Paper-7 Direct Taxation

Time Allowed: 3 hours **Full Marks: 100**

All the questions relate to the assessment year 2014-15, unless stated otherwise.

Working notes should form part of the answers.

Section A

[Question No.1 is compulsory and answer **any four** from Question No. 2 to 6]

Question 1.

(a) Answer the following sub-divisions briefly in the light of the provisions of the Income-tax Act, 1961:

(i) Ms. Damietti, an Italian national has income from house property in Italy, remitted by tenant to her in India through State Bank of India for ₹ 3,20,000 in the previous year 2013-14. What will be the incidence of tax if she is Non-resident in India during the said previous year?

(ii) If Municipal Value (MV), Fair Rent (FR) and Standard Rent of a house property are ₹ 50,000, ₹ 56,000 and ₹ 45,000 respectively for the previous year 2013-14, then what will be its reasonable expected rent?

(iii) Whether unabsorbed depreciation can be set off only against income under "Profits and Gains of Business or Profession" or not?

(iv) A, an individual, gets ₹ 65,000 as a birthday gift from his Grandfather. Is the receipt taxable under the Income Tax Act?

(v) "The provision of Alternate Minimum Tax shall apply to an individual" — critically examine.

(vi) Does tax planning include compliance within law? Clarify.

(vii) Nayanika is employed as resident engineer in WLB Ltd. on a basic salary of ₹ 75,000 per month. A sweeper and a watchman are engaged to look after her bunglow. They are the employees of the company on a salary of ₹ 300 per month each. Nayanika had no shares in the company and she is not related to any of the directors. Discuss the tax treatment in the hands of Nayanika.

(viii) State the deductibility of the expenses in case of profits and gains from business or profession — Initial expenditure incurred on installation of fluorescent tube lights.

[8 × 1]

(b) Choose the correct alternative:

(i) An individual can avail the benefit of Leave Travel Assistance offered by his employer —
(A) twice in a block of two years;
(B) twice in a block of four years;
(C) once in a block of four years;
(D) once in a block of two years.

(ii) How many installments of prior period interest of a house property will be allowed as deduction from the year in which the property was acquired or construction was completed?
(A) five;

(B) ten;
(C) six;
(D) four.

(iii) As per section 80GG of the Income-tax Act, which one of the following is one of the criteria for claiming deduction in respect of rents paid—
(A) 50% of Adjusted Total Income;
(B) 100% of Adjusted Total Income;
(C) 10% of Adjusted Total Income;
(D) 25% of Adjusted Total Income.

(iv) As per section 139A of the Income-tax Act, Permanent Account Number (PAN) comprises of —
(A) 10 alphanumeric characters;
(B) 12 alphanumeric characters;
(C) 10 numeric characters;
(D) 12 numeric characters.

(v) As per section 71B of the Income-tax Act, the permissible limit to carry forward and set off Brought forward loss from House Property is —
(A) 4 Assessment Years immediately succeeding the Assessment Year for which such loss was computed;
(B) Any number of year until it is fully set off;
(C) 8 Assessment Years immediately succeeding the Assessment Year for which such loss was computed;
(D) None of the above.

[5 × 1]

Question 2.

(a) The travelling allowance of ₹ 35,000 is given to Mr. Y by his employer for official purpose during the previous year 2013-14. The amount actually spent by Mr. Y for this purpose is ₹ 32,000. State the taxability of the said item.

(b) Z retires on 30th June, 2013. He submits the following information –

Basic salary (since January 2013): ₹ 20,000 per month, dearness allowance: ₹ 6,000 per month (1/3 of which is part of salary for retirement benefits), employer's contribution towards provident fund : ₹ 3,000 per month (Z makes a matching contribution); interest credited at the rate of 15 per cent on April 30, 2013 : ₹ 7,500; pension after retirement : ₹ 10,000 per month, and payment of provident fund at the time of retirement : ₹ 7,60,000 (out of which employer's contribution: ₹ 3,30,000, interest thereon : ₹ 44,000, Z's contributions : ₹ 3,50,000, interest thereon : ₹ 46,000). Salary and pension become due on the last day of each month. Z has deposited the entire provident fund payment with a company (rate of interest: 9 per cent per annum).

Find out the income of Z for the assessment year 2014-15 on the assumption that the provident fund is (i) statutory provident fund, (ii) recognized provident fund, or (iii) unrecognized provident fund.

(c) What is the due date of filling of return of income in case of a non-working partner of a firm whose accounts are not liable to be audited?

[2+(3+3+3)+2]

Question 3.

(a) Kavita owns a house property which is given on rent. For the previous year 2011-12, she claims a deduction of ₹ 78,000 on account of unrealised rent, out of which the Assessing Officer allows only ₹ 62,000 as deduction. What are the tax consequences if Kavita recovers on June 25, 2013 from the defaulting tenant (i) ₹ 10,000, (ii) ₹ 16,000 or (iii) ₹ 35,000 as full and final payment?

(b) What is the difference between exemption and deduction?

(c) Can assessee follow different method of accounting for different businesses?

(d) During his 195 days' stay in India in the previous year 2013-14, Aman, a citizen of U.K. is all the time moving from one place to another. He claims that he is non-resident in India for the assessment year 2014-15 on the following grounds:

1. He had never visited India before April 1, 2013.
2. During 2013-14, though he is in India for 195 days, he could not spend two consecutive nights at any one place.
3. For the assessment year 2014-15, he is resident in U.K. according to the English Income-tax Act. He insists that he cannot be resident of two countries for the same assessment year. Do you agree with him?

[5+2+2+4]

Question 4.

(a) A purchases a house property in 1995. It is compulsorily acquired by the Government on 20th April, 2012 (indexed cost of acquisition is ₹ 40,000). Compensation paid by the Government on 6th May, 2013: ₹ 6,00,000. The Delhi High Court increases the compensation from ₹ 6,00,000 to ₹ 9,30,000 on the appeal filed by A (legal expenditure incurred by A: ₹ 10,000). The Government on 10th June, 2014 pays the additional compensation of ₹ 3,30,000. Compute the capital gains.

(b) An assessee filed a return of income on 31.8.2014 in respect of Assessment Year 2014-15 disclosing an income of ₹ 6 lakhs from business. It was not accompanied by proof of payment of tax due on self-assessment. Discuss the validity of such a return.

(c) Name few of the property incomes which are exempted from tax.

(d) How the cost of acquisition of Bonus Shares is determined in computation of capital gain?

[4+3+4+2]

Question 5.

(a) Merry International Ltd. incurs an expenditure of ₹ 255 crores for acquiring the right to operate telecommunication services for Assam & Sikkim. The payment was made in November 2011 and the licence to operate the services was valid for 15 years. In December

2012, the company transfers part of the licence, in respect of Assam, to Banerjee International Ltd. for a sum of ₹ 56 crores and continue to operate the licence in Sikkim. What is the deduction allowable u/s 35ABB of the Income-tax Act to Merry International Ltd. for the Assessment Year 2014-15?

(b) Y, a resident individual, submits the following information for the assessment year 2014-15:

	₹
Business A	
Loss of the year 2013-14	(-)48,000
Brought forward loss of the year 2012-13	(-)39,000
Business B	
Profit of year 2013-14	1,56,000
Business C (previous year ends on 31st March, business discontinued on 10th April, 2013)	
Profit of the period from 1st April,2013 to 10th April,2013	Nil
Brought forward loss of 2012-13	(-)39,700
Business D (previous year ends on 31st March, business discontinued on 31st March, 2012)	
Brought forward loss of 2012-13	(-)40,000
Income from other sources	
Loss from the activity of owning and maintaining camels for races	(-)9,000
Dividend on units of UTI held as investment	75,000
Interest on debentures held as investments	99,000
Long-term capital loss on sale of shares	(-) 14,900
Income from house property	57,600

Determine the net income of Y for the assessment year 2014-15. Also calculate the amount of loss which can be carried forward for being set off in the next assessment year.

(c) What is the amount of deduction in respect of royalty of authors allowed as per section 80QQB of the Income-tax Act?

[4+7+2]

Question 6.

(a) On receipt of assessment order for the assessment year 2014-15 of MP Ltd., the chief accountant of that company finds that the following deductions claimed by it in the return of total income have not been allowed:

1. Expenditure of ₹ 17,000 incurred on accommodation maintained, at the place where the factory is located, for the directors and other employees of the company, who visit the factory for the purposes of the company's business.
2. A sum of ₹ 17,500 incurred for lunch at a five-star hotel where seven representatives of a prominent raw material supplier were taken for lunch and the purchase manager of the assessee had accompanied them.
3. Claim for deduction of a sum of ₹ 4,50,000 being the amount of liability for gratuity for the calendar year 1991 calculated on actuarial basis for which no provision was made in the books of account. The company does not maintain any gratuity fund. It maintains its accounts on mercantile basis. So far as gratuity liability is concerned, it has made provision for the same in the book of account for the previous year ended December 31, 1976. Thereafter, it stopped making provision for gratuity liability in the books of account. However, actual payments are debited to the Profit and Loss Account.
4. Expenditure of ₹ 12,000 incurred for drilling a tube-well in the factory. The drilling

operations were given up as the water was hard and not suitable for use. The expenditure thus became infructuous.

5. Annual preference dividend liability of ₹ 1,00,000 on the company's 10 per cent cumulative redeemable preference shares which are not entitled to any further rights to participate in profits or surplus assets. These shares are redeemable on December 1, 2013 according to the terms of issue.
6. The Assessing Officer has also added a sum of ₹ 8,000 pertaining to unclaimed wages for the year 1992 which was transferred to the Profit and Loss Account of the year 2013-14 since the claim has become time barred. The assessee had claimed that the same was not liable to be included in the total income.

The company seeks your advice on the correctness or otherwise of the disallowances.

(b) Write a short note on return of loss [section 139(3) of Income-tax Act].

[9+4]

Section B

[Answer **all** the questions]

Question 7.

State whether the following statements are correct or not with brief reasons:

(i) A farm house situated within 30 kilometres from the local limits of any municipality is asset.

(ii) Coparcenary interest in a Hindu undivided family is exempt from wealth-tax.

(iii) Net wealth in excess of ₹ 30,00,000 is chargeable to wealth tax.

(iv) The return of net wealth is to be filed in form ITR-1.

(v) Motor car used by the assessee in the business of running them on hire, is an asset.

[5 × 1]

Question 8.

Either

(a) Which entities are outside the purview of wealth tax?

(b) What is the basis of valuation of assets of business in the context of wealth tax?

[3+2]

Or

A, an Indian citizen, was ordinarily residing in Canada. He comes to India every year during August for 3 weeks. He comes to India permanently on July 9, 2013. He owns the following assets:

1. A residential house (not being let out) at Bombay gifted by his father-in-law.
2. A house at Bangalore purchased out of money remitted from Canada on August 3, 2012.
3. Two kilograms gold brought at the time of transfer of residence on July 9, 2013.
4. Out of money brought into India at the time of return and out of his Non-resident (External) Account, he acquires the following during July-September 2013:
   two cars, air-conditioners and shares in companies.

5. On December 10, 2013, after selling one kilogram of gold, he purchases a boat.

Discuss the taxability of the above items under the purview of Wealth-tax Act.

[5]

Section C

(All questions in this section relate to the transfer pricing provisions under the Income-tax Act, 1961)

Question 9.

(a) What is the full form of OECD?
(b) State the meaning of "**safe harbour".**
(c) Give few examples of marketing related intangibles.
(d) What is Advance Pricing Agreement (APA)?
(e) Which is meant by "bilateral agreement" in the context of Advance Pricing Agreement?

[5 × 1]

Question 10.

Either

(a) PQ Medical Equipments Inc. (PQ) of Canada has received an order from a leading UK based Hospital for development of a hi-tech medical equipment which will integrate the best of software and latest medical examination tool to meet varied requirements. The order was for 3,00,000 Euros. To execute the order, PQ joined hands with its subsidiary Prestige Components Inc. (PCI) of USA and Chemicals India Ltd (CIL), an Indian Company. PCI holds 30% of CIL. PQ paid to PCI and CIL Euro 90,000 and Euro 1,00,000 respectively and kept the balance for itself. In the entire transaction, a profit of Euro 1,00,000 is earned. Chemicals India Ltd. incurred a total cost of Euro 75,000 in execution of its work in the above contract. The relative contribution of PQ, PCI and CIL may be taken at 30%, 30% and 40% respectively. Compute the Arm's Length Price and the incremental Total Income of Chemicals India Ltd., if any due to adopting Arms Length Price.

(b) Which are the steps to be followed in the Comparable Uncontrolled Price method in computation of arm's length price?

(c) T Ltd. is an Indian company. It has a manufacturing unit in Kerala. It is a subsidiary company of M Ltd., a US company. M Ltd. gets royalty from T Ltd. on supply of technical information which is used by T Ltd. for manufacturing goods in its unit in Kerala. For similar transfer of technical information to any unrelated entity M Ltd. charges ₹ 8,000 per year. However, from T Ltd. it charges (a) $ 11,000 or $ 6,000 per year which is subject to tax deduction by T Ltd. Exchange rate is ₹ 49 per US dollar. Income of T Ltd. for the assessment year 2014-15 before deducting payment for technical information to T Ltd. is ₹ 76,00,000. Find out the income of M Ltd. and T Ltd.

[8+4+8]

Or

(a) Compute the 'arm length price' (ALP) in the following cases:

i) Shisha Instruments Ltd. is a 100% Indian subsidiary of a US company. The parent company sells one of its products to the Indian subsidiary at a price of US$ 100 per unit. The same product is sold to unrelated buyers at a price of US$ 130 per unit.

ii) The US parent company sells the same product to an unrelated company in India @ US$ 80 per unit.

(b) Explain the applicability and the different steps for computation of Arm's Length Price (ALP) by Comparable Uncontrolled Price Method (CUPM)?

(c) Write a note on Compliance Audit of Advance Pricing Agreement.

(d) Describe the tax planning measures in relation to tax liability of Indian collaborators for payments made.

[(2+2)+(2+5)+6+3]