distributed by the REIT to the unit holders.</p>	<p>Any distributed income referred to in section 115UA, to the extent it does not comprise of interest referred to in section 10(23FC) and rental income referred to in section 10(23FCA), received by unit holders is exempt in their hands under section 10(23FD). Hence, the short-term capital gain component in the hands of the unit holders.</p>
3.	Short-term capital gains of ₹ 2crore on sale of developmental properties.	<p>Further the short-term capital gains of ₹ 2crore on sale of developmental properties is taxable at maximum marginal rate: in the hands of the KDS Realty Trust as per section 115UA(2)</p> <p>No tax is deductible at source on the short-term capital gain component of the income distributed by the REIT to the unit holders.</p>	<p>There would be no tax liability on the short-term capital gain component of income distributed to unit holders by virtue of the exemption contained in section 110(23FD).</p>

4.	Interest of ` 1crore received in respect of investment in unlisted debentures of real estate companies	Interest income received in respect of investment in unlisted debentures of real estate companies is taxable at the maximum marginal rate, in the hands of the KDS Realty Trust as per section 115UA(2). No tax is deductible at source on the interest component of the income is distributed to the unit holders by the REIT.	No tax liability on interest component of income distributed to unit holders in their hands by virtue of section 10(23FD).
5.	Dividend income of ` 3.50crore from Brahma Ltd.	<p>There would be no tax liability in the hands of the business trust since dividend is subject to dividend distribution tax in the hands of Brahma Ltd; Hence, the dividend income is exempt in the hands of the business trust under section 10(34).</p> <p>No tax is deductible at source on the dividend component of the income distributed to the unit holders by the REIT. However, as per section 115BBDA the dividend of ` 3.40crores is taxable in hands of business trust @ 10%.</p>	No tax liability on the dividend component of income distributed to unit holders in their hands by virtue of section 10(23FD).

**Question 6 (4 marks) (2 marks for each point)**

Where the Authority finds, on a representation made to it by the Commissioner or otherwise, that an advance ruling pronounced by it has been obtained by the applicant by fraud or misrepresentation of facts, it may, ny order declare such ruling to be void – ab – initio.

Thereupon, all the provisions of the Act shall apply (after excluding the period beginning with the date of such advance ruling and ending with the date of the order declaring the advance ruling as void) to the applicant as of such advance ruling has never been made.

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