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SUGGESTED SOLUTION

FINAL MAY 2019 EXAM

SUBJECT- DT

Test Code – FNJ 7139

BRANCH - () (Date :)

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Answer 1: **(1 mark x 30 =30 marks)**

1) A
2) B
3) A
4) A
5) B
6) A
7) D
8) B
9) A
10) B
11) D
12) C
13) .
14) .
15) A
16) D
17) C
18) C
19) C
20) C
21) C
22) A
23) A
24) A
25) C
26) D
27) D
28) D
29) C
30) A

Answer 2:
(A)

Particulars	Amount (Rs.)
Sale Consideration	2,50,000
Less: Transfer Expenses	10,000
Net Consideration	2,40,000
Less: Cost of Acquisition	70,000
Long-term capital gain	1,70,000
Less: Exemption u/s 115F	1,06,250*
Taxable long-term capital gain	**63,750**

$$* \frac{1,70,000 \times 1,50,000}{2,40,000} = \text{Rs. } 1,06,250$$ **(5 marks)**

(B)

(i) Yes. Since his total turnover for the F.Y.2018-19 is below Rs. 200 lakhs, he is eligible to opt for presumptive taxation scheme under section 44AD in respect of his retail trade business.

(1 mark)

(ii) His income from retail trade, applying the presumptive tax provisions under section 44AD, would be Rs. 15,88,000, being 8% of Rs. 1,98,50,000. **(1 mark)**

(iii) Mr. Praveen had declared profit for the previous year 2017-18 in accordance with the presumptive provisions and if he does not opt for presumptive provisions for any of the five consecutive assessment years i.e., A.Y. 2019-20 to A.Y. 2023-24, he would not be eligible to claim the benefit of presumptive taxation for five assessment years i.e., A.Y. 2020-21 to A.Y. 2024-25 subsequent to the assessment year relevant to the previous year in which the profit has not been declared in accordance the presumptive provisions. **(2 marks)**

(iv) In case he opts for the presumptive taxation scheme under section 44AD, the due date would be 31st July, 2019.

In case he does not opt for presumptive taxation scheme, he is required to get his books of account audited, in which case the due date for filing of return of income would be 30th September, 2019.

(1 mark)

Answer 3:

(A)

Computation of Total Income of Parik Hospitality Ltd. for the A.Y.2019-20

Particulars	Amount (Rs.)	
Profit as per Statement of profit and loss		1,52,00,000
Add: **Items debited but to be considered separately or to be disallowed**		
(a) Payment to middleman for purchase of crab etc. in an amount exceeding Rs. 10,000 [Under section 40A(3), disallowance is attracted in respect of expenditure for which cash payment exceeding Rs. 10,000 is made on a day to a person.Payment of Rs. 25,000 to fishermen for purchase of crab etc. is covered by exception under Rule 6DD. However, payment of Rs. 30,000 to middlemen for purchase of crab etc. is not covered under the exception - *CBDT Circular 10/2008 dated 5/12/2008*].	30,000	
(b) Contribution towards employees' pension scheme in excess of 10% of salary disallowed under section 40A(9) [Contribution to the extent of 10% of salary (basic salary + dearness allowance, if it forms part of pay for retirement benefits) is allowable as deduction under section 36(1)(iva). In this case, it is presumed that dearness allowance forms part of pay for retirement benefits]	50,000	
(c) Payment to transport contractor without deduction of tax at source [Since the contractor opts for presumptive taxation under section 44AE and furnished a declaration to this effect, tax is not required to be deducted at source under section 194C in respect of payment to transport contractor].	-	
(f) Expenses on foreign travel of two directors for a collaboration agreement which failed to materialize	10,00,000	

[Where expenditure is incurred for a project not related the existing business and the project was abandoned without creating a new asset, the expenses are capital in nature as per *Mc Gaw-Ravindra Laboratories (India) Ltd. v. CIT (1994) 210 ITR 1002 (Guj.).* Brewery project is not related to the existing business of running three star hotels]		
(g) Fees paid to directors without deducting tax at source [30% of Rs. 1 lakh]	30,000	
[Disallowance@30% would be attracted under section 40(a)(ia) for non-deduction of tax at source from director's remuneration on which tax is deductible under section 194J]		1,10,000
		1,63,10,000
***Less:* Items credited but to be considered separately/ Expenditure to be allowed**		
(d) Profit on sale of plot of land to 100% subsidiary	12,00,000	
[Short-term capital gains arise on sale of plot of land held for less than 24 months. However, in this case, since the transfer is to a 100% subsidiary company and the subsidiary company is an Indian company, the same would not constitute a transfer for levy of capital gains tax as per section 47(iv). Since this amount has been credited to the statement of profit and loss, the same has to be deducted for computing business income].		
(e) Contribution to IIT for scientific research	1,25,000	
[Contribution to IIT for scientific research programme approved by the prescribed authority qualifies for weighted deduction@150% under section 35(2AA). Since 100% of contribution has already been debited to the statement of profit and loss, the balance 50% has to be deducted while computing business income][7].		
(h) Depreciation	5,00,000	
[Depreciation allowable under the Income-tax Act, 1961 is Rs.15 lakhs whereas the depreciation as per books of account debited to the statement of profit and loss is Rs. 10 lakhs. Hence, the additional amount of Rs. 5 lakhs has to be deducted while computing business income]		
(i) Additional compensation received from State Government	10,00,000	
[Since the additional compensation has been received pursuant to an interim order of the Court, the same would be deemed as income chargeable to tax under the head "Capital Gains" in the year of final order as per section 45(5). Since the compensation has been credited to the statement of profit and loss, the same has to be deducted while computing business income]		

(j) Dividend received from foreign company	5,00,000	
[Dividend received from foreign company is taxable under the head "Income from other sources". Since the said dividend has been credited to the statement of profit and loss, the same has to be deducted while computing business income]		
(i) Interest paid during the year	2,00,000	
[Conversion of unpaid interest into loan shall not be construed as payment of interest for the purpose section 43B. The amount of unpaid interest converted into a new loan will be allowable as deduction only in the year in which such converted loan is actually paid. Since Rs. 2 lakhs has been paid in the P.Y.2018-19, the same is allowable as deduction]		
(iii) Purchases omitted to be recorded in the books	2,00,000	
[Since the purchase is made in March, 2019 (i.e., P.Y.2018-19), in respect of which bill of Rs. 2 lakhs received on 31.3.2019 has been omitted to be recorded in the books in that year, it has to be deducted to compute the business income *[Kedarnath Jute Manufacturing Company Ltd. v. CIT (1971) 82 ITR 363 (SC)]*. It is logical to assume that the company is following mercantile system of accounting.].		37,25,000
Income under the head "Profits and Gains of Business or Profession"		**1,25,85,000**
Income from Other Sources		
Dividend received from foreign company		
[Dividend received from a foreign company is chargeable to tax under the head "Ïncome from other sources".]		5,00,000
Gross Total Income		**1,30,85,000**
Less: Deduction under Chapter VI-A		Nil
Total Income		**1,30,85,000**

(14 marks)

(B)

The income of a person who is trying to alienate his assets with a view to avoid tax will be dealt with as per the provisions of section 175.

Accordingly, if it appears to the Assessing Officer during any current assessment year that any person is likely to charge, sell, transfer, dispose of or otherwise part with any of his assets with a view to avoiding payment of any liability under the Income-tax Act, 1961, the total income of such person for the period from the expiry of the previous year to the date when the Assessing Officer commences proceedings under this section is chargeable to tax in that assessment year.

The total income of each completed year or part of any previous year included in such period shall be chargeable to tax at the rates in force in that assessment year and separate assessments will be made for each completed previous year or part of any previous year.

The Assessing Officer may estimate the income of such individual for such period or any part thereof, where it cannot be readily determined in the manner provided in the Act.

The tax chargeable under this section shall be in addition to tax, if any, chargeable under any

other provision of the Act. **(6 marks)**

Answer 4:

(A)

(i) No, the transaction of demerger would not attract any income-tax liability in the hands of SS(P) or RV(P) Ltd.

As per section 47(vib), any transfer in a demerger, of a capital asset, by the demerged company to the resulting company would not be regarded as "transfer" for levy of capital gains tax if the resulting company is an Indian company.

Hence, capital gains tax liability would not be attracted in the hands of SS(P) Ltd., the demerged company, in this case, since RV(P) Ltd. is an Indian company. **(1.5 marks)**

(ii) There would be no capital gains liability in the hands of Mr. N.K. on receipt of shares of RV (P) Ltd., since as per section 47(vid), any issue of shares by the resulting company in a scheme of demerger to the shareholders of the demerged company will not be regarded as "transfer" for levy of capital gains tax, if the issue is made in consideration of demerger of the undertaking.

(1.5 marks)

(iii) Yes, capital gains would arise in the hands of Mr. N.K. on sale of shares of RV (P) Ltd.

Sale consideration	8,00,000

Less: Indexed cost of acquisition of shares of RV (P) Ltd.

Cost of acquisition of shares of RV(P) Ltd. as per section 49(2C):

$$\text{Cost of acquisition of shares of SS(P) Ltd.} \times \frac{\text{Net book value of assets transferred in a demerger}}{\text{Net worth of the demerged company immediately before demerger}}$$

$$\text{Rs.}600000 \times \frac{10 \text{ crore}}{40 \text{ crore}} = \text{Rs. } 150000$$

Indexed cost of acquisition of shares of RV (P) Ltd. [Rs. 1,50,000 × 280/109]	Rs. 3,85,321
Long-term capital gain (since period of holding of shares in demerged company is also to be considered)	Rs. **4,14,679** **(3 marks)**

(iv) No, sale of shares by Mr. N.K. would not affect the tax benefits availed by SS(P) Ltd. or RV (P) Ltd.

One of the conditions to be satisfied is that the shareholders holding not less than three- fourths in value of the shares in the demerged company become shareholders of the resulting company by virtue of the demerger. It is presumed that the condition is satisfied in this case.

There is no stipulation that they continue to remain shareholders for any period of time thereafter.

(1 mark)

(v) Since the resultant capital gain on sale of shares of RV(P) Ltd. is a long-term capital gain (on account of the period of holding of shares in demerged company being considered by virtue of section 2(42A)(g)), Mr. N.K. can avail exemption –

(1) under section 54EE, by investing the long-term capital gain units of specified fund, within a period of 6 months from the date of transfer.

(2) under section 54F by investing the entire net consideration in purchase (within one year before and two years after the date of transfer) or construction (within three years after the date of transfer) of one residential house in India. If part of the net consideration is invested, only proportionate exemption would be available. **(1 mark)**

(B)

As per section 245T, an advance ruling can be declared to be *void ab initio* by the Authority for Advance Rulings if, on a representation made to it by the Principal Commissioner or Commissioner or otherwise, it finds that the ruling has been obtained by fraud or misrepresentation of facts. Thereafter, all the provisions of the Act will apply as if no such advance ruling has been made. A copy of such order shall be sent to the applicant and the Principal Commissioner or Commissioner. **(3 marks)**

(C)

Double Taxation Avoidance Agreements (DTAAs) generally contain an Article providing that business income is taxable in the country of residence, unless the enterprise has a permanent establishment in the country of source, and such income can be attributed to the permanent establishment. **(1 mark)**

As per section 92F(iiia), the term "Permanent Establishment" includes a fixed place of business through which the business of an enterprise is wholly or partly carried on. **(1 mark)**

As per this definition, to constitute a permanent establishment, there must be a place of business which is fixed and the business of the enterprise must be carried out wholly or partly through this place.

Section 9(1)(i) requires existence of business connection for deeming business income to accrue or arise in India. DTAAs however provide that business income is taxable only if there is a permanent establishment in India.

Therefore, in cases covered by DTAAs, where there is no permanent establishment in India, business income cannot be brought to tax due to existence of business connection as per section 9(1)(i).

However, in cases not covered by DTAAs, business income attributable to business connection is taxable. **(3 marks)**

(D)

(i) Yes, there has been a delay on the part of Mr. Rs. in filing the statement of TDS.

As per section 200(3) read with Rule 31A, the statement of tax deducted at source for the quarter ended 31st December, 2018 has to be filed on or before 31st January, 2019. However, the same has been filed only on 23rd March, 2019. Hence, there has been a 51 day delay on the part of Mr. Rs. in filing the statement of TDS. **(2 marks)**

(ii) As per section 234E of the Income-tax Act, 1961, where a person fails to file deliver or cause to be delivered the statement of tax deducted at source within the prescribed time, then, he shall be liable to pay, by way of fee, a sum of Rs. 200 for every day during which the failure continues.

The amount of fee shall not, however, exceed the amount of tax deductible.

In this case, since Mr. Madhusudhan has delayed filing the statement of TDS by 51 days, he would be liable to pay a fee of Rs. 10,200 (Rs. 200 x 51 days) under section 234E. The said fee does not exceed the tax deductible (Rs. 80,000, in this case). **(2 marks)**

Answer 5:

(A)

Since XYZ Inc. is located in a NJA, the transaction of provision of technical services by the Indian company, A Ltd., would be deemed to be an international transaction and XYZ Inc. and A Ltd. would be deemed to be associated enterprises. Therefore, the provisions of transfer pricing would be attracted in this case.

The price of Rs. 42 lakhs charged for similar services from PQR Inc, being an independent entity located in a non-NJA country, can be taken into consideration for determining the arm's length price (ALP) under Comparable Uncontrolled Price (CUP) Method.

Since the ALP is more than the transfer price, the ALP of Rs. 42 lakhs would be considered as the income arising from the international transaction between A Ltd. and XYZ Inc.

It may be noted that the benefit of permissible variation between the ALP and transfer price is not available in respect of a transaction entered into with an entity in NJA. **(5 marks)**

(B)

Section 254(2A) provides that the Appellate Tribunal, where it is possible, may hear and decide an appeal within a period of four years from the end of the financial year in which such appeal is filed. **(1 mark)**

The Appellate Tribunal may, on merit, pass an order of stay in any proceedings relating to an appeal. However, such period of stay cannot exceed 180 days from the date of such order. The Appellate Tribunal has to dispose off the appeal within this period of stay. **(1 mark)**

Where the appeal has not been disposed off within this period and the delay in disposing the appeal is not attributable to the assessee, the Appellate Tribunal can further extend the period of stay originally allowed. However, the aggregate of period originally allowed and the period so extended should not exceed 365 days even if the delay in disposing of the appeal is not attributable to the assessee. The Appellate Tribunal is required to dispose off the appeal within this extended period. If the appeal is not disposed of within such period or periods, the order of stay shall stand vacated after the expiry of such period or periods.

Therefore, the statement given in the question is not correct. **(3 marks)**

(C)

The core reasons for difference between e-commerce transactions and traditional business transactions causing difficulty to tax the income from e-commerce transactions under the Income- tax Act, 1961 are absence of national boundaries, no requirement of physical presence of goods and no requirement of physical delivery (in certain cases). Since e-commerce transactions are completed in cyberspace, it is often not clear as to the place where the transaction is effected, thereby causing difficulty in implementing source rule taxation. **(4 marks)**

(D)

The total income of a political party registered with the Election Commission is to be computed as per section 13A under which the income derived from house property, income from other sources and income by way of voluntary contributions received from any person, on fulfilling of the conditions as mentioned thereunder are exempt from tax. In this case assuming that the National Political Party fulfils all the conditions mentioned thereunder, the income is computed as under: **(2 marks)**

Computation of total income of National Political Party

	Particulars	**Rs.**
(a)	The rent of the property of Rs. 6 lacs located at Chennai	Nil

(b)	The interest received on deposits of Rs. 5 lacs	Nil
(c)	Cash contributions given by 100 persons of Rs. 3,000 each by secreting their identities (not allowable, since cash contribution in excess of Rs. 2,000 not permissible)	3,00,000
(d)	The contribution of Rs. 1,100 each given by its members being recorded in the books	Nil
(e)	Net profit of cafeteria at Delhi	3,00,000
	Total Income	**6,00,000**

Note: It is presumed that the conditions regarding maintenance of books of account, audit, submission of report under section 29C of the Representation of the People Act, 1951 and filing of return of income under section 139(4B) are fulfilled by the political party. **(4 marks)**

Answer 6:

(A)

ABC Ltd. is deemed to have under-reported its income since:

(1) the assessment under 143(3) has the effect of reducing the loss determined in a return processed under section 143(1)(a); and

(2) the reassessment under section 147 has the effect of converting the loss assessed under section 143(3) into income.

Therefore, penalty is leviable under section 270A for under-reporting of income. **(1 mark)**

Computation of penalty leviable under section 270A

Particulars	Rs.	Rs.
Assessment under section 143(3) Under-reported income:		
Loss assessed u/s 143(3)	(5,00,000)	
(-) Loss determined under section 143(1)(a)	(8,00,000)	
	3,00,000	
Tax payable on under-reported income@30%	90,000	
Add: HEC@4%	3,600	
	93,600	
Penalty leviable@50% of tax payable		46,800
Reassessment under section 147 Under-reported income:		
Total income reassessed under section 147	4,00,000	
(-) Loss assessed under section 143(3)	(5,00,000)	
	9,00,000	
Tax payable on under-reported income@30%	2,70,000	
Add: HEC@4%	10,800	
	2,80,800	
Penalty leviable@50% of tax payable		1,40,400

Notes – The following assumptions have been made -

(1) None of the additions or disallowances made in assessment or reassessment qualifies under section 270A(6); and

(2) The under-reported income is not on account of misreporting. **(5 marks)**

(B)

Raj Dadarkar and Associates v. Assistant Commissioner of Income Tax [2017] 394 ITR 592 (SC)

(1 mark)

Supreme Court's Observations: The Supreme Court held that wherever there is an income from leasing out of premises, it is to be treated as income from house property. However, it can be treated as business income if letting out of the premises itself is the business of the assessee. The question has to be decided based on the facts of each case as was held in *Sultan Brothers Pvt Ltd. v. CIT [1964] 51 ITR 353 (SC)*.

In the given facts, it was an undisputed fact that the assessee would be considered to be a deemed owner under section 27(iiib) read with section 269UA(f) as it had a leasehold right for more than 12 years. The only evidence adduced for proving that letting out and earning rents is the main business activity of the appellant was the object clause of the partnership deed. The clause provided that "*The Partnership shall take the premises on rent to sub-let or do any other business as may be mutually agreed by the parties from time to time*." The Supreme Court held the clause to be inconclusive and observed that the assessee had failed to produce sufficient material to show that its entire or substantial income was from letting out of the property. **(2 marks)**

Supreme Court's Decision: The Supreme Court, accordingly, held that, in this case, the income is to be assessed as "Income from house property" and not as business income, on account of lack of sufficient material to prove that the substantial income of the assessee was from letting out of the property. **(1 mark)**

(C)

Deputy Commissioner of Income Tax v Raghuvir Synthetics Ltd. [2017] 394 ITR 1 (SC) **(1 mark)**

Appellate Authorities' Views: The first appellate authority allowed the assessee's appeal by holding that the concept of "prima facie adjustment" under section 143(1)(a) cannot be invoked as there could be more than one opinion on whether public issue expenses were covered by section 35D or 37. The Tribunal as well as the Division Bench of the High Court dismissed the appeal of the Revenue on the ground that the issue was debatable and hence, the expenditure cannot be disallowed while processing return of income under section 143(1)(a).

Supreme Court's Observations: The Supreme Court noted that there was divergence of opinion amongst the various High Courts on the nature of the expenses incurred on raising share capital. While the High Courts of Madras, Andhra Pradesh and Karnataka had held the preliminary expenses to be revenue in nature, High Courts of Allahabad, Himachal Pradesh, Delhi, Calcutta, Bombay, Punjab and Haryana, Gujarat and Rajasthan had held the expenses to be capital in nature. **(3 marks)**

Supreme Court's Decision: The Supreme Court held that, in the case of the assessee, the issue was not debatable. Since the registered office of the assessee is in Gujarat, the law laid down by the Gujarat High Court is binding on the assessee. **(1 mark)**

(D)

The powers under section 131(1A) deal with power of discovery and production of evidence. They do not confer the power of seizure of cash or any asset. The Director General, for the purposes of making an enquiry or investigation relating to any income concealed or likely to be concealed by any person or class of persons within his jurisdiction, shall be competent to exercise powers conferred under section 131(1), which confine to discovery and inspection, enforcing attendance, compelling the production of books of account and other documents and issuing commissions. Thus, the power of seizure of unaccounted cash is not one of the powers conferred on the Director General under section 131(1A). **(2 marks)**

However, under section 132(1), the Director General has the power to authorize any Additional Director or Additional Commissioner or Joint Director or Joint Commissioner etc. to seize money found as a result of search [Clause (iii) of section 132(1)], if he has reason to believe that any person is in possession of any money which represents wholly or partly income which has not been disclosed [Clause (c) of section 132(1)]. Therefore, the proper course open to the Director General is to exercise his power under section 132(1) and authorize the Officers concerned to enter the premises where the cash is kept by Mr. Mogambo and seize such unaccounted cash. **(3 marks)**