

Problem 5.32-6 - Discuss the following:

1. X Co. Ltd., having its registered office in Mumbai, plies two ocean-going vessels which it owns. The registered tonnage of two vessels are 47,549 tonnes and 800 kgs. and 25,759 tonnes and 400 kgs. respectively. The first vessel, in the accounting year 2008-09, was operated for 360 days and the second for 199 days.

The accounts of the company reveal the following results:

i Profit from core shipping activity	Rs. 60.50 lakh
ii Profit from incidental activity	Rs. 15,000

Compute the tax payable by the company for the assessment year 2009-10, taking note of the new provisions of the law relating to taxation of income of shipping companies. Also indicate the specified conditions for the applicability of the new procedure.

2. M, an individual, is 70 years of age. He is a sitting member of the State Assembly of Karnataka and for the financial year 2008-09 received the following amounts for the Assembly Secretariat:

i. Basic pay	Rs. 10,000 per month
ii. Constituency allowance	Rs. 8,000 per month
iii. Telephone allowance	Rs. 4,000 per month
iv. Electricity allowance	Rs. 3,000 per month [from June, 2008 onwards]

He owns a house in Delhi which has been let out at Rs. 5,000 per month. He received rent for 10 months only, the house having remained vacant for two months. Municipal taxes of Rs. 1,200 were paid by the tenant. Interest of Rs. 14,000 was paid by M on amount borrowed by him to buy the house.

M has an agricultural income of Rs. 55,000.

Compute his tax liability for the relevant assessment year. [NOVEMBER 2005]

Pointwise answer :

1. Computation of daily tonnage income

First 1000 tons @ Rs. 46 for each 100 tons
 Next 9,000 tons @ Rs. 35 for each 100 tons
 Next 15,000 tons @ Rs. 28 for each 100 tons
 Balance [(22,500† tons @ Rs. 19 for each 100 tons) and (800† tons @ 19 for each 100 tons)]

Ship I	Ship II
460	460
3,150	3,150
4,200	4,200
4,275	152
12,085	7,962

Computation of tonnage income	43,50,600
Ship I (Rs. 12,085 × 360 days)	15,84,438
Ship II (Rs. 7,962 × 199 days)	1,59,162
Tonnage income (rounded off)	15,93,600

Computation of tax payable	18,33,927
Tax on tonnage income @ 30.9% [see also para 532]	4,635
Tax on other income	18,38,562

As income under the tonnage tax scheme is lower than normal income (given in question), the tonnage tax scheme is to be taken for computation of tax payable.

2. Computation of total income	Rs.
Basic pay [Rs. 10,000 × 12]	1,20,000
Constituency allowance [see Note I]	72,000
Telephone allowance [see Note I]	48,000
Electricity allowance [see Note I]	30,000
Salary income	2,70,000
Income from house property [see Note III]	21,000
Gross total income	2,91,000
Less: Deduction under sections 80C to 80U	Nil
Total income	2,91,000

†Rounded off to the nearest multiple of 100 tons.

Problem 5.32-7 : May 2004*Miscellaneous*

1410

	Rs.
<i>Computation of tax payable</i>	
Tax on total income [<i>i.e.</i> , tax on Rs. 3,46,000 : Rs. 16,700—tax on Rs. 2,50,000 : Rs. 5,500]	11,200
Add: Education cess [2% of Rs. 11,200]	224
Add : Secondary and higher education cess (1% of income-tax and surcharge)	112
Tax liability	11,540

Notes:

I. Under section 10(17), any allowance other than daily allowance received by any member of State Legislature is exempt up to Rs. 2,000 per month in aggregate [*see* para 38.33].

II. Computation of house property income

	Rs.
Gross annual value [Rs. 5,000 × 10]	50,000
Less: Municipal taxes	Nil
Net annual value	50,000
Less: Deductions under section 24	
Standard deduction [30% of Rs. 50,000]	15,000
Interest on borrowed capital	14,000
House property income	21,000

III. Tax on total income is calculated as per the scheme of partial integration of agricultural income with non-agricultural income.

Problem 5.32-7 - Explain the doctrine of form and substance in the context of tax planning. [MAY 2004]

■
See para 525.

Problem 5.32-8 - Explain the circumstances under which the Assessing Officer can resort to provisional attachment of the property of the assessee. Also state the period of time for which such attachment can take place. [NOVEMBER 2003]

■
See problem 5.32-12 (Annex 5).

Problem 5.32-9 - "Tax Recovery Officer can recover the arrear demands from the assessee in default out of sale proceeds of the property attached after making a proclamation". How such proclamation can be made under the Act? [NOVEMBER 2003]

■
As per Schedule II to the Income-tax Act, when any sale of movable property is ordered by the Tax Recovery Officer, the Tax Recovery Officer shall issue a proclamation, in the language of the district, of the intended sale, specifying the time and place of sale and whether the sale is subject to confirmation or not.

Such proclamation shall be made by beat of drum or other customary mode—

(a) in the case of property attached by actual seizure—

(i) in the village in which the property was seized, if the property was seized in a town or city, then, in the locality in which it was seized; and

(ii) at such other places as the Tax Recovery Officer may direct.

(b) in the case of property attached otherwise than by actual seizure, in such places, if any, as the Tax Recovery Officer may direct.

A copy of the proclamation shall also be affixed in a conspicuous part of the office of the Tax Recovery Officer.

Problem 5.32-10 - X, a stock broker has defaulted with regard to his income-tax payments and the Assessing Officer has attached his membership card of stock exchange under section 281B. X contends that the membership card is not transferable and is not his personal asset. Discuss the validity of attachment of the card by the Assessing Officer in the context of section 281B. [NOVEMBER 2002 (New)]

■
Right of membership of a stock exchange is merely a personal privilege granted to a member, it is non-transferable and incapable of alienation by the member or his legal representatives and heirs except to the limited extent as provided in the rules on fulfilment of conditions provided therein. The nomination wherever provided for is also not automatic. It is hedged by rules.

In *Vinay Bubna v. Stock Exchange* [1999] 6 SCC 215, on consideration of similar rules in respect of Bombay Stock Exchange, the Supreme Court held that membership of the stock exchange is a personal permission from the exchange to exercise the rights and privileges attached thereto. It is not a private asset.

The membership right in question is not the property of the assessee and, therefore, it cannot be attached under section 281B—*Stock Exchange, Ahmedabad v. CIT* [2001] 115 Taxman 471 (SC).

Problem 5.32-11 - X, an individual assessee, died intestate on October 1, 2007 and left three sons Y, Z and A. He had filed a return of income for the assessment year 2006-07, before his death. The Assessing Officer issued a notice of hearing to Y one of the sons, who appeared before him and complied with the notice. The assessment was made on him as legal representative of the deceased. In appeal, a plea was taken that since Z and A were not brought on record, the assessment on Y was not valid. Discuss, how far such a plea is sustainable in law. [NOVEMBER 2002]

■ In the instant case, Y did not raise an objection before the Assessing Officer that unless and until notices to all the other legal representatives were sent, assessment orders could not be made. He raised this question for the first time in the appeals preferred by him to the Commissioner (Appeals) and thereafter before the Tribunal. It appeared rather curious that Y who had voluntarily complied with the notice issued by the Assessing Officer, should raise this issue; no other legal representative of the deceased had come forward with such a plea.

It is incorrect to hold in these circumstances that the assessment orders made were null and void. They were not. At worst, they were defective proceedings or irregular proceedings.

The principle emerging from the decision in *Estate of Late Rangalal Jajodia v. CIT* [1971] 79 ITR 505 (SC), is that an omission to serve or any defect in the service of notices provided by procedural provisions does not efface or erase the liability to pay tax, where such liability is created by distinct substantive provisions. Any such omission or defect may render the order made irregular depending upon the nature of the provision not complied with, but certainly not void or illegal.

Problem 5.32-12 - When does the Assessing Officer resort to a provisional attachment? [NOVEMBER 2001]

■ Section 281B provides provisional attachment to protect revenue in certain cases—

- The proceedings for the assessment or reassessment of any income which has escaped assessment should be pending for attachment to be made.
- Such attachment is necessary for protecting the interest of revenue according to the Assessing Officer.
- The previous approval of the Chief Commissioner, Commissioner, Director General or Director has been obtained by the Assessing Officer.
- The Assessing Officer may by an order in writing, attach provisionally any property belonging to the assessee in the manner provided in the Second Schedule.
- For the purpose of attachment, proceedings under section 132(5) shall be deemed to be proceedings for the assessment or reassessment of any income which has escaped assessment.
- Every such provisional attachment shall cease to have effect after the expiry of a period of six months from the date of the order. However, the aforesaid period of six months may be extended further by the Chief Commissioner, Commissioner, Director General or Director such that the total period of extension does not exceed two years.

Problem 5.32-13 Distinguish between tax planning and tax evasion. [MAY 2001]

■ See para 525.4.

Problem 5.32-14 - Discuss the validity as well as consequences of the alienation of assets of a business by an assessee during the pendency of a proceeding under the Income-tax Act. [MAY 1999]

■ If during the pendency of any proceedings under the Act or after completion thereof an assessee creates a charge on or parts with the possession by way of sale, mortgage, gift, exchange or any other mode of transfer whatsoever of any of his assets in favour of any other person before service of notice of Tax Recovery Officer, then such charge shall be void as against any claim in respect of any tax or any other sum payable by the assessee due to the completion of said proceeding or otherwise.

However, such charge or transfer shall not be void if it is made—

- a. for adequate consideration and without notice of the pendency of the proceedings, or instant notice of such tax or other sum payable by the assessee; or
- b. with the previous permission of the Assessing Officer.

The provisions of section 281 are applicable where the assessee's liability actual or probable, exceeds Rs. 5,000 and asset charged or transferred exceed Rs. 10,000 in value.

6 ANNEX

Questions set for CS (Final) examinations and answers from June 2003 to June 2008

6.1 Basic concepts

6.2 Residential status and tax incidence

Problem 6.2-1 - X Ltd., a foreign company, owns a property in Mumbai. It is given on rent (rent being 5,000 US dollar per month) to Y Ltd., another foreign company. The two companies are non-residents in India. The agreement is made outside India. Rent is payable in foreign currency outside India. As per agreement, rent is accrued outside India. Discuss whether the rental income of X Ltd. is chargeable to tax in India. [DECEMBER 2007]

■
See para 32.2.

Problem 6.2-2 - How will the income be determined in case of outsourcing of business processes by non-residents/foreign companies to Business Process Outsourcing (BPO) units in India under section 9. [JUNE 2006]

■
See para 32.1.

Problem 6.2-3 - The incidence of income-tax of a company depends upon its residential status. Explain. [JUNE 2004 (New)]

■
See para 29.

6.3 Income exempt from tax

Problem 6.3-1 - Undertaking - A is set-up by X Ltd. in Domestic Tariff Area (DTA) and started manufacture or production of computer software in the financial year 2003-04. It got approval as 100% EOU on June 7, 2008. Discuss whether it will be eligible for deduction under section 10B. If yes, how and for what period the deduction will be allowed? [DECEMBER 2005]

■
Yes, X Ltd. will be entitled to deduction under section 10B from the assessment year 2009-10 to the assessment year 2010-11. See para 40.8.

6.4 Salaries

Problem 6.4-1 - A company wants to issue sweat equity shares to its key employees. Explain briefly the concept and its tax implications on the recipient and the company. [JUNE 2008]

■
See para 535.5.

Problem 6.4-2 A company reimburses a sum of Rs. 15,000 during the financial year 2008-09 to one of its employees on account of medical expenditure. Discuss the tax liability of the employer and employee. [JUNE 2007]

■ Reimbursement of medical expenditure of Rs. 15,000 is not a perquisite chargeable to tax in the hands of the employee. In the hands of employer, however, Rs. 15,000 is chargeable to tax under fringe benefit tax.

Problem 6.4-3 - "Employees' tax borne by the employer to the extent it relates to perquisites-in-kind is not chargeable to tax." Comment. [DECEMBER 2003]

■ For provisions of section 10(10CC), see para 38.23A. In the present problem, in view of the aforesaid provisions, the employees tax paid by the employer with respect to perquisites-in-kind is exempt from tax in the hands of the employees.

6.5 Income from house property

6.6 Profits and gains of business or profession

Problem 6.6-1 - A company claims deduction of certain expenditures in computation of its total income. Consider the allowability or otherwise of the following expenditures giving brief reasons for your answers:

1. Payments made by the company for sponsoring a sports tournament.
2. Water pollution treatment plant installed permanently in the factory in compliance with statutory requirements.
3. As a holding company, it has borrowed money and advanced the same to its subsidiary in whose business it has deep interest. The subsidiary uses the same for its business. The company claims interest paid on such borrowings as a deduction.
4. Expenditure incurred for earning share income from a firm.
5. Provision made in the accounts of the company on a scientific basis in respect of liabilities estimated to arise under warranty provided to customers in respect of products sold. [JUNE 2008]

■ The answer is as under:

1. Such expenditure is in the nature of business promotion through advertisement. It is allowable as revenue expenditure.
2. This type of expenditure is incurred to satisfy a statutory stipulation. It is allowable as revenue expenditure.
3. The holding company is entitled to claim deduction under section 36(1)(iii) on account of interest on borrowed capital.
4. Expenditure incurred for earning share income from a firm is not allowable as deduction in view of the provisions of section 14A. See para 7.1.
5. Such a provision is allowable if the warranty arises as per the terms of the contract of sale.

Problem 6.6-2 Discuss the following:

1. What are the considerations that should weigh with a company while deciding on whether to issue equity shares or debentures? Discuss briefly.
2. X Ltd. gets a compensation of Rs. 2 crore from Y Ltd., an Indian company, on termination of an agreement. How would you decide whether this compensation is taxable or not in the hands of X Ltd.
3. What is the tax treatment of expenditure on issue of bonus shares? [JUNE 2007]

■ Pointwise answer:

1. See para 164.4.
2. See para 16.1-14.
3. In *CIT v. General Insurance Corpn.* [2006] 156 Taxman 96, the Supreme Court held that the expenses incurred by the assessee in connection with the issue of bonus shares are expenditure of revenue nature.

Problem 6.6-3 - Discuss the following :

1. A company purchased a machine on March 1, 2006 for Rs. 16 lakh for its laboratory so as to improve the quality of its product.

The research activity for which was purchased ceased in December, 2007 and the machine was brought into business proper on December 21, 2007 (market rate being Rs. 2,50,000); depreciation admissible @ 15 per cent depreciated value of relevant block of assets on April 1, 2007 was Rs. 14 lakh; the scientific research machine was sold for Rs. 4 lakh on April 4, 2008.

What would be the amount of depreciation for the assessment year 2009-10 and the profit taxable under 41(3)?

Would it made any difference in your answer if the research activity for which the machine was purchased had ceased on December 21, 2007 (market rate of the machine Rs. 2,50,000) and the machine was sold on April 4, 2008 without using it for another purpose, the sale being Rs. 4 lakh or Rs. 15 lakh.

2. State the rules relating to amortisation of expenditure incurred on voluntary retirement scheme.

3. State the special provisions for computing profit of business of plying/hiring/leasing of goods carriages.

4. List out a few important considerations to be taken into account for obtaining maximum advantage in the case of a company in availing deduction under section 35D. [JUNE 2005]

■
Pointwise answer :

1. As the scientific research is related to the business of the assessee, the whole of capital expenditure of Rs. 16,00,000 is allowable as deduction under section 35(2)(ia) for the assessment year 2006-07.

The machine is brought into business proper in December 2007. Profit arising on sale of machinery is, in this case, not chargeable to tax under section 41(3).

Tax treatment of depreciation is as under:

Depreciated value of the block of assets on April 1, 2007	Rs. 14,00,000
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Add: Cost of machine transferred from laboratory in December 2007 [i.e., Rs. 16,00,000 - deduction of Rs. 16,00,000 claimed under section 35 - see para 109.10-2]	Nil
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Written down value	14,00,000
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Less: Depreciation for the previous year 2007-08 [15% of Rs. 14,00,000]	2,10,000
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Depreciated value of the block on April 1, 2008	11,90,000
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Less: Sale proceeds of machine sold on April 4, 2008	4,00,000
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Written down value	7,90,000
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Less: Depreciation for the previous year 2008-09 [15% of Rs. 7,90,000]	1,18,500
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Depreciated value of the block on April 1, 2009	6,71,500
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There will be no capital gain or loss in this case [see para 173.1-3].

Tax treatment in case the machine is sold without using it for another purpose

	If sale price is	
	Rs. 4 lakh Rs.	Rs. 15 lakh Rs.
Amount chargeable under section 41(3) [i.e., sale proceeds but subject to maximum of deduction claimed under section 35 for the assessment year 2006-07]	4,00,000	15,00,000
Capital gain under section 45		
Sale proceeds	4,00,000	15,00,000
Less: Cost of acquisition [see para 175.2-2]	16,00,000	16,00,000
Short-term loss	(-) 12,00,000	(-) 1,00,000

2. See para 121B.

3. See para 162.5.

4. See para 121.

Problem 6.6-4 Write short note on additional depreciation. [DECEMBER 2004]

■
See para 109.8.

Problem 6.6-5 - Discuss the following—

1. State the provisions relating to 'amortisation of preliminary expenses' and enumerate tax planning measures in relation thereto.
2. Explain in brief the provisions of section 43A.
3. X Ltd. own Plant-A and Plant-B (depreciation rate 30 per cent). Depreciated value of the block as on April 1, 2008 is Rs. 6,90,000. Plant-B is destroyed by fire on June 6, 2008. The insurance company pays Rs. 7,20,000 as compensation on September 4, 2008. On the same day, the company purchases Plant-C for Rs. 7,10,000. Find out the tax consequences.
4. Write short note on amortisation of expenditure under section 35DD in case of amalgamation or demerger. [JUNE 2004 (Old)]

Pointwise answer:

1. See para 121
2. See para 160.

	Rs.
3. Written down value on April 1, 2008	6,90,000
Add: Purchases made during the previous year 2008-09	7,10,000
Total	14,00,000
Less: Sale proceeds of assets sold, demolished or destroyed during the previous year 2008-09	7,20,000
Written down value on March 31, 2009	6,80,000
Depreciation allowable for the previous year 2008-09 [Rs. 6,80,000 × 30%]	2,04,000
Written down value on April 1, 2009	4,76,000

Note: Section 50 is not applicable and hence, no capital gains tax liability arises.

4. See para 121A.

Problem 6.6-6 - X Ltd. is a wholly-owned subsidiary company of Y Ltd. an Indian company. X Ltd. owns Plant A and Plant B (depreciation rate 30 per cent, depreciated value of the block Rs. 3,00,000 on April 1, 2008). Plant B was purchased and put to use on November 10, 2006 (cost being Rs. 70,000). Plant B is transferred by X Ltd. to Y Ltd. on December 14, 2008 for Rs. 20,000. It is put to use by Y Ltd. on the same day. Y Ltd. owns Plant-C on April 1, 2008 (depreciation rate 30 per cent, depreciated value Rs. 60,000). Find out the amount of depreciation in the hands of X Ltd. and Y Ltd. for the assessment year 2009-10. [JUNE 2004 (New)]

Computation of admissible depreciation

Depreciated value on April 1, 2008	3,00,000
Add: Actual cost of Plant B acquired (see Note)	-
Total	3,00,000
Less: Sale proceeds of Plant B transferred to Y Ltd.	20,000
Written down value on March 31, 2009	2,80,000
Depreciation admissible for the previous year 2008-09	84,000*

Note: Computation of actual cost of Plant-B in the hands of Y Ltd.

Actual cost of Plant-B to X Ltd. on November 10, 2006	70,000
Less: Admissible depreciation for the previous year 2006-07 (70,000 × 30% × 50%)	10,500
Written down value on April 1, 2007	59,500
Less: Admissible depreciation for the previous year 2007-08 (30% of Rs. 59,500)	17,850
Written down value on April 1, 2008	41,650

X Ltd.	Y Ltd.
Rs.	Rs.
3,00,000	60,000
-	41,650
3,00,000	1,01,650
20,000	-
2,80,000	1,01,650
84,000*	24,248†

*30% of Rs. 2,80,000.

†30% of Rs. 60,000 + 30% of 50% of Rs. 41,650.

Problem 6.6-7 Discuss the admissibility or otherwise of the following claims in connection with assessment to income-tax. They do not necessarily relate to the same assessee :

1. An expenditure of Rs. 1 lakh is incurred on the occasion of the silver jubilee of the company for presentation of silver mementos to shareholders and directors, the value of each memento being Rs. 1,000 only.
2. An assessee carries on business in respect of which it holds tenancy rights. It carries out improvements to the said building at a cost of Rs. 2 lakh and claims depreciation @ 10 per cent thereon. The Assessing Officer rejects the claim on the ground that the assessee is not the owner of the building.
3. Excise duty amounting to Rs. 2 lakh for the period 2008-09 is paid by the company by September 30, 2009 before furnishing the return of income for the assessment year 2009-10.
4. A criminal case is filed against a company under the Essential Commodities Act, 1955. The company incurs litigation expenses amounting to Rs. 50,000 to defend the directors. The directors are ultimately acquitted.
5. A company is generating electricity privately for its factory. Later, at its expense, electric lines are laid from the trunk road to the factory. It pays Rs. 5 lakh to the State Electricity Board as its contribution for this purpose. The ownership of the power-line will vest with the State Electricity Board.
6. X and Y are two shareholders of X Ltd., a closely held company. X holds 55 per cent share capital. On January 30, 2009, X transfers his shares to A. X Ltd. wants to set off brought forward loss of Rs. 4 lakh (business loss Rs. 1 lakh; unadjusted depreciation Rs. 3 lakh) of the previous year 2007-08 against the income of the previous year 2008-09 (i.e., Rs. 9 lakh). Can it do so ? [JUNE 2003]

■
Pointwise answer:

1. Directors and shareholders both contribute in the prosperity of the company. Presentation of silver mementos to the directors and shareholders on the occasion of silver jubilee is to recognise their services. The expenditure has been incurred on account of commercial expediency and qualifies for deduction under section 37(1) provided the company is a prosperous one.
2. Explanation 1 to section 32(1) allows depreciation on capital expenditure on building provided the assessee holds a lease or other right of occupancy in respect of said building.
3. Excise duty has been paid before the due date of furnishing return under section 139(1) in respect of the previous year in which the liability to pay such sum is incurred. Hence, it is deductible for the assessment year 2009-10 as per section 43B.
4. It is deductible under section 37(1).
5. The new electric power lines are laid to run the factory efficiently. The fixed capital of the business is not affected. The crux of the issue is that ownership of the power lines will vest with the State Electricity Board. Hence, contribution of Rs. 5 lakh paid to the State Electricity Board is allowable as revenue expenditure under section 37(1).
6. X Ltd. is a closely held company in which shareholders having 51 per cent voting right on March 31, 2008 and on March 31, 2009 are different. Only unadjusted depreciation can be set-off but not brought forward loss by virtue of section 79. Income of previous year 2008-09, will be Rs. 6 lakh (i.e., Rs. 9 lakh — Rs. 3 lakh).

Problem 6.6-8 Discuss whether the following are deductible :

1. Payments made by your company to obtain a report of consultant for improving efficiency of business.
2. Compensation paid by your company for breach of a contract to sell plant and machinery.
3. Payment to a school where children of your company's employees are getting education.
4. Your company is engaged in the business of letting out of premises. Payment is made for getting premises vacated. [JUNE 2003]

■
Pointwise answer:

1. Payments made by the assessee-company to obtain the report of consultants for improving efficiency of business is allowable as a revenue expenditure — *CIT v. Crompton Engineering Co. Ltd.* [2000] 242 ITR 317 (Mad.).
2. Where compensation is paid for breach of contract to purchase capital assets, the payment of compensation is capital expenditure — *Swadeshi Cotton Mills Co. Ltd. v. CIT (No. 2)* [1967] 63 ITR 65 (SC).
3. Payment to school where children of its employees are getting education is deductible revenue expenditure — *CIT v. Travancore Cochin Chemicals Ltd.* [2000] 109 Taxman 91 (Ker.).
4. Where the assessee-company engaged in business of letting out premises, and payment is made to a party to get vacant possession of its premises, which it let out to another party subsequently on higher rent is deductible — *CIT v. Auto Distributors Ltd.* [1994] 210 ITR 222 (Cal.).

Problem 6.6-9 X Ltd. purchased machinery for scientific research for Rs. 15 lakh in the previous year 2007-08 and whole of it was allowed as deduction under section 35. In the previous year 2008-09, the research project was over. It proposes

to sell the machinery for Rs. 14 lakh. It is considering whether (i) to sell machinery without using it in business; or (ii) to sell the machinery after using it in business for 2 months. The profit before current year depreciation is Rs. 38 lakh. Written down value of the machinery on April 1, 2007 is Rs. 18 lakh. Advise X Ltd. [JUNE 2003]

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See problem 114-P2.

6.7 Capital gains

Problem 6.7-1 - Explain briefly special provisions regulating tax incidence on capital gains in case of demerger. [JUNE 2008]

■

See paras 169.2-8, 169.2-9 and 169.2-10.

Problem 6.7-2 - Discuss the following :

1. X Ltd., is a manufacturing company. It transferred shares being held in Y Ltd. for Rs. 46,10,000 on October 6, 2008 (cost being Rs. 3,00,000 on January 20, 2005). It paid Rs. 3,458 as securities transaction tax. Find out the capital gains chargeable to tax for the assessment year 2009-10. Would it make any difference to your answer if the shares were transferred outside a recognised stock exchange on September 30, 2008?

2. On October 10, 2008, X Ltd. purchased 1,00,000 units (debt based) of PNI Mutual Fund @ Rs. 16 per unit. On October 25, 2008 (being the record date), it received 50,000 bonus units. On November 20, 2008, it sold 10,000 original units @ Rs. 9 per unit. What was the cost of acquisition of bonus units if bonus units were transferred on March 31, 2009? Discuss the relevant provisions.

3. State the provisions regarding computation of capital gains in case of slump sale. [JUNE 2005]

■

Pointwise answer:

1. Computation of capital gains

Sales consideration	Rs. 46,10,000
Less: Indexed cost of acquisition (Rs. 3,00,000 × 582/480)	3,63,750
	<u>42,46,250</u>

Long-term capital gain

As securities transaction tax is paid, the resultant long-term capital gain is exempt under section 10(38).

In case the shares are transferred outside a recognised stock exchange then long-term capital gain of Rs. 42,46,250 is taxable and securities transaction tax is not applicable.

2. Computation of capital gains

Sales consideration [10,000 units @ Rs. 9 each]	Rs. 90,000
Less: Cost of acquisition [10,000 units @ 16 each]	1,60,000
	<u>(-) 70,000</u>

Short-term capital loss

This short-term capital loss of Rs. 70,000 is to be ignored and it will be treated as cost of acquisition of bonus units. See para 229.7-2.

3. See para 520.3.

Problem 6.7-3 Write note on slump sale. [DECEMBER 2004]

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See para 520.

Problem 6.7-4 - Write a note on capital gains on transfer of depreciable assets. [DECEMBER 2003]

■

See para 173.1-3.

Problem 6.7-5 - Write a note on long-term capital gains on transfer of an asset other than foreign exchange assets by non-resident Indian. [DECEMBER 2003]

■

See para 186.2.

6.8 Income from other sources

Problem 6.8-1 - Write short note on distribution by a company on reduction of share capital. [DECEMBER 2006]

■

See para 193.2-5.

Problem 6.8-2 - X held 12 per cent shares in a private limited company. He gifted all the shares to his wife, Mrs. X on November 1, 2008. Mrs. X obtained a loan of Rs. 2,17,000 on November 4, 2008 from the company when the company's accumulated profit was Rs. 1,16,000. What are the tax implications of the above transactions? [JUNE 2004]

■

In the present problem, by virtue of section 64(1)(iv), any income arising from transferred shares to Y shall be deemed to be the income of X. Also, the loan of Rs. 60,000 received from the company by Y shall be covered under section 2(22)(e). The accumulated profit was Rs. 1,16,000. Therefore, Rs. 1,16,000 shall be treated as dividend in the hands of Y. The dividend income will be included in the total income of X in accordance with section 64(1)(iv).

6.9 Income of other persons included in assessee's total income

6.10 Set off and carry forward of losses

Problem 6.10-1 - Enumerate the provisions for 'carry forward' and 'set off' of accumulated losses and unabsorbed depreciation on amalgamation. [JUNE 2005]

■

See para 232.

Problem 6.10-2 - Generally speaking, depreciation/loss can be carried forward by a person who has incurred the loss. Section 72A provides an exception to this rule. Discuss with reference to amalgamation of companies. [DECEMBER 2003]

■

See para 516.5.

Problem 6.10-3 - Discuss the provisions relating to 'slump sale'. [DECEMBER 2003]

■

See para 520.3.

Problem 6.10-4 - Discuss the provisions of section 74 relating to capital gains. [DECEMBER 2003]

■

See para 229.3.

Problem 6.10-5 - Discuss in brief the tax incentives available in the case of demerger. [DECEMBER 2003]

■

See para 517.

6.11 Deductions from gross total income and tax liability

Problem 6.11-1 - Discuss the provisions of section 80JIAA relating to deduction in respect of employment of new workmen. [DECEMBER 2007]

■

See para 257.

Problem 6.11-2 - X Ltd. is an Indian company. It owns an industrial undertaking engaged in the manufacture of articles and started production during 2004-05. On March 31, 2008, it has 80 workmen out of which 20 are casual workmen. On May 15, 2008, the company appoints 30 regular workmen and paid Rs. 4,000 per month to each such workman. Find out the amount of deduction under section 80JJAA for the assessment year 2009-10. [DECEMBER 2005]

■

See answer to problem 257-P2.

Problem 6.11-3 State the provisions relating to deduction in respect of repayment of loan taken for higher education. [JUNE 2005]

■

See para 241.

Problem 6.11-4 - What are the deductions available to a resident for projects set-up outside India ? [DECEMBER 2003]

■

See para 247.

Problem 6.11-5 - Your client is engaged in a business of export of music software. Advise him about the deductions available in respect of profits and gains of such business. [DECEMBER 2003]

■

See para 252.

6.12 Agricultural income

6.13 Typical problems on assessment of individuals

6.14 Tax treatment of Hindu undivided family

6.15 Special provisions governing assessment of firms and association of firms

6.16 Taxation of companies

Problem 6.16-1 Discuss the following:

1. What is 'minimum alternate tax' (MAT)? What is the treatment of following debited to profit and loss account while calculating book profit:

- (i) Fringe benefit tax
- (ii) Wealth-tax
- (iii) Provision for doubtful debt
- (iv) Penalty for non-payment of income-tax
- (v) Dividend tax
- (vi) Banking cash transaction tax
- (vii) Proposed dividend
- (viii) Excise duty due, but not paid
- (ix) Provision for gratuity
- (x) Depreciation ?

2. X Ltd., an Indian company, furnishes following particulars of its income for the previous year 2008-09. Calculate its total income and income-tax liability for the assessment year 2009-10:

Problem 6.16-1 : June 2007*Taxation of companies*

1422

	Rs.
Income from business	5,20,000
Dividend received during the year:	
- from Indian company	20,000
- from foreign company	5,000
Gains from transfer of capital assets:	
- short term capital gains	25,000
- long term capital gains	50,000
Agricultural income in India	35,000

Additional information :

- i. Income from business includes Rs. 1,50,000 profit earned from a new small scale industry set up on October 1, 1999 which is eligible for deduction under section 80-IB.
- ii. Business expenses already charged from business income include Rs. 10,000 revenue expenditure and Rs. 30,000 capital expenditure on family planning programme for employees.
- iii. Company has debited following donations in the profit and loss account of the business of company:
 - Rajiv Gandhi Foundation : Rs. 50,000; and
 - Prime Minister's National Relief Fund : Rs. 25,000. [JUNE 2007]

■ *Pointwise answer:*

1. The answer is as under:

(i) Not added back; (ii) Not added back; (iii) Not added back; (iv) Not added back; (v) Added back to net profit; (vi) Not added back; (vii) Added back to net profit; (viii) Not added back; (ix) Not added back; and (x) Entire amount of depreciation debited to the profit & loss account is added back and thereafter that part of depreciation which does not relate to revaluation of assets is deducted from the net profit.

2. *Computation of total income of X Ltd. for the assessment year 2009-10*

	Rs.
Income from business [see Note I]	6,19,000
Income from capital gains	
- STCG	25,000
- LTCG	50,000
Income from other sources	
- Dividend from Indian company [exempt]	-
- Dividend from foreign company	5,000
Gross total income	<u>6,99,000</u>
Less: Deductions under Chapter VI-A	
- Under section 80-IB (30% of Rs. 1,50,000)	45,000
- Under section 80G [(100% of Rs. 25,000) + (50% of Rs. 50,000)]	50,000
Taxable income	<u>6,04,000</u>
<i>Computation of tax liability</i>	
Tax on Rs. 6,04,000 [20% of Rs. 50,000 + 30% of Rs. 5,54,000]	1,76,200
Add: Surcharge [@10% of tax in case net income exceeds Rs. 1 crore]	-
Tax and surcharge	<u>1,76,200</u>
Add: Education cess [@ 2% of tax and surcharge]	3,524
Add: Secondary and higher education cess [@1% of tax and surcharge]	1,762
Tax liability (rounded off)	<u>1,81,490</u>

*Notes:*I. *Computation of business income*

Income from business	5,20,000
Add: Inadmissible expenses	
Capital expenditure on family planning [Rs.30,000 - (1/5 of Rs. 30,000)]	24,000

	Rs.
Donation to Rajiv Gandhi Foundation	50,000
Donation to Prime Minister's National Relief Fund	25,000
Business income	<u>6,19,000</u>

II. Scheme of partial integration of non-agricultural income with agricultural income is not applicable in case of a corporate assessee.

Problem 6.16-2 - Discuss the following:

1. Distinguish between 'domestic company' and 'foreign company'. Are they treated alike under the income-tax rate structure?

2. P. Ltd. owns two undertakings. Undertaking-A is eligible for deduction under section 80-IA and undertaking-B is not eligible for such deduction. Date of commencement of operation in both the undertakings is September 14, 2003.

The profits earned by both the undertakings are as under:

Previous year	Undertaking-A (Rs. in lakhs)	Undertaking-B (Rs. in lakhs)
2004-05	(-) 6	(-) 4
2005-06	(-) 4	10
2006-07	5	9
2007-08	8	6
2008-09	9	(-) 3

Calculate total income of P Ltd. for last three assessment years. [DECEMBER 2006]

Pointwise answer:

1. See paras 333.3 and 333.4. For tax rate, see Appendix 1.

2. See para 253.1-3d.

Problem 6.16-3 - From the following particulars of X Ltd., calculate the amount of tax payable by the company for the assessment year 2009-10:

	Rs. (in crore)
Business income from sale of equity shares and units of equity oriented mutual fund (non-delivery based)	8.00
Speculative income from other transactions	4.00
Non-speculative business income	12.00
Income other than business income	9.00
Securities transaction tax (it is deducted from above incomes)	2.50
Deductions allowed under sections 80C to 80U	3.00
Fringe benefit advance tax (not deducted from above income)	0.01
	[JUNE 2006]

Computation of tax payable by X Ltd.	
	Rs. (in crore)
Speculative business income	12
Business income (non-speculative)	12
Other income	9
Gross total income	<u>33</u>
Less: Deductions under sections 80C to 80U	<u>3</u>
Net taxable income	<u>30</u>
Tax on taxable income	9
Add: Surcharge (10% of Rs. 9 crore)	<u>0.9</u>
Tax and surcharge	9.9
Add: Education cess	0.198
Add: Secondary and higher education cess (1% of income-tax and surcharge)	0.099
Tax liability	<u>10.197</u>

Problem 6.16-4 - Write short note on minimum alternate tax (MAT) under section 115JB. [DECEMBER 2005]

■
See para 336.

Problem 6.16-5 - Discuss the following :

1. Discuss the admissibility or otherwise of the following claims in connection with assessment to income-tax. They do not necessarily relate to the same assessee:

- a. A company had imported machinery at a cost of Rs. 40 lakh in 2007-08. Depreciation on the original cost on the straight line basis is provided in the books (Rs. 5 lakh). The company obtained on June 10, 2008 from the supplier Rs. 80,000 by way of compensation for the defective machinery supplied in 2007-08. This has been credited to reserve account. If depreciation rate for the income-tax is 15 per cent and no other asset is owned by the company, find out the depreciation.
- b. Legal expenses include Rs. 15,000 paid to an advocate for conducting income-tax appeal and Rs. 5,000 (paid as advance) in connection with prosecution of a director for alleged smuggling of goods from a foreign country for the company's benefit. A profit of Rs. 70,600 was made on the sale of these smuggled goods and included in company's revenue.
- c. During the year 2008-09, a company transferred a sum of Rs. 17,100 to the credit of its profit and loss account being unclaimed wages relating to employees who have left the services of the company long ago.
- d. A new plant was installed costing Rs. 46 lakh on June 24, 2008. Since, the plant was unsuitable, it was sold on September 8, 2008 for Rs. 40 lakh. The company has charged depreciation of Rs. 72,000 and debited the balance of Rs. 5,28,000 to the capital reserve.
- e. A company has paid Rs. 2 lakh towards the cost of electric service lines (the ownership of service lines shall rest with the State Electricity Board).

2. X Ltd., a domestic company has an undertaking newly established for export of computer software in a free trade zone, the profits of which have been merged in the net profit of the company as per profit and loss account prepared in accordance with the provisions of Parts II and III of Schedule VI of the Companies Act, 1956. It has furnished the following particulars in respect of the assessment year 2009-10 and sought your opinion on the application of section 115JB. You are also required to compute tax payable by the company:

	Rs.
Net profit shown by profit and loss account	12 lakh
Credit side of profit and loss account includes dividend income	2 lakh
Gains on sale of land held as investment	4 lakh
Profit of the undertaking newly established for export of computer software	26 lakh
Debit side of Profit and Loss Account includes:	
Depreciation on straight line basis	10 lakh
Other expenses	4 lakh
Provision for losses of subsidiary companies	6 lakh
Other information:	
Depreciation allowed as per income-tax law	15 lakh
Loss brought forward as per books of account	25 lakh
Unabsorbed depreciation as per books of account	1 lakh
Brought forward loss as per income-tax law	15 lakh
Unabsorbed depreciation as per income-tax law	5 lakh
The company's tax department is of the opinion that gains realised on sale of land cannot form part of book profit for purposes of section 115JB. [JUNE 2005]	

■
1. Pointwise answer:

a. The answer is as under :	
Computation of depreciation	Rs.
Cost of machinery [Rs. 40,00,000 – Rs. 80,000]	39,20,000
Less: Depreciation @ 15% for previous year 2007-08	5,88,000
Written down value as on April 1, 2008	33,32,000
Less: Depreciation @ 15% for previous year 2008-09	4,99,800
Written down value as on April 1, 2009	28,32,200

b. Legal expenses of Rs. 15,000 on account of conducting an income-tax appeal are allowable. However, legal expenses of Rs. 5,000 in connection with prosecution of a director for alleged smuggling of goods are not allowable in view of provisions of section 37(1).

c. Unclaimed wages of Rs. 17,000 are chargeable to tax under section 41(1), see para 156.1.

d. Tax treatment is as under:

	When the assessee does not own any other asset falling in the same block Case I	When the assessee owns other assets falling in the same block Case II
	Rs.	Rs.
Depreciated value of the block on April 1, 2008 (*assumed)	Nil	10,00,000
Add: Purchases made during the previous year 2008-09	46,00,000	46,00,000
Less: Sale proceeds made during the previous year 2008-09	40,00,000	40,00,000
Written down value of the block on March 31, 2009	6,00,000	16,00,000

In Case I, no depreciation is admissible as the block of asset ceases to exist as on the last day of the relevant previous year. However, Rs. 6,00,000 can be claimed as short-term capital loss under section 50.

In Case II, the assessee can claim depreciation on Rs. 16,00,000 i.e., the closing balance for the previous year 2008-09.

e. Rs. 2,00,000 is allowable as deduction under section 37(1).

2. Book profit

	Rs. in lakh
Net profit as per profit and loss a/c	12
Add: Provision for loss of subsidiary companies	(+ 6)
Less:	
Income exempt under section 10A	(-) 26
Dividend income (being exempt under section 10)	(-) 2
Brought forward loss or depreciation, whichever is lower	(-) 1
Book profit	<u>(-) 11</u>
Computation of income under normal provisions	12
Net profit as per Profit and Loss A/c	(-) 2
Less: Dividend (being exempt under section 10)	(-) 4
Less: Capital gain	(-) 26
Less: Income exempt under section 10A	(+ 10)
Add: Depreciation as per books of account	(-) 15
Less: Depreciation under section 32	(+ 6)
Add: Provision for loss of subsidiary company	<u>(-) 19</u>
Business income	4
Capital gain	<u>4</u>
Net income	
Tax on net income [20% of Rs. 4 lakh plus education cess @ 2% plus secondary and higher education cess @ 1%]	0.824
Minimum alternate tax	Nil
Tax payable	0.824

Notes:

I. It is assumed that capital gain is long-term capital gain.

II. Capital profit is part of book profit [see Accounting Standard 13]. See also *CIT v. Veekayal Investment Co. (P) Ltd.* [2001] 249 ITR 597 (Bom.).

Problem 6.16-6 Discuss the following :

1. See Problem 530.1-P1(2).
2. What are the tax concessions available in the case of conversion of a firm into a private limited company?

3. *X Ltd. amalgamated with Y Ltd. Discuss the benefits available to the shareholders of X Ltd., the amalgamated company.* [DECEMBER 2004]

■
Pointwise answer :

1. See answer to Problem 530.1-P1(2).
2. See para 519.
3. See para 516.

Problem 6.16-7 - Discuss the following:

1. *For the year ended March 31, 2009, X Ltd., incurred a net loss of Rs. 12,50,000 after providing depreciation of Rs. 3,20,000 (depreciation under the Income-tax Act, 1961 is Rs. 4,10,000). Perusal of the profit and loss account revealed the following items debited under various heads and also from the additional information provided, you are required to compute the taxable income for the assessment year 2009-10 giving reasons for allowance or disallowance and taxability or otherwise of each item:*

- *The company has taken overdraft from its bankers for payment of income-tax and the interest charged by the bank is Rs. 25,000.*
 - *The Cotton Textiles Export Promotion Council has levied a penalty of Rs. 50,000 on the company for shortfall in export performance in respect of import of cotton from Egypt. The penalty is stipulated in the permit itself and was duly paid by the company which contends that the penalty is less than the loss which would have been incurred by it, if the export as undertaken had been made.*
 - *The company collected charity @ 0.1 per cent of its domestic sales and it had spent Rs. 30,000 on charity out of the total amount of Rs. 50,000 collected. The balance is shown as a liability.*
 - *During the financial year 2008-09, the company made a lump sum payment of Rs. 30,00,000 to acquire technical know-how from a laboratory owned by the Government. This has been treated as deferred revenue expenditure and a sum of Rs. 5,00,000 has been debited in profit and loss account and the balance being carried forward.*
 - *A development loan of Rs. 10 lakh granted by the State Government to the company has been waived off to the extent of 20 per cent, which has been credited to the profit and loss account.*
 - *The company debited Rs. 32,000 as bad debts by writing off the amount due from Y, a cotton merchant, to whom it had given an advance for purchase of cotton. He did not deliver the cotton nor could any recovery be made from him.*
 - *Salaries and wages debited to profit and loss account include bonus provisions made of Rs. 75,000, which remains unpaid till the due date of filing of tax return.*
 - *Payment of interest of Rs. 40,000 on amount borrowed from its bankers for payment of dividends to shareholders has been charged to profit and loss account.*
2. *Write short note on company in which public is substantially interested.*
 3. *Write short note on book profit under MAT.* [JUNE 2004 (Old)]

■
Pointwise answer:

1. *Computation of taxable income of X Ltd.*

	Rs.
Net profit as per Profit & Loss A/c	(-) 12,50,000
<i>Adjustments:</i>	
Interest on bank overdraft [not allowable since it was taken for payment of income-tax]	(+) 25,000
Penalty for shortfall in export performance [allowable since Export Promotion Council has levied the penalty for a purpose which is not an offence or prohibited by any law]	—
Charity collected as a percentage of sale price [allowable if utilized exclusively for charitable purpose— <i>CIT v. Bijli Cotton Mills (P) Ltd.</i> [1979] 116 ITR 60 (SC)]	—
Lump sum payment for acquisition of technical know how [25% of Rs. 30,00,000 is allowable as depreciation; as Rs. 5,00,000 has already been debited to Profit and Loss A/c, Rs. 2,50,000 more needs to be debited]	(-) 2,50,000
Waiver of development loan [not a revenue receipt as it is not covered by section 41(1)]	(-) 2,00,000
Write off of advance [allowable]	—
Bonus [unpaid not allowable as per section 43B]	(+) 75,000
Interest on amount borrowed for payment of dividend [allowable]	—
Depreciation [Rs. 4,10,000 - Rs. 3,20,000]	(-) 90,000
Net income	(-) 16,90,000

2. See para 333.6.
3. See para 336.

Problem 6.16-8 - Explain the concept of 'amalgamation' with reference to companies. Under the Income-tax Act, 1961, what benefits accrue to the (i) shareholders; (ii) amalgamating company; and (iii) amalgamated company. Explain the same with reference to settled case laws and specific provisions of the aforesaid Act. [JUNE 2004 (NEW)]

■

See para 516.

Problem 6.16-9 - As a Company Secretary, prepare a report for the Board of directors of your company pinpointing the relevance of 'minimum alternate tax' (MAT). [JUNE 2004]

■

See para 336.

Problem 6.16-10 - Briefly explain the provisions of MAT. [DECEMBER 2003]

■

See para 336.

Problem 6.16-11 - A State Industrial Development Corporation recommends a project in a backward State to your client (a company). The estimated outlay is about Rs. 10 lakh (of which 60 per cent being cost of plant and machinery). Your client will have to borrow Rs. 5 lakh, which will be lent by the corporation at the interest rate of 10 per cent per annum. Sales tax and energy concessions are available. The project will qualify for relief under section 80-IB. If the annual income after making provision for depreciation but prior to deduction of interest on borrowed capital and allowances under section 80-IB is expected to generate Rs. 1.1 lakh, advise your client as to whether it should accept the project or not. Give reasons. Make suitable assumptions. [DECEMBER 2003]

■

Computation of taxable income

	Assessment years 2009-10 to 2013-14 Rs.	Assessment years 2014-15 to 2018-19 Rs.	Assessment year 2019-20 onwards Rs.
Income before interest and tax	1,10,000	1,10,000	1,10,000
Less : Interest (Rs. 5,00,000 @ 10% per annum)	50,000	50,000	50,000
Gross total income	60,000	60,000	60,000
Less : Deduction under section 80-IB	60,000 ⁱ	18,000 ⁱⁱ	0 ⁱⁱⁱ
Taxable income	Nil	42,000	60,000

Notes :

I. Deduction under section 80-IB is available @ 100% for first 5 years.

II. Deduction under section 80-IB is available @ 30% for the next 5 years.

III. No deduction under section 80-IB is available after 10 years.

Computation of return on capital employed

	Assessment years 2009-10 to 2013-14 Rs.	Assessment years 2014-15 to 2018-19 Rs.	Assessment year 2019-20 to onwards Rs.
Taxable income	Nil	42,000	60,000
Less : Tax @ 30.9% or MAT	6,180	12,980	18,540
After tax income	53,820	47,020	41,460
Return on capital employed of Rs. 5,00,000	10.76%	9.40%	8.29%

As the return is 11% in the first 5 years and less than 10% after 5 years, the project should not be accepted.

Problem 6.16-12 - On April 1, 2008, X and Mrs. X purchased all the shares of a private limited company. The company had the following unabsorbed allowances/losses :

	Rs.
Accumulated loss	3,00,000
Unabsorbed depreciation	8,00,000

State the effect of change of shareholders on the right of the company to carry forward the above items.

Does it make any difference if the company is a manufacturing company or a trading company engaged in export of goods ? [DECEMBER 2003]

■
For provisions of section 79, see para 335. In the present problem, in view of the aforesaid provisions, the company cannot carry forward the accumulated business loss of Rs. 3,00,000 though it can carry forward the unabsorbed depreciation of Rs. 8,00,000. The unabsorbed depreciation can be set off against income under any head. It does not make any difference if the company is a manufacturing company or a trading company engaged in export of goods.

Problem 6.16-13 *How are dividends taxed in India? Explain the concept of deemed dividends. [JUNE 2003]*

■
See para 337.

6.17 Assessment of co-operative societies

6.18 Assessment of charitable and other trusts

6.19 Return of income and assessment

Problem 6.19-1 - *Discuss briefly whether the following return can be revised under section 139(5):*

1. *Return of loss filed under section 139(3)*
2. *Belated return filed under section 139(4)*
3. *Revised return filed under section 139(5)*
4. *Defective or incomplete return filed under section 139(9)*
5. *Return filed knowing it to be false; and*
6. *Return filed for the assessment year 2007-08, assessment of which is yet to be completed. [JUNE 2008]*

-
1. *Loss return can be revised under section 139(5) as it is deemed to be return filed under section 139(1). See para 354.*
 2. *Belated return cannot be revised as it is not declined to be a return filed under section 139(1). See para 356.*
 3. *See para 357.*
 4. *Return filed knowing it to be false cannot be revised.*
 5. *Defective or incomplete return cannot be revised.*
 6. *Revised return can be filed at any time before the expiry of one year from the end of the relevant assessment year or before the completion of assessment, whichever is earlier.*

Problem 6.19-2 - *Can an assessee claim a particular deduction, which he has failed to claim in his original return of income, otherwise than by filing a revised return? Discuss. [DECEMBER 2007]*

■
No, the assessee cannot claim a particular deduction which he has failed to claim in his original return of income otherwise than by filing a revised return.

Problem 6.19-3 - *Write short note on annual information return. [DECEMBER 2006]*

■
See para 372A.

Problem 6.19-4 *Discuss the following:*

1. *Distinguish between revised return and defective return.*
2. *Who is required to sign the return of income on behalf of the company. [JUNE 2006]*

■
Pointwise answer:

1. *See paras 357 and 358.*
2. *See para 360.*

Problem 6.19-5 What is the time limit for completion of re-assessment in consequence of a finding given in an order under section 254 ? [DECEMBER 2004]

■

See para 370.4.

Problem 6.19-6 - Write short note on income escaping assessment. [JUNE 2004]

■

See para 367.1

6.20 Penalties and prosecutions

Problem 6.20-1 - It is right to say that once penalties under section 271(1)(c) are cancelled on the ground that there is no concealment, quashing of prosecution under section 276C is automatic? [DECEMBER 2005]

■

The statement is correct. See para 374 for provisions of section 271(1)(c) and para 379 for provisions of section 276C [see also *K.C. Builders v. CIT* [2004] 135 Taxman 461 (SC)].

Problem 6.20-2 - As a tax consultant of your client, advise the penal consequences of following defaults:

- (i) Failure to comply with furnishing of prescribed information and returns; and
- (ii) False statement in verification. [JUNE 2005]

■

The answer is as under:

- i. For provisions of section 272A, see para 373.
- ii. For provisions of section 271(1)(c)/(d), see para 373.

6.21 Interest

Problem 6.21-1 - As the Company Secretary of X Ltd., an Indian company, ascertain from the following particulars the minimum amount of advance tax payable by way of different instalments to ensure that interest liability under section 234C is not attracted:

	Rs.
- Business income	2,00,000
- Long-term capital gain on sale of Government securities on October 10, 2008	20,000
- Winnings from lottery on December 31, 2008 (out of which tax deducted at source is Rs. 30,900)	1,00,000
	[JUNE 2006]

■

Computation of minimum advance tax payable	Rs.
On June 15, 2008	
Business income	2,00,000
Tax payable (@ 30.9%)	61,800
Minimum advance tax payable on June 15, 2008 [12% of Rs. 61,800]	7,416
On September 15, 2008	
Minimum advance tax payable on September 15, 2008 [(36% of Rs. 61,800) - Rs. 7,416]	14,832
On December 15, 2008	Rs.
Business income	2,00,000
Long-term capital gain	20,000
Taxable income	2,20,000

Problem 6.21-2 : June 2005	<i>Advance payment of tax</i>	1430
		Rs.
Tax payable [(30.9% of Rs. 2,00,000) + (20.6% of Rs. 20,000)]		65,920
Minimum advance tax payable on December 15, 2008 [(75% of Rs. 65,920) – Rs. 7,416 – Rs. 14,832]		27,192
<i>On March 15, 2009</i>		
Business income		2,00,000
Long-term capital gain		20,000
Winnings from lottery		1,00,000
Taxable income		3,20,000
Tax payable [(30.9% of Rs. 3,00,000) + (20.6% of Rs. 20,000)]		96,820
Minimum advance tax payable on March 15, 2009 [(100% of Rs. 96,820) – Rs. 7,416 – Rs. 14,832 – Rs. 22,446 – Rs. 30,900]		21,226

Problem 6.21-2 - Mention the provisions relating to interest payable for failure to pay advance tax. [JUNE 2005]

■
See para 385.3.

Problem 6.21-3 - Explain the provisions of section 234C. [JUNE 2004 (OLD)]

■
See para 385.4.

6.22 Advance payment of tax

Problem 6.22-1 - Write short note on tax management in respect of advance payment of income-tax in the case of a company. [DECEMBER 2005]

■
See para 381.

Problem 6.22-2 - Explain in brief the provisions relating to payment of advance tax. [DECEMBER 2003]

■
See paras 381 to 383.

Problem 6.22-3 As an entrant to a new tax management department of the company, you find that the company has not paid any advance tax instalments up to December 31 of the year. Write a note to the managing director suggesting suitable corrective action. [JUNE 2003]

■
The liability for advance tax payment shall be as per the schedule given in para 381.2. Since the company has not paid the first, second and third instalments of advance tax, interest at the rate of 1% per month under section 234C has to be paid.

6.23 Tax deduction or collection at source

Problem 6.23-1 - X Ltd. has taken a machinery on rent. The rent is payable in advance on the first day of each month @ Rs. 12,000 per month. Explain in brief whether the rent for the financial year 2008-09 is subject to tax deduction at source or not under section 194-I. [DECEMBER 2007]

■
Yes, tax is to be deducted at source under section 194-I with respect to rent for the financial year 2008-09, see para 418 for detail.

Problem 6.23-2 - Discuss the liability to deduct tax at source on the following payment for the financial year 2008-09:

1. Sikkim Government pays a sum of Rs. 50,000 as commission to its agent on sale of lottery tickets.

2. A turf club gives a prize of Rs. 2,00,000 to the owner of a winning horse.
3. Bank of India is the tenant of a building owned by the Central Government. It pays a sum of Rs. 75,000 per month by way of rent.
4. Y Ltd. pays a sum of Rs. 2,500 per month as retainer fee to its counsel.
5. Dividend of Rs. 25,000 is paid on preference shares on November 15, 2008 by an Indian company.
6. Rs. 1,00,000 paid to X being amount of 1st prize in the lottery conducted by the Nagaland Government. [DECEMBER 2006]

■
Pointwise answer:

1. Tax is deductible @ 10.3% under section 194G.
2. Rs. 61,800 (i.e., 30.9% of Rs. 2,00,000) under section 194BB, see para 410.
3. If recipient is Government, tax is not deductible—see para 428.1
4. TDS rate is 10.3%. TDS is, therefore, Rs. 2,833
5. Dividend from an Indian company is exempt from tax in the hands of shareholders under section 10(34) except deemed dividend under section 2(22)(e), see para 407]. TDS is not required.
6. Rs. 30,900 (i.e., 30.9% of Rs. 1,00,000) as per section 194B, see para 409.

■
Problem 6.23-3 - Write short note on tax deducted at source on fees paid for professional or technical services. [DECEMBER 2005]

■
See para 419.

■
Problem 6.23-4 - Explain the provisions relating to deduction of tax at source in regard to fees for professional or technical services under section 194J. [JUNE 2005]

■
See para 419.

■
Problem 6.23-5 - Discuss the following -

1. As a company secretary, list out your duties with regard to tax deduction at source for transactions involving payment in respect of the following:
 - a. Payment of rent.
 - b. Payment of professional fee to a non-resident.
 - c. Payment of insurance commission to a resident.
 - d. Payment of interest other than interest on securities.
2. Write a note on 'e-tds' return. [JUNE 2004]

■
Pointwise answer:

1. The answer is as under:
 - a. See para 418.
 - b. Tax is deductible at source under section 195, see para 421.
 - c. See para 412.
 - d. See para 408.
2. See para 427.

■
Problem 6.23-6 - As a Company Secretary, what are your duties to file annual TDS return? [JUNE 2004]

■
See para 427.

■
Problem 6.23-7 - Your client company has not obtained a 'tax collection account number' (TCAN). Advice what shall be its consequences and also state the procedures for obtaining the TCAN. [DECEMBER 2003]

■
In case tax collection account number is not obtained, the client company is liable to a penalty of Rs. 10,000 as per the provisions of section 272BBB [i.e., failure to comply with the provisions of section 206CA]. See para 429.10 for knowing the procedure for obtaining the tax collection account number.

■
Problem 6.23-8 - You are asked to head the tax department of a company and there have been a lot of transactions involving payment in respect of the following: (a) Payment to non-residents; (b) Interest other than interest on securities;

(c) Payment to contractors; (d) Payment for technical services. List out your duties for tax deduction at source (TDS) in the above cases. [JUNE 2003]

■
See paras 420, 408, 411 and 419.

6.24 Refund of excess payments

6.25 Appeals and revisions

Problem 6.25-1 - What is the remedy available against the revisional order passed by Commissioner under section 264? Explain briefly. [DECEMBER 2007]

■
See para 438.2.

Problem 6.25-2 - Write short note on revision of orders favourable to assessee by Commissioner of Income-tax. [DECEMBER 2006]

■
See para 438.2.

Problem 6.25-3 Discuss the nature of the cases where Commissioner of Income-tax can revise an order passed by the Assessing Officer. [JUNE 2003]

■
See para 438.1.

6.26 Income-tax authorities

6.27 Settlement of cases

6.28 Purchase of immovable properties

6.29 Advance ruling for non-residents

Problem 6.29-1 - Can advance ruling be sought on a question relating to tax liability of a resident? Discuss. [DECEMBER 2005]

■
No, advance ruling cannot be sought on a question relating to tax liability of a resident. See para 486.2.

Problem 6.29-2 - Define 'advance rulings'. State the procedure to get advance ruling. [JUNE 2005]

■
See paras 486 to 491.

Problem 6.29-3 Write note on applicability of advance ruling. [DECEMBER 2004]

■
See para 486.

Problem 6.29-4 - Write short note on authority for advance rulings. [JUNE 2004 (Old)]

■
See para 486.1

Problem 6.29-5 What do you understand by 'advance rulings'? Are the residents seeking advance ruling at par with non-residents or residents dealing with non-residents ? [June 2003]

■

See paras 486 to 491.

6.30 Special procedure for assessment of search cases

6.31 Tax planning

Problem 6.31-1 - Briefly discuss the legal propositions in case of any conflict between the provisions of the Double Tax Avoidance Agreement (DTAA) and the Income-tax Act, 1961. [JUNE 2008]

■

See para 530.1.

Problem 6.31-2 - There are many factors that should be kept in mind while designing the salary package of employees having regard to the need for minimizing the tax impact on them. Discuss briefly. [DECEMBER 2007]

■

See para 529.

Problem 6.31-3 You are the Company Secretary of a manufacturing company. Your company is going to appoint a consultant on a monthly salary of Rs. 60,000. Prepare a remuneration plan so that the company's fringe benefit tax liability and employee's personal tax liability is reduced to minimum possible level. [JUNE 2007]

■

See para 529.3.

Problem 6.31-4 - Write short note on tax relief in India where there is no double taxation avoidance agreement. [DECEMBER 2006]

■

See para 530.1-2.

Problem 6.31-5 - Discuss the following:

1. Why is tax planning necessary?
2. Explain briefly the propositions of law in case of any conflict between the provisions of the Double Taxation Avoidance Agreement (DTAA) and the Income-tax Act, 1961. [JUNE 2006]

■

Pointwise answer:

1. See para 525.
2. See para 530.1.

Problem 6.31-6 - Discuss the following :

1. You are appointed as General Manager (Taxation) of a software company. The company is in the process of formulating a salary structure for its marketing field staff. You are required to submit a detailed note containing tax considerations in respect of pay structure.
2. What are the tax considerations a corporate assessee has to look into relating to its dividend policy and issue of bonus shares?
3. Explain leasing vs. buying of a business asset as a tool of tax planning. [JUNE 2004 (Old)]

■

Pointwise answer :

1. See para 529.
2. See paras 527.2 and 527.4.
3. See para 528.2

Problem 6.31-7 Discuss and differentiate between the concepts of 'tax avoidance' and 'tax evasion' with the help of relevant legal pronouncements. [JUNE 2004 (New)]

■
See para 525.

Problem 6.31-8 - Prepare a note for consideration of the board of directors of your company for granting interest-free or concessional loans to company's employees. [DECEMBER 2003]

■
See para 52.10.

Problem 6.31-9 - The board of directors want to extend medical facilities to the company's employees. Advise. [DECEMBER 2003]

■
See para 52.13.

Problem 6.31-10 - Suggest a suitable scheme for grant of leave travel concession to the employees of a company employing more than 1,000 employees so that such amount is exempt in the hands of the employees. [DECEMBER 2003]

■
See para 52.7.

Problem 6.31-11 - Your board of directors are considering issue of bonus shares or payment of dividends in cash. Advise on the tax considerations in choosing a particular course of action. [DECEMBER 2003]

■
For bonus shares, see para 527.4 and for dividend policy, see para 527.2.

Problem 6.31-12 - "Tax management has come to have a significant role in the running of business enterprises or industrial ventures". Having regard to this statement, give in brief some of the important areas of its coverage. [DECEMBER 2003]

■
Tax management involves the procedures of compliance with the statutory provisions of law. Its objective is to comply with the provisions of law. The following are the broad areas of its coverage :

- a. filing of return of income on time on the basis of updated records;
- b. payment of advance tax, self-assessment tax, etc. on time;
- c. computation of various allowances, rebates and reliefs admissible under the provisions of law;
- d. timely preparation of statements relating to tax deduction at source for submission purposes; and
- e. review of assessment proceedings, rectification, revision, appeals, etc.

In this way, tax management relates to past, present and future. However, it has a limited scope, i.e., it deals with specific activities such as filing of returns of income in time, drafting appeals, deduction of tax at source on time, updating records from time to time, etc. However, as a result of effective tax management, penalty, penal interest, prosecution, etc., can be avoided.

Problem 6.31-13 - See Problem 528.1-P1 [DECEMBER 2003]

■
See answer Problem to 528.1-P1.

Problem 6.31-14 Tax avoidance vs. tax evasion. [DECEMBER 2003]

<i>Tax avoidance</i>	<i>Tax evasion</i>
<p>1. Any planning of tax which though done strictly according to legal requirement but defeats the basic intention of the Legislature behind the statute, could be termed as an instance of tax avoidance.</p> <p>2. Tax avoidance takes into account the loopholes of law.</p> <p>3. Tax avoidance is tax hedging.</p> <p>4. Tax avoidance is legitimate but an element of <i>mala fide</i> motive is involved.</p> <p>5. Tax avoidance is intentional tax planning before the actual tax liability arises.</p>	<p>1. All methods by which tax liability is illegally avoided is termed as tax evasion.</p> <p>2. Tax evasion is an attempt to evade tax liability with the help of unfair means/methods.</p> <p>3. Tax evasion is tax omission.</p> <p>4. Tax evasion is unlawful and an assessee guilty of tax evasion may be punished under the relevant laws.</p> <p>5. Tax evasion is intentional attempt to avoid payment of tax after the liability to tax has arisen.</p>

Problem 6.31-15 - What are the tax concessions available in the case of conversion of a firm into a private limited company? [DECEMBER 2003]

■

See para 519.

Problem 6.31-16 Explain the tax planning aspects with regard to specific management-decisions (i) own or lease; and (ii) make or buy. [JUNE 2003]

■

Own or lease - See para 164.3.

Make or buy - See para 528.1.

6.32 Wealth-tax

Problem 6.32-1 - X Ltd. is engaged in the manufacture of steel. On the basis of the following particulars of its properties as on March 31, 2009, compute the net wealth of X Ltd. for the assessment year 2009-10:

	Rs. (in lakh)
Guest house situated in a rural area	40
Residential flat provided to a director whose salary is Rs. 2 lakh per annum	10
Urban land on which no construction is permitted as per municipal laws	30
Cars used for business of the company	8
Cash balance as per books	2.50
Bank balance as per books of account	7
Aircraft used for the business of the company	800
Gold	5

Note:

- Loans taken for purchase of - i. Urban land : Rs. 40 lakh and ii. Aircraft : Rs. 300 lakh.
- Outstanding fringe benefit tax liability : Rs. 2 lakh [JUNE 2008]

■

Computation of net wealth of X Ltd. for the assessment year 2009-10

	Rs. (in lakh)
Guest house	40
Residential flat provided to a director whose salary is Rs. 2 lakh per annum (not an asset as salary is less than Rs. 5 lakh)	Nil
Urban land on which no construction is permitted as per municipal laws (not an asset)	Nil
Cars used for business of the company	8
Cash balance as per books [not an asset]	Nil
Bank balance as per books of account [not an asset]	Nil
Aircraft used for the business of the company [not an asset, see para 545.4]	Nil
Gold	5
Gross wealth	53
Less: Debt owed	
Loan for aircraft	Nil
Loan for urban land	Nil
Fringe benefit tax liability	Nil
Net wealth	53

Note : Gold is an asset provided it is not held as stock-in-trade.

Problem 6.32-2 - Discuss the following:

1. A non-resident company having business connections in India seeks your advice in respect of the following issues under the Wealth-tax Act, 1957:

- a. Taxability of its assets and debts located outside India.
- b. Urban land situated within the jurisdiction of New Delhi Municipal area.
- c. Motor cars used for transportation of employees of the company.
- d. Due date for filing return of wealth.
- e. Time-limit for filing belated or revised return of wealth, if necessary.

2. How would you explain 'wealth escaping assessment' under the Wealth-tax Act, 1957 and when can it be assessed? Is there any time limit for wealth escaping assessment? [DECEMBER 2007]

■

Pointwise answer:

1. The answer is as under:

- a. See para 544.
- b. See para 544.5.
- c. Motor cars are subject to wealth tax, see para 545.7 (point 15).
- d. See para 551.
- e. Late return or revised return can be submitted within one year from the end of the assessment year or before completion of the assessment, whichever is earlier.

2. See para 553.

Problem 6.32-3 When is a house property not considered as an 'asset' under the Wealth-tax Act, 1957? [JUNE 2007]

■

See para 545.1-1.

Problem 6.32-4 - Discuss the following:

1. Are all companies liable to wealth-tax? What is wealth-tax rate applicable in case of companies?

2. Discuss whether the wealth-tax is attracted in the following cases:

- a. Value of assets and debts located outside India.
- b. Land in urban area where construction is not allowed.
- c. Residential quarters allotted by the firm to its employees.
- d. Aircraft used for business purposes.
- e. Guest house and land appurtenant thereto.
- f. Motor car for use by officers for official purposes only.
- g. Shares, debentures, fixed deposits in banks - Rs. 20 lakh.
- h. Cash in hand in the books of a sole-proprietor amounting to Rs. 70,000. [DECEMBER 2006]

■

Pointwise answer:

1. No, all companies are not liable to wealth-tax, see para 540. The rate of wealth-tax in the case of a company is 1 per cent (on surcharge and education cess) of net wealth in excess of Rs. 15,00,000.

2. The answer is as under:

- a. Value of assets and debts located outside India - This is part of net-wealth in the case of resident and ordinarily resident only.
- b. Land in urban area where construction is not allowed - Not considered as an asset under section 2(ea)(v), see para 545.5-2.
- c. Residential quarters allotted by the firm to its employees - Not an asset under section 2(ea) in certain cases, see para 545.1-1.
- d. Aircraft used for business purposes - Not an asset under section 2(ea)(iv), see para 545.4.
- e. Guest house and land appurtenant thereto - It is an asset under section 2(ea)(i), see para 545.1.
- f. Motor car for use by officers for official purposes only - It is an asset under section 2(ea)(ii), see para 545.2.

- g. Shares, debentures, fixed deposits in banks - Rs. 20 lakh - It is not an asset under section 2(ea).
 h. Cash-in-hand in the books of a sole proprietor amounting to Rs. 70,000 - Cash-in-hand in excess of Rs. 50,000 is includible in the net wealth, see para 545.6.

Problem 6.32-5 - Write short note on deemed assets under the Wealth-tax Act, 1957. [DECEMBER 2005]

■

See para 546.

Problem 6.32-6 X company is engaged in the construction and sale of buildings. It has the following assets as at March 31, 2009. You are required to compute the net wealth of the company in respect of the assessment year 2009-10:

	(Rs. in lakh)
Residential flats ready for sale	210
Commercial properties ready for sale	290
Guest house situated 30 km. away from Delhi, but within one km. from Faridabad	16
Two residential houses occupied by:	
An officer having an annual salary of Rs. 3 lakh	18
An officer having an annual salary of Rs. 7 lakh	17
Cars used for company's business	10
Aircraft used by officers for business purposes	1,780
Urban land since March 31, 1995 on which no building could be built	37
Cash in hand [JUNE 2005]	1

■

Computation of net wealth of X company for the assessment year 2009-10	-
Resident flats ready for sale [not an asset under section 2ea (d)(2)]	-
Commercial properties (not an asset)	-
Guest house	16
Residential house allotted to employee drawing annual salary of Rs. 8 lakh [not an asset under section 2(er)(i)(1)]	-
Residential house allotted to employee drawing annual salary of Rs. 7 lakh	17
Cars	10
Aircrafts used by officers for business purposes (not taxable as wealth)	-
Urban land since March 31, 1995 on which no building could be built	-
Cash-in-hand	-
Net wealth	43

Problem 6.32-7 Write short note on taxability of urban land under the Wealth-tax Act, 1957. [DECEMBER 2004]

■

See para 545.5-1.

Problem 6.32-8 Discuss the following :

1. X Ltd. made a cash gift of Rs. 5 lakh to Mrs. Y, a director in the company in 2000. Mrs. Y bought jewellery with that money. The value of that jewellery as on March 31, 2009 was Rs. 8,75,000. What would be the implication of this in the net wealth computation of X Ltd. for the assessment year 2009-10?
2. X Ltd. obtained a loan of Rs. 8 lakh from an associate company by mortgaging its house property, which is let out to the State Bank of India. As on March 31, 2009, the loan outstanding was Rs. 2 lakh. The loan was utilised for the purchase of plant and machinery. Can the amount of unpaid loan of Rs. 2 lakh be claimed as a deduction under section 2(m) of the Wealth-tax Act, 1957?
3. Under what circumstances will the urban land not be liable to wealth-tax?
4. In what status will a society registered under the Societies Registration Act, 1860 be assessed to wealth-tax? [JUNE 2004 (Old)]

■

Pointwise answer :

1. The value of jewellery of Rs. 8,75,000 of Mrs. X shall be included in the net wealth computation of Mrs. X.
 2. For provisions of section 2(m), see para 543.
- In the present problem, in view of the aforesaid provisions, since the loan has been utilized for purchase of plant and machinery, which is not an asset as per section 2(ea), no deduction can be claimed.

3. See para 545.5-2.

4. See para 540. A society registered under the Societies Registration Act, 1860 is not liable to pay wealth tax.

Problem 6.32-9 - Discuss whether the following are 'assets' under section 2(ea) of the Wealth-tax Act, 1957 :

1. Aircraft held by Air India.

2. Guest house (not held as stock-in-trade) for entertaining personal guests.

3. Motor car (Indian or foreign) held as fixed assets by a company and given for business use to a full time employee drawing Rs. 5,00,000 per annum.

4. A residential house which has been let during the previous year for 280 days. [DECEMBER 2003]

1. Not an asset as per section 2(ea)(iv).

2. Guest house (not held as stock-in-trade) for entertaining personal guests is an asset as per section 2(ea).

3. Motor car (Indian or foreign) held as fixed assets by a company and given for business use to a full time employee drawing Rs. 5,00,000 per annum is an asset.

4. A residential house which has been let during the previous year for 280 days is an asset.

Problem 6.32-10 - Under what circumstances can the Assessing Officer make a reference to the Valuation Officer for the purpose of making an assessment in respect of jewellery under the Wealth-tax Act, 1957 ? [DECEMBER 2003]

See para 549.6.

Problem 6.32-11 - What do you understand by the term 'deemed assets' under section 4 of the Wealth-tax Act, 1957 ? Enumerate any eight items. [DECEMBER 2003]

See para 546.

Problem 6.32-12 An American company wants to incorporate an Indian subsidiary company. The whole of the share capital will be owned by the American company. The Indian subsidiary company will manufacture goods in a backward district in West Bengal. As a consultant to the American company, prepare a report pinpointing the wealth-tax liability in India in respect of different assets, which will be owned by the Indian subsidiary company. [JUNE 2003]

See paras 540, 544, 545, 547 and 549.

6.33 Special provisions in case of non-residents

Problem 6.33-1 - What are the special provisions regarding computation of tax on non-resident sportsman being foreign citizen and non-resident sports association? Are these assesseees required to file their return of income? [JUNE 2008]

See para 162.13.

Problem 6.33-2 X Ltd. a foreign company enters into an agreement with Y Ltd., an Indian company. The agreement relates to a matter included in the industrial policy of the Central Government and is in accordance with the policy. During the year 2008-09, a royalty of Rs. 60 lakh is paid by Y. Ltd. to X Ltd. X Ltd. has spent Rs. 15 lakh on expenses covered under sections 28 to 44. Compute the tax payable by X Ltd. under the following situations :

1. Y Ltd. pays the income-tax payable by X Ltd. as per the terms of agreement entered into before June 1, 2002.

2. The agreement does not provide that Y Ltd. will pay the tax, but it is mutually agreed between the parties that royalty of Rs. 60 lakh will be paid net of taxes. [JUNE 2004 (Old)]

For provision of section 10(6A), see para 38.12.

The answer is as under :

1. Computation of tax payable by X Ltd.

Total income X Ltd.	Rs. 60,00,000
---------------------	---------------

Tax payable on royalty income [@ 20% as per section 115A]	12,00,000
---	-----------

Add : Surcharge @ 2.5% of tax in case net income exceeds Rs. 1 crore	Nil
--	-----

	Rs.
Tax and surcharge	12,00,000
Add : Education cess @ 2% of tax and surcharge	24,000
Add : Secondary and higher education cess (1% of income-tax and surcharge)	12,000
Tax payable	12,36,000
Less : Tax payable by Y Ltd.	12,36,000
Net tax payable	<u>Nil</u>
<i>Note : Expenses are not allowed as deduction.</i>	
<i>2. Computation of tax payable by X. Ltd.</i>	
Net income	60,00,000
Grossing up of net income [Rs. 60,00,000 ÷ 0.794]	75,56,675
Tax payable @ 20.6% of Rs. 75,56,675	15,56,675
Less : Tax borne by Y Ltd.	15,56,675
Net tax payable	<u>Nil</u>

Problem 6.33-3 - Write a short note on unilateral relief under section 91? [DECEMBER 2003]

■

See para 530.1-2.

Problem 6.33-4 Your client company is a subsidiary of a foreign company, having its registered office in India. This company has transaction of imports of raw materials and components and also exports of its manufacture components from and to the holding company in Finland and also other group companies in South East Asian countries. What are the income-tax regulations governing such international transactions? [JUNE 2003]

■

See paras 507 to 509.

6.34 Business Restructuring

Problem 6.34-1 - What is the difference between slump sale and demerger? [DECEMBER 2007]

■

See para 520 for provisions of slump sale and para 517 for provisions of demerger.

Problem 6.34-2 - Write short note on slump sale. [DECEMBER 2006]

■

See para 520.

Problem 6.34-3 - What are the conditions in which a merger will not be called as amalgamation as per the provisions of the Income-tax Act, 1961? [JUNE 2006]

■

See para 516.1.

Problem 6.34-4 - Define 'demerged company' and 'resulting company'. What are the tax concessions available to a demerged company and its shareholders? [DECEMBER 2005]

■

See para 517.

6.35 Miscellaneous

Problem 6.35-1 - Discuss briefly the provisions governing 'deemed fringe benefits' given in section 115WB(2). [DECEMBER 2007]

■

See para 535.3.

Problem 6.35-2 When is depreciation subject to fringe benefit tax (FBT)? How is FBT charged on such depreciation? [JUNE 2007]

■

See paras 535.4-10 and 535.4-11.

Problem 6.35-3 - Discuss the following:

1. What is the tax base for the purpose of 'fringe benefit tax' (FBT)? Who is liable to pay FBT? What is the current FBT rate?

2. Will the FBT liability arise, even if (i) the employer is not liable to pay income-tax on his total income; and (ii) the employer does not have any employee? [DECEMBER 2006]

■

Pointwise answer:

1. See para 535.4 for meaning and value of fringe benefits. The employer is liable to pay fringe benefit tax, on value of fringe benefit provided or deemed to have been provided to employees, see para 535.4. For current rate of fringe benefit, see para 535.5-1.

2. Yes FBT liability will arise even if the employer is not liable to pay income-tax on his total income, see para 535.3. FBT liability will not, however, arise if the employer does not have any employee, see para 535.3.

■

See problem 6.31-17(2) Annex 6.

Problem 6.35-4 - What is 'tonnage tax'? Explain briefly. [DECEMBER 2005]

■

See para 532.

7 ANNEX

Questions set for ICWA (Final) examinations and answers from June 2003 to June 2008

7.1 Income exempt from tax

Problem 7.1-1 - Write short note on quantum of income-tax exemption for SEZ unit. [DECEMBER 2007]

■

See para 39A.

7.2 Salaries

Problem 7.2-1 X, a Government officer living in Agra, has been provided with furnished rent-free quarters. His salary is Rs. 20,000 per month. The rent of unfurnished house per Government rules is Rs. 1,000 per month, but its fair rental value is Rs. 7,500 per month. He is provided with furniture costing Rs. 70,000. Find out value of rent-free furnished house as a perquisite for income-tax purposes. [DECEMBER 2004]

■

Value of rent-free furnished house	Rs.
Value of rent-free unfurnished house (Rs. 1,000 × 12) [see para 52.1-1]	12,000
Add: 10% of cost of furniture (see para 52.2-1)	7,000
Value of rent-free furnished house	<u>19,000</u>

Problem 7.2-2 X, a Government employee, gets Rs. 40,000 per annum as basic pay. In addition, he receives Rs. 8,500 as entertainment allowance. His actual expenditure on entertainment for official purposes, however, was Rs. 9,800. Discuss taxability of entertainment allowance received by X. [JUNE 2004]

■

In the case of Government employee, entertainment allowance is deductible under section 16(ii) to the extent of least of the following three :

- 20% of basic salary, i.e., Rs. 8,000;
- Rs. 5,000; or
- Rs. 8,500 (actual entertainment allowance received).

Thus, Rs. 5,000 (being the least) is deductible from gross salary.

Computation of taxable salary	Rs.
Basic pay	40,000
Entertainment allowance	<u>8,500</u>
Gross salary	48,500
Less : Deductions under section 16	
Standard deduction	—
Entertainment allowance	<u>5,000</u>
Taxable salary	<u>43,500</u>

Problem 7.2-3 - A company offers its shares to employees under employees' stock option scheme at concessional rate. Discuss tax liability of an employee who has received such shares under the scheme. [DECEMBER 2003]

■

Value of any benefit provided free of cost or at a concessional rate by a company to its employees by way of allotment of shares, debentures or warrants, directly or indirectly, under the employees' stock option plan or scheme in accordance with the guidelines issued by the Central Government, is a tax-free perquisite.

7.3 Residential status

Problem 7.3-1 - Fill in the blank. An Indian citizen came to India for the first time (after 20 years) on May 28, 2008 and stayed up to December 5, 2008. His residential status is [DECEMBER 2007]

■
Resident but not ordinarily resident.

Problem 7.3-2 - X staying in USA, wishes to come to India during 2009 and stay for at least 100 days. He has been in India for more than 365 days during the four years preceding the relevant previous year. Advise as to how he can fulfil his desire without losing his non-residential status. [DECEMBER 2003]

■
X should plan his stay in India so that in each of the two previous years 2008-09 and 2009-10 he is in India for less than 60 days. In this way, he can fulfil his desire without losing his non-resident status (he can plan his visit to India on February 1, 2009).

7.4 Profits and gains of business or profession

Problem 7.4-1 - State with reasons, whether the statement is true or false. A client presents a computer to X, a Chartered Accountant, who represents his case before the income-tax authorities. The value of the benefit is taxable in the hands of X. [DECEMBER 2007]

■
True, see para 101.11.

Problem 7.4-2 Discuss the following:

1. Fill in the blanks.

- a. The rate of depreciation on general plant and machinery is _____ and on motorcars other than those used for running them on hire is_____.
- b. The deduction for amortization of preliminary expenses under section 35D is allowed at _____of the qualifying expenditure in each of the _____successive years beginning with the year in which business commences.

2. State the factors to be considered in taking a management decision relating to owning or leasing fixed assets. [JUNE 2007]

■
Pointwise answer:

1. The answer is as under:

- a. 15 per cent, 15 per cent.
- b. One-fifth, 5 successive years.

2. See para 164.2.

Problem 7.4-3 - X Ltd. started on September 5, 2008, a new industrial unit for manufacturing special heating equipment. Four new plants costing Rs. 1 lakh, 2 lakh, 3 lakh and 5 lakh respectively were purchased and installed on October 5, 2008. A new car costing Rs. 3 lakh also was purchased on September 15, 2008, and all these were immediately put to use. Find out the depreciation allowable for the assessment year 2009-10, and WDV at the end of that year. [DECEMBER 2006]

<i>Computation of admissible depreciation</i>	<i>Rs.</i>
Block I Plant and Machinery : (rate of depreciation : 15%)	
Purchase of new plants	11,00,000
Car	3,00,000
Total	14,00,000
Less: Sale proceeds	Nil
WDV as on March 31, 2009	14,00,000
Depreciation [(50% of 15% of Rs. 11,00,000)] + (15% of Rs. 3,00,000)	1,27,500
Additional depreciation [50% of 20% of Rs. 11,00,000]	1,10,000
WDV as on April 1, 2009	<u>11,62,500</u>

Problem 7.4-4 - X Co. Ltd., providing telecommunication services, obtains a telecom licence on April 1, 2005 for a period of 10 years ending on March 31, 2015. The licence is not renewable. The company has two options for making the payment:

- to pay Rs. 10 lakh on April 1, 2005, or
- to pay Rs. 12 lakh on April 1, 2009.

Assuming that each year's total receipts and expenses (excluding the licence fees) will be Rs. 50 lakh and Rs. 30 lakh, find out the better option. [JUNE 2006]

■
OPTION I : Licence fees paid on April 1, 2005

	Assessment years	
	2006-07 to 2010-11	2011-12 to 2015-16
Gross total receipts	50,00,000	50,00,000
Less:		
Deduction under section 35ABB	1,00,000	1,00,000
Other expenses	30,00,000	30,00,000
Net receipts	19,00,000	19,00,000
Less: Deduction under section 80-IA [(*100% for first 5 years) (**30% for next 5 years)]	19,00,000*	5,70,000**
Net income	Nil	13,30,000

OPTION II : Licence fees paid on April 1, 2009

	Assessment years		
	2006-07 to 2009-10	2010-11	2011-12 to 2015-16
Gross receipts	50,00,000	50,00,000	50,00,000
Less:			
Deduction under section 35ABB for licence fees [1/6 of Rs. 12 lakh]	-	2,00,000	2,00,000
Other expenses	30,00,000	30,00,000	30,00,000
Net receipts	20,00,000	18,00,000	18,00,000
Less: Deduction under section 80-IA [(*100% for first 5 years) (**30% for next 5 years)]	20,00,000*	18,00,000*	5,40,000**
Net income	Nil	Nil	12,60,000

Option II is better as compared to Option I.

Problem 7.4-5 - Discuss the following:

- Depreciation under section 32 of Income-tax Act, 1961 is available if - (i) Asset is leased by the assessee; (ii) Asset is owned by the assessee; (iii) Asset is not used during the year at all; (iv) Asset is used for personal purposes but not for business.
- The gross turnover of X is Rs. 30 lakh and that of his minor child whose income is clubbed in his hands, Rs. 15 lakh. The Assessing Officer contends that X is liable to tax audit under section 44AB.
- X Ltd. have obtained a term loan from Bihar State Financial Corporation. The company maintains books of account on mercantile basis. They have made a provision of Rs. 3,00,000 in their books of account towards interest payable to the Bihar State Financial Corporation for 2007-08. However, actual payments were made as follows: (i) Rs. 40,000 on April 10, 2007; (ii) Rs. 55,000 on January 5, 2008; (iii) Rs. 35,000 on September 21, 2008; (iv) Rs. 65,000 on December 14, 2008; (v) Rs. 25,000 on July 25, 2009; (vi) Rs. 60,000 on April 2, 2010; (vii) Rs. 20,000—requested for waiver to Financial Corporation on April 3, 2010.

State how much payment will be allowed as deduction for income-tax and in which assessment year/s [DECEMBER 2005]

■
Pointwise answer:

- ii. Asset is owned by the assessee.
- The Assessing Officer is not correct in his contention that X is liable to get his accounts tax audited under section 44AB. This is no because what is clubbed under provisions of section 64(1A) is income and not turnover.

2. If capital is borrowed for purchasing machinery, then interest on borrowed capital till the machine is put to use (for the first time) is not deductible under section 36. Such interest should be capitalized. Therefore, the action of the Assessing Officer is legally tenable in law.
3. Depreciation is available. See para 109.1-1a.

7.5 Income under the head "Capital gains"

Problem 7.5-1 - Answer the following:

1. State with reasons whether it is true or false. The maximum amount, which an eligible assessee can invest in 'long-term specified assets' like NABARD Bonds for claiming exemption under section 54EC is Rs. 50 lakh.
2. "Short-term capital loss can be set off only against short-term capital gains". Discuss. [JUNE 2008]

Pointwise answer:

1. True, see para 182.
2. See para 229.3.

Problem 7.5-2 - State with reasons, whether the statement is true or false. A taxpayer converts his capital asset into stock-in-trade. There is "no transfer" since the person, who holds the asset before and after the act, is the same. [DECEMBER 2007]

False, see para 176.

Problem 7.5-3 - X Ltd. shifted in March 2009 one of its industrial undertaking in Bangalore to a non-urban area. The relevant details are :

	(Rs. in lakh)
Capital gain under section 50 in respect of plant and machinery (purchased 30 months back)	20
Capital gain under section 50 in respect of factory building (acquired 40 months back)	12
Capital gain on transfer of the land portion of factory building and surroundings	8
Expenses of shifting to non-urban area	2
New machinery had been acquired at Rs. 3 lakh for use at the proposed new site. The assessee intends to invest Rs. 13 lakh and Rs. 16 lakh in new plant and machinery and in new factory land and building at the new site.	
What will be the capital gain for the assessment year 2009-10, if the requisite conditions for relief are satisfied? [DECEMBER 2006]	

For provisions of section 54G, see para 184.
Computation of taxable capital gains

Short-term capital gain	20,00,000	-
Long-term capital gain	-	8,00,000
Less: Exemption under section 54G (see Note I)	20,00,000	2,00,000
Long-term capital gain taxable	Nil	6,00,000
Rs.		
Note I : Exemption under section 54G is as under:		
Expenses of shifting to non-urban area		2,00,000
New machinery acquired		3,00,000
New plant and machinery		13,00,000
New factory land		16,00,000
Total exemption		34,00,000

Problem 7.5-4 - Discuss the following:

1. The capital gain on transfer of a long-term capital asset other than a house is exempt under section 54F for – (i) an individual, (ii) an individual and a Hindu undivided family, (iii) an individual who is a senior citizen, (iv) a resident individual.

2. See problem 105-P4 Students Guide to Income-tax. [JUNE 2006]

■

Pointwise answer:

1. (ii) An individual and a Hindu undivided family.

2. See answer to Problem 105-P4.

Problem 7.5-5 - Identify the correct answer : Deduction under section 54F for capital gains on transfer of a long-term capital asset other than a house property is available only if - (i) On the date of transfer of original asset assessee does not own more than one residential house property; (ii) On the date of transfer of original asset assessee does not own more than one commercial house property; (iii) On the date of transfer of original asset assessee does not own any other house property; (iv) On the date of transfer of original asset assessee owns at least one other house property [DECEMBER 2005]

■

(i) On the date of transfer of original asset assessee does not own more than one residential house property.

Problem 7.5-6 See Problem 7.5-3 (Annex 7).

■

See answer to Problem 7.5-3 (Annex 7).

Problem 7.5-7 X purchases 2000 equity shares in B Ltd. at the rate of Rs. 32 per share (brokerage 2 per cent) on January 1, 1980. He gets 1000 bonus shares (by virtue of his holding 2000 shares) on March 15, 1984. Fair Market value of shares of B Ltd. on April 1, 1981 is Rs. 48. On February 15, 2009, he transfers 2000 original shares @ 272 per share (brokerage 3 per cent). On March 15, 2009, he transfers 1000 bonus shares @ Rs. 275 per share (brokerage 3 per cent).

Compute the total capital gain on transfer of shares which are a recognised stock exchange. [JUNE 2004]

■

Computation of capital gain

Sale consideration

Less :

Indexed cost of acquisition (*Rs. 96,000 × 582 ÷ 100; Nil)

Brokerage

Long-term capital gain (see Note)

Original shares Rs.	Bonus shares Rs.
5,44,000	2,75,000
5,58,720	Nil
16,320	8,250
(-) <u>31,040</u>	<u>2,66,750</u>

Note : The above long-term capital gain is not chargeable if transaction of sale is liable for securities transaction tax.

7.6 Income from other sources

Problem 7.6-1 X is shareholder of an unlisted public company, holding 15 per cent shares of the company. He takes loan of Rs. 2,00,000 from the public company in April 2007. It is repaid in March 2009. The Assessing Officer proposes to treat the amount of Rs. 2,00,000 as income of X. Is his action justified? [JUNE 2004 (NEW)]

■

The action of the Assessing Officer is justified as Rs. 2,00,000 is to be treated as deemed dividend under section 2(22)(e) in the hands of X for the assessment year 2009-10 [for relevant provisions, see para 193.2-6a].

7.7 Set off and carry forward of losses

Problem 7.7-1 - State the conditions to be fulfilled for carry forward of unabsorbed depreciation and accumulated losses in the hands of the amalgamated company. [DECEMBER 2005]

■

See para 516.5.

Problem 7.7-2 - State the provisions in respect of set off and carry forward of loss under the head 'Profits and gains of business or profession'. [DECEMBER 2003]

■

See paras 227, 228 and 229.

7.8 Deductions from gross total income

Problem 7.8-1 - X an individual, aged 50, has made the following payments during the financial year 2008-09:

- i. Prepayment of entire outstanding housing loan balance of Rs. 80,000 as on April 1, 2008. The loan was taken from HDFC Ltd. 10 years ago. He repaid this amount out of the maturity proceeds of his life insurance policy (Rs. 1,90,000) which he received on April 1, 2008.
- ii. He contributed Rs. 15,000 to recognized provident fund (by way of deduction from salary).
- iii. He purchased National Savings Certificates Rs. 5,000.
- iv. He paid his health insurance premium of Rs. 10,000 through his credit card on March 31, 2009. He paid the credit card company the amount on April 25, 2009.

What is the amount of deduction to which X is entitled to under sections 80C and 80D for the assessment year 2009-10? [DECEMBER 2007]

	Rs.
Computation of deduction	
<i>Deduction under section 80C</i>	
Prepayment of housing loan	80,000
Contribution to recognized provident fund	15,000
NSC	5,000
	1,00,000
<i>Deduction under section 80D</i>	
Payment of health insurance premium	10,000

7.9 Taxation of companies

Problem 7.9-1 - A foreign company means a company which is not a - (i) Indian company; (ii) Private company; (iii) Domestic company; (iv) Public company. [JUNE 2006]

I. (iii) Domestic company.

Problem 7.9-2 - The accounts of the X Ltd., an Indian company for the year ending March 31, 2009 prepared in accordance with the provisions of Parts II and III of Schedule VI to the Companies Act, 1956 reveals the following:

	Rs. in lakh
PAT but prior to depreciation	200
Less: Depreciation for the year	30
Net profit after depreciation	170
Less: Provision for loss of Z Ltd., its subsidiary	10
Balance	160

As per its books, the company has unabsorbed business loss of Rs. 30 lakh for the assessment year 2007-08 and Rs. 80 lakh for the assessment year 2008-09. The unabsorbed depreciation as per books are Rs. 20 lakh and Rs. 90 lakh respectively. The carried forward business losses eligible for set off under the Income-tax Act for these two years are Rs. 56 lakh and Rs. 90 lakh respectively.

For the current year, income-tax debited is Rs. 3 lakh and depreciation allowable as per the Income-tax Act is Rs. 40 lakh. The net profit includes a sum of Rs. 40 lakh from export turnover.

Compute the tax payable by X Ltd. for the assessment year 2009-10 [DECEMBER 2005]

Pointwise answer:

	Rs. (in lakh)
<i>Computation of book profit by X Ltd.</i>	
Net profit (given)	160
Add:	
Provision for loss of Z Ltd., its subsidiary	(+) 10
Income-tax	(+) 3

	Rs. (in lakh)
<i>Less:</i>	
Brought forward unabsorbed depreciation	(-) 20
Brought forward unabsorbed loss	(-) 80
	73
Book profit	
<i>Computation of taxable income by X Ltd.</i>	
Net profit (given)	160
<i>Add:</i>	
Provision for loss of Z Ltd., its subsidiary	(+) 10
Income-tax	(+) 3
<i>Less:</i>	
Depreciation	(-) 10
Brought forward unabsorbed loss	(-) 146
	-
Brought forward unabsorbed depreciation	
Taxable income	17
<i>Computation of tax liability under normal provisions</i>	
Tax on net income (i.e., 30% of Rs. 17 lakh)	5.1
<i>Add:</i> Surcharge (@ 10% of tax in case net income exceeds Rs. 1 crore)	Nil
	5.1
Tax and surcharge	
<i>Add:</i> Education cess (2% of 5.1)	0.102
<i>Add:</i> Secondary and higher education cess (1% of income-tax and surcharge)	0.051
Tax liability	5.253
<i>Computation of tax under section 115JB</i>	
10% of book profit	7.3
<i>Add:</i> Surcharge (10% of tax in case net income exceeds Rs. 1 crore)	Nil
	7.3
Tax and surcharge	
<i>Add:</i> Education cess (2% of tax and surcharge)	0.146
<i>Add:</i> Secondary and higher education cess (1% of income-tax and surcharge)	0.073
Tax liability	7.519

Tax payable as computed under normal provisions (i.e., ignoring provisions of section 115JB) is less than the amount determined as tax payable under section 115JB. Therefore, section 115JB is applicable.

Note - It is assumed that brought forward unabsorbed loss is before depreciation.

7.10 Return of income

Problem 7.10-1 - Answer the following:

1. Fill in the blank - Time-limit for filing revised return when assessment has not been completed, isfrom the end of the assessment year.
2. X & Co., a partnership firm, whose turnover is Rs. 62,00,000 filed its return of income on September 29, 2009, showing a loss of Rs. 2,40,000. On October 29, 2009, it is seen that certain expenses to the extent of Rs. 80,000 have been omitted to be claimed. Can a revised return be filed in December 2009? Will your answer be different if the origin return had been filed on October 3, 2009? [DECEMBER 2007]

■

Pointwise answer:

1. Before the expiry of one year from the end of the relevant assessment year.
2. See para 357. In case original return is filed on September 29, 2009, revised return can be filed in December 2009. However, in case original return is filed on October 3, 2009, revised return cannot be filed by X & Co.

Problem 7.10-2 - Specify the correct answer:

1. If a return of income filed by an assessee is considered defective under section 139(9) the assessee is allowed to rectify the defect within - (i) 30 days, (ii) 1 month, (iii) 60 days, (iv) 15 days.

2. Fill up the gaps:

A revised return under section 139(5) may be filed withinyears from the end of assessment year or before completion of assessment whichever is..... [JUNE 2006]

Pointwise answer:

1. (iv) 15 days.
2. 1 year; earlier.

Problem 7.10-3 - The time-limit for moving a rectification petition under section 154 is four years from the date of the order of the AO sought to be rectified. Discuss. [DECEMBER 2005]

No amendment under section 154 can be made after the expiry of 4 years from the end of the financial year in which the order sought to be amended was passed. See para 369.4.

Problem 7.10-4 - See Problem 372-P3 (points 10 and 11). [JUNE 2004 (NEW)]

See answer to Problem 372-P3 (points 10 and 11).

7.11 Business restructuring

Problem 7.11-1 - State the conditions to be satisfied for a 'merger' to qualify as 'amalgamation' for purposes of the Income-tax Act and give two instances of transactions not to be treated as amalgamation. [DECEMBER 2007]

See para 516.1 and para 516.2.

Problem 7.11-2 Detail the implications of 'demerger' with reference to income-tax. [JUNE 2007]

See para 517.

Problem 7.11-3 Discuss the following:

1. A machinery costing Rs. 2,00,000 acquired four years back and used in the assessee's factory was destroyed by fire on March 21, 2008. As per the reinstatement clause with the insurance company, the latter replaced on May 12, 2008 the destroyed machine by a new one whose current cost is Rs. 3,00,000. Discuss the implications of the same in the context of capital gains and impact on the written down value of the concerned block of asset stating clearly the assessment year involved.

2. Continuing the above problem, assuming that there is some capital gains, can the same be avoided if the assessee is willing to invest his surplus funds in eligible investments under section 54EC? The company is advised that since the resultant capital gain is short-term gain under section 50 the same is not possible. State your views.

3. X Ltd., has unit C which is not functioning satisfactory. The details of its fixed assets are:

Asset	Date of acquisition	Book value (Rs. in lakh)
Land	February 10, 2007	30
Goodwill (raised in books on March 31, 2008)		10
Machinery	April 5, 2001	40
Plant	April 12, 2007	20

The written down value is Rs. 25 lakh in case of machinery and Rs. 15 lakh in case of plant. The liabilities on this unit on March 31, 2009 are Rs. 35 lakh. There are two options (as on March 31, 2009):

1. Slump sale to Y & Co. for a consideration of Rs. 85 lakh.
2. Individual sale of assets for the following consideration:
 - (a) Land Rs. 48 lakh, (b) Goodwill Rs. 20 lakh, (c) Machinery Rs. 32 lakh, (d) Plant Rs. 17 lakh.

Which option is to be chosen and why? The other units are deriving taxable income and there are no carried forward losses or depreciation for the company as a whole. Unit C was started on January 1, 2001. [DECEMBER 2004]

Pointwise answer:

1. See problem 176.15-P4 Situation 2 for detailed discussion.

2. See para 182.4.

3. Option I: Slump sale

Computation of net worth of Unit C

Rs. (in lakh)

Land (book value)	30
Goodwill (book value) [not to be considered as it is raised in books by book entry; not actually purchased]	Nil
Machinery (WDV given)	25
Plant (WDV given)	15
Total	<u>70</u>
Less: Liabilities	<u>35</u>
Net worth	<u>35</u>
Computation of capital gain	
Sales consideration	85
Less: Net worth	<u>35</u>
Long-term capital gain (Unit C started on January 1, 2001)	<u>50</u>
Computation of tax liability	
Tax on Rs. 50 lakh @ 20%	10
Add: Surcharge (10% of tax in case net income exceeds Rs. 1 crore)	<u>Nil</u>
Tax and surcharge	10
Add: Education cess (2% of tax and surcharge)	0.2
Add: Secondary and higher education cess (1% of income-tax and surcharge)	<u>0.1</u>
Tax liability under option I	<u>10.3</u>
Receipt after tax [Rs. 85 lakhs - Rs. 10.3 lakh]: Rs. 74.7 lakhs	
Option II: Sale of individual assets	
Computation of capital gains	

Sale consideration	48	20	32	17
Less: Cost of acquisition*/written down value**	30*	-	25**	15**
Long-term capital gain*/Short-term capital gain**	18**	20*	7**	2**

Computation of tax liability	Rs. (in lakh)
Tax on long-term capital gain @ 20%	4
Tax on short-term capital gain @ 30%	<u>8.1</u>
Total	12.1
Add: Tax and surcharge (10% of tax in case net income exceeds Rs. 1 crore)	<u>Nil</u>
Tax and surcharge	12.1
Add: Education cess (2% of tax and surcharge)	0.242
Add: Secondary and higher education cess (1% of income-tax and surcharge)	<u>0.121</u>
Tax liability	<u>12.463</u>
Receipt after tax [i.e., sale consideration Rs. 117 lakhs - Rs. 12.463 lakh]: Rs. 104.537 lakhs	
Option II is better option for X Ltd. as it leads to higher after-tax receipts.	

Problem 7.11-4 - What is 'slump sale'? Explain provisions relating to slump sale. [JUNE 2004 (NEW)]

■

See para 520.

Problem 7.11-5 - State the conditions that should be satisfied for a merger to qualify as an "amalgamation" for the purpose of Income-tax Act. [DECEMBER 2003]

■

See para 516.1-1.

7.12 Tax planning

Problem 7.12-1 Discuss the following:

1. Distinguish between Tax Planning and Tax Management.
2. Discuss tax considerations with reference to specific management decision regarding 'make' or 'buy'. [JUNE 2004]

Pointwise answer:

1. See para 525.
2. See para 528.1

Problem 7.12-2 - State the factors that influence the managerial decision-making relating to owning or leasing fixed assets. [JUNE 2004, (NEW)]

See para 164.4.

Problem 7.12-3 - State the main ingredients which make tax planning a legitimate exercise. [DECEMBER 2003]

See para 525.

Problem 7.12-4 X (25 years), a resident Indian, furnishes the following information for the year ended March 31, 2009 :

	Rs.
Business income	4,60,000
Brokerage earned from Country Y	60,000
Tax paid in Country Y for above (in equivalent INR)	36,000
Long-term capital gains	1,40,000

India does not have any double taxation avoidance agreement with Country Y. Is he entitled to any double taxation relief, and if so, how much? [DECEMBER 2003]

	Rs.
1. Computation of double taxation relief available to X	
Business income	4,60,000
Foreign business income (brokerage earned from Country Y)	60,000
Long-term capital gains	1,40,000
Total income	6,60,000
Tax	89,000
Add: Surcharge (not applicable as net income does not exceed Rs. 10 lakh)	Nil
Tax and surcharge	89,000
Add: Education cess (2% of tax and surcharge)	1,780
Add : Secondary and higher education cess (1% of income-tax and surcharge)	890
Indian tax liability	91,670
Indian average rate of tax (a)	13.89%
Country Y average rate of tax (b)	60%
Rate at which rebate is admissible under section 91 [(a) or (b), whichever is less]	13.89%
Doubly taxed income	60,000
Amount of double taxation relief [13.89% of Rs. 60,000]	8,334
Tax payable in India	83,340

Problem 7.12-5 - What are the various taxation aspects to be considered by management in deciding to shut down or continue a business unit? [DECEMBER 2003]

See para 528.6.

Problem 7.12-6 - Distinguish between tax avoidance and tax evasion. [DECEMBER 2003]

See para 525.

Problem 7.12-7 - If you are asked to design the remuneration package for an employee, state the tax planning measures you will consider to minimize the tax liability of the employee and at the same time no disallowances are faced by the employer. [JUNE 2003]

See para 529.

7.13 Interest

Problem 7.13-1 - X Co. Ltd., is required to submit its income-tax return by September 30, 2009. According to the draft return prepared by it, the gross amount of tax payable works out at Rs. 10 lakh, while it had paid Rs. 6 lakh by way of advance tax and Rs. 80,000 by way of deduction of tax at source. It wants to delay the submission of the return up to March 30, 2010. It expects to earn income @ 30 per cent per annum on the money employed in the business, by taking overdraft from the bank at 15 per cent per annum. Advise X Co. Ltd. whether it is worthwhile to delay the submission of the return. [JUNE 2006]

Return should be submitted by September 30, 2009. See problem 372-P1.

Problem 7.13-2 - Tax liability of X, an individual, for the financial year 2008-09 (assessment year 2009-10) is computed as Rs. 1,00,000. X has paid advance tax as follows:

(i) September 10, 2008 - Rs. 20,000, (ii) December 21, 2008 - Rs. 30,000, (iii) March 11, 2009 - Rs. 35,000.

X intends to file his income-tax return with balance tax and interest payable. There was no TDS from any of his income. Compute the tax and interest payable if (i) Balance tax and interest are paid on July 21, 2009 and return is filed on same date. (ii) Balance tax and interest are paid on January 4, 2010 and he files return on same date. (iii) Balance tax and interest are paid on July 21, 2009, but he forgot to file return and return is later filed on January 4, 2010. [DECEMBER 2004]

Computation of interest payable under section 234C for deferment of advance tax

Due date for payment of advance tax	Amount which should have been paid Rs.	Amount actually paid Rs.	Difference Rs.	Interest chargeable	Interest 1% per month Rs.
September 15, 2008	30,000	20,000	10,000	3	300
December 15, 2008	60,000	20,000	40,000	3	1,200
March 15, 2009	1,00,000	85,000	15,000	1	150

Total interest under section 234C (in all cases)

Rs. 1,650

Computation of interest payable under section 234B for default in payment of advance tax

Case I (Rs. 15,000 × 4 × 1%)

Rs. 600

Case II (Rs. 15,000 × 10 × 1%)

Rs. 1,500

Case III (Rs. 15,000 × 4 × 1%)

Rs. 600

Computation of interest payable under section 234A for default in filing return of income

Case I - No interest under section 234A as return for the assessment year 2009-10 is filed before the due date of filing return of income, i.e., July 31, 2009.

Case II - There is delay in filing return of income by 6 months and, consequently, interest payable under section 234A is Rs. 900 (Rs. 15,000 × 6 × 1%).

Case III - Interest under section 234A is not applicable as balance tax and interest are paid before the due date of filing return of income though the return is actually filed in January 2010. See also para 385.1-2a.

The answer is summarized as under :

	Case I Rs.	Case II Rs.	Case III Rs.
Balance tax payable	15,000	15,000	15,000
Interest under section 234A	Nil	900	Nil
Interest under section 234B	600	1,500	600
Interest under section 234C	1,650	1,650	1,650
Total tax and interest	17,250	19,050	17,250

7.14 Transfer pricing

Problem 7.14-1 - Fill in the gaps.

The Assessing Officer may refer the computation of _____ price under section 92C to the Transfer Pricing Officer if he considers it necessary and expedient. [JUNE 2007]

■
Arm's length

Problem 7.14-2 - Define 'Arm's length price'. State the context in which this term has been defined. [JUNE 2005]

■
See paras 508.1 and 507.1.

Problem 7.14-3 - Discuss the following :

1. What is "transfer pricing"? Why the provisions were introduced in the Income-tax Act in respect of transfer pricing? What are the methods provided in the Income-tax Act to determine price, where provisions of transfer pricing are applicable?

2. A Ltd., an Indian company, sells computer monitor to its 100 per cent subsidiary X Ltd. in United States @ \$ 50 per piece. A Ltd. also sells its computer monitor to another company Y Ltd. in United States @ \$ 80 per piece. Total income of A Ltd. for the assessment year 2009-10 is Rs. 12,00,000 which includes sales made for 100 computer monitors @ \$ 50 to X Ltd. Compute the arm's length price and taxable income of A Ltd. The rate of one dollar may be assumed to be equivalent to Rs. 49 for the sake of simplicity. [JUNE 2003]

■
Pointwise answer :

1. See paras 507 to 509.
2. See problem 509.6-P4.

7.15 Wealth-tax

Problem 7.15-1 - Answer the following:

1. State with reason if the following is True or False.

Shares held by an individual are not to be included in computing his net wealth.

2. Enumerate the list of persons/entities treated as "individual" under section 3.

3. Who are the persons/entities to whom Wealth-tax is not applicable under section 45?

4. Is wealth-tax a debt owed on the valuation date and hence deductible while computing net wealth?

5. On what grounds can it be said that partial partition is de-recognized?

6. How far is the exemption of public charitable trust under the Income-tax Act, 1961 relevant for exemption under the Wealth-tax Act? [DECEMBER 2007]

■
Pointwise answer:

1. True, shares are not assets.
2. As per section 3 of the Wealth-tax Act, only an individual, HUF and a company is chargeable to wealth-tax.
3. See para 540.
4. No, see para 548.1-1.
5. See para 550.3.
6. See para 550.1.

Problem 7.15-2 Discuss the following:

1. Net wealth of an assessee in excess of Rs. _____ is taxable under the Wealth-tax Act, 1957 at _____ per cent.

2. Enumerate entities to which provisions of Wealth-tax Act do not apply.

3. Under Wealth-tax Act, what is the scope of taxation of an individual not residing in India?

4. A company incorporated outside India is not liable to Wealth-tax. Discuss.

5. Is the interest in Co-operative Society taxable in the hands of its members?

6. A child artist, acting in films, amassed a wealth of Rs. 20 lakh over a few years which was held in the form of shares by his father and guardian. The shares were sold in 2008-09 resulting in a capital gain of Rs. 15 lakh, which was invested in a plot of land. The Wealth-tax Officer proposes to include the value of the plot land in the net wealth of the father under section 4(1). Is this in order? [JUNE 2007]

■

Pointwise answer:

1. Rs. 15,00,000, 1 per cent.

2. See para 540 (point 3).

3. In case of a resident but not ordinarily resident or a non-resident, the value of assets and debts located in India are includible in his net wealth. However, the value of assets and debts located outside India is not includible in his net wealth. [sec. 6]

4. A company incorporated outside India is not liable in respect of assets and debts located outside India. However, in respect of its net wealth located within India, the company is liable for Wealth-tax.

5. As per the decision in *Kishore B. Setalvad v. CWT* [2001] 256 ITR 637, the interest in co-operative society is not liable for Wealth-tax in the hands of the members of the co-operative society.

6. The decision of the Wealth-tax Officer to include the value of the plot of land in the net wealth of the father under section 4(1) is correct. The plot of land cannot be considered as having been invested from out of the income earned by exercising skill and talent (on the part of the minor) and it is invested only out of capital gains.

Problem 7.15-3 - The following is the summarized balance sheet of X Ltd. as on March 31, 2009:

Capital and Liabilities	Rs.	Assets	Rs.	Rs.
Paid up capital	90,00,000	Plant and machinery	12,00,000	(10,00,000)
Reserves	20,00,000	Motor car	2,00,000	(1,50,000)
Sundry creditors	20,10,000	Helicopters for business purposes	68,00,000	(50,00,000)
Secured and unsecured loans	16,00,000	Factory plot (purchased January 2, 2007)	14,00,000	(20,00,000)
		House property - used for Director - 1's residence	12,00,000	(6,00,000)
		Used for Director - 2's residence	18,00,000	(28,00,000)
		Jewellery	8,00,000	(14,00,000)
		Shares in other companies	10,00,000	(15,00,000)
		Cash in hand	60,000	(60,000)
		Cash at bank	1,50,000	(1,50,000)
	1,46,10,000		1,46,10,000	(1,46,60,000)

Additional information:

i. Gross annual salaries of Directors 1 and 2 are Rs. 4,80,000 and Rs. 6,00,000 respectively.

ii. Loans of Rs. 16,00,000 represent Rs. 2 lakh for machinery, Rs. 4 lakh for factory plot and Rs. 10 lakh for helicopters.

iii. The factory plot is within municipal limits.

Compute the net wealth of the company as on March 31, 2009 and the wealth tax payable.

■

Pointwise answer:

1. Computation of net wealth

	Rs.
House property used for Director -2 [in case annual salary exceeds Rs. 5 lakh only then, it is included in net wealth]	28,00,000
Factory plot [unused plot for over 2 years is part of net-wealth]	20,00,000
Motor car (it is an asset)	2,00,000
Helicopters for business purposes [helicopter used for commercial purpose not an asset, see para 545.4]	—
Jewellery	14,00,000
Shares in other companies [not an asset]	—
Cash in hand [only unrecorded cash in hand is an asset]	—

Problem 7.15-4 : June 2006*Wealth-tax*

1456

	Rs.
Cash at bank [not an asset]	—
Gross wealth	64,00,000
Less: Loan for factory plot	4,00,000
Net wealth	60,00,000
<i>Computation of wealth tax payable</i>	
Net wealth	60,00,000
Less: First Rs. 15 lakh	15,00,000
Balance	45,00,000
Wealth tax payable [@ 1% of Rs. 45,00,000]	45,000

Problem 7.15-4 - Specify the correct answer:

A motor car is not a chargeable asset under section 2(ea) of the Wealth-tax Act, 1957, if it is used by the assessee in the business of—(i) running it on hire, (ii) infrastructure development, (iii) a new industrial undertaking, (iv) a factory in a remote locality. [JUNE 2006]

■

(i) running it on hire.

Problem 7.15-5 - Identify the correct answer: Land is an asset for Wealth-tax Act, 1957 if it is - (i) Vacant land located in a municipality; (ii) Located beyond 8 kilometres of a municipality/town; (iii) Land on which construction is not permissible; (iv) Land occupied by a building used for business. [DECEMBER 2005]

■

(i) Vacant land located in a municipality.

Problem 7.15-6 - Discuss the following:

X owns the following assets as on March 31, 2009:

Guest house located beyond 30 km. for municipal limits of Patna	20
Let out house (vacant for 3 months) at Udaipur	30
Building used for running own business	18
Cars used exclusively for business use	5
Aircraft	100
Commercial complex at Bangalore	90

The assessee entered into an agreement for sale of Udaipur house in February, 2009 and received an advance of Rs. 15 lakh. The registration of the house was effected on April 10, 2009.

X had gifted cash of Rs. 2 lakh on April 10, 2006 to his wife. She bought jewellery using the cash. The market value of such jewellery as on March 31, 2009 is Rs. 3 lakh. Determine the net wealth and wealth-tax payable by X.

[JUNE 2005]

■

Pointwise answer:

	Rs. in lakh
Computation of net wealth	
Guest house located outside municipal limits	20
Let out house at Udaipur	30
Building used for running own business [not an asset under section 2(ea)]	-
Car used for building purpose	5
Aircraft [assuming it is not used for commercial purpose]	100
Commercial complex at Bangalore [not an asset under section 2(ea)]	-
Jewellery [market value on March 31, 2009 is includible]	3
Net wealth	158

Problem 7.15-7 - State with reasons the treatment of the following for wealth tax purposes:

- a. Urban land on which construction is not permitted.
- b. Urban land bought 12 years ago for construction of factory but construction yet to start.
- c. In the case of an individual, interest in the coparcenary property of the HUF of which he is a member.

- d. The assessee gifted cash of Rs. 2,00,000 on April 10, 2008 to his wife. She bought jewellery using the cash. The market value of such jewellery as on March 31, 2009 is Rs. 3,00,000.
- e. Guest house located beyond 30 km. from municipal limits of Patna.
- f. Building used for running own business.
- g. Residential quarters allotted to workers in a company.
- h. Residential quarters allotted to officers drawing Rs. 40,000 p.m.
- i. The assessee obtained a loan of Rs. 4,00,000 by mortgaging his house. The loan was utilized for purchase of shares. As on March 31, 2009 outstanding loan was Rs. 2,00,000.
- j. Urban land transferred without consideration to minor handicapped child valued as on March 31, 2009 at Rs. 6,00,000.
- k. The assessee transferred assets worth Rs. 10,00,000 to his son's wife for Rs. 3,00,000. [DECEMBER 2004]

■
The answer is as under:

- a. Urban land on which construction is not permitted is not treated as an asset as per section 2(ea)(v).
- b. It is treated as an asset under section 2(ea)(i).
- c. Exempt from wealth tax, see para 547.2.
- d. Rs. 3,00,000 i.e., value as on March 31, 2009 shall be included in the net wealth of the assessee, see para 546.1-1.
- e. Asset as per section 2(ea)(i), see para 545.1.
- f. Not an asset under section 2(ea)(i), see para 545.1-1.
- g. Not an asset under section 2(ea)(i), see para 545.1-1.
- h. Not an asset under section 2(ea)(i), see para 545.1-1.
- i. Shares are not treated as assets as per section 2(ea) of the Wealth-tax Act. Consequently, loan in relation to such shares is not deductible.
- j. Clubbing provisions of section 4(1)(a)(ii) (see para 546.2) are not applicable in the case of minor child who is suffering from any disability of the nature specified under section 80U.
- k. Clubbing provisions of section 4(1)(a)(v) [see para 546.5-1] are applicable and consequently assets transferred to son's wife for inadequate consideration shall be treated as deemed wealth in the hands of transferor assessee.

■
Problem 7.15-8 - Discuss whether the following are taxable assets under Wealth-tax Act for assessment year 2009-10.

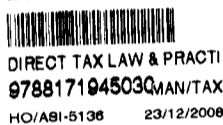
1. a. Motor car, b. Gold deposit bonds;
2. Urban land;
3. Assets held by a minor child;
4. Assets transferred to son's wife. [JUNE 2004]

■
Pointwise answer:

1. The answer is as under:
 - a. See para 545.2.
 - b. See para 545.3-3.
2. See para 545.5.
3. See para 546.2.
4. See para 546.5.

■
Problem 7.15-9 - Discuss whether the following are taxable assets under Wealth-tax Act for the assessment year 2009-10 :

1. Guest house for entertaining personal guests.
2. Office building given on rent.
3. Residential house owned by an individual and allotted to one of his officers whose salary is Rs. 40,000 per month.
4. Residential house owned by a company and allotted to one of its whole-time directors, whose salary is Rs. 40,000 per month.
5. Motor car used by a person as a tourist taxi.



ways.

held by an individual for industrial purposes and which was acquired on March 31, 2006.

10 gm. of gold in 1996 to his wife, who sells it for Rs. 12,50,000 in March 2007 and purchases it again on March 31, 2009 for Rs. 18 lakh. In whose wealth, the value of the house will be included?

What value?

130(25) RS. 500 00

trust for the benefit of his wife in 1973. Who is assessable thereon?

10. X sells a house worth Rs. 10 lakh to his daughter-in-law for Rs. 6 lakh in June 2004. The value of the house on March 31, 2009 is Rs. 12 lakh. Who is assessable thereon? [DECEMBER 2003]

1. See para 545.1.
2. It is an asset as per section 2(ea).
3. It is an asset as per section 2(ea).
4. Residential house owned by a company and allotted to one of its whole-time director (salary is less than Rs. 5,00,000) is not an asset as per section 2(ea).
5. Motor car used by the assessee in the business of running them on hire, i.e., as a tourist taxi is not an asset as per section 2(ea)(ii).
6. Aircraft used by the assessee for commercial purposes is not an asset as per section 2(ea)(iv).
7. See para 545.5-2. It is an asset under section 2(ea)(v).
8. See para 546.1-1. The value of the house, i.e., Rs. 18 lakh shall be included in the net wealth of X.
9. See para 546.3-1. X is assessable with respect to the house.
10. See para 546.5-1. X is assessable with respect to 40% of the house as the consideration is inadequate to the extent of 40%.

Problem 7.15-10 Discuss the following :

1. What are the assets that are included as 'deemed wealth' in computation of net wealth?
2. State how the following would be treated in computation of net wealth for assessment year 2009-10 - Urban land transferred by the assessee to minor handicapped child - Cost price in 1998 : Rs. 3 lakhs, valued on March 31, 2009 at Rs. 5 lakh.

Residential property in Kolkata (let out for residence from September 1, 2008) - Market value Rs. 2.5 lakh.

Yacht purchased in April 2008 by a person of Indian origin who was working in Bahrain from 1985 and returned to India in May 2008, when he remitted the money into India. The yacht was purchased out of money remitted to India from Bahrain : Rs. 2,00,000.

Jewellery received by an assessee from her father at the time of her marriage in 1956 valued on March 31, 2009 at Rs. 1,50,000. [JUNE 2003]

1. Deemed wealth - See para 546.
2. Different assets given in the problem are as follows —
Urban land - It is held by a handicapped child. It is taxable in the hands of the child.
Residential house - Since it is let out for residential purposes for less than 300 days, it is an "asset" chargeable to tax. However, one can claim exemption under section 5(vi).
Yacht - It is exempt under section 5(v) for 7 assessment years commencing from the assessment year 2009-10.
Jewellery - It is an "asset" chargeable to tax in the hands of the taxpayer.

7.16 Taxation of partnership firms

Problem 7.16-1 - What is the maximum remuneration allowable as deduction under income-tax to working partner of a firm which is carrying on a legal profession? [JUNE 2005]

See para 317.4.