Paper 7: Direct Taxation

Question 1:

(a) Define the term Assessment Year & Previous Year?

Answer:

Assessment Year [Section 2 (9)]

Assessment Year means the period of twelve months commencing on the 1st day of April every year.

It relates to the previous year for which the income is assessed to tax.

The present Assessment Year is 2014-15 relating to Previous Year 2013-14.

Previous Year [Section 3]

"Previous Year" means the Financial Year immediately preceding the Assessment Year.

The year in respect of the income of which tax is levied is called Previous Year.

The present Previous Year 2013-14 and its Assessment Year is 2014-15.

Note : Previous Year for newly established business from the date of setting up of the business to the end of the Financial Year in which business was set up.

(b) Under which cases Assessment year and Previous year is same?

Answer:

Previous year & Assessment year will be same in the following cases :

1. Shipping business of nonresident [Section 172]
2. Persons leaving India [Section 174]
3. AOP or BOI or Artificial Juridical Person formed for a particular event or purpose [Section 174A]
4. Persons likely to transfer property to avoid tax [Section 175]
5. Discontinued business [Section 176]

Question 2:

(a) Compute Income for Mr. Roy for the Previous Year 2013-14.

	Particulars	₹
(a)	Salary accrued and received in India	60,000
(b)	Profit from hotel business in Japan	1,20,000
(c)	Dividends declared in Japan received in India	30,000
(d)	Gain from transfer of capital asset in India	70,000
(e)	Interest on Debentures of a company in New York received in India	38,000
(f)	Royalty received in Germany from a resident in India for technical services	40,000

provided for a business in Germany

(g) Interest received in UK from Mr. Robert, a non-resident, on loan provided to him for business in India 12,000

(h) Fees from an Indian company carrying on business in the UK for technical services rendered in London, directly deposited in his bank account in India 50,000

Compute the Gross Total Income Mr. Roy for the relevant Previous Year 2013-14, if he is (i) Ordinarily Resident, (ii) Not Ordinarily Resident, (iii) Non Resident.

Solution:

Computation of Gross Total Income of Mr. Roy for the Previous Year 2013-2014

Particulars	ROR	RNOR	NR
(a) Salary accrued and received in India	60,000	60,000	60,000
(b) Profit from hotel business in Japan	1,20,000	—	—
(c) Dividends declared in Japan received in India	30,000	30,000	30,000
(d) Gains from transfer of a capital asset in India deemed to accrue or arise in India	70,000	70,000	70,000
(e) Interest on debentures of a company in New York but received in India	38,000	38,000	38,000
(f) Royalty received in Germany from a resident in India for technical services provided for a business in Germany	40,000	—	—
(g) Interest received in UK from Mr. Robert, a non-resident, on loan provided to him for business in India	12,000	12,000	12,000
(h) Fees from an Indian company, carrying on business in UK for technical services rendered in London, directly deposited in his Bank Account in India	50,000	50,000	50,000
Gross Total Income	**4,20,000**	**2,60,000**	**2,60,000**

(b) Mr.X furnishes the following particulars of his income earned during Previous Year 2013-14:

(i) Income from agriculture in Bangladesh, received there ₹ 4,80,000, but later on remitted to India.

(ii) Interest on Pakistani Development Bonds, ₹ 1,90,000, one-sixth of which received in India.

(iii) Gift of ₹ 1,70,000 received in foreign currency from a relative in India.

(iv) Arrears of salary ₹ 2,50,000 received in Pakistan from a former employer in India.

(v) Income from property received outside India ₹ 4,00,000 (₹2,00,000 is used in Bahrain for the educational expenses of his son in Bahrain, and ₹ 3,00,000 later on remitted to India).

(vi) Income from business in Iran which is controlled from India (₹2,00,000 being received in India) ₹3,00,000.

(vii) Dividends received on 30.06.2013 outside India from an Indian company, ₹ 3,50,000.

(viii) Untaxed profit of the FY 2007-2008 brought to India in July 2013, ₹ 3,50,000.

(ix) Profit from business in Kolkata managed from outside India ₹ 2,00,000, 60% of which is received outside India.

Determine the Gross Total Income of Mr. X for Previous Year 2013-2014, if Mr. X is (a) Resident and Ordinarily Resident; (b) Resident but not Ordinarily Resident; (c) Non Resident.

Solution:

Computation of Gross Total Income for the Previous Year 2013-14

Particulars	ROR	RNOR	NR
(i) Income from agriculture in Bangladesh, received there but later on remitted to India	4,80,000	-	-
(ii) Interest on Development Bonds in a foreign land :			
(a) 1/6th of ₹1,90,000 received in India	31,667	31,667	31,667
(b) 5/6th of ₹1,90,000 being received in India	1,58,333	-	-
(iii) Gift received from a relative in India is exempted u/s 57(v)	-	-	-
(iv) Salary arrears received in Pakistan from a former employer in India	2,50,000	2,50,000	2,50,000
(v) Income from property received outside India but later on remitted to India	4,00,000	-	-
(vi) Profit from a business in foreign land but controlled from India			
(a) Profits received in India	2,00,000	2,00,000	2,00,000
(b) Profits received outside India	2,00,000	2,00,000	-
(vii) Dividends received from an Indian Company, outside India, deemed to accrue or arise but exempted u/s 10(34)	-	-	-
(viii) Untaxed foreign profit of 2007-08 brought to India	-	-	-

(ix) Profit from business in India ₹2,00,000, 60% of which was received outside India	2,00,000	2,00,000	2,00,000
Gross Total Income	**19,20,000**	**8,81,667**	**6,81,667**

Question 3:

(a) Amal Kumar, an Indian citizen, is posted in the Indian High Commission at Nairobi during the Previous Year 2013-14. His emoluments consist of Basic Pay of ₹2,50,000 per month and overseas allowance of ₹ 70,000 per month. Besides, he is entitled to & from journey to India and also use Government's car at Nairobi. He has no taxable income except salary income stated above.

Compute tax liability if he is a non-resident during the Previous Year 2013-14.

Solution:

(1) U/s 9(1)(iii), Salary paid by the Government of India to an Indian citizen for services rendered outside India is deemed to accrue or arise in India and is therefore taxable in India.

(2) U/s 10(7), allowances or perquisites paid by the Government of India to an Indian citizen or services rendered outside India, is fully exempt from tax.

(3) **Computation of Gross Salary for the Previous Year 2013-14**

Particulars	Amount (₹)	Amount (₹)
Salary : ₹ 2,50,000 x 12 months		30,00,000
Add: Overseas allowance ₹70,000 x 12 months	8,40,000	
Less: Exemption u/s 10(7)	8,40,000	Nil
Gross Salary		**30,00,000**
Less: Deduction u/s 16		Nil
Income under the head Salaries		**30,00,000**

Computation of Tax Liability

Particulars	Amount (₹)	Amount (₹)
Upto ₹ 2,00,000	Nil	
₹ 2,00,001 to ₹ 5,00,000 = @ 10% of ₹ 3,00,000	30,000	
₹ 5,00,001 to ₹ 10,00,000 = @ 20% of ₹ 5,00,000	1,00,000	
₹ 10,00,001 to ₹ 30,00,000 = @ 30% of ₹ 20,00,000	6,00,000	7,30,000
Tax (excluding cess)		**7,30,000**
Add: Education Cess @ 2%		14,600
Add: Secondary and Higher Education Cess @ 1%		7,300

Tax Liability (including Cess)		**7,51,900**

(b) A, is entitled to a basic salary of ₹ 20,000 p.m. and dearness allowance of ₹ 4,000 p.m., 40% of which forms part of retirement benefits. He is also entitled to HRA of ₹ 8,000 p.m. He actually pays ₹ 8,000 p.m. as rent for a house in Delhi. Compute the taxable HRA.

Solution:

Salary for House Rent Allowance = Basic Pay + D.A. (considered for retirement benefits) + Commission (if received as a fixed percentage on turnover as per terms of employment) = (20,000 × 12) + (40% × 4,000 ×12) = 2,59,200

Computation of Taxable House Rent Allowance

Particulars	₹	₹
Amount received during the financial year for HRA		96,000
Less: Exemption u/s 10(13A) Rule 2A		
Least of the followings:		
(a) Actual amount received	96,000	
(b) 50% of Salary of ₹ 2,59,200	1,29,600	
(c) Rent paid less 10% of Salary [8,000 × 12 - 10% of ₹ 2,59,200]	70,080	70,080
Taxable House Rent Allowance		**25,920**

Question 4:

(a) Mr. Smart was retrenched from service of Hungry Ltd. The scheme of retrenchment is approved by the Central Government. Retrenchment compensation received ₹ 12 lakhs. What is the taxability?

Solution :

When retrenchment compensation is received in accordance with any scheme, which is approved by the Central Government, it is fully exempted from tax.

(b) Mr. Rahul Khanna is employed with HUD Co. Ltd. @ ₹ 50,000 p.m. He is the owner of a house property construction of which was completed on 1st April 2004. Since then, it has been in his self-occupancy for residential purposes. The particulars in respect of the house for financial year 2013-2014 are given below :

Municipal Valuation	**₹3,00,000**
Municipal tax paid	**₹30,000**
Ground rent outstanding	**₹10,000**
Insurance premium paid	**₹6,000**

Interest on loan, taken on 1-6-2012 for renovation of the house, is ₹ 95,000 for the year 2013-2014. However, he could pay only, ₹ 45,000 during the year. He is transferred in February 2014 to the Nagpur Branch of the Company. He intends to allow his sister to occupy the house free of rent in

his absence. He seeks your advice in this connection. Compute his total income for AY 2014-2015.

Solution :

Computation of Total Income

Assessee : Mr. Ranjit Sinha **A. Y : 2014-15**

Particulars	**Case I House kept vacant (₹)**	**Case II House is occupied by his sister in his absence (₹)**
Income from House Property :		
Gross Annual Value	Nil	3,00,000
Less : Municipal taxes paid	Nil	(-) 30,000
Net Annual Value	Nil	2,70,000
Less : Permissible deduction (Sec. 24)		
(i) Statutory deduction – 30% of Net annual value	Nil	(-) 81, 000
(ii) Interest on loan for renovation	(-) 30,000	(-) 95,000
Income from House Property	(-) 30,000	94,000
Statement of Total Income :		
Income from Salary	6,00,000	6,00,000
Income from House Property	(-) 30,000	94,000
Total Income	5,70,000	6,94,000

Advise : From tax angle it is not advisable to allow his sister to occupy the house in his absence.

Question 5:

(a) Mr. L is the owner of a commercial property let out at ₹ 40,000 p.m. The Municipal tax on the property is ₹ 25,000 annually, 60% of which is payable by the tenant. This tax was actually paid on 15.4.2014. He had borrowed a sum of ₹ 30 Lakhs from his cousin, resident in USA (in dollars) for the construction of the property on which interest at 8% is payable. He has also received arrears of rent of ₹ 60,000 during the year, which was not charged to tax in the earlier years. What is the Property Income of Mr. L for A.Y. 2014-15?

Solution :

Assessee : Mr. L **Previous Year : 2013-2014** **Assessment Year : 2014-15**

Computation of Income from House Property

Particulars	**₹**	**₹**
Let Out : So, Annual Value u/s 23(1)(a)/(b) = Actual Rent = ₹ 40,000×12		4,80,000
Less : Municipal Taxes Paid during the F.Y. 2013-14		NIL
Net Annual Value		**4,80,000**
Less : Deduction u/s 24		
- 30% of NAV - ₹ 4,80,000 × 30%	1,44,000	
- Interest on Housing Loan (Note) ₹ 30,00,000 × 8%	2,40,000	(3,84,000)
Income from House Property before considering Arrears of Rent		**96,000**
Arrears of Rent Received	60,000	
Less : Deduction u/s 25B - 30% of Arrears received - ₹ 60,000 × 30%	(18,000)	42,000
Net Income from House Property		**1,38,000**

Note : It is presumed that the tax has been deducted at source on the amount of interest payable outside India.

(b) Will the provision of section 40A(3) be attracted in the following cases:

(i) R purchases goods worth ₹30,000 from G against one bill but makes payment of ₹18,000 & ₹12,000 at different times on the same date.

(ii) R makes a payment of ₹40,000 as donation by cheque to National Defence Fund.

(iii) R makes a purchase of goods of ₹60,000 and makes payment of ₹ 45,000 by account payee cheque and ₹ 15,000 in cash.

(iv) R makes a purchase of goods of ₹60,000 on 14.2.2014 and makes the payment as under:

(I) ₹ 30,000 by account payee cheque on 15.2.2014,

(II) ₹ 15,000 in cash on 15.2.2014,

(III) ₹15,000 in cash on 16.2.2014.

(v) R purchases a building for ₹10,00,000 and makes the payment in cash.

(vi) R, a dealer in real estate purchases buildings for ₹10,00,000 and makes the payment by crossed cheque.

Answer:

(i) Section 40A(3) shall be applicable and ₹ 30,000 shall be disallowed.

(ii) Section 40A(3) shall not be applicable. As donation is not allowable as deduction under section 30 to 37 but allowable under section 80G from GTI.

(iii) Section 40A(3) is not applicable.

(iv) Section 40A(3) is not applicable.

(v) No, section 40A(3) is not applicable for purchase of a capital asset.

(vi) Entire ₹10,00,000 shall be disallowed as payment is not by account payee cheque.

Question 6:

(a) Compute the taxable income of a Chamber of Commerce from the following data.

	1 ₹	2 ₹	3 ₹
Gross receipts for specific services rendered to members	**2,60,000**	**2,60,000**	**2,60,000**
Expenses incurred in connection with the above	**60,000**	**1,10,000**	**2,00,000**
Interest on bank deposits	**40,000**	**40,000**	**80,000**
Receipt from members	**2,00,000**	**3,00,000**	**2,60,000**
Expenditure incurred on members	**1,50,000**	**4,10,000**	**3,50,000**

Solution:

Profit and gains of business and profession			
Net income from rendering specific services (Gross receipts-Expenses)	2,00,000	1,50,000	60,000
Less: Deficiency set off (maximum to the extent of 50% of total assessable income before set off of deficiency i.e. ₹1,90,000 and ₹1,40,000 in case of 2 and 3 respectively)	---	95,000	60,000
(A)	2,00,000	55,000	Nil
Interest on bank deposit under other heads	40,000	40,000	80,000
Less: Deficiency although allowable upto 50% of total assessable income which could not be set off against business income			10,000
Income (B)	40,000	40,000	70,000
Gross Total Income (A + B)	2,40,000	95,000	70,000
Less: Deduction under sections 80C to 80U	Nil	Nil	Nil
	2,40,000	95,000	70,000

Note:-

1. Surplus of ₹ 50,000 under case 1 is not taxable as it is from mutual activity.
2. Deficiency under case 2 and 3 would not have been allowed but for the benefit given under section 44A.
3. Assessable income in case of 2 and 3 is as under:

	Case I ₹	Case II ₹
Surplus from specific services	1,50,000	60,000
Interest income	40,000	80,000
	1,90,000	1,40,000
Less: Under section 80C to 80U	Nil	Nil
	1,90,000	1,40,000

4. In case 3, 50% of the assessable income is ₹70,000 (i.e. 50% of ₹1,40,000) but first it will be set off from business income which in this case is ?60,000 and the balance shall be set off from other income.

(b) X Airlines incorporated as a company in USA operates its flights to India and vice versa during the previous year 2013-14 and collects charges of ₹1,25,00,000 for carriage of passengers and cargo out of which ₹65,00,000 were received in US dollars for the passenger fare booked from New York to Mumbai. The total expenses for the year on operation of such flights were ₹1, 95,00,000. Compute the income chargeable to tax of the foreign airlines.

Solution:

As per section 44BBA, in case of an Airlines the income is presumed to be 5% of the following:

(i) the amount paid or payable (whether' in or out of India) to the assessee or to any person on his behalf on account of the carriage of passengers, livestock, mail or goods from any place in India, and

(ii) the amount received or deemed to be received in India by or on behalf of the assessee on account of the carriage of passengers, livestock, mail or goods from any place outside India.

Hence, the taxable income will be determined as under:

	Passenger fare booked from Mumbai to New York whether paid in India or not ₹	Passenger fare booked from New York to Mumbai if received in India ₹
Fare	60,00,000	65,00,000
Taxable income	3,00,000	3,25,000

Note—If the passenger fare booked from New York to Mumbai in not received in India, then such fare shall not be included for calculating presumptive income.

Question 7:

(a) Ramesh owns a residential house which was purchased by him in 1975 for ₹1,05,000. The FMV as on 1.4.81 was ₹ 3,00,000. This house is sold by him on 16.7.2013 for a consideration of ₹ 25,00,000. The brokerage and expenses on transfer was ₹ 25,000. Compute Capital Gains for the Assessment Year 2014-15.

If he invests ₹ 8,00,000 for purchase of a new house on 15.3.2014.

If the HP so purchased in 15.3.2014 is again sold in 21.10.14 for ₹ 12 lacs, what will be the tax liability?

Solution :

Computation of Capital Gains for the A.Y. 2014-15

Particulars	₹
Consideration for transfer	25,00,000
Less : Expenses on transfer	25,000
Net Consideration	**24,75,000**
Less : Indexed Cost of Acquisition 3,00,000 x $\frac{939}{100}$	28,17,000

Long Term Capital Loss	**3,42,000**
Less : **Exemption u/s 54**	
Cost of New HP Purchased ₹ 8,00,000	
(exemption restricted upto the balance of LTCG)	NIL
Taxable Long Term Capital Loss	**3,93,000**

If the HP purchased in 15.3.2014 is again sold on 21.10.14 for ₹ 12 lacs, there arise Short Term Capital Gain. The cost of acquisition shall be adjusted to the extent of Long Term Capital Gain exemption already availed.

Computation of Capital Gains for the A.Y. 2015-16

Particulars	₹	₹
Consideration for transfer		12,00,000
Less : **Cost of Acquisition**		
Cost of purchase	8,00,000	
Less : Exemption u/s 54 availed during A.Y. 2014-15 now withdrawn	NIL	8,00,000
Short Term Capital Gains		**4,00,000**

(b) Suman acquired shares of G Ltd. on 15.12.99 for ₹6 lacs which were sold on 14.6.13 for ₹ 18 lacs. Expenses on transfer of shares ₹ 30,000. He invests ₹ 10 lacs in the bonds of Rural Electrification Corporation Ltd. on 16.10.2013.

(i) Compute Capital Gain for the Assessment Year 2014-15.

(ii) State the period for which the bonds should be held by the assessee. What will be the consequences if such bonds are sold within the specified period?

(iii) What will be the consequences if Suman takes a loan against the security of such bonds?

Solution :

(i)

Computation of Capital Gains for the A.Y. 2014-15

Consideration for transfer	18,00,000
Less : Expenses on Transfer	30,000
Net Consideration	17,70,000
Less : **Indexed Cost of Acquisition** $6,00,000 \times \frac{939}{389}$	14,48,329
Long-term Capital Gains	3,21,671
Less : **Exemption u/s 54EC Taxable**	3,21,671
Long-term Capital Gain	NIL

(ii) Suman should not transfer or convert (otherwise than transfer) into money such bonds within 3 years from the date of their acquisition.

If these bonds are transferred or converted into money within 3 years, Capital Gain of ₹3,21,671 exempted earlier shall attract taxability towards Long-term Capital Gain of the Previous Year in which such asset is transferred or converted into money.

(iii) If any loan is taken against security of such bonds, it shall be taxable as Long-term Capital Gains of the Previous Year in which such loan is taken against the security of such bonds.

Question 8:

(a) Dharmendra received the following gifts during the year ending 31.03.2014:

(i) ₹ 80,000 from her elder sister.
(ii) ₹ 90,000 from the daughter of her elder sister.
(iii) ₹ 2,25,000 from various friends on the occasion of her marriage,
Discuss the taxability or otherwise of these gifts in the hands of Dharmendra.

Solution :

(i) ₹ 80,000 received from elder sister, is not taxable, as elder sister is a relative.
(ii) ₹ 90,000 received from the daughter of her elder sister, is taxable, as the donor, in this case, is not a relative as per the definition of the Act.
(iii) ₹ 2,25,000 is not taxable as it is received on the occasion of her marriage.

(b) Discuss the taxability of Family Pension.

Solution:

Family pension means pension received by the family members of the deceased employee. It is chargeable to tax under the head 'Income from Other Sources'. Deduction u/s 57: Least of the following is allowed as a deduction -
(i) 33 1/3 % of gross pension
(ii) ₹ 15,000

Exemptions :
(i) Family pension received by family members of Army personnel who are recipient of gallantry awards [Section 10(18)].

(ii) Family pension received by the widow or children or nominated heirs of a member of the armed forces (including para-military forces) whose death has occurred in the course of operational duties [Section 10(19)].

Question 9:

(a) Dhoni had placed a deposit of ₹ 20 Lakhs in a bank on which he received interest of ₹1,60,000. He had also borrowed ₹ 8 Lakhs from the same bank on the security of the deposit and was liable to pay ₹ 80,000 by way of interest to the bank. He therefore offered the difference between two amounts of ₹ 80,000 as Income from Other Sources. Is this correct?

Solution :

U/s 57, any expenditure (not being capital expenditure) expended to earn income chargeable under the head "Income from Other Sources" will be allowed as deduction against such income.

Interest on Bank FD was the income in the hands of the assessee and the interest on the loan taken from bank on that deposit is not an allowable expenditure.

Therefore, in the given case, the interest of ₹ 80,000 paid by Dhoni is not allowable as deduction, and the entire interest of ₹ 1,60,000 is fully taxable.

(b) Mr. Kholi gets the following gifts during the Previous Year 2013-2014.

	Date of Gift	Name of the Donor	Amount of Gift (₹)
1.	01.07.2013	Gift from R, a friend, by cheque	1,00,000
2.	01.09.2013	Cash gift from N, nephew	2,00,000
3.	01.12.2013	Gift of diamond ring on his birthday, by a friend, C	1,50,000
4.	15.12.2013	Cash gifts of ₹62,000 each made by four friends on the occasion of his marriage	2,48,000
5.	21.12.2013	Cash gift made by wife's sister on house opening ceremony	1,02,000
6.	15.01.2014	Cash gift from a close friend of father-in-law.	3,02,000
7.	31.01.2014	Cash gift made by great-grandfather	3,02,000
8.	01.02.2014	Cash gift received under the Will of a friend, who is seriously ill.	3,30,000
9.	15.02.2014	Cash gift made by a business friend on his birthday	1,02,000
10.	31.03.2014	Cash gifts made by three friends of ₹50,000 each	1,50,000

Besides this, Kholi is engaged in the business of sale and purchase of retail goods.

He maintains no account books. Gross turnover from retail trading is ₹ 65,00,000. Compute his total income for the Assessment Year 2014-2015.

Solution :

Computation of Taxable Income for the AY 2014-2015

Particulars	Amount (₹)
1. Income from retail trading business [Sec. 44 AD] 8% ₹ 65,00,000	5,20,000
2. Income from Other Sources (money gifts):	
(i) Cash gift from a friend, by cheque	1,00,000
(ii) Cash gift from nephew, not covered by the definition of relative	2,00,000
(iii) Gift of diamond ring — Jewellery gift taxable	1,50,000
(iv) Cash gifts on the occasion of marriage are not chargeable even if such gifts are made by unrelated persons	--
(v) Cash gift made by wife's sister, a relative, not taxable	--
(vi) Cash gift by a friend of father-in-law, unrelated person	3,02,000
(vii) Cash gift made by great-grand father, a relative	--
(viii) Cash gift received under Will in contemplation of death of a friend	--
(ix) Cash gift made by a business friend on his birthday	1,02,000
(x) Cash gifts, made by three friends, of ₹50,000 each	1,50,000
Total Income	**15,24,000**

Question 10:

(a) Mr. Khan, out of his own funds, had taken a FDR for ₹ 2,00,000 bearing interest @ 10% p.a. payable half-yearly in the name of his wife Dipika. The interest earned for the year 2013-2014 of ₹20,000, was invested by Mrs. Dipika in the business of packed spices which resulted in a net profit of ₹1,10,000 for the year ended 31st March, 2014. How shall the interest on FDR and income from business be taxed for the Assessment Year 2014-2015?

Solution:

Where an individual transfers an asset (excluding house property), directly or indirectly to his/her spouse, otherwise than for adequate consideration, or in connection with an agreement to live apart, income from such asset is included in the total income of such individual [Sec. 64(1)(iv)].

Accordingly, interest on FDR, accruing to wife, is included in the total income of her husband. However, business profits cannot be clubbed with total income of husband. Clubbing applies only to the income from assets transferred without adequate consideration. It does not apply to the income from accretion of the transferred assets. Hence, business profit is taxable as the income of wife.

(b) Discuss whether the loss could be set-off in the following case:

Smt. Baid carried on business with the gifted funds of her husband Mr. Dabur. For the Previous Year ending 31.3.2014, Baid incurred loss of ₹7 lakh which Dabur wants to set-off from his taxable income.

Solution:

Funds for business were gifted by husband to wife. Accordingly, income from business should be clubbed with the income of husband [Sec. 64(1)(iv)].

"Income" includes "loss" also. Hence, husband is entitled to set-off the business loss of wife against his taxable income.

Question 11:

(a) Mr. Nandi discloses the following incomes for the Previous Year 2013-2014:

House Property ₹	Business or Profession		Capital Gains		Income from Other Sources
	Speculation ₹	Non-speculation ₹	STCG ₹	LTCG ₹	
A 75,000	P 4,50,000	X 7,50,000	C 9,00,000	F 10,50,000	Family pension 1,42,500
B (-) 60,000	S (-)3,00,000	Y (-) 4,50,000	D (-) 4,50,000	E (-)7,50,000	Loss from (-) 75,000 letting out from machinery/plant

Determine income under head of income for the A. Y. 2014-2015.

Solution :

Aggregation of income under each head of income: A. Y. 2014-2015

House Property ₹	Business or Profession		Capital Gains		Income from Other Sources ₹
	Speculation ₹	Non-speculation ₹	STCG ₹	LTCG ₹	
A 75,000	P 4,50,000	X 7,50,000	C 9,00,000	F 10,50,000	Family pension 1,42,500
B (-)60,000	S (-)3,00,000	Y (-)4,50,000	D (-)4,50,000	E (-)7,50,000	Loss from (-) 75,000 letting out machinery/ plant
15,000	1,50,000	3,00,000	4,50,000	3,00,000	67,500

(b) A discloses the following incomes from business or profession for the Previous Year 2013-2014:

		₹
(i)	**Proft from A business**	**7,00,000**
(ii)	**Loss from B business**	**(-) 3,00,000**
(iii)	**Loss from profession C**	**(-) 3,50,000**
(iv)	**Proft from speculation business – P**	**3,00,000**
(v)	**Loss from speculation business – Q**	**(-) 4,00,000**

Determine the Income from Business or Profession for the Assessment Year 2014-2015

Solution :

Income from Business or Profession for the AY 2014-2015

Particulars	₹
(i) A	7,00,000
(ii) B	(-) 3,00,000
(iii) C	(-) 3,50,000
Total Income from Non Speculation Business and Profession	50,000
Income from Speculation Business	
(i) P	3,00,000
(ii) Q	(-)4 ,00,000
Loss from Speculation Business	(-) 1,00,000

Speculation loss cannot be set-off against the income from business profit, though both of them fall under the same head of income.

Thus, taxable business profits for the Assessment Year 2014-2015 is ₹ 50,000. The speculation loss will be carried forward for future set-off for 4 assessment years, immediately succeeding the Assessment Year for which it was first computed [Sec. 73(4)].

The time-limit of 4 years is applicable from the Assessment Year 2015-2016 and subsequent year.

Question 12:

(a) Mr. Alok a senior citizen, owns a property consisting of two blocks of identical size. The first block is used for business purposes. The other block has been let out from 1.4.2013 to his cousin for ₹ 30,000 p.m. The cost of construction of each block is ₹ 6 lacs (fully met from bank loan), rate of interest on bank loan is 10% p.a. The construction was completed on 31.3.2013. During the year ended 31.3.2014, he had to pay a penal interest of ₹ 5,000 in respect of each block on account of delayed payments to the bank for the borrowings. The normal interest paid by him in respect of each block was ₹ 62,000. Principal repayment for each block was ₹33,000. An identical block in the same neighbourhood fetches a rent of ₹ 35,000 per month. Municipal Tax paid in respect of each block was ₹ 15,000.

The income from business prior to adjustment towards depreciation on any asset is ₹ 3,20,000. He follows Mercantile System of Accounting. Depreciation on equipments used for business is ₹ 40,000.

On 23.2.2014, he sold shares of B Ltd., a listed share in BSE for ₹ 2,50,000. The share had been purchased 10 months back for ₹ 1,90,000. Security transaction tax paid may be taken as ₹250.

Brought forward business loss of a business discontinued on 12.1.2011 is ₹ 1,00,000. This loss has been determined in pursuance of a return of income fled in time and the current year is the seventh year.

The following payments were affected by him during the year :

- **LIP of ₹ 24,000 on his life and ₹ 15,000 for his son aged 22, engaged as a software engineer and drawing salary of ₹ 25,000 per month.**
- **Mediclaim premium of ₹ 8,000 for himself & ₹ 5,000 for above son. The premiums were paid by cheque.**

You are required to compute the Total Income for the Assessment Year 2014-15. The various heads of income should be properly shown. Ignore the interest on bank loan for the period prior to 1.4.2013, as the bank had waived it.

Solution :

Computation of Total Income of Mr. Ashok for A.Y. 2014-15

Particulars	**Amount ₹**	**Amount ₹**	**Amount ₹**
(1) **Income from House Property (Let out)**			
Gross Annual Value (being Fair rent)		4,20,000	
Less: Municipal Tax		15,000	
Net Annual Value (NAV)		4,05,000	
Less: Deduction:-			
u/s 24(a) Standard Deduction (30% of NAV)	1,21,500		
u/s 24(b) Interest on loan	62,000	1,83,500	2,21,500
(2) **Profits and Gains of Business or Profession**			
Net Profit before depreciation		3,20,000	
Less: Expenditure allowed but not debited in P & L Account			
Depreciation on equipment	40,000		
Depreciation on building i.e. 10% of ₹ 5,00,000	60,000	1,00,000	
Profits and Gains of Business or Profession of current year		2,20,000	
Less: Brought forward losses set off u/s 72		1,00,000	1,20,000
(3) **Capital Gains**			
Consideration for Transfer		2,50,000	
Less: Cost of acquisition		(1,90,000)	
Short Term Capital Gains			60,000
Gross Total Income			4,01,500
Less: Deduction u/s			
80C: LIC Premium paid	39,000		
Repayment of bank loan	33,000	72,000	

80D: Medical insurance premium		8,000	80,000
Total Income			**3,21,500**

Notes :

1. Penal interest is not allowed u/s 24(b)
2. It has been assumed that interest, municipal tax on property used for business have already being charged while computing "Business Income Before Depreciation" i.e. ₹3,20,000.
3. STT is not allowed as expenditure on transfer.

(b) B Ltd. grows sugarcane to manufacture sugar. The data for the fnancial year 2013-14 is as follows :

Cost of cultivation of sugarcane	**₹ 6,50,000**
Market value of sugarcane when transferred to factory	**₹10,50,000**
Other manufacturing cost	**₹ 6,50,000**
Sales of sugar	**₹ 28,00,000**

Salary of Managing Director who looks after all operations of the Company ₹ 4,00,000

Determine its Business Income and Agricultural Income.

Solution :

(1)	**Business Income :**	
	Sales of Sugar	₹28,00,000
	Less: Market value of sugarcane when transferred to factory	₹10,50,000
	Other manufacturing cost	₹ 6,50,000
	Salary of Managing Director	₹ 4,00,000
(2)	**Agricultural Income :**	
	Market value of sugarcane when transferred to factory	₹10,50,000
	Less: Cost of cultivation	₹ 6,50,000

Question 13:

(a) Mr. Q has estates in Rubber, Tea and Coffee. He has also a nursery wherein he grows plants and sells. For the Previous Year ending 31.3.2014, he furnishes the following particulars of his sources of income from estates and sale of Plants. You are requested to compute the taxable income for the Assessment Year 2014-2015:

Manufacture of Rubber	**₹7,00,000**
Manufacture of Coffee grown and cured	**₹4,50,000**
Manufacture of Tea	**₹8,00,000**
Sale of Plants from Nursery	**₹2,00,000**

Solution :

Computation of Taxable Income for the Assessment Year 2014-15

Rule	Nature of Business	Agl Inc.	Non-Agl. Inc.
7A	Sale of centrifuged latex or cenex manufactured from rubber [65% is Agricultural Income]	4,55,000	2,45,000
7B	Sale of grown and cured coffee by seller in India [75% is Agricultural Income]	3,37,500	1,12,500
8	Growing and Manufacturing Tea [60% is Agricultural Income]	4,80,000	3,20,000
	Sale of plants from nursery	2,00,000	—
	Total	**14,72,500**	**6,77,500**

Computation of Tax Liability :

	₹
(a) Total Income (Agricultural Income + Non-agricultural Income)	21,50,000
(b) Tax on (a) above	4,75,000
(c) Total of (Agricultural Income + Basic Exemption Limit)	16,72,500
(d) Tax on (c) above	3,31,750
(e) Tax Payable (b) – (d)	1,43,250
Add: Education Cess @ 2%	2,865
Add: SHEC @ 1%	1,433
Total Tax Liability	1,47,548
Tax payable rounded off u/s 288B	1,47,550

(b) The following particulars are furnished for the Previous Year 2013-14

	₹
Net Proft as per Proft & Loss A/c (after deducting Depreciation of ₹ 6,80,000)	**90,97,000**
Depreciation allowable u/s 32 of Income Tax Act	**7,77,000**
Disallowable expenses	**85,000**
Deduction received u/s 10AA (as calculated)	**78,00,000**
Long Term Capital Gains (on sale of land)	**3,00,000**
Deduction received under Chapter VI A(as calculated):	
80G	**55,000**
80IB	**80,000**

Calculate Tax Liability assuming that the Assessee is an LLP, Firm, Individual, HUF, AOP and BOI.

Solution:

Statement showing computation of Total Income (applicable for all types of Assessee)

Particulars	₹	₹
Net Profit as per Profit & Loss A/c		90,97,000
Add: Depreciation	6,80,000	
Disallowable expenses	85,000	7,65,000 98,62,000
Less: Depreciation allowable u/s 32 of Income Tax Act.		7,77,000 90,85,000
Less: Deduction received u/s 10AA		78,00,000
Business Proft		12,85,000
Add: Long Term Capital Gains		3,00,000
Gross Total Income		15,85000
Deduction received under Chapter VI A :		
80G	55,000	
80IB	80,000	1,35,000
Total Income		14,50,000

Computation of Adjusted Total Income (applicable for all types of Assessee)

Particulars	₹
Total Income (as computed above)	14,50,000
Add: Deduction claimed u/s 80IB	80,000
Add: Deduction claimed u/s 10AA	78,00,000
Adjusted Total Income	**93,30,000**

Minimum Alternate Tax (Mat) and Alternate Minimum Tax (AMT)

Statement showing computation of Tax Liability and Alternate Minimum Tax and Credit on Alternate Minimum Tax for the Assessment Year 2014-15

Particulars	**Firm/ LLP**	**Individual/ HUF/AOP/BOI**
Tax on Long Term Capital Gains (@ 20% of ₹ 3,00,000)	60,000	60,000
Tax on balance Total Income (@ 30% for Firm or LLP and at Slab Rate for Individual or HUF or AOP or BOI)	3,45,000	1,75,000
	4,05,000	2,35,000
Add: Education Cess @ 2%	8,100	4,700
Add: Secondary and Higher Secondary Education Cess @ 1%	4,050	2,350
Tax Liability (a)	4,17,150	2,42,050
Tax on Adjusted Total Income @ 18.5%	17,26,050	17,26,050
Add: Education Cess @ 2%	34,521	34,521
Add: Secondary and Higher Secondary Education Cess @ 1%	17,261	17,261

Alternate Minimum Tax (b)	**17,77,832**	**17,77,832**
Tax Payable [Higher than (a) and (b)]	17,77,830	17,77,830
Alternate Minimum Tax credit [(a) – (b)]	13,60,680	15,35,780

Question 14:

(a) Who can sign the return of HUF, if HUF does not have a major member?

Answer :

If the HUF has no major members as its Karta, a return may validly be signed by the eldest minor member of the family who manages the affairs of the family [Sridhar Udai Narayan vs.CIT(1962) 45 ITR 577 (All.)]

(b) Is thumb impression valid for furnishing the Return of Income?

Answer :

The General Clauses Act accepts the thumb impression, as one of the modes of signing, valid and binding. [CIT vs. Kanhaiya Lal And Sons (2005) 273 ITR 425 (All.)]

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

Answer:

If an assessee is carrying on more than one business, he can follow cash system of accounting for one business and mercantile system (accrual system) of accounting for other business. Similarly, if he had more than one sources of income under the head Income from Other Sources, he can follow accrual system for one source of income under the head Income from Other Sources, and cash system for other sources of income.

(d) What can Assessing Offcer do when the assessment is not set aside for fresh assessment but annulled?

Answer:

Where an assessment is not set aside for fresh assessment but annulled, no extended limitation is available. However, if the original time limit is available, the Assessing Offcer may proceed from the stage at which illegality which resulted into the annulment of the assessment supervened and make the assessment afresh. [CIT vs.Mrs.Ratanbai N.K. Dubhash (1998) 230 ITR 495(Bom.)]

Question 15:

(a) Swastik Charitable Trust furnishes the following particulars, for the year 2013-2014:

(₹)

Sale price of capital assets	**18,30,000**
Expenses incurred in connection with sale of the asset	**40,000**
Cost of the asset sold (purchased in 2012-2013)	**6,00,000**
Compute Capital Gain in the following cases:	
(a) Cost of the new asset to be acquired	**17,00,000**
(b) Cost of the new asset to be acquired	**10,00,000**
(c) Cost of the new asset to be acquired	**5,00,000**

Solution:

Computation of Capital Gain: PY 2013-2014/AY 2014-2015

Particulars	**Case-I**	**Case-II**	**Case-III**
Sale price	18,30,000	18,30,000	18,30,000
Less: (i) Selling expenses	(-) 40,000	(-) 40,000	(-) 40,000
(ii) Cost of the asset Short-term Capital Gain	(-) 6,00,000	(-) 6,00,000	(-) 6,00,000
	11,90,000	11,90,000	11,90,000
Less: Exemption in respect of Capital Gain	11,90,000	4,00,000	Nil
Taxable Capital Gain	Nil	7,90,000	11,90,000

Note : 1. Cost of new asset - cost of asset sold: 10,00,000 - 6,00,000 = 4,00,000

2. Cost of new asset - cost of asset sold: 5,00,000 - 6,00,000 = Nil

(b) S, the Karta of a Hindu Undivided Family, was appointed as the treasurer of a private sector bank on his furnishing security of the family property valued at ₹ 3,00,000, as required by the service rules of the bank. S does not own any self-acquired property.

(i) Discuss how the remuneration of S as the treasurer should be assessed.

(ii) Will your answer be different if S had joined a partnership firm as a partner by contributing family funds of ₹ 50,000.

Solution:

(i) Remuneration from bank cannot be treated a return on the security of family property, pledged with the bank to secure the continuity of service. It cannot be treated as income of the HUF.

Remuneration is a compensation for services rendered by S, in his personal capacity on account of personal qualifications. S is assessable on remuneration as income from "salary". He can claim standard deduction under Sec. 16.

(ii) Membership of partnership has been obtained because of HUF funds and not because of personal skill or qualification of S. Therefore, any income from partnership frm will be treated as income of the HUF.

Question 16:

(a) In the case of Ms Shanti, you are required to compute the interest u/s 234A, 234B & 234C from the following details—

Tax on total income ₹ 3,00,000; Due date for filing the return 30.09.2014; Actual date of filing the return 1.10.2014 and tax paid on 30.09.2014 ₹ 3,00,000.

Solution :

Computation of interest u/s 234A

Particulars	**Asper assessed income**	
Tax Less : Advance tax paid TDS Amount on which interest is payable Period of default (October being part of a month shall be considered)	Nil Nil	₹ 3,00,000 Nil
		₹ 3,00,000 1 month
Interest u/s 234A (1% × ₹ 3,00,000 × 1 month)		**₹ 3,000**

Computation of interest u/s 234B

Since assessee did not pay any amount by way of advance tax, hence she is liable to pay interest u/s 234B.

Particulars	**Assessed income**
Shortfall	₹ 3,00,000
Period of default (From April to September)	6 months
Interest (1% × ₹ 3,00,000 × 6 months)	**₹ 18,000**

Computation of interest u/s 234C

Due date	**Advance Tax Payment** ₹	**Advance Tax paid** ₹	**Cumulative Advance Tax paid before due date** ₹	**Shortfall in Payment** ₹	**Surplus** ₹	**Months**	**Interest @ 1% p.m.** ₹
15.9.2013	30% of ₹ 3,00,000 = 90,000	Nil	Nil	90,000	—	3	2,700
15.12.2013	60% of ₹ 3,00,000 = 1,80,000	Nil	Nil	1,80,000	—	3	5,400
15.3.2014	100% of ₹ 3,00,000	Nil	Nil	3,00,000	—	1	3,000

	= 3,00,000						
							11,100

Total interest payable	Particulars	Amount
U/s 234A		3,000
U/s 234B		18,000
U/s 234C		11,100
	Total	**32,100**

(b) Ms. Sonam, a resident Indian, furnishes the details for the Assessement Year 2014-2015 :

Particulars	**Amount (₹)**
(1) Income from profession	**2,54,000**
(2) Share of income from a partnership in country X (tax paid in Country X for this income in equivalent Indian Rupees 14,000)	**70,000**
(3) Commission income from a concern in country Y (tax paid in country Y @ 20%, converted in equivalent Indian Rupees	**40,000**
(4) Interest on scheduled banks [other than savings account]	**20,000**

Ms. Sonam wishes to know whether she is eligible to any double taxation relief, if so, its quantum. India does not have any Double Taxation Avoidance Agreement with countries X and Y.

Solution :

(1) Computation of Total Income for the Assessment Year 2014-15

Particulars	**Amount (₹)**	**Amount (₹)**
(a) Income from Business or Profession:		
(i) Income from Profession	2,54,000	
(ii) Share of income in partnership frm in country X	70,000	3,24,000
(b) Income from other sources:		
(i) Interest from scheduled bank	20,000	
(ii) Commission earned in Country Y, assumed from other sources	40,000	60,000
Total Income		**3,84,000**

(2) Computation of Tax Liability on Total Income for the Assessment Year 2014-15

Particulars	**Amount (₹)**
Tax on Total Income of ₹ 3,84,000	18,400
Add: Surcharge on Income Tax	Nil
Add: Education Cess @ 2%	368
Add: Secondary and Higher Education Cess @ 1%	184
	18,952
Less: Double taxation relief : 1,10,000 x 4.94%	5,434

Tax Payable	**13,518**
Rounded off u/s 288B	**13,520**

Note : (i) Average rate of tax in the foreign country = 20% i.e. [(₹ 14,000 + 20% of ₹.40,000)/(70,000+40,000)] ×100 (ii) Average rate of tax in India = (18,952/3,84,000) × 100 = 4.94%

Question 17:

(a) Mr. M is a musician deriving income from foreign concerts performed outside India, ₹70,000. Tax of ₹ 14,000 was deducted at source in the country where the concerts were given. India does not have any agreement with that country for avoidance of double taxation. Assuming that Indian income of M is ₹ 3,00,000, what is the relief due to him under Sec. 91 for the Assessement Year 2014-2015.

Solution:

(1) Computation of Total Income for the Assessment Year 2014-15

Particulars	**Amount (₹)**
Indian Income	3,00,000
Foreign Income	70,000
Gross Total Income or Total Income	3,70,000

(2) Computation of Tax Liability on Total Income for the Assessment Year 2014-15

Particulars	**Amount (₹)**
Tax on Total Income	17,000
Add: Education Cess @ 2%	340
Add: Secondary and Higher Education Cess @ 1%	170
Less: Double taxation relief u/s 91 = ₹ 70,000 × 4.73%	3,311
Tax Payable	**14,199**

Note: 1. Average rate of Indian income tax: (17,510 ÷ 3,70,000) × 100 = 4.73%

2. Average rate of foreign income tax:

Relief is allowed either at the average rate of Indian Income Tax or the average rate of Foreign Income Tax = (14,000/70,000) × 100 = 20% whichever is lower. Accordingly, the relief has been allowed at the average rate of Indian Income tax.

(b) Deepak, a person of Indian origin was working in Austria since 1991. He returned to India for permanent settlement in May 2013 when he remitted money into India. For the valuation date 31.3.2014, the following particulars were furnished. You are required to compute the taxable wealth. The reason for inclusion or exclusion should be stated -

- **Building owned and let-out for 290 days for residence. Net maintainable rent ₹2,00,000 and the Market Value (Excess of Unbuilt Area over Specified Area is 20% of the Aggregate Area) ₹ 60 lakhs.**

- **Jewellery : (a) Purchased in April 2013 out of money remitted to India from Austria ₹24,00,000**
  (b) Purchased in May 2013 out of sale proceeds of motor-car brought from abroad and sold for ₹80 lakhs.
- **Value of interest in urban land held by a firm in which he is a partner ₹20 lakhs.**
- **Bonds held in companies ₹20 lakhs.**
- **Motor car used for own business ₹ 50 lakhs.**
- **Vacant house plot of 480 sq. mts. (purchased in December 2004) market value of ₹40,00,000.**
- **Cash in hand ₹ 90,000.**
- **Urban land purchased in the year 2013 out of withdrawals of NRE Account ₹ 30,00,000.**

Solution :
Assessee : Abhishek **Valuation Date : 31.3.2014** **Assessment Year : 2014-15**

Computation of Net Wealth

Nature of the Asset	₹	₹	**Reasons**
Value of the House		35,00,000	Asset u/s 2(ea). Working Note 1
Jewellery: Purchased in April 2013	24,00,000		
Less: Exempt u/s 5(v)	(24,00,000)	Nil	Asset u/s 2(ea). Purchased out of money brought into India
Jewellery: Purchased in May 2013	80,00,000		
Less: Exempt u/s 5(v)	(80,00,000)	Nil	Asset u/s 2(ea).Purchased out of sale proceeds of assets brought into India
Interest in Urban Land held by firm		20,00,000	Deemed Asset u/s 4(1)(b)
Bonds held in companies		Nil	Not an asset u/s 2(ea)
Motor car		50,00,000	Asset u/s 2(ea). Not held as stock-in-trade
Vacant House Plot (480 sq. mts.)	40,00,000		
Less: Exempt u/s 5(vi)	(40,00,000)	Nil	Asset u/s 2 (ea).House/part of house/ plot less than 500 sq.mts.
Cash in hand		Nil	Since not exceeding ₹ 50,000
Urban Land Purchased	30,00,000		Purchased out of money brought into India
Less: Exempt u/s 5(v)	(30,00,000)	Nil	
NET WEALTH		1,05,00,000	
Less : Basic Exemption		30,00,000	
Net Taxable Wealth		75,00,000	
Tax Payable @ 1%		75,000	

(1) Working Notes: Valuation of Building :

Net Maintainable Rent(NMR) = ₹2,00,000

Capitalized Value of NMR = NMR×12.5 (Owner of the land) = ₹ 2,00,000 × 12.5 = ₹25,00,000 *Add* : Premium for excess of unbuilt area (20%) over specifed area = 40% of CNMR = ₹10,00,000

VALUE OF THE HOUSE ₹ 35,00,000.

Question 18:

(a) Compute the taxable income of a Chamber of Commerce from the following data.

	1 ₹	2 ₹	3 ₹
Gross receipts for specific services rendered to members	**2,60,000**	**2,60,000**	**2,60,000**
Expenses incurred in connection with the above	**60,000**	**1,10,000**	**2,00,000**
Interest on bank deposits	**40,000**	**' 40,000**	**80,000**
Receipt from members	**2,00,000**	**3,00,000**	**2,60,000**
Expenditure incurred on members	**1,50,000**	**4,10,000**	**3,50,000**

Solution:

Profit and gains of business and profession			
Net income from rendering specific services (Gross receipts-Expenses)	2,00,000	1,50,000	60,000
Less: Deficiency set off (maximum to the extent of 50% of total assessable income before set off of deficiency i.e. ₹1,90,000 and ₹1,40,000 in case of 2 and 3 respectively)	---	95,000	60,000
(A)	2,00,000	55,000	Nil
Interest on bank deposit under other heads	40,000	40,000	80,000
Less: Deficiency although allowable upto 50% of total assessable income which could not be set off against business income			10,000
Income (B)	40,000	40,000	70,000
Gross Total Income (A + B)	2,40,000	95,000	70,000
Less: Deduction under sections 80C to 80U	Nil	Nil	Nil
	2,40,000	95,000	70,000

1. Surplus of ₹ 50,000 under case 1 is not taxable as it is from mutual activity.
2. Deficiency under case 2 and 3 would not have been allowed but for the benefit given under section 44A.
3. Assessable income in case of 2 and 3 is as under:

	Case I ₹	Case II ₹
Surplus from specific services	1,50,000	60,000
Interest income	40,000	80,000
	1,90,000	1,40,000
Less: Under section 80C to 80U	Nil	Nil
	1,90,000	1,40,000

4. In case 3, 50% of the assessable income is ₹70,000 (i.e. 50% of ₹1,40,000) but first it will be set off from business income which in this case is ?60,000 and the balance shall be set off from other income.

(b) X Airlines incorporated as a company in USA operates its flights to India and vice versa during the previous year 2013-14 and collects charges of ₹1,25,00,000 for carriage of passengers and cargo out of which ₹65,00,000 were received in US dollars for the passenger fare booked from New York to Mumbai. The total expenses for the year on operation of such flights were ₹1, 95,00,000. Compute the income chargeable to tax of the foreign airlines.

Solution:

As per section 44BBA, in case of an Airlines the income is presumed to be 5% of the following:

(i) the amount paid or payable (whether' in or out of India) to the assessee or to any person on his behalf on account of the carriage of passengers, livestock, mail or goods from any place in India, and

(ii) the amount received or deemed to be received in India by or on behalf of the assessee on account of the carriage of passengers, livestock, mail or goods from any place outside India. Hence, the taxable income will be determined as under:

	Passenger fare booked from Mumbai to New York whether paid in India or not ₹	Passenger fare booked from New York to Mumbai if received in India ₹
Fare	60,00,000	65,00,000
Taxable income	3,00,000	3,25,000

Note—If the passenger fare booked from New York to Mumbai in not received in India, then such fare shall not be included for calculating presumptive income.

Question 19:

(a) Construction Company Ltd. has let-out a premise with effect from 1.10.2013 for monthly rent of ₹2.5 lakh. The lease is valid for 10 years and the tenant has made a deposit equivalent to 3 months rent. The tenant has undertaken to pay the municipal taxes of the premises amounting to ₹ 3 lakh. What will be the value of the property under Schedule III of the Wealth Tax Act for assessment to wealth tax?

Solution :

Assessee: Property Company Ltd. **Valuation Date: 31.3.2014** **Assessment Year: 2014-15**

Computation of Value of Let-out Property

Actual Annual Rent Receivable - ₹ 2,50,000 × 12 Months	30,00,000
Add: Municipal Taxes borne by the Tenant	3,00,000
GROSS MAINTAINABLE RENT	33,00,000
Less: Municipal Taxes levied by the Municipal Authority	3,00,000
Less: 15% of Gross Maintainable Rent ₹ 30,00,000 × 15%)	4,50,000
NET MAINTAINABLE RENT	25,50,000

Value of the Property = Capitalized Value of NMR

NMR × 8 (unexpired period of lease is less than 50 years) = ₹ 25,50,000×8 = ₹ **2,04,00,000**

(b) Explain the role of market forces in determination of Arm's Length Price?

Answer:

Role of market forces in determining the "Arm's Length Price"

In case of transactions between Independent enterprises, the conditions of their commercial and fnancial relations (eg. The price of goods transferred or services provided and the conditions of the transfer or provision) are, ordinarily, determined by the market force.
Whereas,
In case of transactions between MNEs (Multinational Enterprises), their commercial and fnancial relations may not be affected by the external forces in the same way, although associated enterprises often seek to replicate the dynamics of the market forces in their dealings with each other.

(c) What are the difficulties arises in applying the Arm's Length Principle?

Answer:

Diffculties in applying the arm's length principle

The arm's length principle, although survives upon the international consensus, does not necessarily mean that it is perfect. There are diffculties in applying this principle in a number of situations.

The most serious problem is the need to fnd transactions between independent parties which can be said to be exact compared to the controlled transaction.

It is important to appreciate that in an MNE system, a group frst identifes the goal and then goes on to create the associated enterprise and fnally, the transactions entered into. This procedure obviously does not apply to independent enterprises. Due to these facts, there may be transactions within an MNE group which may not be between independent enterprises.

Further, the reductionist approach of splitting an MNE group into its component parts before evaluating transfer pricing may mean that the benefts of economies of scale, or integration between the parties, is not appropriately allocated between the MNE group.

The application of the arm's length principle also imposes a burden on business, as it may require the MNE to do things that it would otherwise not do (i.e. searching for comparable transactions, documenting transactions in detail, etc).

Arm's length principle involves a lot of cost to the group.

Question 20:

(a) Kango Inc. a US Company, sells Laser Printer Cartridge Drums to its Indian Subsidiary Quality Printing Ltd at $ 30 per drum. Basin Solutions Inc. has other takers in India for its Cartridge Drums, for whom the price is $ 40 per drum. During the year, Kango had supplied 12,000 Cartridge Drums to Quality Printing Ltd.

Determine the Arm's Length Price and taxable income of Quality Printing Ltd if its income after considering the above is ₹ 75,00,000. Compliance with TDS provisions may be assumed and Rate per USD is ₹ 60. Also determine income of Basin Inc.

Solution:

A. Computation of Total Income of Quality Printing Ltd.

Particulars	₹	₹
Total Income before adjusting for differences due to Arm's Length Price		75,00,000
Add: Difference on account of adopting Arm's Length price [12,000 x $ 30 × ₹60]	2,16,00,000	
Amount actually paid to Doc Solutions [12,000 × $ 40 × ₹60]	(2,88,00,000)	
Incremental Cost on adopting ALP U/s 92(3), Taxable Income cannot be reduced on applying ALP. Therefore,	72,00,000	
Total Income of Quality Printing Ltd		75,00,000

B. Computation of Total Income of Kango Inc.

The provisions relating to taxing income of Kango Inc., on applying Arm's Length Price for transactions entered into by a Foreign Company is given in Circular 23 dated 23.7.1969, which is as follows:

(i) **Transactions Not Taxable in India :** Transactions will not be subject to tax in India if transactions are on principal-to-principal basis and are entered into at ALP, and the subsidiary also carries on business on its own.

(ii) **Transactions Taxable in India** if the Indian Subsidiary does not carry on any business on its own. The following are the other considerations in this regard -

  (i) Adopting ALP does not affect the computation of taxable income of Kango Inc. if tax has been deducted at source or if tax is deductible.

  (ii) Where ALP is adopted for taxing income of the Parent Company, income of the recipient Company (i.e. Quality Printing Ltd) will not be recomputed.

(b) R Ltd. has two units. One of these units is situated in Uttrakhand for which A Ltd. is claiming 100% deduction of profits under section 80-IC. A Ltd. filed the return of income as under:

	₹
Business income	
Profit from non-eligible business	**54,00,000**
Profit for business eligible for deduction u/s 80-IC	**32,00,000**
Gross total income	**86,00,000**
Less: Deduction u/s 80-IC	**32,00,000**
	54,00,000

Eligible unit has purchased goods worth ₹6 crores from non-eligible unit whose fair market value as determined by A.O. is ₹6.30 crore. Compute the total income of R Ltd.

Solution:

	₹
Gross total income as computed above	86,00,000
Less: Deduction u/s 80-IC (32,00,000-30,00,000) (Lower value of purchase price due to which excess profit has been computed)	2,00,000
Total income	84,00,000

(c) R Ltd. furnishes the following return of income for the previous year 2013-14.

	₹
Business income of a unit eligible for deduction u/s 80-IE	**49,00,000**
Profit from other unit B	**81,00,000**
	1,30,00,000
Less: Deduction u/s 80-IE	**49,00,000**
Total income	**81,00,000**

Unit A made a sale of ₹8.4 crores to unit B. Assessing Officer referred the determination of FMV to TPO. TPO determines the arm's length price to be 8.1 crore.

Determine the total income of the assessee.

Solution:

	₹
Gross total income as computed	1,30,00,000
Less: Deduction u/s 80-IE (49,00,000 - 30,00,000) (Overstated sale price 8.4 - 8.1 crores = 30,00,000)	19,00,000
Total income	1,11,00,000