



J.K. SHAH[®]
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SUGGESTED SOLUTION
CA FINAL MAY 2017 EXAM
DIRECT TAX LAWS
Test Code - F M J 4 0 1 3

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Answer-1 (a) :

Computation of total income of XYZ Private Ltd. for the A.Y. 2017-18

Particulars	Rs.	Rs.
Income from House Property (Note 1)		
Gross Annual Value (GAV) (Rental income has been taken as GAV in the absence of other information)	6,00,000	
Less: Municipal Taxes (not deductible since it has not been paid)	<u>Nil</u>	
Net Annual Value (NAV)	6,00,000	
Less: Deduction under section 24 (30% of NAV)	<u>1,80,000</u>	4,20,000
Profits and gains of business or profession		
Net profit as per profit and loss account	1,50,00,000	
Add: Licence fee for obtaining franchise (Note 2)	20,00,000	
Municipal taxes in respect of let-out part of office premises (Note 1)	15,000	
Contribution to approved and notified university (treated separately) (Note 4)	2,00,000	
Loss due to destruction of machinery by fire (Note 5)	3,00,000	
Amount paid to contractor without deduction of tax at source @ 30% of Rs.5 lakhs (Note 6)	1,50,000	
Short-term capital loss on sale of shares of P. Ltd. (Note 7)	20,000	
Depreciation on tangible fixed assets (Note 8)	<u>1,10,000</u>	
	1,77,95,000	
Less: Depreciation under section 32 (Note 8)		
Tangible fixed assets (Note 8)	1,75,000	
Intangible asset (Franchise)		
25% of Rs. 20,00,000 (Note 2)	<u>5,00,000</u>	6,75,000
<u>Weighted deduction under section 35(1)(ii) (Note 4)</u>		
Rs. 2,00,000 x 175% (Contribution of University)	3,50,000	
Rental income to be taxed under "Income from house property" (Note 1)	6,00,000	
Dividend credited to profit and loss account to be excluded (Note 7)	<u>10,000</u>	1,61,60,000
Capital Gains (Note 7)		
Short-term capital loss (Rs. 20 x 1000 shares)	20,000	
Less: Dividend exempt under section 10(34)	<u>10,000</u>	
Short-term capital loss to be carried forward to A.Y. 2018-19	<u>10,000</u>	
Income from Other Sources (Note 9)		
Deemed dividend under section 2(22)(e)		<u>50,000</u>
Total Income		1,62,10,000

(7.5 Marks)

Notes:

- (1) Rental income from letting out a part of the office premises is taxable under "Income from house property". Therefore, it has to be deducted while calculating business income, since the income has been credited to profit and loss account. Likewise, municipal taxes due in respect of such property, debited to profit and loss account has to be added back to compute business income
Note - There is an alternate view that rental income from letting out part of the excess premises by an assessee who is engaged in business is only exploitation of the commercial asset by an assessee who is engaged in business and hence, the same constitutes business income only. In such a case also, municipal taxes is not allowable as deduction since the same has not been paid on or before the due date of filing of return of income as required under section 43B.
- (2) Franchise is an intangible asset eligible for depreciation @ 25%. Since one-time licence fees of Rs. 20 lakh paid for obtaining franchise has been debited to profit and loss account, the same has to be added back. Depreciation @ 25% has to be provided in respect of the intangible asset since it has been used for more than 180 days during the year.
- (3) Rs. 29,000 paid to A & Co., a goods transport operator in cash is deductible while computing business income, as the limit for disallowance under section 40A(3) would be attracted in case of payment to a transport contractor only when it exceeds Rs.35,000. Since it is already debited to profit and loss account, no further adjustment is required.
- (4) Contribution to a university approved and notified under section 35(1)(ii) is eligible for a weighted deduction of 175%. Therefore, the contribution of Rs. 2,00,000 debited to profit and loss account

has been added back and Rs. 3,50,000 (being 175% of Rs. 2,00,000) has been deducted while computing business income.

- (5) Loss of Rs. 3 lakh due to destruction of machinery caused by fire is not deductible since it is capital in nature.
- (6) Payment to contractor would attract disallowance at 30% of the expenditure.
- (7) As per section 94(7), where any person buys any shares within 3 months prior to the record date and sells such shares within 3 months after such date and the dividend received on such shares is exempt, then the loss arising out of such purchase and sale of shares shall be ignored to the extent of dividend income.

	Rs.
Loss on purchase and sale of shares (Rs. 100 - Rs. 80) x 1000 shares	20,000
Less: Dividend exempt under section 10(34)	<u>10,000</u>
Short-term capital loss	10,000

Since short term capital loss can be set-off only against income under the head "Capital Gains", the short-term capital loss of Rs. 10,000 has to be carried forward to the next year. Dividend of Rs. 10,000 credited to profit and loss account has to be deducted and short-term capital loss of Rs. 20,000 debited to profit and loss account has to be added back.

- (8) Depreciation as per Income-tax Rules, 1962, is deductible while calculating business income. Therefore, Rs. 1.75 lakh depreciation on tangible fixed assets and Rs. 5 lakh on intangible assets is deducted. The amount of Rs. 1 lakh depreciation debited to profit and loss account has been added back.
- (9) As per section 2(22)(e), any payment by a company in which the public are not substantially interested by way of loan to a shareholder, who is the beneficial owner of shares holding not less than 10% of voting power, is deemed as dividend to the extent to which the company possesses accumulated profits. Accordingly, in this case, Rs. 50,000 would be deemed as dividend under section 2(22)(e).

(9 x 0.5 = 4.5 Marks)

Answer-1 (b) :

Computation of total income of Mr. Ayush for the Assessment Year 2017-18

Particulars	Rs.	Rs.
Salaries		
Gross salary received	3,00,000	
Add: Shares allotted at concessional price – fair market value less the amount recovered from the employee [Section 17(2)(vi)] (i.e. Rs. 1,00,000 minus Rs. 20,000)]	<u>80,000</u>	
	3,80,000	
Less: Conveyance allowance exempt under section 10(14) [See Note (i) below]	<u>30,000</u>	3,50,000
Capital gains [See Note (ii) below]		
Sale consideration of equity shares sold on 28.02.2017	1,80,000	
Less: Fair Market Value of shares on the date of exercise of option (i.e., 30.5.2016)	<u>1,00,000</u>	<u>80,000</u>
Gross Total Income		4,30,000
Less: Deduction under Chapter VIA		
Under section 80C [See Note (iii) below]		
For investment in notified bonds of NABARD	40,000	
Under section 80CCD [See Note (iv) below]		
For deposit in pension scheme notified by Central Government	30,000	
Under section 80D [See Note (v) below]		
For payment of health insurance premium by credit card	9,000	
Under section 80E [See Note (vi) below]		
For payment of interest on loan taken from bank for higher studies of daughter	<u>60,000</u>	<u>1,39,000</u>
Total Income		2,91,000

(5 Marks)

Notes:

- (i) Conveyance allowance received for official duties is fully exempt under section 10(14).

- (ii) The value of any specified security or sweat equity shares allotted or transferred by the employer, free of cost or at a concessional rate to the employee would be treated as a perquisite in the hands of the employee. The value would be the fair market value of the specified security or sweat equity shares on the date on which the option is exercised by the employee as reduced by the amount actually paid by, or recovered from the employee in respect of such security or shares. Consequently, section 49(2AA) provides that for the purpose of computing capital gains in the hands of the employee at the time of sale of such securities/shares by the employee, the cost of acquisition shall be the fair market value which has been taken into account for the purpose of computing the perquisite value in the hands of the employee.
- (iii) Subscription to notified bonds issued by NABARD will qualify for deduction under section 80C(2)(xxii).
- (iv) Section 80CCD provides for deduction of both employee's and employer's contribution to pension scheme notified by the Central Government. This deduction has been extended also to individuals employed by any other employer. However, if the amount contributed exceeds 10% of salary, then, the deduction under section 80CCD(1) would be restricted to 10% of salary. [As per *Explanation* to section 80CCD, 'salary' for this purpose would include dearness allowance if the terms of employment so provide, but excludes all other allowances and perquisites]. Therefore, "salary" for the purpose of section 80CCD would be Rs. 2,70,000 (Rs. 3,00,000 – Rs. 30,000). Deduction under section 80CCD(1) would be restricted to Rs. 27,000, being 10% of Rs. 2,70,000. The balance Rs. 3,000 can be claimed as deduction under section 80CCD(1B). In the alternative, the entire Rs. 30,000 can be claimed as deduction under section 80CCD(1B), since the maximum limit thereunder is Rs.50,000.
- (v) For claiming deduction under section 80D, the payment of medical insurance premium has to be made by any mode other than cash. Hence, payment of Rs. 8,500 made in cash will not qualify for deduction under section 80D.
- (vi) The deduction under section 80E available to an individual in respect of interest on loan taken for his higher education has been extended to include interest on such loan taken for higher education of his relative i.e. his or her spouse and children. Hence, interest on loan taken by Mr. Ayush from bank for the higher studies of his daughter is eligible for deduction under section 80E.

(6 x 0.5 = 3 Marks)

Answer-2 :

In the case of a company, it has been provided that where tax on 18.50% of book profit exceeds tax on total income computed as per normal provisions, the book profit shall be deemed to be the total income for tax purposes.

It is therefore necessary to compute total income as per Income-tax Act, 1961 as well as book profits.

(1 Mark)

I. Computation of Total income as per the Income-tax Act, 1961

Particulars		Rs. (in Lacs)
Net profit as per profit and loss account		215
<i>Add:</i> Depreciation debited to profit and loss account	100	
Provision for losses of subsidiary company	<u>60</u>	<u>160</u>
		375
<i>Less:</i> Dividend income – exempt under section 10(34)	20	
Excess realized on sale of land (considered separately)	30	
Depreciation allowable as per Income-tax Rules, 1962	<u>150</u>	<u>200</u>
Business Income		175
<i>Less:</i> Set-off of brought forward business loss		<u>50</u>
		125
Capital gains		<u>40</u>
		165
<i>Less:</i> Set-off of unabsorbed depreciation		<u>60</u>
Total Income as per Income-tax Act, 1961		105

(3 Marks)

II. Computation of book profit under section 115JB

Particulars	(Rs. in Lacs)
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Net profit as per profit and loss account		215
Add: Provision for loss of subsidiary		60
Depreciation		<u>100</u>
		375
Less: Dividend income exempt under section 10(34)	20	
Depreciation	100	
Business loss which is less than unabsorbed depreciation	<u>50</u>	<u>170</u>
" Book Profit"		205

(3 Marks)

I. Computation of Tax liability under the normal provisions of the Income-tax Act, 1961

Total income as per the Income-tax Act, 1961 is Rs. 105 Lacs,

Particulars	Rs.
Tax payable Rs. 105 Lacs x 30%	31,50,000
Add: Surcharge @ 7%	<u>2,20,500</u>
	33,70,500
Add: Education cess & SHEC@ 3%	<u>1,01,115</u>
Total Tax payable	34,71,615

(3 Marks)

II. Computation of Minimum Alternate Tax

Particulars	Rs.
Tax @18.50% of book profit of Rs. 205 lacs	37,92,500
Add: Surcharge @ 7%	<u>2,65,475</u>
	40,57,975
Add: Education cess & SHEC@ 3%	<u>1,21,739</u>
Minimum Alternate Tax payable	<u>41,79,714</u>
Round off	41,79,710

(3 Marks)

Since 18.50% of book profit exceeds the tax payable as per the Income-tax Act, 1961 the book profit of Rs. 205 lacs would be deemed to be the total income and the tax payable on such total income shall be 18.5% thereof i.e. 37,92,500 plus surcharge @ 7% being Rs. 2,65,475 plus education cess and SHEC @ 3% (of tax and surcharge) being Rs. 1,21,739. Total tax liability would be Rs. 41,79,710.

Note: With regard to the company's representation, in respect of long term capital gain whether liable for book profit tax under section 115JB, it may be noted that since the excess realized on sale of land has been included in net profit computed under Schedule III of the Companies Act, 2013, it will form part of book profit [Bombay High Court judgment in *CIT v. Veekay Lal Investment Co. Pvt. Ltd. (2001) 249 ITR 597*].

(3 Marks)

Answer-3 (a) :

Computation of total income of the trust for the A.Y. 2017-18

Particulars	Rs.	Rs.
Income from properties held by trust	20,00,000	
Income from business incidental to the main objects of the trust	17,00,000	
Voluntary Contribution other than corpus donation (Note 1)	<u>6,00,000</u>	43,00,000
Less: 15% of income accumulated or set apart under section 11(1)(a)		<u>6,45,000</u>
		36,55,000
Less: Amount applied for charitable purposes		
Activities and programmes for the benefit of autistic persons	20,00,000	
Repayment of loan taken for construction of training centre (Note 2)	<u>10,00,000</u>	<u>30,00,000</u>
Taxable Income		6,55,000

Computation of tax liability of the trust for the A.Y. 2017-18

Particulars	Rs.	Rs.
Upto Rs. 2,50,000	Nil	
Rs. 2,50,000 – Rs. 5,00,000	25,000	
Rs. 5,00,000 – Rs. 6,55,000	<u>31,000</u>	56,000
Add: Education cess @ 2%		1,120
Add: Secondary and higher education cess @ 1%		<u>560</u>
Total tax liability		57,680

(6 Marks)

Notes:

- (1) Section 11(1)(d) excludes from the total income of the person, any income in the form of voluntary contributions made with a specific direction that they shall form part of the corpus of the trust or institution.
- (2) In CIT vs. Janmabhoomi Press Trust (2000) 242 ITR 703, the Karnataka High Court held that where a debt is incurred for the purpose of the trust, the repayment of the debt would amount to an application of the income for the purpose of the trust. Therefore, repayment of loan taken for construction of training centre for disabled persons is to be considered as application for charitable purpose.

(2 Marks)

Answer-3 (b) :

- (i) Section 35AD provides for investment-linked tax incentive for specified business. One such specified business is business of laying and operating a cross-country natural gas or crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of such network. The benefit will be available in a case where the business relates to laying and operating a cross country natural gas pipeline network for distribution, if such business commences its operations on or after 1st April, 2007.

Under section 35AD, 100% of the capital expenditure incurred during the previous year, wholly and exclusively for the above business would be allowed as deduction from the business income. However, expenditure incurred on acquisition of any land, goodwill or financial instrument would not be eligible for deduction.

Further, the expenditure incurred, wholly and exclusively, for the purpose of specified business prior to commencement of operation would be allowed as deduction during the previous year in which the assessee commences operation of his specified business. A condition has been inserted that such amount incurred prior to commencement should be capitalized in the books of account of the assessee on the date of commencement of its operations.

Therefore, the deduction admissible under section 35AD for A.Y.2017-18 would be:

Particulars	Rs. (in lacs)
Capital expenditure incurred during the previous year 2016-17	200
Capital expenditure incurred during the period from 1st April 2016 to 30th June, 2016 (i.e. prior to commencement of business) and capitalized in the books of account on 1st July, 2016 (Rs. 300 lacs - Rs. 50 lacs)	<u>250</u>
Total deduction under section 35AD for A.Y.2017-18	450

However, the actual deduction under section 35AD for A.Y. 2017-18 would be restricted to the profits derived from specified business for that year. The difference would be treated as loss from specified business to be carried forward as per section 73A.

(4 Marks)

- (ii) Section 73A provides that any loss computed in respect of the specified business shall be set off only against profits and gains, if any, of any other specified business. The unabsorbed loss, if any, will be carried forward for set off against profits and gains of any specified business in the following assessment year and so on. There is no time limit specified for carry forward and set-off and therefore, such loss can be carried forward indefinitely for set-off against income from specified business.

However, loss determined as per section 73A can be carried forward and set -off only if it has been determined in pursuance of a return filed under section 139(3). Section 139(3) requires filing of return of loss mandatorily within the time allowed under section 139(1) for claiming carry forward of loss under, *inter alia*, section 73A.

Answer-4 (a) :

For the previous year, Mr. X, an American National, was a resident in India. Accordingly, the income received by him by way of rent of the house property located in USA is subject to tax in India. Municipal taxes so paid in the country where the property is situated are also to be allowed as held in the case of CIT v. R. Venugopala Reddiar (1965) 58 ITR 439 by the Madras High Court.

The income chargeable to tax will be as under -

Particulars	Rs.	Rs.
Income from House Property		
House property located in New York		
Annual rental value being actual rent received of US \$ 12,500 p.m. converted into Indian Rupees @ 63	94,50,000	
Less: Municipal taxes paid (US \$ 10,000 × 63)	<u>6,30,000</u>	
Net Annual Value (NAV)	88,20,000	
Less: Deduction under section 24 @ 30% of NAV	<u>26,46,000</u>	61,74,000
Income from other sources		
Rental income from the land located at Delhi given on rent for 6 months		<u>18,000</u>
Total income		61,92,000

(4 Marks)

Note: Rent from vacant land is chargeable to tax under the head “Income from other sources”.

Answer-4 (b) :

Section 50C(1) enjoins that where the consideration received or accruing as a result of the transfer by an assessee of a capital asset, being land or building or both, is less than the value adopted or assessed or assessable by the “stamp valuation authority” for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed or assessable shall for the purposes of section 48, be deemed to be the full value of the consideration received or accruing as a result of such transfer.

(1 Mark)

In CIT v. Thiruvengadam Investments Private Limited (2010) 320 ITR 345 (Mad.), the issue under consideration was whether the provisions of section 50C are applicable where the property is held as a business asset.

(1 Mark)

The High Court pointed out that it was not in dispute that the assessee was engaged in real estate business. As the property in the hands of the assessee was treated as a business asset and not as a capital asset, there is no question of invoking the provisions of section 50C.

(1 Mark)

Section 50C pertains to determining the full value of consideration of a capital asset. However, the Assessing Officer can invoke the provisions of section 43CA, which provides that where the consideration for transfer of an asset (other than capital asset), being land or building or both, is less than the stamp duty value, the value so adopted or assessed or assessable (i.e., the stamp duty value) shall be deemed to be the full value of the consideration for the purposes of computing income under the head ‘Profits and gains of business or profession.

(1 Mark)

Therefore, the Assessing Officer can invoke the provisions of section 43CA to adopt the value of Rs. 60 lacs for computing the profit arising on sale of land.

Answer-4 (c) :

Mr. Pervez, an employee of a Pharma company, has received a car as a gift from a distributor of the company. Since there is no employer-employee relationship in this case between the distributor and Mr. Pervez, the value of gift is not a perquisite chargeable to tax under the head “Salaries”.

(2 Marks)

Section 56(2)(vii), brings within its scope the value of any property received by an individual or Hindu Undivided Family without consideration. For this purpose, “property” means immovable property being

land or building or both, shares and securities, jewellery, archaeological collections, drawings, paintings, sculptures, any work of art or bullion.

(1 Mark)

Therefore, for the purpose of attracting the provisions of section 56(2)(vii) for chargeability under the head "Income from Other Sources", an individual should be in receipt of property as defined therein. Since, car is not included in the definition of "property", the provisions of section 56(2)(vii) would not be attracted in the hands of Mr. Pervez.

(1 Mark)

Answer-4 (d) :

The accumulated business loss and unabsorbed depreciation of the demerged company shall be carried forward and set off by the resulting company under section 72A(4) in the following manner:

(i) Where such loss or unabsorbed depreciation is not directly relatable to the undertaking transferred to the resulting company, such loss shall be apportioned between the demerged company and the resulting company in the same proportion in which assets of the undertaking have been retained by the demerged company and transferred to the resulting company and shall be allowed to be carried forward and set off in the hands of the demerged company or the resulting company, as the case may be. In this case, therefore, 30% of Rs. 130 lacs and Rs. 250 lacs, shall be allowed to be carried forward and set off by the resulting company and the balance by the demerged company.

(4 Marks)

(ii) Where such loss or unabsorbed depreciation is directly relatable to the undertaking transferred to the resulting company, the entire loss or unabsorbed depreciation shall be allowed to be carried forward and set off in the hands of the resulting company. Accordingly, in such a case, the entire amount of Rs. 130 lacs and Rs. 250 lacs shall be allowed to be set off in the hands of the resulting company.

(4 Marks)

Answer-5 (a) :

Computation of capital gains and business income of Tani for A.Y. 2017-18

Particulars	Rs.
Capital Gains	
Fair market value of land on the date of conversion deemed as the full value of consideration for the purposes of section 45(2)	1,50,00,000
Less: Indexed cost of acquisition [Rs. 10,00,000 × 711/109]	<u>65,22,936</u>
	<u>84,77,064</u>
Proportionate capital gains arising during A.Y.2017-18 [Rs. 84,77,064 × ¾]	63,57,798
Less: Exemption under section 54EC	<u>50,00,000</u>
Capital gains chargeable to tax for A.Y.2017-18	<u>13,57,798</u>
Business Income	
Sale price of flats [15 × Rs. 20 lakhs]	3,00,00,000
Less: Cost of flats	
Fair market value of land on the date of conversion [Rs. 150 lacs × ¾]	1,12,50,000
Cost of construction of flats [15 × Rs. 8 lakhs]	<u>1,20,00,000</u>
Business income chargeable to tax for A.Y.2017-18	67,50,000

(5 Marks)

Notes:

- (1) The conversion of a capital asset into stock-in-trade is treated as a transfer under section 2(47). It would be treated as a transfer in the year in which the capital asset is converted into stock-in-trade.
- (2) However, as per section 45(2), the capital gains arising from the transfer by way of conversion of capital assets into stock-in-trade will be chargeable to tax only in the year in which the stock-in-trade is sold.
- (3) The indexation benefit for computing indexed cost of acquisition would, however, be available only up to the year of conversion of capital asset to stock-in-trade and not up to the year of sale of stock-in-trade.

- (4) For the purpose of computing capital gains in such cases, the fair market value of the capital asset on the date on which it was converted into stock-in-trade shall be deemed to be the full value of consideration received or accruing as a result of the transfer of the capital asset.
In this case, since only 75% of the stock-in-trade (15 flats out of 20 flats) is sold in the P.Y.2016-17, only proportionate capital gains (i.e., 75%) would be chargeable in the A.Y.2017-18.
- (5) On sale of such stock-in-trade, business income would arise. The business income chargeable to tax would be the difference between the price at which the stock-in-trade is sold and the fair market value on the date of conversion of the capital asset into stock-in-trade.
- (6) In case of conversion of capital asset into stock-in-trade and subsequent sale of stock-in trade, the period of 6 months is to be reckoned from the date of sale of stock-in-trade for the purpose of exemption under section 54EC [CBDT Circular No.791 dated 2.6.2000]. In this case, since the investment in bonds of RECL has been made within 6 months of sale of flats, the same qualifies for exemption under section 54EC.

(6 x 0.5 = 3 Marks)

Answer-5 (b) :

Computation of total income and tax liability of Miss Vivitha for the A.Y. 2017-18

Particulars		Rs.
Indian Income [Income from playing snooker tournaments in India]		19,20,000
Foreign Income [Income from playing snooker matches in country L]		<u>12,00,000</u>
Gross Total Income		31,20,000
<i>Less: Deduction under Chapter VIA</i>	Rs.	
<u>Deduction under section 80C</u>		
Life insurance premium of Rs. 1,10,000 paid during the previous year deduction, is within the overall limit of 1.5 lakh. Hence, fully allowable as deduction		1,10,000
<u>Deduction under section 80D</u>		
Medical insurance premium of Rs. 32,000 paid for her father aged 62 years. Since her father is a senior citizen, the deduction is allowable to a maximum of Rs. 30,000 (assuming that her father is also a resident in India). Further, deduction is allowable where payment is made by any mode other than cash. Here payment is made by credit card hence, eligible for deduction.		30,000
		<u>1,40,000</u>
Total Income		<u>29,80,000</u>
<u>Tax on Total Income</u>		
Income-tax		7,19,000
Add : Education cess @ 2%		14,380
Add: Secondary and higher education cess @ 1%		<u>7,190</u>
Average rate of tax in India (i.e. Rs. 7,40,570/Rs. 29,80,000 × 100)		24.8513%
Average rate of tax in foreign country (i.e. Rs. 1,80,000/Rs. 12,00,000 × 100)		15.00%
Rebate under section 91 on Rs. 12 lakh @ 15% (lower of average Indian-tax rate or average foreign tax rate)		<u>1,80,000</u>
Tax payable in India (Rs. 7,40,570 – Rs. 1,80,000)		5,60,570

(6 Marks)

Note : Miss Vivitha shall be allowed deduction under section 91, since the following conditions are fulfilled:-

- (a) She is a resident in India during the relevant previous year.
- (b) The income accrues or arises to her outside India during that previous year and such income is not deemed to accrue or arise in India during the previous year.
- (c) The income in question has been subjected to income-tax in the foreign country L in her hands and she has paid tax on such income in the foreign country L.
- (d) There is no agreement under section 90 for the relief or avoidance of double taxation between India and country L where the income has accrued or arisen.

(4 x 0.5 = 2 Marks)

Answer-6 (a) :

Under section 245U, the Authority of Advance Ruling will have all the powers vested in the Civil Court under the Code of Civil Procedure, 1908 as are referred to in section 131. Accordingly, the Authority of Advance Ruling shall have the same powers as are vested in a court under the Code of Civil Procedure, 1908, when trying a suit in respect of the following matters, namely -

- (1) discovery and inspection;
- (2) enforcing the attendance of any person, including any officer of a banking company and examining him on oath;
- (3) compelling the production of books of account and other documents; and
- (4) issuing commissions.

(4 Marks)

Answer-6 (b) :

(a) The action of the Commissioner in issuing the second notice is not justified. The term “record” has been defined in clause (b) of *Explanation* to section 263(1). According to this definition “record” shall include and shall be deemed always to have included all records relating to any proceeding under the Act available at the time of examination by the Commissioner. In other words, the information, material, report etc. which were not in existence at the time the assessment was made and came into existence afterwards can be taken into consideration by the Commissioner for the purpose of invoking his jurisdiction under section 263(1). However, at the same time, in view of the express provisions contained in clause (b) of the *Explanation* to section 263(1), such information, material, report etc. can be relied upon by the Commissioner only if the same forms part of record when the action under section 263 is taken by the Commissioner, Issuance of a notice under section 263 succeeds the examination of record by Commissioner. In the present case, the Commissioner initially issued a notice under section 263, after the examination of the record available before him. The subsequent second notice was on the basis of material collected under section 133A, which was totally unrelated and irrelevant to the issues sought to be revised in the first notice.

Accordingly, the material on the basis of which the second notice was issued could not be said to be “record” available at the time of examination as emphasised in *Explanation (b)* to section 263(1).

(4 Marks)

(b) As per Rule 46A(1) of the Income-tax Rules 1962, an appellant shall be entitled to produce before the Commissioner (Appeals), evidence, either oral or documentary, other than the evidence produced by him during the course of proceedings before the Assessing Officer, only in the following circumstances -

- (a) where the Assessing Officer has refused to admit evidence which ought to have been admitted; or
- (b) where the appellant was prevented by sufficient cause from producing the evidence which he was called upon to produce by the Assessing Officer; or
- (c) where the appellant was prevented by sufficient cause from producing before the Assessing Officer any evidence which is relevant to any ground of appeal; or
- (d) where the Assessing Officer has made the order appealed against without giving sufficient opportunity to the appellant to adduce evidence relevant to any ground of appeal.

(4 Marks)

Answer-6 (c) :

The penalty that could be levied in each case is:-

- (i) Failure to get books of accounts audited as required under section 44AB of the Income tax Act, 1961 – a sum equal to ½% of the total sales, turnover or gross receipts, as the case may be, in business, or of the gross receipts in profession, in such previous year or years, or a sum of Rs. 1,50,000, whichever is less [Section 271B].
- (ii) Failure to comply with a direction issued under section 142(2A) – a sum of Rs. 10,000 [Section 272A(1)(d)].
- (iii) Failure to furnish report from an accountant as required by section 92E - a sum of Rs. 1,00,000 [Section 271BA].

(4 Marks)

Answer-7 (a) :

Section 194B provides that the person responsible for paying to any person, any income by way of winnings from any lottery or crossword puzzle, card game or any other game of any sort and the amount of winning exceeds Rs.10,000, tax shall be deducted at source @ 30%.

However, in case where the winning is wholly in kind, the person responsible for paying the prize shall before releasing the winning, ensure that the **tax has been paid in respect of such winning.**

(1 Mark)

The Karnataka High Court in the case of *CIT v. Hindustan Lever Ltd. (2014) 361 ITR 1* has held that where the winnings are wholly in kind, the responsibility cast under section 194B is to ensure that the tax is paid by the winner of the prize before the prize is released in his favour. In this regard, the *CBDT Circular No.763 dated 18/2/1998* clarifies that the person responsible for paying the winnings shall, before releasing such winnings, ensure that the tax is paid by the winner. He can do so, for example, by collecting from the winner a sum equal to the tax deductible at source on the winnings in kind, before releasing the winnings. For this purpose, the value of the winnings in kind shall be taken as the cost incurred by the payer in acquiring the said winnings in kind.

(2 Marks)

Therefore, in this case since the entire winning is in kind, it must be ensured that the sum equal to the tax deductible at source (i.e. Rs. 1,50,000, being @ 30% of Rs. 5 lacs) is paid by Mr. Govind, before the car is released in his favour. This can be done by collecting Rs. 1,50,000 from Mr. Govind before releasing the Maruti car to him and remitting the said sum to the Government account or verifying the tax payment by the winner and thereafter releasing the prize.

(1 Mark)

Answer-7 (b) :

(a) Tax implications on sale of rural agricultural land and house property representing a capital asset in the hands of Mr. Harish, a salaried employee

(i) Tax implications in the hands of Mr. Harish, a salaried employee

Since rural agricultural land is not a capital asset, the gains arising on sale of such land is not taxable in the hands of Mr. Harish. However, capital gains would arise on sale of house property, being a capital asset.

As per section 50C(1), the stamp duty value of house property on the date of agreement (i.e., Rs. 75 lakh) would be deemed to be the full value of consideration arising on transfer of property. Therefore, Rs. 35 lakh (i.e., Rs. 75 lakh – Rs. 40 lakh, being the purchase price) would be taxable as short-term capital gains in the A.Y.2017-18.

It may be noted that under first and second proviso to section 50C(1), the stamp duty value on the date of agreement is to be adopted as the advance was received on the date of agreement through the specified mode. As the date of agreement is different from the date of registration and part of the consideration was received on or before the date of agreement by way of account payee cheque, the stamp duty value on the date of agreement is to be adopted as the deemed sale consideration.

(ii) Tax implications in the hands of the buyer – Mr.Suresh, a retail trader

The house property purchased would be a capital asset in the hands of Mr. Suresh, who is a retail trader of garments. The provisions of section 56(2)(vii) is attracted in the hands of Mr. Suresh who has acquired the immovable property, being a capital asset, for inadequate consideration. For the purpose of section 56(2)(vii), Mr. Suresh can take the stamp duty value on the date of agreement instead of the date of registration since he has paid a part of the consideration by a mode other than cash on the date of agreement.

Therefore, Rs. 15 lakh, being the difference between the stamp duty value of the property on the date of agreement (i.e., Rs. 75 lakh) and the actual consideration (i.e., Rs. 60 lakh) would be taxable as per section 56(2)(vii) under the head "Income from other sources" in the hands of Mr. Suresh.

As rural agricultural land is not a capital asset, the provisions of section 56(2)(vii) are not attracted in respect of acquisition of agricultural land for inadequate consideration, since the definition of "property" under section 56(2)(vii) includes only capital assets specified thereunder.

(iii) TDS implications in the hands of the buyer, Mr. Suresh

Since the sale consideration of house property exceeded Rs. 50 lakh, Mr. Suresh is required to deduct tax at source under section 194-IA. The tax deduction under section 194-IA would be Rs. 60,000, being 1% of Rs. 60 lakh.

TDS provisions under section 194-IA are not attracted in respect of transfer of rural agricultural land.

(4 Marks)

(b) Tax implications on sale of house property representing stock-in-trade in the hands of Mr. Harish, a property dealer

(i) Tax implications in the hands of Mr. Harish for A.Y.2017-18

If Mr. Harish is a property dealer who has sold the house property in the course of his business, the provisions of section 43CA would be attracted, since the house property represents his stock-in-trade and he has transferred the same for a consideration less than the stamp duty value.

For the purpose of section 43CA, Mr. Harish can take the stamp duty value on the date of agreement instead of the date of registration, since he has received part of the sale consideration by a mode other than cash on the date of agreement. Therefore, Rs. 35 lakh, being the difference between the stamp duty value on the date of agreement (i.e., Rs. 75 lakh) and the purchase price (i.e., Rs. 40 lakh), would be chargeable as business income in the hands of Mr. Harish.

(ii) TDS implications and taxability in the hands of Mr. Suresh for A.Y.2017-18

There would be no difference in the TDS implications or taxability in the hands of Mr. Suresh, whether Mr. Harish is a property dealer or a salaried employee. Therefore, the provisions of section 56(2)(vii) would be attracted in the hands of Mr. Suresh who has received house property, being a capital asset, for inadequate consideration. The TDS provisions under section 194-IA would also be attracted since the actual consideration for house property exceeds Rs. 50 lakh.

(4 Marks)

Answer-7 (c) :

Any income arising from an international transaction, where two or more “associated enterprises” enter into a mutual agreement or arrangement, shall be computed having regard to arm’s length price as per the provisions of Chapter X of the Act.

Section 92A defines an “associated enterprise” and sub-section (2) of this section speaks of the situations when the two enterprises shall be deemed to associated enterprises. Applying the provisions of section 92A(2)(a) to (m) to the given facts, it is clear that “Anush Motors Ltd.” is associated with :-

- (i) Rida Ltd. as per section 92A(2)(a), because this company holds shares carrying more than 26% of the voting power in Anush Motors Ltd.;
- (ii) Kyoto Ltd. as per section 92A(2)(g), since this company is the sole owner of the technology used by Anush Motors Ltd. in its manufacturing process;
- (iii) Dorf Ltd. as per section 92A(2)(c), since this company has financed an amount which is more than 51% of the book value of total assets of Anush Motors Ltd.

The transactions entered into by Anush Motors Ltd. with different companies are, therefore, to be adjusted accordingly to work out the income chargeable to tax for the A.Y. 2017-18.

Particulars	Rs. (in crores)
Income of Anush Motors Ltd. as computed under Chapter IV-D, prior to adjustments as per Chapter X	300.00
<i>Add:</i> Difference on account of adjustment in the value of international transactions:	
(i) Difference in price of car @ \$ 200 each for 10,000 cars (\$ 200 x 10,000 x 63)	12.60
(ii) Difference for excess payment of royalty of \$ 30,00,000 (\$ 30,00,000 x 63) [See Note below]	18.90
(iii) Difference for excess interest paid on loan of EURO 1000 crores (84*1000*1/100)	<u>840.00</u>
Total Income	1,171.50

(4 Marks)

The difference for excess payment of royalty has been added back presuming that the manufacture of cars by Anush Motors Ltd is wholly dependent on the use of know-how owned by Kyoto Ltd.

Note: It is presumed that Anush Motors Ltd. has not entered into an Advance Pricing Agreement or opted to be subject to Safe Harbour Rules.