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SUGGESTED SOLUTION

FINAL MAY 2019 EXAM

SUBJECT- DT

Test Code – FNJ 7101

BRANCH - () (Date :)

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Answer 1:**(A)**

Computation of tax of AOPs is governed by section 167B of the Income-tax Act, 1961. Tax on total income of AOP is computed as follows:

- (i) If individual share of a member is known, and the total income of any member, excluding his share from such AOPs, exceeds the basic exemption limit, then the AOPs will pay tax at the maximum marginal rate.
- (ii) If individual share of a member is known and no member has total income (excluding his share from AOPs) exceeding the basic exemption limit, then the AOP will pay tax at the rates applicable to an individual.

Section 86 provides for assessment of share in the hands of members of AOPs as follows:

A member's share in the total income of AOPs will be treated as follows:-

- (i) If an AOPs has paid tax at the maximum marginal rate or a higher rate, the member's share in the total income of AOPs will not be included in his total income and will be exempt.
- (ii) If the AOPs has paid tax at regular rates applicable to an individual, the member's share in the income of AOPs will be included in his total income and he will be allowed rebate at the average rate of tax in respect of such share. **(2 marks)**

Tax Liability of J K Associates, AOPs

- (i) As K's income, other than that from the AOPs, exceeds the basic exemption limit, the AOPs shall pay tax at maximum marginal rate of 35.88 % (i.e. 30% plus 15% surcharge plus health and education cess@4%). Thus, the tax payable by AOP = Rs. 6,00,000 x 35.88 % = Rs. 2,15,280. **(1 mark)**
- (ii) Since none of the members have income, other than income from the AOPs, exceeding the basic exemption limit, the AOPs would be taxed at the rates applicable to an individual. Therefore, the AOP's tax liability = Rs. 32,500 + Rs. 1,300 = Rs. 33,800.

Tax Liability of J and K

	Particulars	J Rs.	K Rs.
(i)	Share of profit from AOP	Exempt	Exempt
	Income from other sources	1,00,000	2,70,000
	Total Income	1,00,000	2,70,000
	Tax liability	NIL	1,000
	Less: Rebate under section 87A	-	1,000
	Total tax payable	NIL	NIL
(ii)	Share of profit from AOP	3,60,000	2,40,000
	Income from other sources	1,00,000	1,20,000
	(A)	4,60,000	3,60,000
	Tax liability	10,500	5,500
	Add: Health and Education cess@4%	420	220
	Total tax payable	10,920	5,720
	(B)	10,920	5,720
	Average rate of tax [B/A x 100]	2.374%	1.589%
	Total tax liability	10,920	5,720

Less: Rebate under section 86 read with section 110 in respect of share of profit from AOP (share in AOP x Average rate of tax)	8,546	3,814
Tax liability of members	2,374	1,906
Tax Payable (Rounded off)	2,370	1,900

(3 marks)

(B)

The **Apex Court, in CIT vs. Om Prakash Mittal** (2005) 273 ITR 326, observed that a plain reading of section 245D(6) shows that every order passed under sub-section (4) has to provide for:-

- (i) the terms of settlement; and
- (ii) that the settlement would become **void**, if it is **subsequently found** by the Settlement Commission that it has been **obtained by fraud or misrepresentation of facts.** (1 mark)

The decision that the order has been obtained by fraud or misrepresentation is that of the Settlement Commission. However, there is no requirement that the action be initiated by the Settlement Commission, **suo moto**. The Revenue can move the Settlement Commission for decision on an issue **if it has material to show** that the order was obtained by fraud or misrepresentation of facts. (1 mark)

The Supreme Court observed that the foundation for settlement is an application which an assessee can file at any stage of a case relating to him in such form and manner as may be prescribed. **The fundamental requirement of the application under section 245C is that there must be full and true disclosure of the income along with the manner in which it has been derived.** If an order is obtained by fraud or misrepresentation of facts, it cannot be said that there is a full and true disclosure and therefore, the Legislature has prescribed the condition relating to declaration of the order void when it is obtained by fraud or misrepresentation of facts. (1 mark)

The Supreme Court held that merely because section 245-I provides that the order of settlement is conclusive, **it does not take away the power of the Settlement Commission to decide whether the settlement order has been obtained by fraud or misrepresentation of facts.** If the Commissioner is able to establish that the earlier decision was void because of misrepresentation of facts, then it is open for the Settlement Commission to decide the issue. **It cannot be called by any stretch of imagination to be a review of the earlier judgment or the subsequent Bench sitting in appeal over the earlier Bench's decision.** (1 mark)

Therefore, Mr. Sunder's contention is, therefore, not correct.

Answer 2:

Determination of net worth of Unit B of M/s. J.B. Opticals Ltd.

	Rs. (in lacs)
Written down value of fixed assets	120
Debtors	75
Stock-in-trade	25
	220
Less : Liabilities	50
Net worth	170

(3 marks)

Comparative calculation of chargeable capital gains

	Sale before 31.3.2019	Sale after 31.03.2019
Sale consideration	2,25,00,000	2,25,00,000
Less: Discount	2,25,000	Nil
Net sale consideration	2,22,75,000	2,25,00,000
Less: Net worth	1,70,00,000	1,70,00,000
Short term capital gain	52,75,000	N.A.
Long term capital gain	N.A.	55,00,000
Tax rate	31.2%	20.8%
Tax thereon	16,45,800	11,44,000

(3 marks)

Computation of Net Cash flow

	Sale before 31.3.2019	Sale after 31.03.2019
Net sale consideration	2,22,75,000	2,25,00,000
Less: Income-tax	16,45,800	11,44,000
Net Cash flow	2,06,29,200	2,13,56,000

(2 marks)

Note: The assessee is advised to effect slump sale after 31.03.2019 as the tax liability arising out of long term capital gains is less than the tax liability arising on short term capital gains and the net cash flow is also higher, if Unit B is transferred after 31.03.2019.

(2 marks)

Answer 3:

(A)

- (a) The authorised officer being DDI, Delhi is not having any jurisdiction over Shri Krishna Ltd., Mumbai, and therefore as per section 132(9A), **the papers seized relating to this company shall be handed over by him to the Assessing Officer having jurisdiction over Shri Krishna Ltd., Mumbai within a period of 60 days** from the date on which the last of the authorisations for search was executed for taking further necessary action thereon.
- (b) The contention raised by the Director will not be acceptable because as per the provisions of sub-section (4A)(i) of section 132, where any books of account, other documents, money, bullion, jewellery or other valuables are found in the possession or control of any person in the course of search, then, in respect thereof, **it may be presumed that the same belongs to that person.**
- (c) As per section 132(4A), the presumptions in respect of the papers, indicating transactions not recorded in the books but having direct nexus with the business of the company, are that the same belong to the company, contents of such papers are true and the handwriting in which the same are written is/are of the persons(s) whose premises have been searched.

(2 marks x 3 = 6 marks)

(B)

The Supreme Court in **Rajesh Kumar & Ors. v. DCIT** (2006) 287 ITR 91 observed that the order under section 142(2A) is a quasi judicial order. Therefore, the **principles of natural justice have to be applied** and the assessee has to be given an **opportunity of being heard before directing the special audit.** The principles of natural justice are based on two principles, namely, (i)

nobody shall be condemned unheard; (ii) nobody shall be a judge of his own cause. Once it is held that the assessee suffers civil consequences and any order passed would be prejudicial to him, the principles of natural justice must be held to be implicit. If the principles of natural justice were to be excluded, the Parliament could have said so expressly.

Accordingly, to give effect to the observation of the Supreme Court, it has been provided that the Assessing Officer is required to give the assessee an opportunity of being heard before issuing directions for special audit under section 142(2A).

Therefore, on the basis of above discussion we can conclude that The contention of Mr. Abhishek is tenable under law. (4 marks)

Answer 4:

(A)

CIT v. Govindbhai Mamaiya (2014) 367 ITR 498 (SC)

Supreme Court's Observations: The Supreme Court referred to its earlier decision in the case of Meera & Co v. CIT (1997) 224 ITR 635 in which the earlier precedent in the case of CIT v. Indira Balakrishna (1960) 39 ITR 546 (SC) was followed. The Apex Court noted that **“Association of Persons” means an association in which two or more persons join in a common purpose or common action.**

The Supreme Court also referred to its judgment in G. Murugesan & Bros. v. CIT (1973) 4 SCC 211. In that case, it was held that **an association of persons could be formed only when two or more persons voluntarily combined together for certain purposes.**

In this case, the property in question came to the assessee's possession through inheritance i.e., by operation of law. It is not a case where any ‘association of persons’ was formed by volition of the parties. Further, even the income earned in the form of interest is not because of any business venture of the three assessee's, but is the result of the act of the Government in compulsorily acquiring the said land. Thus, the **basic test to be satisfied for making an assessment in the status of AOP is absent in this case.**

Apex Court's Decision: The Apex Court, accordingly, held that the income from asset inherited by the legal heirs is taxable in their individual hands and not in the status of AOP. (5 marks)

(B)

Hemant Kumar Sindhi & Another v. CIT (2014) 364 ITR 555 (All)

High Court's Observations: The High Court observed that section 132B(1)(i) uses the expression “the amount of any existing liability” and “the amount of the liability determined”. The words **“existing liability” postulates a liability that is crystallized by adjudication**; Likewise, “a liability is determined” **only on completion of the assessment.** Until the assessment is complete, it cannot be postulated that a liability has been crystallized. (2 marks)

As per the first proviso to section 132B(1)(i), the assessee may make an application to the Assessing Officer for release of the assets seized. However, he has to explain the nature and source of acquisition of the asset to the satisfaction of the Assessing Officer. It is not the ipse dixit of the assessee but the satisfaction of the Assessing Officer on the basis of the explanation tendered by the assessee which is material. (1 mark)

High Court's Decision: The High Court, accordingly, held that the Assessing Officer was justified in his conclusion that **it is only when the liability is determined on the completion of assessment** that it

would stand crystallized and in pursuance of which a demand can be raised and recovery can be initiated. Therefore, in the present case, the first proviso to section 132B(1)(i) would not be attracted. The High Court, thus, dismissed the writ petition. **(2 marks)**

Answer 5:

As per section 80AC, while computing the total income of an assessee of a previous year (P.Y.2018-19, in this case) relevant to any assessment year (A.Y.2019-20, in this case), any deduction is admissible, inter alia, under section 80-IA, such deduction shall not be allowed unless it furnishes a return of income for such assessment year on or before the 'due date' specified in section 139(1).

Since the turnover of the partnership firm has exceeded Rs. 200 lacs in the previous year 2018-19, it would be subject to audit under section 44AB, in which case the 'due date' of filing its return of income for A.Y.2019-20 would be 30th September, 2019 as per section 139(1).

(2 marks)

Computation of total income and tax liability of M/s. Victory Polyfibres for A.Y.2019-20

I. Where the firm files its return of income on 30th September 2019:

(1 mark)

Particulars	Rs. in lacs
Gross Total Income	300.00
Less: Deduction under section 80-IA	200.00
Total Income	100.00
Tax liability@ 30%	30.00
Add: Health and Education cess@4%	1.20
Regular income-tax payable	31.20

Computation of Alternate Minimum Tax payable [Section 115JC]

Particulars	Rs. in lacs
Total Income	100.00
Add: Deduction under section 80-IA	200.00
Adjusted Total Income	300.00
Alternate Minimum Tax (AMT) @ 18.5% on Rs. 300 lacs	55.50
Add: Surcharge@12% (Since adjusted total income >Rs. 1 crore)	6.66
	62.16
Add: Health and Education cess@4%	2.49
Total tax payable (AMT)	64.65

Since the regular income-tax payable by the firm is less than the alternate minimum tax payable, the adjusted total income shall be deemed to be the total income of the firm for P.Y.2018-19 and it shall be liable to pay income-tax on such total income@18.5% [Section 115JC(1)]. Therefore, the tax payable for the A.Y.2019-20 would be Rs. 64.65 lacs.

Tax credit for Alternate Minimum Tax [Section 115JD]

	Rs. in lacs
Total tax payable for A.Y.2019-20 (Alternate Minimum Tax)	64.65
Less: Regular income-tax payable	31.20
To be carried forward for set-off against regular income-tax payable (upto a maximum of fifteen assessment years).	33.45

(2 marks)

II. Where the firm files its return of income on 7th December 2019:

Where the firm files its return on **7-12-2019**, it would be a **belated return** under section 139(4). Consequently, as per section 80AC, **deduction under section 80-IA would not be available**. In such circumstances, the gross total income of Rs. 300 lacs would be the total income of the firm.

Particulars	Rs. in lacs
Income-tax@30% of Rs. 300 lacs	90.000
Add: Surcharge@12% (since total income exceeds Rs. 100 lacs)	0.800
Income-tax (plus surcharge)	100.800
Add: Health and Education cess@4%	4.032
Total tax liability	104.832

(2 marks)

Practical solution regarding obtaining clarifications

The practical solution regarding obtaining clarifications would be to file the return of income under section 139(1) on or before the 'due date', i.e., 30.9.2019, and claim deduction under section 80-IA. In such a case, the firm can claim deduction of Rs. 200 lacs under section 80-IA. Thereafter, consequent to the clarifications obtained, if any change is required, it can file a revised return under section 139(5) within 31.3.2020 (i.e., within the end of A.Y.2019-20) which would replace the original return filed under section 139(1).

If the firm files the return of income under section 139(1) on or before 30.9.2019, its tax liability would stand reduced to Rs. 64.65 lacs, as against Rs. 104.832 lacs to be paid if return is furnished after due date. Further, it would also be eligible for tax credit for alternate minimum tax under section 115JD to the extent of Rs. 33.45 lacs. Therefore, the firm is advised to file its return of income on or before 30.9.2019.

(3 marks)