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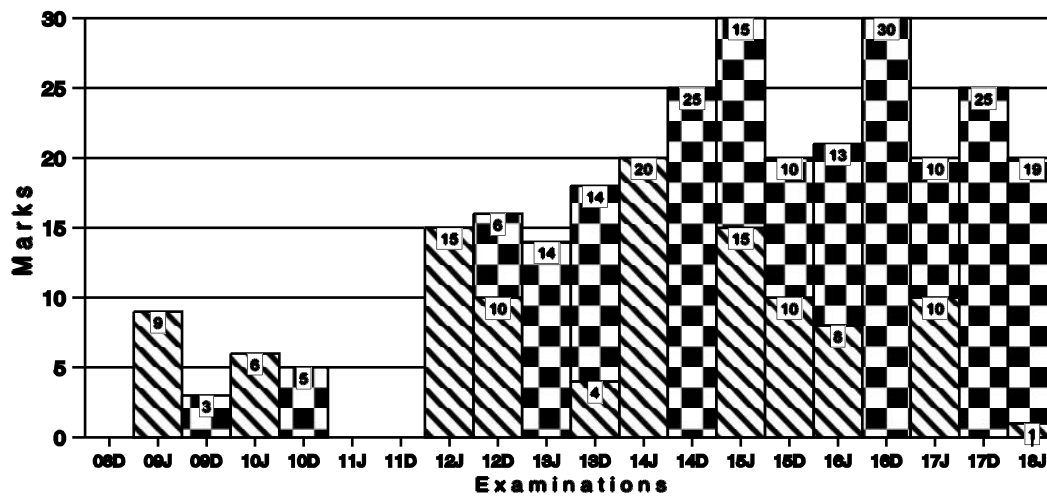
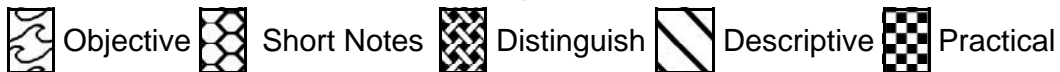
## TAXATION OF INDIVIDUALS PARTNERSHIP FIRMS/LLP AND COMPANIES

### THIS CHAPTER INCLUDES

- Basic Concepts and Taxation of Individuals
- Taxation of Companies.
- Taxation of Partnership Firm/Limited Liability Partnership (LLP)

Marks of Objective, Short Notes, Distinguish Between, Descriptive & Practical Questions

### Legend



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## CHAPTER AT A GLANCE

Topic	Important Highlight
<b>"Assessment Year" Section 2(9)</b>	It means the period of twelve months commencing on the 1st day of April every year.
<b>Person [Section 2(31)]</b>	It includes Individual, HUF, Firm (or Limited Liability Partnership), Company, AOP/BOI – whether incorporated or not, Local Authority, AJP (Artificial Juridical Person).
<b>Assessee [Section 2(7)]</b>	It means person by whom any sum of tax, interest or penalty is payable. It includes a person in respect of whom any proceeding has been undertaken, a deemed assessee and an assessee in default.
<b>Section 115BA</b>	In order to provide relief to newly setup domestic companies engaged solely in the business of manufacture or production of article or thing, a new section 115BA inserted to provide that the income-tax payable in respect of the total income of a domestic company for any previous year relevant to the assessment year beginning on or after the 1st day of April, 2017 shall be computed @ 25% at the option of the company, if, - (i) the company has been setup and registered on or after 1st day of March, 2016 and is engaged in the business of manufacture or production of any article or thing and is not engaged in any other business;

	<p>(ii) the company while computing its total income has not claimed any benefit under section 10AA, benefit of accelerated depreciation, benefit of additional depreciation, investment allowance, expenditure on scientific research and any deduction in respect of certain income under Part-C of Chapter-VI-A other than the provisions of section 80JJAA; and</p> <p>(iii) the option is furnished in the prescribed manner before the due date of furnishing of income.</p>
<p><b>Notional Income From House Property [Section 23(5)]</b></p>	<p>Annual value of house property held by a person as stock in trade shall be taken as <b>NIL</b> if following conditions are satisfied:</p> <p>(a) The Property (consisting of buildings or land appurtenant thereto ) is held as stock in trade by the owner of the property;</p> <p>(b) The property (or any part of property) is not let out during whole or any part of the previous year.</p> <p>Above benefit/concession is available only for 1 year from the end of the financial year in which certificate of completion of construction of the property is obtained from the competent Authority. <b>(Amendment vide Finance Act, 2017)</b></p>
<p><b>Deemed Ownership [Section 27]</b></p>	<p>Transferor/any other person will be deemed to be owner in the following cases and not the legal owner:</p> <p>(a) <b>Transfer to Spouse for inadequate consideration:</b> Transferor will be treated as deemed owner. However, transferor will not be treated as owner if property is transferred to spouse in pursuance of an agreement to live</p>

	<p>apart.</p> <p>(b) <b>Minor Child:</b> Parent will be treated as deemed owner. However, in case of transfer to minor married daughter, parent will not be treated as deemed owner.</p> <p>(c) <b>Co-operative Society or Company:</b> In case house property is in the name of co-operative society or company but the beneficial owner is member or shareholder of these, then deemed owner will be member/shareholder of such co-operative society or company.</p> <p>(d) <b>Part performance of contract:</b> In case possession of immovable property has been transferred in part performance of the contract, then deemed owner would be the person having possession.</p> <p>(e) <b>Lease of at least 12 years:</b> In case immovable property is on lease and lease period exceeds 12 years and at least one year at a time renewable thereafter, then, lessee will be deemed as owner in this case.</p>
<p><b>Method of Accounting [Section 145]</b></p>	<p>Income from business or profession is computed as per the method of accounting followed by the assessee.</p> <p>Assessee has the choice of following either the accrual/mercantile method or cash basis of accounting.</p> <p>If the assessee maintains its accounts on mercantile basis, the income would be taxable on accrual basis irrespective of receipt. A company is required to maintain its accounts only on mercantile system. However, if the accounts are maintained on the cash basis, then, income would be chargeable to</p>

	tax in that financial year in which it is received irrespective of accrual.
	<p><b>Note:</b> In this chapter, the word 'paid' means actually paid or payable as per the method of accounting followed by the assessee.</p> <p>The Central Government has notified in the Official Gazette from time to time [income computation and disclosure standards] to be followed by any class of assessee or in respect of any class of income. Where the Assessing Officer is not satisfied about the correctness or completeness of the accounts of the assessee, or where the method of accounting provided in sub-section (1) [has not been regularly followed by the assessee, or income has not been computed in accordance with the standards notified under sub-section (2)], the Assessing Officer may make an assessment in the manner provided in section 144.</p>
<b>Block of Assets</b> <b>[Section 2(11)]</b>	It means a group of assets falling within a class of assets in respect of which same rate of depreciation is prescribed. There are four classes of assets on which depreciation is allowed i.e. Building, Furniture or fittings, Plant & Machinery and Intangible assets. Separate rates of depreciation are prescribed for these asset classes. Therefore, example of a block of asset may be two buildings (same class) having depreciation rate of 10% (same rate) (this will constitute one block of asset for calculating depreciation) and another block could be three machines (same class) having depreciation rate of 15% (same rate).

<p><b>Eligible Projects or Schemes [Section 35AC]</b></p>	<p>Assessee shall be allowed a deduction of the amount of expenditure paid to a public sector company or a local authority or to an association or institution approved by the National Committee for carrying out any eligible project or scheme or for the payment made to a corporate assessee who itself carries out any eligible project or scheme.</p> <p><b>Note:</b> No deduction under this section shall be allowed in respect of any assessment year commencing on or after the 1st April, 2018.</p> <p><b>[Amendment vide Finance Act, 2016]</b></p> <p>Eligible project or scheme means such project or scheme for promoting the social and economic welfare of, or the uplift of, the public.</p>
<p><b>Deductions [Section 36]</b></p>	<p>Following expenses are allowed as deduction while computing income from business or profession:</p> <p>(a) <b>Insurance of stock [Section 36(1)(i)]:</b> Insurance premium paid in respect of insurance against risk of damage or destruction of stocks or stores used for purpose of business is allowed as deduction;</p> <p>(b) <b>Insurance premium for life of cattles [Section 36(1)(ia)]:</b> Premium paid by a federal milk cooperative society insuring the life of the cattle owned by a member of a primary co-operative society, engaged in supplying milk raised by its members to such federal milk co-operative society.</p> <p>(c) <b>Insurance premium on health of employees [Section 36(1)(ib)]:</b> Any premium paid by employer on health of employees by modes other than cash, is allowed as deduction. Premium should be paid under a scheme</p>

	<p>framed in this behalf by the General Insurance Corporation of India and approved by the Central Government or any other insurer and approved by IRDA.</p> <p>(d) <b>Bonus or commission paid to employees [Section 36(1)(ii)]:</b> Any sum paid to an employee as bonus or commission for services rendered, is allowed as deduction subject to section 43B of the Act.</p> <p>(e) <b>Interest paid on money borrowed for the purpose of business or profession [Section 36(1)(iii)]:</b> Interest paid in respect of capital borrowed for the purpose of business or profession shall be allowed as deduction subject to Section 43B if loan is borrowed from banks or financial institution. Interest before commencement of business is not allowed as deduction. However, it can be amortised over a period of 5 years under Section 35D from the Financial year in which business is commenced.</p>
	<p>(f) <b>Employer's contribution towards Recognised provident fund or an approved superannuation fund [Section 36(1)(iv)]:</b> It is allowed as deduction subject to section 43B. As per section 40A(9), contribution towards any non-statutory fund or unapproved fund is not allowed as deduction.</p> <p>(g) <b>Employer's contribution towards pension scheme referred in section 80CCD [Section 36(1)(iva)]:</b> It will be allowed as deduction to the extent of 10% of salary of the employee in the previous year, subject to section 43B.</p>

Salary includes Basic salary and Dearness allowance (forming part of salary for superannuation benefits), but it excludes all other allowances and perquisites.

(h) **Employer's contribution towards an approved gratuity fund [Section 36(1)(v)]:** It is allowed as deduction subject to section 43B of the Act. As per section 40A(7), contribution towards unapproved gratuity fund is not allowed as deduction. Where employee retires during the year, gratuity actually paid to employee is allowed as deduction if no deduction was claimed earlier.

(i) **Employee's contribution towards provident funds etc. [Section 36(1)(va)]:** Any sum received by the assessee from his employees as contributions to any provident fund or superannuation fund or any fund set up under the provisions of the Employees' State Insurance Act, or any other fund for the welfare of such employees, is treated as income in the hands of the assessee as per section 2(24) of the Act.

The aforesaid amount is allowed as deduction under section 36(1)(va) only if such employee's contribution is credited in employee's account on or before the 'due date' specified under the specific act relating to provident fund, superannuation fund etc. If this amount is paid after due date, then deduction is never allowed to the assessee.

(j) **Dead or useless animals [Section 36(1)(vi)]:** In respect of animals which have been used for the purpose of business or profession



otherwise than as stock in trade and have died or become permanently useless for such purposes, the differences between the actual cost of the animals and the amount, if any, realised in respect of the carcasses or animals is allowed as deduction.

(k) **Bad Debts [Section 36(1)(vii)]:** Bad debt should be allowed as deduction if it relates to a debt and such debt should be in respect of a business carried on by the assessee. Such debt has been taken into account in computing the business income of the assessee in any of the earlier previous year. Provided that where the amount of such debt or part thereof has been taken into account in computing the income of the assessee of the previous year in which the amount of such debt or part thereof becomes irrecoverable or of an earlier previous year on the basis of income computation and disclosure standards without recording the same in the accounts, then, such debt or part thereof shall be allowed in the previous year in which such debt or part thereof becomes irrecoverable and it shall be deemed that such debt or part thereof has been written off as irrecoverable in the accounts for the purposes of this clause.

(l) **Bad and Doubtful Debt to Scheduled Bank and Co-operative Society [Section 36(1)(viiia)]:**

Deduction in respect of provision for bad and doubtful debt to scheduled bank and co-operative society is allowed @ 8.5% of total income (before taking deduction under this

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	<p>section and deductions under chapter VI-A of Income Tax Act) instead of 7.5%.</p> <p>(m) <b>Special reserve created and maintained by Financial Corporation [Section 36(1)(viii)]:</b> Deduction is allowed for special reserve so created by financial corporation to the extent of lower of the following 3 amounts:</p>
	<ul style="list-style-type: none"><li>(i) 20% of the profits derived from such business before making deduction under this clause carried to such reserve account, or</li><li>(ii) Amount transferred to special reserve</li><li>(iii) Where such special reserve exceeds from time to time 200% of (paid up share capital and general reserve as on the last day of the previous year minus the balance of the special reserve account on the first day of the previous year), no allowance under this clause shall be made in respect of such excess.</li></ul>

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|  | <p>(n) <b>Family planning expenditure incurred by Company [Section 36(1)(ix)]:</b> Revenue expenditure incurred by the company for promoting family planning is fully allowed as deduction. Capital expenditure for promoting family planning amongst its employees is allowed as deduction in 5 equal annual instalments from the year in which expenditure is incurred.</p> <p>(o) <b>Securities transaction tax (STT) [Section 36(1)(xv)]:</b> STT paid by the assessee during the previous year shall be allowed as deduction subject to the condition that income from taxable securities transaction is included under the head PGBP.</p> |
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	<p>(p) <b>Commodities Transaction Tax [Section 36(1)(xvi)]:</b> A new tax called Commodities Transaction Tax (CTT) is levied on taxable commodities transactions entered into in a recognised association. Section 36 of the Income-tax Act is amended to provide that an amount equal to the commodities transaction tax paid by the assessee in respect of the taxable commodities transactions entered into in the course of his business during the previous year shall be allowable as deduction, if the income arising from such taxable commodities transactions is included in the income computed under the head "Profits and gains of business or profession".</p> <p>(q) <b>Expenditure incurred by a co-operative society [Section 36(1)(xvii)]:</b> The amount of expenditure incurred by a co-operative society engaged in the business of manufacture of sugar for purchase of sugarcane at a price which is equal to or less than the price fixed or approved by the Government.</p>
<p><b>Tax Audit [Section 44AB]</b></p>	<p>Following assesseees are required to get their accounts of previous year audited by a Chartered Accountant:</p> <p>(a) In case of a business: If total sales, turnover or gross receipts exceed ₹ 1 crore in any previous year; or</p> <p>(b) <b>In case of a profession:</b> if gross receipts exceed ₹ 50 lakhs in any previous year. [Amendment vide Finance Act, 2016 w.e.f. 1st April, 2017]</p>

	<p><b>Note1:</b> Person falling under section 44AD, 44ADA, 44AE, 44BB or 44BBB and claiming a lower income than specified in these sections also need to get their accounts audited.</p> <p><b>Note2:</b> Section 44AB is not applicable to person whose turnover/sales/gross receipts does not exceed 2 crores and who opts to declare profits as per provisions of Section 44AD(1). [Amendment vide Finance Act, 2017 w.e.f. AY 2017-18]</p>
<p><b>Tax Treatment of Gold Monetization Scheme, 2015</b></p>	<p>Under the existing provisions of section 10, interest on Gold Deposit Bonds issued under Gold Deposit Scheme, 1999 is exempt. Further, these bonds are excluded from the definition of capital asset and therefore exempt from tax on capital gains.</p> <p>The Gold Monetization Scheme, 2015 has since been introduced by the Government of India. With a view to extend the same tax benefits to the scheme as were available to the Gold Deposit Scheme, 1999 Clause (14) of section 2 has been amended, so as to exclude Deposit Certificates issued under Gold Monetisation Scheme, 2015 notified by the Central Government, from the definition of capital asset and thereby to exempt it from capital gains tax. Further, clause (15) of section 10 has also been amended so as to provide that the interest on Deposit Certificates issued under the Scheme, shall be exempt from income-tax.</p> <p><b>This amendment effective from 1st April, 2017 and accordingly apply in relation to assessment year 2017-18 and subsequent assessment years.</b></p>

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<b>Conversion of Company Into LLP</b>	Section 47(xiiib) of the Act has been amended to provide that in addition to the existing conditions to be satisfied for not considering the conversion of private limited company into LLP as transfer, a further condition that the value of the total assets in the books of accounts of the company in any of the three previous years preceding the previous year in which the conversion takes place, should not exceed five crore rupees is also required to be satisfied. <b>These amendments effective from the 1st day of April, 2017 and accordingly apply in relation to assessment year 2017-18 and subsequent years.</b>
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**SHORT NOTES**

**2008 - Dec [4]** (b) Write a short note on the following:

- (i) The activities of a co-operative society which are eligible for deduction under section 80P. **(3 marks) [CSEPM - I]**

**Answer:**

The activities of a co-operative society which are eligible for deduction @ 100% under **Section 80P** are as follows:

- (i) Income from banking business & providing credit facilities to its members
- (ii) Cottage Industry
- (iii) Marketing agricultural produce
- (iv) Purchase of agricultural implements
- (v) Processing of agricultural produce without aid of power of its member
- (vi) Collective disposal of Labour for its members
- (vii) Primary Society engaged in supply of milk, oilseeds, fruits etc
- (viii) Investment in securities

(ix) Letting of Godowns & warehouses.

**2010 - Dec [6]** (a) Write a short note on the following:

- (v) Tax on income of foreign institutional investors from capital gains arising from transfer of their securities. **(3 marks) [CSEPM - I]**

**Answer:**

Tax on income of Foreign Institutional Investors from securities or capital gains arising from their transfer [**Section 115AD**] – (Applicable only to Foreign Institutional Investors)

**Special provisions regarding rate of tax:**

Where the total income of the above assessee includes:

- (a) Income received in respect of securities (other than units of mutual funds covered **under section 10(23D)** or of Unit Trust of India); or  
(b) Income by way of short-term or long-term capital gains arising from the transfer of such securities.

The income-tax on the total income shall be chargeable as under:

- |                                                                                        |                                                  |
|----------------------------------------------------------------------------------------|--------------------------------------------------|
| (i) on the income in respect of securities referred to in clause (a) above             | 20%                                              |
| (ii) on the income by way of interest referred to in section 194LD                     | 05%                                              |
| (iii) on the income by way of short-term capital gains referred to in clause (b) above | 30%                                              |
| (iv) on the income by way of long term capital gains referred to in clause (b)above    | 10%                                              |
| (v) on the balance income included in total income                                     | special/<br>normal rate<br>as the case<br>may be |

**2011 - Dec [5]** (a) Write a short note on the following:

- (i) Deduction in respect of interest on loan taken for higher education.

**(3 marks) [CSEPM - I]**

**Answer:**

The deduction **under section 80E** is available to an individual if following

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conditions are satisfied:

1. Deduction available only to Individual not to HUF or other type of Assessee.
2. **Deduction amount:** The amount of interest paid is eligible for deduction and moreover there is no cap on the amount to be deducted. You can deduct the entire interest amount from your taxable income. However there is no benefit available on the repayment of principal amount of the loan.
3. Deduction available if Interest has been paid during the previous year and was paid out of income chargeable to tax which means if repayment is made from income not chargeable to tax then deduction will not be available.
4. Interest should have been paid on loan taken by him from any financial institution or any approved charitable institution for the purpose of pursuing his higher education. Interest on Loan taken from relatives or friends will not be eligible for deduction **under section 80E**.
5. Loan should have been taken for the purpose of pursuing higher studies of Individual, Spouse, Children of Individual or of the student of whom individual is legal Guardian.
6. The whole of the amount paid during previous year towards interest is allowed as deduction and deduction shall be allowed for 8 assessment years starting from the assessment year in which the assessee starts paying the interest on loan, or until the interest thereon is paid by the assessee in full, whichever is earlier.

**DESCRIPTIVE QUESTIONS**

**2009 - June [3]** (a) When will the 'book profits' of a company deemed to be the total income of the company for the purposes of levy of minimum alternate tax (MAT) under section 115JB? **(3 marks)**

**(b)** Indicate briefly the points to be taken into account while preparing



- annual accounts for the purpose of MAT. (3 marks)
- (c) The MAT does not apply to foreign companies operating in India. Do you agree? Give reasons. (3 marks)

**Answer:**

- (a) Minimum alternate tax on certain companies under **Section 115 JB** Wherein the case of a company, the income tax payable on the total income as computed under the Income Tax Act, in respect of previous year relevant to the assessment year 2018-19 or thereafter is less than 18.5% of its book profit, such book profit shall be deemed to be the total income of the assessee and the tax payable by the assessee on such total income (book profit) shall be the amount of the income tax at the rate of 18.5%.
- “Mat rate to be 9% instead of 18.5% in case of a unit located in an International Financial Services Centre [Section 115JB(7), inserted by the Finance Act, 2016, w.e.f. A.Y. 2017-18.]”
- (b) According to **sub-section (2) of section 115 JB** requires the company to prepare its profit and loss account for the relevant previous year in accordance with provisions of Part II and III of Schedule III of the **Companies Act, 2013**. However, while preparing the annual accounts including profit and loss account:
- The accounting policies of the company;
  - The accounting standards followed for preparing such accounts including profit and loss accounts;
  - The method and rates adopted for calculating the depreciation by the company, shall be the same as have been adopted for the purpose of preparing such accounts including profit and loss account as laid before the company at its annual general meeting in accordance with on the provisions of **Section 129** of the **Companies Act, 2013**. But where the company has adopted or adopts the financial year which is different from the previous year under the Income Tax Act, (a), (b) and (c) aforesaid shall correspond to the accounting policies, accounting standards and the method

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and rates for calculating the depreciation which have been adopted for preparing such accounts including profit and loss account for such financial year or part of such financial year falling within the relevant previous year.

- (c) No, MAT is applicable to any Company (whether Indian or Foreign, resident or non-resident, closely held or widely held company). So MAT is applicable to foreign companies too which is operating in India.

**Judicial Decisions:**

Applicability of **Section 115JB** is not confined to a domestic company but it applies to both resident company and a non-resident company.

**2009 - Dec [4]** (a) What are the special provisions for computing profits and gains of retail business? **(5 marks) [CSEPM - I]**

(b) What are the provisions relating to clubbing of income arising to spouse from the assets transferred? **(5 marks) [CSEPM - I]**

**Answer:**

(a) Provisions **under section 44 AD** shall become Applicable in case of an assessee engaged in any business except the business of plying, hiring or leasing goods carriage, 8% of the total turnover or such higher income as may be filed by the assessee in his income tax return shall be deemed to be the profits of such business. This provision applies only if the total turnover of sales of such retail business does not exceed ₹ 2 crore. In calculating such presumptive profits @ 8% of sales the said provisions shall have to be considered:

- (i) All deductions **u/s 30 to 38** including depreciation shall be deemed to have been allowed [i.e no expenditure shall be allowed as deduction from such income @ 8% of T/o]
- (ii) Provisions of **Sec. 44AA & 44AB** pertaining to maintaining of books of Accounts & disallowance with reference to monetary limits of transactions shall not apply. However all such data which [i.e. maintenance of books of accounts is not required] shall show the calculation of sales, stock, debtors, creditors shall be maintained by

the assessee.

- (iii) In case of an assessee which is a firm to which prov. of 44AD are applied, the salary/remuneration & interest paid to its partners shall be deducted from the income computed under this provisions & the allowance of salary/Remuneration & interest shall be subject to the conditions & limits specified in **Sec. 40(b)**.

“Amendment made by the Finance Act, 2016, w.e.f. A.Y. 2017-18. The above point (iii) relating to payment of salary and interest paid to the partners shall be omitted w.e.f. A.Y. 2017-18. In other words, w.e.f. A.Y. 2017-18, a firm shall not be entitled to deduction on account of interest and salary paid to the partners if he is covered under section 44AD.”

- (iv) WDV of assets used for the purpose of such business shall be calculated as if depreciation has been actually provided.

- (b)** As per the provision of **Sec. 64(1) (iv)** in computing the total income of the individual, all such income arising directly or indirectly to the spouse of such individual from assets transferred to the spouse by such individual otherwise than for adequate consideration or in connection with an agreement to live apart shall be clubbed in the income of transferor. However any further income earned on such clubbed income shall be taxable in the hands of spouse.

Income from assets transferred to any person for the benefit of the spouse of the transferor as per the provision of **Sec. 64(1) (vii)** shall be taxable in the hands of transferor of the asset.

**Condition for clubbing:**

1. The relationship of husband and wife must exist both at the time of transfer of asset and at the time of accrual of income.
2. Consideration must be NIL or inadequate.
3. Where such assets or cash transfer by way of gift to the spouse is invested by the transferee in any business (except by way of capital contribution in a partnership firm), the income shall be clubbed in the following manner.

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$$\frac{\text{Investment in the business on the 1}^{\text{st}} \text{ day of the p. y out of the transfer fund made by the spouse}}{\text{Total investment in the business as on the 1}^{\text{st}} \text{ day of the p. y made by the spouse}} \times \text{Income such business of the spouse}$$

No clubbing provision shall persist where both the spouse are prof. qualified and are partners earning income by virtue of the qualifications.

**2009 - Dec [5]** (c) “Loss under any head of income for any assessment year can be set-off against the income from other heads of income but when it has to be carried forward for being set-off, it can only be set-off from income under the same head.” Explain. **(5 marks) [CSEPM - I]**

**Answer:**

Income of a person is computed under five heads. ‘Sources’ of income derived by an individual may be many but yet they could be classified under the same head. For instance, an individual may have a dual employment, yet the income would be classified under the head ‘Salaries’. However, given the mechanism of computing taxable salary income, it would be safe to say that an individual cannot incur losses under this head of income. Consider a situation where Harsh has two properties – one, occupied by him and the other, let out. Harsh pays interest on loan of ₹ 1.50 lakh on the property occupied and derives net rental income of ₹ 1.50 lakh from the let-out property. In case of a self-occupied property, income is computed as nil and interest expenditure results in loss. The loss of ₹ 1.50 lakh can be set off against rent income of ₹ 1.50 lakh; the income chargeable under the head ‘House property’ will be ‘Nil’.

An exception to intra head set off is loss under the head ‘Capital gains’, which may arise from transfer of any capital asset. Long-term capital loss arises from transfer of shares or units where holding period is more than 12 months and in respect of other assets holding period is more than 36 months prior to sale. Transfer of assets held for less than prescribed period results in short-term capital loss. Long-term capital loss cannot be set off against short-term capital gains. but S. Term loss can be adjusted against S.T.C.G or LTCG.

Further, loss incurred from speculation loss (e.g. from shares or commodities) cannot be set off against any other income.

Also, it is unlikely that the benefit of set off of loss under an activity or

source will be available, where the income from an activity or source is exempt from taxation.

**2010 - June [2]** (a) Answer the following :

- (i) What is the quantum of Minimum Alternate Tax (MAT) for a 'domestic company' and 'foreign company' for the assessment year 2018-19?  
 (c) Discuss the concept of 'deemed dividend' under section 2(22).

**(3 marks each)**

**Answer:**

- (a) (i)** The quantum of Minimum Alternate Tax (MAT) for a 'domestic company' and 'foreign company' for the assessment year 2018-19 are as under:

Company	Rate
In the case of a Domestic Company	18.5%
In the case of a Foreign Company	18.5%

**Surcharge for assessment year 2018-19:** The amount of income tax computed as above shall be increased by a surcharge of 7% in case of domestic companies and 2% in case of foreign companies provided the total income of such domestic/ foreign company exceeds ₹ 1 cr. If total income of the company exceeds ₹ 10 cr., surcharge in case of domestic company shall be 12% and 5% in case of foreign company.

**Education Cess:** Education Cess @ 2% shall be levied on the total tax (including surcharge) payable by the assessee.

**SHEC:** SHEC @ 1% shall be levied on the total tax (including surcharge) payable by the assessee. In other word SHEC shall be half of education cess.

"Mat rate to be 9% instead of 18.5% in case of a unit located in an International Financial Services Centre [Section 115JB(7), inserted by the Finance Act, 2016, w.e.f. A.Y. 2017-18".]

**Answer:**

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(c) Dividend in its ordinary connotation means the sum paid to or received by a shareholder proportionate to his shareholding in a company out of the total sum distributed. However, **Section 2(22)** of the **Income tax Act, 1961** has devised a special inclusive definition of dividend. As per the definition given in **Section 2(22)**, 'dividend' includes the following disbursements by the company to the shareholders, to the extent of accumulated profits:

- (a) **Distribution** of accumulated profits, whether capitalized or not, when such distribution by the Company to its Shareholders, entails the release of all or any part of the Company's assets.
- (b) **Distribution** of Debentures, Debentures-Stock or Deposits Certificates in any form, with or without interest and Distribution of Bonus Shares to Preference Shareholders, to the extent the Company possesses accumulated profits, whether capitalized or not.

Bonus Shares	Market Value of such shares shall be taxable in the hands of preference shareholders. Bonus shares given to equity shareholders are not treated as dividend.
Debentures, Debenture Stock, etc.	Market rate shall be adopted. If not, it shall be valued according to the accepted principles of valuation.

- (c) **Distribution** on liquidation, to the extent such distribution is attributable to the accumulated profits of the Company immediately before its liquidation, whether capitalized or not. Any Distribution after the date of liquidation shall not be treated as dividend. It is a repayment towards capital.
- (d) **Distribution** on reduction of capital, to the extent the Company possesses accumulated profits, whether such profits are capitalized or not.
- (e) **Payment** of any sum by a Company **in which the public are not substantially interested, by way of Advance or Loan**, to the extent the Company possesses accumulated profits, to-

- (i) A Shareholder, who is the beneficial owner of shares carrying not less than 10% voting power.
- (ii) Any concern in which such shareholder is a member or partner, having beneficial entitlement to not less than 20% of such concern's income.
- (iii) Any payment on behalf, or for the individual benefit, of such Shareholder.

**Note:** "Concern" means a HUF or a Firm or an AOP or BOI or a Company.

"Dividend received not to be exempt in case it is chargeable to tax in accordance with the provisions of Section 115BBDA [Proviso inserted under section 10(34) [w.e.f. A.Y. 2017-18]"

**Exceptions:** Dividend does not include:

- Distribution covered by (c) and (d) above, in respect of Shares issued for full cash consideration, where the Shareholder is not entitled to participate in the surplus assets upon liquidation.
- Advance or Loan to a shareholder or concern, by a Company carrying on lending business, in the ordinary course of its business.
- Dividend paid by a Company, which is set off wholly, or in part against previous payments made and deemed as dividend by (e) above, to the extent it is so set-off.
- Payment made on purchase of its own shares as per 68 of **Companies Act, 2013**.
- Distribution of shares pursuant of a demerger by the resulting company, to the shareholders of the demerged company, whether or not, there is a reduction of capital in the demerged company.

**Illustration 1:**

YOYO Ltd. is a company in which the public are not substantially interested, Kunal is a shareholder of the company holding 15% of the equity shares. The accumulated profits of the company as on 31-03-2017 amounted to ₹ 10,00,000/-. The company rent ₹ 1,10,000/- to Kunal by an account payee bank draft on 01-10-2017. The loan was not connected

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with the business of the company. Kunal repaid the loan to the company by an account payee bank draft on 30-03-2018. Examine the effect of the borrowal and repayment of the loan by Kunal on the computation of his total income for the assessment year 2018-19.

**Solution:**

As per **Section 2(22)(e)**, any payment by a company, by way of advance or loan to a shareholder, being a person who is the beneficial owner of shares holding not less than 10% of the voting power, shall be treated as deemed dividend to the extent to which the company possesses accumulated profits.

Since, YOYO Ltd. is a company in which the public are not substantially interested i.e. closely held company and the company has accumulated profits of ₹ 10,00,000/- on 31-03-2017, the loan of ₹ 1,10,000/- given by the company to Kunal, who holds more than 10% of the equity shares in the company, shall be treated as deemed dividend in the hands of K as per **Section 2(22)(e)**.

Further, the liability arises the moment the loan is borrowed by the shareholder and it is immaterial whether the loan is repaid before the end of the accounting year or not.

**NOTE:**

- Any income by way of dividends referred **u/s 115-O** is excluded from the total income of shareholder **u/s 10(34)**
- **U/s 115-O** any dividend declared, distributed or paid by a domestic company, whether out of current or accumulated profits, shall be charged to additional tax @ 15% in addition to normal income tax chargeable on the income of the company. This is known as Corporate Dividend Tax.
- Corporate Dividend Tax is not leviable on deemed dividend **u/s 2(22)(e)**, and it will be taxed in the hands of shareholders.
- Meaning of Substantial part of Business: Advance or Loan to a Shareholder or Concern, by a Company carrying on lending business (substantial), in the ordinary course of its business will not be liable for



deemed dividend **u/s 2(22)**. The word substantial can be in relation to turnover, overall profitability, percentage of manpower and also the capital employed for that division. **[CIT vs. Parle Plastics Ltd. (2011)]**

- Dividend received from an Indian Company which has suffered dividend distribution tax is exempt from tax under section 10(34). However, as per Section 115BBDA (as inserted by Finance Act, 2016), in the case of resident individual/HUF/firm, dividend shall be chargeable to tax at the rate of 10% if aggregate amount of dividend received from a domestic company during the year exceeds ₹ 10,00,000. Exemption under section 10(34) is granted to dividend received from an Indian Company and not to a dividend received from a foreign company.

**Tax on certain dividends received from domestic companies.**

**115BBDA**

1. Notwithstanding anything contained in this Act, where the total income of an assessee, being an individual, Hindu undivided family or a firm, resident in India, includes any income in aggregate exceeding ten lakh rupees, by way of dividends declared, distributed or paid by a domestic company or companies, the income-tax payable shall be the aggregate of:
  - (a) the amount of income-tax calculated on the income by way of such dividends in aggregate exceeding ten lakh rupees, at the rate of ten per cent; and
  - (b) the amount of income-tax with which the assessee would have been chargeable had the total income of the assessee been reduced by the amount of income by way of dividends.
2. No deduction in respect of any expenditure or allowance or set off of loss shall be allowed to the assessee under any provision of this Act in computing the income by way of dividends referred to in clause (a) of sub-section (1)
3. In this section, "dividends" shall have the same meaning as is given to "dividend" in clause (22) of Section 2 but shall not include sub-clause (e) thereof.

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**2010 - June [3]** (a) An asset is transferred by a person to another person under a partly revocable transfer whereby a part of the asset will revert back to the transferor. Who shall be liable to pay tax in respect of income from the asset transferred as per Section 61? **(2 marks) [CSEPM - I]**

**Answer:**

All income arising to any person by virtue of a revocable transfer or partly revocable transfer of assets shall be chargeable to income-tax as the income of the transferor and shall be included in his total income. Therefore transferor shall be liable to pay tax in respect of income from the assets transferred as per **Section 61**.

**2010 - June [4]** (c) Discuss the cases in which payment by way of loan/advance to the extent of accumulated profits by a closely held company is treated as dividend under section 2(22)(e). **(4 marks) [CSEPM - I]**

**Answer:**

As per **Section 2(22)(e) of Income Tax Act, 1961** "any payment by a company, not being a company in which the public are substantially interested, of any sum (whether as representing a part of the assets of the company or otherwise) [made after the 31st day of May, 1987, by way of advance or loan to a shareholder, being a person who is the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) holding not less than ten per cent of the voting power, or to any concern, in which such shareholder is a member or a partner and in which he has a substantial interest (hereafter in this clause referred to as the said concern)] or any payment by any such company on behalf, or for- the individual benefit, of any such shareholder, to the extent to which the company in either case possesses accumulated profits".

Private Limited Companies generally give Loan or Advance to their director and family members who are again shareholders holding 10% or more voting power or to a concern in which such shareholder has substantial interest.

Such loan or advance is treated as deemed dividend covered **under section 2(22)(e)** and taxable in the hands of shareholders or concern as the case may be.

**Following points are to be understood with reference to the above:**

- (i) Sub-clause (e) applies when distribution or payment referred to therein are connected with accumulated profits. The undistributed income, when accumulated from year to year, generates what is known as "accumulated profit". Accumulated profits shall include all profits of the company till the date of distribution or payment.
- (ii) Current profits are included in "accumulated profits" in **Section 2(22)(e) of I.T. Act, 1961**. The expression "accumulated profits" was defined in the 1961 Act so as to include current profit up to date of distribution or payment.
- (iii) The phrase "accumulated profits" does not mean aggregate of assessed profits but commercial profits. If certain disbursements have been disallowed in the assessment proceedings but the expenditure had in fact been incurred, they should be excluded from accumulated profits. In computing commercial profits, all the disbursements made and expenditure incurred for the purpose of business should be taken into account.

**2012 - June [3]** What is the difference between 'minimum alternate tax' under section 115JAA and 'alternate minimum tax' under section 115JC? Who is subject to these taxes? Also discuss the implication of these tax es in the case of an overseas entity having a permanent establishment (PE) in India. **(15 marks)**

**Answer:**

**Difference between MAT & AMT:**

Minimum Alternate Tax (MAT)	Alternate Minimum Tax (AMT)
It is applicable on Company assessee only. Here Company includes the	It is applicable to a person who has claimed any deduction under: • Section 80-IA to 80RRB other

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following :

- Any company incorporated and registered in India
- Any body corporate incorporated outside India (i.e. foreign companies)
- Any concern declared by the board to be a company
- A guarantee company including a mutual association or company carrying on charitable activities

than section 80P;

- Section 10AA; or
- Section 35AD

AMT shall not apply to Individual, HUF, BOI or Artificial or Juridical persons (AJP) if their adjusted total income does not exceed ₹ 20,00,000/-.

It is calculated on Book Profit	It is calculated on Adjusted Total Income
Rate of MAT is 18.5% + surcharge + cess	Rate of AMT is 18.5% + surcharge + cess
Companies are liable to pay MAT on the income exempted u/s 10(38)	LLP will not be liable to pay AMT on incomes exempt from tax

**2012 - June [3]** (c) What is meant by 'block of assets'? Explain.

**(3 marks) [CSEPM - I]**

**Answer:**

**Block of Assets**

As per **Section 2(11)**, Block of assets means a group of assets falling within a class of assets comprising,

- (a) Tangible assets being buildings, machinery, plant or furniture.
- (b) Intangible assets, being Know-how, patents, copyrights, trademarks, licenses, in respect of which the same percentage of depreciation is prescribed.

Each class of assets other than intangible assets may have different blocks or groups on which separate rates of depreciation are prescribed and for each such rate, separate block will be formed.

**2012 - Dec [1]** (a) Discuss briefly the treatment of un-availed tax credit of minimum alternate tax (MAT) in case of conversion of a private company or unlisted public company into a limited liability partnership (LLP). **(3 marks)**

**Answer:**

**Section 115JAA(7)** w.e.f. 1.04.2011, Assessment Year 2011-12 and onwards, provides that in case of conversion of a private company or unlisted public company into a **Limited Liability Partnership Act, 2008**, the provisions of **Section 115JAA** shall not apply to the successor LLP, that is to say tax credit will not be allowed to such LLP.

**2012 - Dec [1] {C} (Or)** (c) What are the provisions of section 54F in relation to capital gains on transfer of asset other than a residential house?

**(5 marks) [CSEPM - I]**

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**Answer:**

Any long term capital gain, arising to an individual or HUF from the transfer of any long term capital asset, not being residential house property shall be exempt in full, if the entire net sales consideration is invested in purchase of one residential house within one year before or 2 years after the date of transfer of such an asset or in the construction of one residential house within 3 years after the date of such transfer. Where part of the net sales consideration is invested, then Long term capital gain shall be exempted proportionately.

The proportionate exemption shall be that amount of capital gains which bears the same proportion which the amount invested in the new house bears to the net consideration price of the asset transferred i.e.

$$\frac{\text{Capital Gain} \times \text{Amount Invested}}{\text{Net Sales Consideration}}$$

The above exemption shall be available only when the assessee does not own more than one residential house property on the date of transfer of such asset exclusive of the one which he has bought for claiming exemption **u/s 54F**.

**2012 - Dec [3]** (a) Discuss with the help of an example, the cascading effect of dividend distribution tax and the remedial action taken by the government.  
**(7 marks)**

**Answer:**

**Tax on distributed profits of domestic companies [Section 115-O (1)]:**

The Domestic Company shall, in addition to the income tax chargeable in respect of its total income, be liable to pay additional income-tax on any amount declared, distributed or paid by such company by way of dividend (whether interim or otherwise), whether out of current or accumulated profits. Such additional income-tax shall be payable @15% plus surcharge @12% plus education cess @2% plus SHEC @1% of the amount so declared, distributed or paid.

**Tax Rates:**

Tax on distributed profit shall be computed after grossing up the tax by using following formula:

Rate of Dividend Distribution Tax before surcharge and cess =

$$\frac{\text{Amount Distributed} \times 15\%}{85\%} = 17.647\%$$

**Dividend received from subsidiary company to be reduced from the above dividend to be distributed [Section 115-O (1A)]:**

For the purpose of computation of tax on distributed profits, the amount of dividend distributed by the domestic company during the financial year shall be reduced by the following:

- (i) The amount of dividend, if any, received by the domestic company during the financial year, if such dividend is received from its subsidiary and,-
  - (a) where such subsidiary is a domestic company, the subsidiary has paid the tax which is payable under this section on such dividend;  
or
  - (b) where such subsidiary is a foreign company, the tax is payable by the domestic company **under section 115BBD** on such dividend;  
However, the same amount of dividend shall not be taken into account for reduction more than once;
- (ii) The amount of dividend, if any, paid to any person for, or on behalf of, the New Pension System Trust referred to in **Section 10(44)**.

For the purpose of **Section 115-O (1A)**, a company shall be a subsidiary of another company, if such other company holds more than half in nominal value of the equity share capital of the company.

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**NOTE:**

- *The above additional tax shall be payable even if no income-tax is payable by such company on its total income. [Section 115-O (2)]*
- *For the purposes of Section 115-O (1A), a company shall be a subsidiary of another company, if such other company holds more than half in nominal value of the equity share capital of the company.*
- *Section 115BBD is applicable when an Indian company holds 26% or more in nominal value of equity shares in the foreign company. But for taking the benefit under section 115-O (1A) the Indian company should hold more than half (instead of 26%) in the nominal value of the equity share capital of the company.*

**Example:**

Where the amount of dividend paid or distributed by a company is ₹ 85, then DDT under the amended provision would be calculated as follows:

Dividend amount distributed	=	₹ 85
Increase by ₹ 15 [i.e.(85*0.15)/(1-0.15)]		
Increased amount	=	₹ 100
DDT @ 15% of ₹ 100	=	₹ 15
Tax payable u/s 115-O is	=	₹ 15
Dividend distributed to shareholders	=	₹ 85

Effective rate of dividend distribution tax

The effective rate of dividend distribution tax payable shall be as under:

Tax payable u/s 115-O on ₹ 85 distributed	=	₹ 15
Therefore DDT rate on ₹ 100 distributed shall be $15 / 85 \times 100$	=	17.64706%
Add: Surcharge @ 12% of 17.647	=	2.11764%
Total		19.7647%
Add: EC & SHEC @ 3%	=	0.59294%
Total effective DDT rate applicable	=	20.35764%

Hence, the effective rate of DDT has been increased to 20.35764% approximately.

Alternatively the net amount of dividend paid on distributed should first be grossed up and DDT should be paid @17.304% (15%+12%SC+3%EC & SHEC)



**Question:**

Chitti Ltd., an Indian company wishes to distribute ₹ 10 lakhs as dividend to its shareholders. It has received ₹ 5 lakhs as dividend from its subsidiary domestic company on which subsidiary company has already paid D.D.T. Determine the amount of dividend distribution tax payable if such dividend on or after 01-10-2017.

**Answer:**

<b>Net dividend on which DDT is payable</b>	(₹)
Amount of dividend to be distributed to shareholders	10,00,000
Less: Dividend received from subsidiary company on which DDT has already been paid	5,00,000
Net dividend liable to DDT	<b>5,00,000</b>
<b>Computation of DDT</b>	
<b>Alternative 1</b>	
₹ 5,00,000 x 20.35765% (effective rate)	1,01,788
<b>Alternative 2</b>	
Net dividend to be grossed up	
₹ 5,00,000 x 100/85	
Gross amount ₹ 5,88,235	
DDT payable on ₹ 5,88,235 @ 17.304%	1,01,788

**2013 - Dec [3]** (b) What is the time-limit in the following different cases:

- (i) To file return of income under section 139(1) by an assessee who is required to furnish audit report under section 92E.
- (ii) To file a revised return, if the assessee discovers any omission or wrong statement in the originally filed return. **(2 marks each)**

**Answer:**

- (i) 30<sup>th</sup> November of the assessment year.
- (ii) Revised return can be filed at any time before the end of the relevant assessment year.

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**2014 - June [2]** (b) A CEO of an unlisted public company approached you with a proposal to convert the company into a Limited Liability Partnership (LLP) without attracting any liability towards capital gain tax. Draft a suitable reply. **(5 marks)**

**Answer:**

To,  
CEO  
XYZ LTD.  
Sir,

As per **Section 45** of the **Income Tax Act, 1961**, Income will be chargeable as Capital gains if there is a capital asset and there is transfer of the capital asset during relevant previous year.

But as per **Section 47 (xiib)** Nothing contained in **Section 45** shall apply to any transfer of a capital asset or intangible asset by a private company or unlisted public company (hereafter in this clause referred to as the company) to a limited liability partnership or any transfer of a share or shares held in the company by a shareholder as a result of conversion of the company into a limited liability partnership in accordance with the provisions of **Section 56** or **Section 57** of the Limited Liability Partnership Act.

**Provided that:**

- (a) all the assets and liabilities of the company immediately before the conversion become the assets and liabilities of the limited liability partnership;
- (b) all the shareholders of the company immediately before the conversion become the partners of the limited liability partnership and their capital contribution and profit sharing ratio in the limited liability partnership are in the same proportion as their shareholding in the company on the date of conversion;
- (c) the shareholders of the company do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of share in profit and capital contribution in the limited liability partnership;

- (d) the aggregate of the profit sharing ratio of the shareholders of the company in the limited liability partnership shall not be less than 50%, at any time during the period of 5 years from the date of conversion;
- (e) the total sales, turnover or gross receipts in the business of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed ₹ 60,00,000; and
- (f) no amount is paid, either directly or indirectly, to any partner out of balance of accumulated profit standing in the accounts of the company on the date of conversion for a period of 3 years from the date of conversion.

Thanking You  
Company Secretary  
XYZ LTD.

**Question Under LLP**

- (i) Who shall verify the return of income of a limited liability partnership?
- (ii) ABC LLP is liquidated. What is the liability of partners of ABC LLP in respect of its tax dues?
- (iii) DCB LLP has a profit of ₹ 500 lacs after charging interest on capital for B amounting to ₹ 10 lacs calculated at 15% p.a. as per the agreement, but before considering remuneration to partners. What is the maximum admissible amount of remuneration to partners who are working partners and remuneration is authorized by the LLP instrument?

**Answer:**

- (i) **Under section 140**, in the case of a limited liability partnership (LLP), the return of income shall be verified by the designated partner.  
Where for any unavoidable reason, such designated partner is not able to verify the return, or where there is no designated partner as such, the return of LLP can be verified by any partner.
- (ii) **Section 167C** provides for the liability of partners of LLP in

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liquidation. In the case of liquidation of an LLP and where tax due from the LLP cannot be recovered, every person who was a partner of the LLP at any time during the relevant previous year will be jointly and severally liable for payment of tax unless he proves that non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the LLP.

(iii) **Computation of maximum admissible remuneration to working partners:**

Particulars	₹ (in lacs)
Net profit before considering partners' remuneration	500
Add: Interest in excess of 12% p.a. allowed to B (₹ 10 lacs x 3/15)	2
<b>Book profit</b>	<b>502</b>
Maximum amount admissible as remuneration to working partners under section 40(b):	
On first ₹ 3 lacs of book profit, 90% of books profit or ₹ 1,50,000 whichever is more	2.7
On balance book profit 60% of ₹ 499 lacs	299.4
<b>Maximum admissible remuneration</b>	<b>302.1</b>

**2014 - June [2A] (Or)** (i) A corporate assessee, who inadvertently failed to claim deduction under section 80IB during the initial years, cannot claim deduction under the said section for the remaining years during the period of eligibility, in spite of fulfillment of stipulated conditions. Examine the assertion contained in the above para in the background of judicial decision.

**(5 marks)**

(ii) Whether MAT credit admissible under section 115JAA has to be set-off against the assessed tax payable before calculating interest under sections 234A, 234B and 234C.

**(5 marks)**

(iii) Discuss the provisions regulating determination of fair market value of

ESOPs.

(5 marks)

**Answer:**

- (i) Where assessee is a company entitled to deduction **under section 80 IB** which it did not claim in the initial years, it can claim the said deduction for the remaining years during the period of eligibility, if the conditions are satisfied. [*Praveen Soni vs. CIT (2011) (Del)*]
- (ii) No, MAT credit admissible in terms of **Section 115JAA** has to be set off against the tax payable before calculating interest only **under sections 234B and 234C**. [*CIT vs. Deccan Creations Pvt. Ltd. (2011) (Kar)*]
- (iii) **Determination of Fair Market Value (FMV) of ESOPs on the date of exercise of option:**
  - (a) **Where shares in the company are listed on a single stock exchange:** FMV will be average of opening and closing prices of shares on the date of exercise of option. If on the date of exercise of option there is no trading in shares, the FMV shall be the closing price of the share on any recognised stock exchange on a date closest to the date of exercise of option and immediately preceding such date of exercise of option.
  - (b) **Where shares in the company are listed on more than one recognised stock exchange:** FMV will be average of opening and closing price of shares on the date of exercise of option on a recognised stock exchange which records the highest volume of trading in the shares.  
If on the date of exercise of option there is no trading in shares, the FMV shall be the closing price of the share on a recognised stock exchange which records the highest volume of trading on a date closest to the date of exercise of option and immediately preceding such date of exercise of option.
  - (c) **Where shares in the company are not listed on a recognised stock exchange:** FMV will be value on a “specified date” as determined by a Category I merchant banker registered with SEBI. Specified date means the date of exercise of option or any date

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earlier than the date of exercise of option, not being a date which is more than 180 days earlier than the date of exercise of option.

**2015 - June [1]** (c) Explain whether the benefit of exemption under section 54EC would be available in the case of 'capital gains arising on transfer of depreciable asset'. **(5 marks)**

**Answer:**

**Benefit under section 54EC, etc. available even on transfer of depreciable assets:**

Although as per **Section 50** the profit arising from the transfer of depreciable asset shall be a gain arising from the transfer of short term capital asset, hence short term capital gain but **Section 50** nowhere says that depreciable asset shall be treated as short term capital asset. **Section 54EC** [or say 54EC or 54F, etc.] is in independent provision which is not controlled by **Section 50**. If the conditions necessary **under Section 54E** are complied with by the assessee, he will be entitled to the benefit envisaged in **Section 54E** even on transfer of depreciable assets held for more than 36 months. **[CIT V Assam Petroleum Industries (P.) Ltd. (2003)].**

**2015 - June [2]** (b) Comment on the following in the context of provisions contained in the Income-tax Act, 1961:

- (i) The provisions of section 115JB are applicable in case of foreign companies. **(2 marks)**
- (ii) The provisions of dividend distribution tax are applicable to an undertaking or enterprise engaged in developing, operating and maintaining a special economic zone (SEZ). **(3 marks)**

**Answer:**

- (i) **Section 115JB** of the **Income Tax Act, 1961**, states that all companies having book profits under the Companies Act shall have to pay MAT at the rate of 18.5%, there is no provision restricting its applicability to only domestic companies. Thus, MAT is applicable to all companies irrespective of it being a domestic company or a foreign company.

However, MAT is required to be computed with reference to book

profits computed on the basis of profit and loss account prepared as per the Companies Act, and the Companies Act requires only foreign companies, having a place of business within India, to prepare and file its financial statements with the Registrar of Companies. Hence, the MAT provisions shall not apply to foreign companies, which do not have any presence in India.

**Alternative Answer:**

The Authority for Advance Ruling has delivered the ruling in the case of the Timken Company holding that the provisions of **Section 115JB** of the **Income-tax Act, 1961** levying MAT on the book profit of a company would not apply to a foreign company not having any physical presence in India. Hence, provisions of **Section 115JB** are applicable only to those foreign companies which have physical presence in India.

**(ii) Applicability of DDT on SEZ**

**Finance Act, 2011** inserted a proviso to sub-section 6 of **Section 115-O** by which the provisions of **Section 115-O** shall also be applicable on an enterprise or undertaking engaged in developing, operating and maintaining a SEZ.

**2015 - June [2]** (c) Explain the meaning of 'eligible expenses' for the purposes of claiming benefit under section 35D. Also enumerate these eligible expenses. **(5 marks)**

**Answer:**

Preliminary expenses are specified expenses incurred before setting up of the business or the expenses are incurred in connection with extension of an undertaking or in connection with setting up of a new unit.

Specified preliminary expenses are:

- (a) Preparation of feasibility report;
- (b) Conducting market survey or any other survey necessary for the business;
- (c) Preparation of Project report;
- (d) Engineering services relating to the business;
- (e) Legal charges for drafting an agreement relating to the setting up or

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conduct of the business;

- (f) Legal charges for drafting and printing of Memorandum of Association (MOA) and Articles of Association (AOA);
- (g) Registration fees of a company paid to Registrar of Companies;
- (h) Expenses and legal charges incurred in drafting, printing and advertising for prospectus;
- (i) Expenditure incurred on issue of shares or debentures like underwriting commission, brokerage.

**2015 - Dec [2]** (b) Narrate the provisions of the Income-tax Act, 1961, with respect to surcharge on income-tax for various types of assessees for the assessment year 2018-19. **(5 marks)**

**(c)** State the rate of deduction allowable under the Income-tax Act, 1961 while assessing income from business or profession in the following cases:

- (i) For acquisition and installation of new plant or machinery by a manufacturing company.
- (ii) For expenditure (revenue or capital) on in-house scientific research by a company engaged in business or manufacture or production of any article other than those specified in the Eleventh Schedule of the Income-tax Act, 1961.
- (iii) Contribution to approved scientific research association including social and statistical research.
- (iv) Capital expenditure (other than on acquisition of land, goodwill or financial instrument) incurred for setting-up and operating cold chain facility.
- (v) Expenditure incurred by companies on notified skill development projects. **(5 marks)**

**Answer:**

**(b)** Provisions of **Income Tax Act, 1961** with respect to Rate of Surcharge are discussed below:



1. For resident individuals (including senior citizens and super senior citizens) whose total income exceeds ₹ 1 crore = 15% on income tax payable. Co-operative societies, firms and local authorities whose total income exceeds ₹ 1 crore - 12% on income tax payable.
  2. For domestic company having a total income of exceeding ₹ 1 crore but not exceeding ₹ 10 crore - 7% on income tax payable.
  3. For domestic company having a total income of exceeding ₹ 10 crore - 12% on income tax payable.
  4. For company other than a domestic company having a total income exceeding ₹ 1 crore but not exceeding ₹ 10 crore - 2% on income tax payable.
  5. For company other than a domestic company having a total income exceeding ₹ 10 crore - 5% on income tax payable.
- (c)** (i) Section 32 AC(1) — @ 15%
- (ii) Section 35 – An assessee can claim the following expenditure as a deduction:
- (a) revenue expenses (Sec. 35)
  - (b) capital expenses

All revenue expenses laid out or expended on scientific research during the previous year are full allowed as a deduction. It has further been provided that following revenue expenses, expended or laid out during three years immediately preceding the commencement of the business shall be deemed to be the expenditure of the previous year in which the business commences and therefore, shall be allowable in that year to the extent these are certified by the prescribed authority.

- (iii) Payment to outside agencies for:
  - (a) Scientific research [Sec. 35 (1) 150% & ii (a)]-100%
  - (b) Research in Social Science or Statistical - 100% [Sec. 35 (1) (iii)]
- (iv) Sec. 35AD (1A) — 100%
- (v) Sec. 35CCD — 100%

**2016 - June [2]** (c) Give examples of five incomes in India which are exempt

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under section 10 in respect of non-residents.

**(5 marks)**

**Answer:**

The following are the income exempt from tax under section 10 of the Income tax Act, 1961 in the hands of non-residents:

1. **Interest on NRE A/c [Section 10(4) (ii)]:** In the case of an individual, any income by way of interest on moneys standing to his credit in a Non-Resident (External) Account in any bank in India in accordance with the Foreign Exchange Management Act, 1999 ('FEMA') is exempt.
2. **Tax payable on Royalty or FTS on behalf of foreign company:** Tax payable, under the terms of the agreement, on Royalty or FTS on behalf of foreign company is exempt under section 10(6A).
3. **Tax payable on certain incomes on behalf of foreign company or Non-Resident 'NR':** Tax payable on certain incomes (not being salary, royalty or FTS) on behalf of foreign company or a NR is exempt u/s 10(6B).
4. **Tax payable by Indian Company on behalf of foreign Government etc.:** Tax payable, on behalf of foreign Govt. or foreign enterprises by, Indian company engaged in business of operation of aircraft, on income from leasing of aircraft etc. u/s 10(6BB).
5. **Royalty or FTS received by a specified foreign company:** Royalty or FTS received by specified foreign company is exempt u/s 10(6C).

**2016 - June [2A] (Or) (iii) What is an LLP? How is it different from a partnership firm?**

**(3 marks)**

**Answer:**

Entrepreneurs now have an alternative and innovative form of business organization i.e. Limited Liability Partnership (LLP) which combines the benefits of company and general partnership form of business organizations. LLP has separate legal entity, perpetual succession and limited liability of partners.

From income-tax point of view, LLP is treated as general partnership firm and therefore, its profits will be taxed in the hands of the LLP and not in the hands of its partners.

**Difference between Partnership Firm Vs. LLP**

Traditional Partnership	LLP
Not a Legal Entity	Legal Entity
Minimum 2 Partners	Minimum 2 Partners
Maximum 100 Partners	No Limit
Partners are jointly liable	To the extent of their contribution
Registration is not compulsory	Compulsory
BS etc. need not be filled	Filing is compulsory
Audit is not Compulsory	Compulsory if Turnover is ₹ 40 Lakhs or contribution is ₹ 25 Lakhs
Name may be any	Must be approved by Registrar and must have LLP as suffix
Minor can become Partner	Minor can not become Partner

**2017 - June [1] (a)** Explain the cases of exception under the Income Tax Act, 1961, if any from the general rule “Income earned by a person during a previous year is always taxable in the Assessment Year”. **(5 marks)**

**Answer:**

Income earned by a person during the previous year is always taxable in the Assessment Year as per Income tax Act, 1961. However, there is an exception to this general rule and the Income earned during a previous year is taxable in the previous year itself in the following cases:

- Income of non-resident shipping companies **[Section 172]**
- Income of persons leaving India with no intention of returning back to India **[Section 174]**
- Association of Persons (AOP)/Body of Individuals (BOI)/Artificial Juridical Person (AJP) formed for a particular purpose likely to be dissolved in the same year of formation **[Section 174A]**

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- Cases of transfer of assets with a view to avoid tax [**Section 175**]
- Income of a discontinued business [**Section 176**]

**2017 - June [2] (a)** Explain the provisions contained under the Income Tax Act, 1961 relating to set-off and carry forward of:

- (i) Speculative Business Losses
- (ii) Short-term Capital Losses. **(5 marks)**

**Answer:**

**The provisions related to set off and carry forward of losses under the Income tax Act, 1961 in the following cases are as follow:**

**(i) Speculative Business Losses:** Loss from speculation business is set-off in the same year from available profits and gains of any other speculative business. However, where, for any assessment year, any loss computed in respect of a speculation business has not been wholly set-off against the profits of another speculation business, it shall be carried forward to the following assessment year and shall be set-off against the profits of any speculation business carried on by him and assessable for the assessment year. This loss can be carried forward to a maximum of four consecutive assessment years immediately succeeding the assessment year for which the loss was first computed.

**(ii) Short-term Capital Losses (Sec. 74):** Where in respect of any assessment year, the net result of the computation under the head "Capital gains" is a loss to the assessee, whether short-term or long-term. Such short-term and long-term capital losses shall be separately carried forward. Further, such carried forward short-term capital loss can be set off in the subsequent assessment year from income under the head capital gains, whether short-term or long-term. But brought forward long-term capital loss shall be allowed to be set off only from the long-term capital gain.

**2018 - June [1]** (a) (i) State the period of holding for considering the shares in a private limited company to be treated as long-term capital asset.

**(1 mark)**

## PRACTICAL QUESTIONS

**2008 - Dec [5]** (a) Gulshan submits the following information relevant for the financial year 2017-18:

	Profit (₹)	Loss (₹)
Salary income	8,00,000	–
Income from house property:		
House-A	25,000	–
House-B	–	30,000
Profits and gains of business or profession:		
Business-A	12,000	–
Business-B	–	20,000
Business-C ( <i>Speculative</i> )	22,000	–
Business-D ( <i>Speculative</i> )	–	35,000
Capital gains:		
Short term capital gains	10,000	–
Short term capital loss	–	30,000
Long-term capital gains on sale of building	16,000	–
Income from other sources:		
Loss on maintenance of race horses	–	15,000

Determine the net income of Gulshan for the assessment year 2018-19.

**(7 marks) [CSEPM - I]**

**Answer:**

Income from Salary		8,00,000
Income from HP (House A)	25,000	
(House B)	(30,000)	(5,000)

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Income from Business & Profession

Business A	12,000	
Business B	(20,000)	(8,000)
<u>Income from speculative business</u>		
Business C	22,000	
Business D	(35,000)	(13,000)
<u>Income from Capital gain</u>		
Short term capital gain	10,000	
Short term capital loss	(30,000)	
Long term capital gains	16,000	(4,000)
Income from other sources		
Loss on maintenance of race horses		(15,000)
<b>Net Income of Gulshan</b>	<b>₹ 7,95,000*</b>	

**\*Notes:**

- *Loss from PGBP can not be set-off against salary income.*
- *Loss from speculative business can be set-off against speculative income only.*
- *Capital loss would be allowed to adjusted against capital gain only.*
- *Loss on maintenance of race horses can not be set off against other incomes.*

**2009 - June [5]** (b) Discuss the taxability or otherwise of the following gifts received by Madhuri, a lady, during the financial year 2017-18:

- ₹ 30,000 from her elder sister.
- ₹ 50,000 from the daughter of her elder sister.
- Wrist watch valued at ₹ 6,000 from her friend. **(3 marks) [CSEPM - I]**

**Answer:**

Applicable section: - 56(2)(vi)

- Gift received from elder sister will not be taxable as per the **IT Act, 1961** as she is a relative of Madhuri and any sum received from a relative is not taxed as per the provisions of the Act.
- Amount received from the daughter of her sister would have been taxable, had it exceeded ₹ 50,000. Up to ₹ 50,000 it is not chargeable to tax.

(iii) Wrist watch is not a cash gift, hence will not be taxable.

**2009 - Dec [2]** (b) Modern Ltd. entered into an agreement with Synergy Ltd. for granting on lease to Synergy Ltd. its 8000 sq. mtr. land lying vacant adjacent to the factory premises of Synergy Ltd. for a period of 12 years commencing from May, 2004. Under the terms of the agreement, Synergy Ltd. had to build a factory building, pay an annual rent @ ₹100 per sq. mtr. of the leased land of 8,000 sq. mtr. and surrender the building to Modern Ltd. at the end of the lease without any consideration. Synergy Ltd. complied with the terms and conditions of the lease agreement.

The depreciated value of the building surrendered and taken possession by Modern Ltd. in May, 2017 was ₹4.22 crore. Accounts department of Modern Ltd. is of the opinion that an equivalent amount is to be taken in the accounts of the year 2017-18 as income received.

Critically examine the matter and offer your comments.

**(3 marks)**

**Answer:**

Accounts Department's opinion of Modern Ltd. is incorrect. The depreciated value of the building is of course to be brought into the books of accounts.

However, the equivalent amount viz. ₹ 4.22 crores cannot be treated as income from the business. By its very nature it is a capital receipt and is not a revenue income. The amount cannot be treated as a revenue receipt unless it is conclusively established that this represented deferred rent as the lease rent was unreasonably low. Further Modern Ltd. is not in the business of real estate to treat the benefit as incidental revenue receipt earned during the course of such business.

**2010 - June [3]** (c) Ram and Shyam are partners in Mozart Co., a partnership firm, which is engaged in manufacturing carpets. They share profits and losses in the ratio of 2:3. The profit and loss account of the firm for the year ended 31st March, 2018 is as follows:

<i>Liabilities</i>	₹
Cost of goods sold	10,00,000
Depreciation	50,000

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Salary to staff		1,00,000
Remuneration to partners:		
Ram	₹ 2,50,000	
Shyam	₹ <u>1,20,000</u>	3,70,000
Interest on capital @ 15%:		
Ram	₹ 45,000	
Shyam	₹ <u>67,500</u>	1,12,500
Sundry expenses		1,00,500
Net profit		<u>7,35,200</u>
		<u>24,68,200</u>
<b>Assets</b>		
Sales		23,00,000
Dividends		28,200
Winnings from lotteries (₹ 2,00,000)		<u>1,40,000</u>
		<u>24,68,200</u>

Additional information:

- The firm donated ₹ 30,000 to National Defence Fund and this amount is included in sundry expenses.
- Depreciation admissible under the income-tax rules is ₹ 68,000.
- The firm is evidenced by partnership deed.

Compute the taxable income and amount of tax liability of the firm for the assessment year 2018-19. **(7 marks) [CSEPM - I]**

**Answer:**

<b>Computation of book – profit</b>		₹
Net Profit as per P&L		7,35,200
Add: Interest paid to partners in excess of 12%	Ram	9,000
	Shyam	13,500
Remuneration of partners		3,70,000
Donation		<u>30,000</u>



	11,57,700
Less: Dividends	28,200
Winning from lotteries	1,40,000
Depreciation	<u>18,000</u>
	9,71,500
Less: Remuneration of partners	<u>3,70,000</u>
	<u>6,01,500</u>
<b>Income from other sources</b>	
Winning from lotteries	2,00,000
Dividends	<u>exempt</u>
	<u>2,00,000</u>
<b>Gross total income</b>	8,01,500
Less: Deduction u/s 80G	<u>30,000</u>
Total Income	<u>7,71,500</u>

**Calculation of Tax**

30% on 2,00,000	60,000
On balance 30 % (7,71,500 – 2,00,000)	<u>1,71,450</u>
	2,31,450
Add: cess	6,944
Less: TDS	<u>60,000</u>
Tax payable	<u>1,78,394</u>
Tax payable rounded off	1,78,390

**2010 - Dec [3]** (a) The book profits of a company in the previous year 2017-18 computed in accordance with Section 115JB is ₹ 15 lakh. If the total income computed for the same period as per the provisions of the Income-tax Act, 1961 is ₹ 3 lakh, calculate the tax payable by the company in the assessment year 2018-19 and also indicate whether the company is eligible for any tax credit. **(5 marks)**

**Answer :**

**1. Calculation of tax liability u/s 115JB:**

Particulars	Details	Amount
Book profit	Given	15,00,000
Tax Liability	18.5% of ₹ 15 lakhs	2,77,500

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Add: Surcharge		NIL
Tax Liability after surcharge		2,77,500
Add: Education cess and SHEC @ 3%	3% of ₹ 2,77,500	8,325
Tax Liability after cess		2,85,825

**2. Calculation of tax liability as per Income Tax Act, 1961:**

Particulars	Details	Amount
Total Income	Given	3,00,000
Tax Liability	30% of ₹ 3 lakhs	90,000
Add: Education cess and SHEC @ 3%		2,700
Tax Liability after cess		92,700

**3. Computation of Final Tax payable:**

Particulars	Details	Amount
Tax Liability	Tax Liability u/s 115JB > Normal Tax liability	2,85,825
Actual tax liability		2,85,825

The company is eligible for MAT tax credit of ₹ 1,93,125 (₹ 2,85,825 - ₹ 92,700), which can be carried forward for 10 years or is to be awaited within 10 years **u/s 115JAA**.

**2010 - Dec [3]** (a) Sanjay furnishes following particulars of income from his business for the previous year 2017-18:

- (i) Net profit as per profit and loss account ₹ 72,000 after charging the following:
  - (a) Depreciation on building ₹ 31,000
  - (b) Provision for discount on debtors ₹ 40,000
  - (c) Private household expenses ₹ 50,000
  - (d) Charity (unapproved) ₹ 7,000
  - (e) Computer for scientific research ₹ 60,000
  - (f) Payment of expenses made through bearer cheque ₹ 25,000
  - (g) Security deposit ₹ 16,000
  - (h) Audit fee paid in cash ₹ 25,000

- (i) Patent purchased during the year ₹ 75,000
- (j) Market survey feasibility report expenses ₹ 50,000 on new project costing ₹ 6,00,000.
- (ii) Opening stock ₹ 66,000 valued at 10% above cost and closing stock ₹ 72,000 valued at 10% below cost.
- (iii) Income credited to profit and loss account include—
  - (a) Bank interest on fixed deposits ₹ 9,000
  - (b) Refund of excise duty ₹ 18,000 earlier allowed as deduction
  - (c) Bad debts recovered ₹ 5,000.

Compute total income of Sanjay and his tax liability if he is a senior citizen assuming depreciation on building as per the Income-tax Act, 1961 is ₹ 50,000. **(7 marks) [CSEPM - I]**

**Answer:**

**Computation of tax Liability of Mr. Sanjay  
for the Assessment Year 2018-19**

**Profits and Gains of Business and Profession**

Net Profit	72,000
------------	--------

**Add: Expenses Inadmissible**

Depreciation on Building	31,000	
Provision for discount on debtors	40,000	
Household Expenses	50,000	
Charity	7,000	
Expenses paid through bearer cheque	25,000	
Security deposit	16,000	
Audit Fees	25,000	
Patent (Depreciation considered separately)	75,000	
Market Survey Expenses	44,000	
opening stock over valued	6,000	
closing stock under valued	<u>8,000</u>	3,27,000

**Less: Expenses Allowed**

Depreciation on Building	50,000	
Depreciation on Patent	<u>18,750</u>	68,750

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Less: Income from other head	
Bank Interest on Fixed Deposits	9,000
<b>Profits and Gains of Business and Profession</b>	<b>3,21,250</b>
Income from other source-Bank Interest	9,000
<b>Gross Total Income</b>	<b>3,30,250</b>
Less: Deductions	Nil
<b>Total Income</b>	<b>3,30,250</b>
Tax Liability	
Tax on ₹ (3,30,250 – 3,00,000)	1,512
Less: Rebate u/s 87A	<u>1,512</u>
	<u>Nil</u>
Tax Payable	<u>Nil</u>

**Working Notes:**

1. Least of the following shall be eligible as Market Survey Expenses

- |                                 |          |
|---------------------------------|----------|
| (a) Actual Expenditure incurred | ₹ 50,000 |
| (b) 5% of project cost          | ₹ 30,000 |

Hence, ₹ 30,000 shall be allowed for deduction in 5 equal installments i.e. ₹ 6,000 (1/5 of ₹ 30,000)

**2012 - June [2]** (b) Savita submits the following information regarding her salary income:

Basic salary	...₹ 11,000 per month
City compensatory allowance	...₹ 150 per month
Children education allowance	...₹ 400 per month (for 3 children)
Reimbursement of medical expenses	...₹ 25,000

She was entitled to house rent allowance of ₹ 6,000 per month from 1<sup>st</sup> April, 2017 to 31<sup>st</sup> August, 2017. However, she was paying a rent of ₹ 7,000 per month for a house in New Delhi. With effect from 1<sup>st</sup> September, 2017, she was provided with an accommodation by the company for which the company was paying a rent of ₹ 5,000 per month. Compute her gross salary for the assessment year 2018-19.

**(5 marks)**

**(c)** For the previous year 2017-18, gross total income of Gopal is ₹ 12,50,700. During the previous year he has made the following payments:

	₹
(i) Contribution to recognised provident fund	18,000
(ii) Donation to Rajiv Gandhi Foundation	50,000
(iii) Donation to Prime Minister Drought Relief Fund	30,000
(iv) Donation to Prime Minister National Relief Fund	20,000
(v) Donation to a government hospital for family planning	1,00,000
(vi) Financial assistance to poor students	50,000
(vii) Medical insurance premium	20,000

Compute total income of Gopal for the assessment year 2018-19.

**(5 marks) [CSEPM - I]**

**Answer:**

**(b) Computation of Gross Salary of Savita for Assessment Year 2018-19**

Basic Salary (11,000 × 12)		1,32,000
City Compensatory allowance (150 × 12)		1,800
Children Education Allowance (400 × 12)	4,800	
Less: Exempt 100 p.m. upto 2,400 2 children (200 × 12)	<u>2,400</u>	2,400
Reimbursement of Medical Expenses	25,000	
Less: Exempt	<u>15,000</u>	10,000
House Rent Allowance (6,000 × 5)	30,000	
Less: Exempt (see Note 1)	<u>27,500</u>	2,500
Rent Free Accommodation (See Note 2)		11,918
<b>GROSS SALARY</b>		<b>1,60,618</b>

**Note:**

(i) HRA shall be exempted to the minimum of the following:

(a) HRA received	30,000
(b) Actual rent - 10% of salary [7,000 × 5 - (10% of 55,000)]	29,500
(c) 50% of ₹ 55,000 (as she resides in Delhi)	<u>27,500</u>

**Therefore, House rent allowance of ₹ 27,500 shall be exempted.**

(ii) Value of Rent free accommodation:

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*Least of following shall be taxable*

(a) Actual amount of Rent paid by employer (5,000×7)	35,000
(b) 15% of Salary [(1,32,000+1,800+2,400)×15%]	20,430

**Therefore, value for rent free accommodation shall be ₹ 11,918.**

**(c) Computation of Total Income of Gopal for the Assessment Year 2018-19**

Gross Total Income		12,50,700
<i>Less: Deduction under chapter VI-A</i>		
Deduction under section 80-C (RPF)	18,000	
Deduction under Section 80-D (Medical Insurance Premium)	20,000	
Deduction under section 80-G (Donation)	<u>1,60,000</u>	1,98,000
<b>Total Income</b>		<b>10,52,700</b>

**Working Note:**

(i) Calculation of Deduction under section 80-G

**(A) Donations to which qualify limit does not apply**

(a) Allowed 100%		
PMNRF (20,000 × 100%)		20,000
(b) Allowed 50%		
PMDRF (30,000 × 50%)	15,000	
RGF (50,000 × 50%)	<u>25,000</u>	40,000

**(B) Donations which are subject to qualifying limit**

(a) Donation to Government for family planning (100% of ₹ 1,00,000)		
		1,00,000
Within 10% of adjusted total income (10% of 12,17,700) i.e. ₹ 1,21,770		

**Total Donation Allowed 1,60,000**

Adjusted total income: (Gross Income - Deductions under Chapter VI-A except under Section 80G) i.e. 12,50,700 - 18,000 - 20,000 = 12,12,700.

**2012 - Dec [2] (b) Whether minimum alternate tax (MAT) under section**

115JB is payable in advance and interest under sections 234B and 234C is payable on failure to pay such advance tax? Also explain whether MAT credit admissible under section 115JAA has to be set-off against the assessed tax payable before calculating the interest under sections 234A, 234B and 234C. You may take help of decided case law, if any. (6 marks)

**Answer :**

Companies liable to pay tax on the basis of MAT under **section 115JB** are required to pay advance tax and interest under **sections 234B** and **234C** is payable on failure to pay such advance tax. [*JCIT v Rolta India Ltd. (2011)*]

For the purpose of computing interest chargeable under **section 234A, 234B** and **234C**, credit of MAT under **section 115JAA** has to be set off against the assessed tax payable. [*CIT v Tulsian NEC Ltd. (2011)*]

**2012 - Dec [2]** (b) Following is the trading and profit and loss account of Narendra for the year ended 31<sup>st</sup> March, 2018:

	₹		₹
Opening stock	20,250	Sales	3,83,600
Purchases	1,80,500	Closing stock	23,200
Wages	10,200	Gift from father	10,000
Donation to Prime Minister		Income-tax refund	2,500
National Relief Fund	20,000		
Building rent	60,000		
Repairs of car	5,300		
Medical expenses ( <i>personal</i> )	8,000		
General expenses	4,200		
Depreciation on car	12,000		
Profit for the year	98,850		
	<u>4,19,300</u>		<u>4,19,300</u>

Additional information:

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- (i) Opening stock has been undervalued by 10% of cost while closing stock has been valued at its cost.
  - (ii) One-third of the building rent is related to self-residential house.
  - (iii) The car is used equally for business as well as for personal purposes.
  - (iv) Wages includes wages of household servant ₹ 250 per month.
- From the above information, you are required to determine the taxable income of Narendra under the head income from business and profession.

**(10 marks) [CSEPM - I]**

**Answer:**

**Computation of taxable Income of Narendra under the head Income from business and profession**

	₹	
Net profit as per Profit & Loss Account		98,850
<i>Add:</i> Items disallowed		
	₹	
Donation to PMRF	20,000	
Building Rent 60,000 × 1/3	20,000	
Repairs of Car 5,300 × ½	2,650	
Medical Expenses	8,000	
Depreciation of Car 12,000 × ½	6,000	
Wages of servant 250 × 12	3,000	59,650
		1,58,500
<i>Less:</i> Items not taxable:		
Gift from father	10,000	
Income tax refund	2,500	12,500
		1,46,000
<i>Less:</i> Opening stock undervalued $\frac{20,250}{90} \times 10$		2,250
Income from Business and Profession		1,43,750



**2012 - Dec [4]** (a) Anand owns a house at Delhi. From the following particulars, compute the income from house property for the assessment year 2018-19:

	₹
Municipal valuation	2,50,000
Fair rent	2,80,000
Actual rent (₹ 25,000 per month)	3,00,000
Standard rent	2,60,000
Municipal taxes paid (half of it was borne by the tenant)	25,000
Expenses on repairs	5,000
Fire insurance premium paid	5,000
Ground rent	6,000
Unrealised rent	1 month
Vacancy period	1 month

He had borrowed a sum of ₹ 20,00,000 @ 10% p.a. from LIC Housing Ltd. on 1<sup>st</sup> August, 2013 and the construction of the house was completed on 1<sup>st</sup> January, 2017. Total loan is still unpaid. **(5 marks) [CSEPM - I]**

**Answer:**

**Calculation of Income from House Property  
for the Assessment Year 2018-19**

	₹
Gross Annual Value	
(i) Expected Rent ( Higher of fair value of ₹ 2,80,000 and municipal value of ₹ 2,50,000 but subject to standard rent of ₹ 2,60,000)	2,60,000
(ii) Rent actually received/ receivable (₹ 25, 000 × 11)	<u>2,75,000</u>
Higher of (i) and (ii)	2,75,000
Less: Loss due to vacancy	<u>25,000</u>
<b>Gross annual value</b>	<b><u>2,50,000</u></b>
Less: Municipal taxes (borne by the owner)	<u>12,500</u>
	<b><u>2,37,500</u></b>

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Less: Standard deduction @ 30% under section 24	71,250
	<b>1,66,250</b>
<b>Income from house property</b>	3,86,667
(A - B)	1,66,250
	<b>2,20,417</b>

**Interest on Loan**

**1. Pre-construction period 1.8.2013 to (1.1.2017) i.e. 31.3.2017**

Previous year	2012-13	1,33,333	i.e. ₹ 2,00,000 × 8/12
	2013-14	2,00,000	
	2014-15	2,00,000	
	2015-16	2,00,000	
	2016-17	2,00,000	
		9,33,333	

1/5<sup>th</sup> of ₹ 9,33,333 = ₹ 1,86,667

<b>2. Interest for Previous year</b>	2,00,000
1 + 2	₹ 3,86,667

**2012 - Dec [5]** (a) Lalit submits the following details of his income for the assessment year 2018-19:

	₹
Income from salary	3,00,000
Loss from let-out house property	40,000
Income from sugar business	50,000
Brought forward loss of iron ore business (discontinued in financial year 2007-08)	1,20,000
Short-term capital loss	60,000
Long-term capital gains	40,000
Dividend	5,000
Income from lottery winnings ( <i>gross</i> )	50,000
Winnings in card games ( <i>gross</i> )	6,000
Agricultural income	20,000
Long-term capital gains from the shares ( <i>STT paid</i> )	10,000
Short-term capital loss from shares under section 111A	15,000
Bank interest	5,000

Calculate gross total income and losses to be carried forward.

(5 marks) [CSEPM - I]

Answer:

**Computation of Income of Lalit  
for the Assessment Year 2018-19**

	Salary	Business Income	Long-term capital gain	Income from other sources
	₹	₹	₹	₹
Salary	3,00,000	-	-	-
Business Income	-	50,000	-	-
Long term capital gain	-	-	40,000	-
Winning from lottery	-	-	-	50,000
Winnings from card games	-	-	-	6,000
Bank interest	-	-	-	5,000
<b>Total</b>	<b>3,00,000</b>	<b>50,000</b>	<b>40,000</b>	<b>61,000</b>
<i>Less: Current year losses</i>				
Loss from house property	40,000	-	-	-
Short term capital loss	-	-	40,000	-
Balance	2,60,000	50,000	-	61,000
<i>Less: Brought forward business loss</i>	-	50,000	-	-
<b>Net income (Total 3,21,000)</b>	<b>2,60,000</b>	<b>-</b>	<b>-</b>	<b>61,000</b>

The following losses will be carried forward:

1. Current year's short term capital loss of ₹ 60,000 is adjusted against long-term capital gain of ₹ 40,000. The unadjusted amount of ₹ 20,000 will be carried forward.
2. Short-term capital loss of ₹ 15,000 pertaining to transfer of securities (subject to STT) will be carried forward.
3. Brought forward loss of iron ore business is set off against the current year's business to the extent of ₹ 50,000. The unadjusted amount of ₹ 70,000 will be carried forward.

**Assumptions:**

- (i) Dividend is from an Indian company, therefore exempt.
- (ii) Agricultural income is generated in India, therefore exempt.

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**2013 - June [2]** (a) The net profit of Renuka Ltd., an Indian company, as per its profit and loss account prepared as per the Income-tax Act, 1961 is ₹ 90,00,000 after debiting and crediting following items:

	₹
Provision for income-tax	5,00,000
Provisions for deferred tax	3,00,000
Proposed dividend	7,50,000
Depreciation including depreciation on revaluation of assets	
₹ 20,00,000 debited to profit and loss account	60,00,000
Profit from industrial unit in SEZ area	80,000
Provision for permanent diminution in the value of investments	70,000
Compute tax liability under section 115JB for the assessment year 2018-19.	
	<b>(9 marks)</b>

**Answer:**

Computation of Tax Liability of Renuka Limited for Assessment Year 2018-19.

**(a) Computation of Book Profits :**

		₹
Net Profit as per Profit & Loss A/c		90,00,000
<i>Add:</i> Non-admissible expenditure :		
— Provision for Income-tax	5,00,000	
— Provision for Deferred tax	3,00,000	
— Proposed Dividend	7,50,000	
— Depreciation	60,00,000	
Provision for diminution	70,000	76,20,000
		1,66,20,000
<i>Less:</i> Inadmissible Incomes and Expenditure :		
Depreciation allowed		40,00,000
Book Profits		1,26,20,000

<b>(b) Computation of Tax liability under section 115 JB</b>	
Book Profit u/s 115 JB	1,26,20,000
18.5% of Book Profit	23,34,700
Add: Surcharge (as total income is exceed ₹ 1,00,00,000/-) hence surcharge is applicable @ 7%	1,63,429
Tax & Surcharge	24,98,129
Add: Education Cess & SHEC @ 3%	74,944
Tax liability u/s 115 JB (R/off)	25,73,073
Total Tax liability as per normal tax rates @ 3% of ₹ 1,26,20,000	37,86,000
Add: 7% Surcharge	2,65,020
+ Cess @ 3%	40,51,020
	1,21,530
Here, the tax liability as per MAT provision is less than the tax liability as per normal tax provisions, therefore the tax payable shall be ₹ 41,72,550.	41,72,550

**2013 - June [3]** (a) A limited liability partnership (LLP) has following income for the assessment year 2018-19: ₹

Profit from business eligible for deduction @ 100% of profits under section 80-IA	32,00,000
Profit from other business	48,00,000
Compute the tax payable by the LLP, assuming that it has no other income during the assessment year 2018-19.	<b>(5 marks)</b>

**Answer:**

(i) **Computation of Total Income and Income Tax Payable  
For Assessment Year 2018-19**

As per the normal provisions of the Act	₹
Profits & gains of business or profession (Total)	80,00,000
Less: Deduction under section 80-IA	<u>32,00,000</u>
Total Income	<u>48,00,000</u>
Tax payable @ 30%	14,40,000

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Add: EC @ 2% & SHEC @ 1%	43,200
Tax Payable	<u>14,83,200</u>

(ii) **Computation of Alternate Minimum Tax (AMT)**

	₹
Profits & Gains of business or profession	48,00,000
Add: Deduction under section 80IA	<u>32,00,000</u>
Adjusted Total Income	<u>80,00,000</u>
AMT @ 18.5%	14,80,000
Add: EC @ 2% & SHEC @ 1%	<u>44,400</u>
AMT Payable	<u>15,24,400</u>

Here, as per **Section 115JC**, since the income tax payable as per normal provisions of the Income Tax Act is less than the AMT, the LLP would be liable to pay ₹ 15,24,400 as tax.

**2013 - Dec [2]** (b) X Ltd. charged depreciation on its fixed assets at the rate prescribed in the income tax rules. However, the Assessing Officer disallowed the same and allowed the rate as prescribed in the Companies Act, 2013 for the purpose of computation of book profit under section 115JB for the previous year 2017-18. Examine the legality of action taken by the Assessing Authority. **(5 marks)**

**Answer:**

The action of the Assessing Officer is not sustainable in law. He has limited power to look into that the books of account have been properly maintained as per Indian **Companies Act, 2013**. He does not have the power to question the profit shown in the profit and loss account. This issue was settled by the Supreme Court in **Malayala Manorama Co. Ltd. v. CIT (2008) 300 ITR 251**. The Apex Court observed that for the purpose of computation of book profit under **section 115JB**, the Assessing Officer's power is restricted to examining whether the books of account are certified by the authorities under the Companies Act as having been properly maintained in accordance with the Companies Act. Thereafter, he only has the limited power of making additions and deductions as provided for in Explanation 1 to **Section 115JB**. The Assessing Officer does not have the jurisdiction to go behind the net profit shown in the profit and loss account except to the

extent provided in Explanation 1 to **Section 115JB**. Where an assessee is consistently charging depreciation in its books of account at the rates prescribed in Income-tax Rules and the accounts of the assessee have been prepared and certified as per the provisions of the Companies Act, the Assessing Officer does not have any jurisdiction under **section 115JB** to rework the net profit of the assessee by substituting the rates of depreciation prescribed under the Companies Act.

Applying the ratio of the Supreme Court decision to this case, it may be concluded that the action of the Assessing Officer is not correct.

**2013 - Dec [3]** (a) Comment in brief on allowability of following expenditure while computing the income under the head 'profits and gains of business or profession' for the assessment year 2018-19:

- (i) Kanha commenced operations of the business of setting-up a warehousing facility for storage of sugar on 1<sup>st</sup> June, 2017. He incurred capital expenditure on purchase of building during the period from January, 2017 to March, 2017 exclusively for the above business and capitalised the same in its books of account on 1<sup>st</sup> June, 2017.
- (ii) Ms. Radha incurred expenditure on purchase of computer software and capitalised such expenditure in her books of account.
- (iii) Murli is operating a pharmaceutical factory. he incurred expenditure in providing freebies to medical practitioners. **(3 marks each)**

**Answer:**

- (i) Deduction of 150% for A.Y. 2018-19 of the capital expenditure is available under **section 35AD** for Assessment year 2018-19 in respect of specified business of setting up and operating a warehousing facility for storage of sugar, if following conditions are fulfilled:
  - (a) Operations are commenced on or after 01-04-2016.
  - (b) If expenditure is incurred prior to the commencement of its operations wholly and exclusively for the specified business, and the amount is capitalised in the books of accounts of the assessee on the date of commencement of its operations; and
  - (c) Expenditure should not be incurred on acquisition of any land, goodwill or financial instrument.

Hence, 150% deduction will be allowed for capital expenditure incurred and capitalised, excluding the expenditure incurred on acquisition of land.

- (ii) The expenses incurred by assessee on purchase of computer softwares are revenue in nature in view of rapid advances and changes in technical know how.

Thus, such expenditure shall be allowable.

- (iii) As per Circular No. 5/2012, Dated 1-8-2012, some pharmaceutical and allied health sector industries are providing freebies (freebies) to medical practitioners and their professional associations in violation of the regulations issued by Medical Council of India (the 'Council') which is a regulatory body constituted under the **Medical Council Act, 1956**. The Claim of any expense incurred in providing above mentioned or similar freebies in violation of the provisions of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002 shall be inadmissible under **section 37(1)** of the Income Tax Act being an expense prohibited by the law.

This disallowance shall be made in the hands of such pharmaceutical or allied health sector Industries or other assessee which has provided aforesaid freebies and claimed it as a deductible expense in its accounts against income.

The sum equivalent to value of freebies enjoyed by the aforesaid medical practitioner or professional associations is also taxable as business income or income from other sources as the case may be depending on the facts of each case.

Thus, expenditure incurred by Murli in providing freebies to medical practitioners is disallowed.

**2014 - Dec [1]** (b) XYZ LLP has income of ₹ 72,00,000 under the head 'profits and gains of business or profession'. One of its business is eligible for deduction @ 100% of profits under section 80-IB for the assessment year



2018-19. The profit from such business included in the business income is ₹ 58,00,000. Compute the tax payable by the LLP, assuming that it has no other income during the previous year 2017-18. **(5 marks)**

(c) The book profits of a company in the previous year 2017-18 computed in accordance with section 115JB are ₹ 60,00,000. If the total income for the same period computed as per the provisions of the Income-tax Act, 1961 is ₹ 12,00,000, calculate the tax payable by the company in the assessment year 2018-19 and also indicate whether the company is eligible for any tax credit. **(5 marks)**

**Answer:**

(b) (i) Computation of Total Income and Income Tax Payable for Assessment Year 2018-19.

	₹
As per the normal provision of the Act Profits & Gains of business or Profession (Total)	72,00,000
<i>Less:</i> Deduction under section 80-IB	58,00,000
Total income	14,00,000
Tax payable @ 30%	4,20,000
<i>Add:</i> EC @ 2% SHEC @ 1%	12,600
Tax Payable	4,32,600

(ii) **Computation of Alternate Minimum Tax (Amount)**

	₹
Profits & Gains of business or profession	14,00,000
<i>Add:</i> Deduction under section 80 IB	58,00,000
Adjusted Total Income	72,00,000
AMT @ 18.5%	13,32,000
<i>Add:</i> EC @ 2% & SHEC @ 1%	39,960

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13,71,960

Here, as per **Section 115JC**, Since, the income tax payable as per normal provisions of the Income Tax Act is less than the AMT, the LLP would be liable to pay ₹ 13,71,960 as tax.

(iii)	Particulars	Amount (₹)
	<b>Computation of Alternate Minimum Tax (AMT)</b>	
	Adjusted Total Income (including profit u/s 80-IB)	72,00,000
	AMT on adjusted Total Income @ 18.5%	13,32,000
	Education Cess & SHEC @ 3% (2% + 1%)	39,960
	Total Tax	13,71,960
(iv)	<b>Tax payable (higher of AMT or Normal Tax)</b>	<b>13,71,960</b>
(v)	<b>Tax Credit</b>	<b>9,39,360</b>

**Note:**

*Since the regular income tax payable is less than AMT, the adjusted total income would be deemed to be the income of LLP and it would be liable to tax @ 18.5% plus cess. Further the LLP would be eligible for credit in 10 subsequent years to the extent of difference between the AMT and Normal Tax, in the year in which the tax payable under regular provisions exceeds the AMT.*

**Answer:**

**(c)**

**1. Calculation of tax liability u/s 115 JB:**

Particulars	Details	Amount
Book profit	Given	60,00,000
Tax liability	18.5% of 60 lakh	11,10,000
Add: Surcharge		NIL

Tax liability after surcharge	11,10,000
Add: Edu. cess & SHEC @ 3%	33,300
Tax liability after cess	<u>11,43,300</u>

**2. Calculation of tax liability as per Income Tax Act, 1961:**

Particulars	Details	Amount
Total income	Given	12,00,000
Tax liability	30% of 12 lakh	3,60,000
Add: Edu. cess & SHEC @ 3%		10,800
Tax liability after cess		<u>3,70,800</u>

**3. Computation of final tax payable:**

Particulars	Details	Amount
Tax liability	Tax liability u/s 115J B> Normal Tax liability	11,43,300
Actual Tax liability		11,43,300

The company is eligible for MAT tax credit of ₹ 7,72,500 (₹ 11,43,300 - ₹ 3,70,800) which can be carried forward for 10 years or is to be awaited within 10 years **u/s 115 JAA**.

**2014 - Dec [2A] (Or)** (a) You are the Financial Controller in a manufacturing company having turnover exceeding ₹ 800 crore. Write a report for your Managing Director highlighting the legal position pertaining to the following:

- (i) Tax on distributed income by a company for buy-back of unlisted shares.
- (ii) Time-limit for completion of assessment/ reassessment when a reference is made to the Transfer Pricing Officer (TPO).
- (iii) Allowance for acquisition and installation of new plant and machinery under section 32AC.
- (iv) Tax consequences of assignment of keyman insurance policy before maturity by employer-company to its employee. **(15 marks)**

**Answer:**

- (i) A company, having distributable reserves, has two options to distribute

the same to its shareholders either by declaration and payment of dividends to the shareholders or by way of purchase of its own shares (i.e. buy back of shares) at a consideration fixed by it. In the first case, the payment by company is subject to DDT and income in the hands of shareholders is exempt. In the second case the income is taxed in the hands of shareholder as capital gains.

Unlisted Companies, as part of tax avoidance scheme, are resorting to buy back of shares instead of payment of dividends in order to avoid payment of tax by way of DDT particularly where the capital gains arising to the shareholders are either not chargeable to tax or are taxable at a lower rate.

**In order to curb such practice the Act has amended the Act, by insertion of new Chapter XII-DA, to provide as under:**

**(1) Tax on distributed income to shareholders [Section 115QA]**

**(A) Additional income tax on buy back of shares [Section 115QA(1)]**

- (i) In addition to the income tax payable by the company on its total income as per the provisions of the Act, the domestic company shall be liable to pay additional income tax @ 20% on any amount of distributed income paid by the company on buy back of shares not being shares listed on a recognised stock exchange.
- (ii) Rate of additional income tax is 20%+12%SC+3%Cess i.e. 23.072%

**(B) Additional income tax payable even if the total income of domestic company is exempt [Section 115QA(2)]**

Notwithstanding that no income tax is payable by a domestic company on its total income computed in accordance with the provisions of this Act, the tax on the distributed income under **section 115QA(1)** shall be payable by such company.

**(C) Time limit for deposit of additional income tax [Section 115QA(3)]**

The principal officer of the domestic company and the

company shall be liable to pay the tax to the credit of the Central Government within 14 days from the date of payment of any consideration to the shareholders on buy back of shares referred to in **Section 115QA(1)**.

**(D) Additional income tax to be treated as final payment [Section 115QA(4)]**

The tax on the distributed income by the company shall be treated as the final payment of tax in respect of the said income and no further credit therefore shall be claimed by the company or by any other person in respect of the amount of tax so paid.

**(E) Income charged to tax not allowed as deduction [Section 115QA(5)]**

No deduction under any other provision of this Act shall be allowed to:

- (a) the company; or
- (b) a shareholder

In respect of the income which has been charged to tax under **section 115QA(1)** or the tax thereon.

**(2) Interest payable for delayed payment of tax [Section 115QB]**

Where the principal officer of the domestic company and the company fails to pay the whole or any part of the tax on the distributed income referred to in **Section 115QA(1)**, within the time allowed under **section 115QA(3)** of that section, he or it shall be liable to pay simple interest @ 1% for every month or part thereof on the amount of such tax for the period beginning on the date immediately after the last date on which such tax was payable and ending with the date on which the tax is actually paid.

**(3) When company is deemed to be assessee in default [Section 115QC]**

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If any principal officer of a domestic company and the company does not pay tax on distributed income in accordance with the provisions of **Section 115QA**, then, he or it shall be deemed to be an assessee in default in respect of the amount of tax payable by him or it and all the provisions of this Act for the collection and recovery of income tax shall apply.

**Exemption to the shareholder on account of buy back of shares [Section 10(34A)] [W.e.f. A.Y. 2014-15]**

Since, the company has to pay additional income tax on buy back of shares, any income arising to an assessee, being a shareholder, on account of buy back of shares (not being listed on recognised stock exchange), shall be exempt.

- (ii) Where a reference under **section 92CA(1)** is made, an order under **section 92CA(3)** may be made at any time before 60 days prior to the date on which the period of limitation referred to in **Section 153**, or as the case may be, in **Section 153B** for making the order of assessment or re-assessment or re-computation or fresh assessment, as the case may be, expires.
- (iii) The date of installation of machinery or plant costing more than ₹ 100 crores for investment allowance @ 15% **u/s 32AC** extended to 31.03.2018 and 15% shall also be allowed to any assessee who installed new asset of ₹ 100 crore or less but more than ₹ 25 crores in any previous year upto 31.03.2018.
- (iv) Where maturity amount is received by the legal heir on the death of employee under keyman insurance policy, then such amount is taxable as Income from other sources in the hands of recipient.

**2015 - June [1]** (a) Amar, an individual, resident of India, receives the following payments after TDS during the previous year 2017-18:

	₹
(i) Professional fees on 17.08.2017	2,40,000
(ii) Professional fees on 04.03.2018	1,60,000

Both the above services were rendered in Pakistan on which TDS of ₹ 50,000 and ₹ 30,000 respectively has been deducted. He had incurred an expenditure of ₹ 2,40,000 for earning both these receipts/income. His income from other sources in India is ₹ 3,00,000 and he has made payment of ₹ 70,000 towards LIC.

Compute the tax liability of Amar and also the relief under section 91, if any, for assessment year 2018-19. **(5 marks)**

**(b)** Apple Industries Ltd. provides the following information for the financial year 2017-18:

Net profit as per statement of profit and loss after debiting/crediting the following: ₹ 120 lakh

Proposed dividend ₹ 30 lakh

Profit from unit established in SEZ ₹ 20 lakh

Provision for income-tax ₹ 18 lakh

Provision for deferred tax ₹ 10 lakh

Provision for permanent diminution in value of investments ₹ 3 lakh

Depreciation debited to statement of profit and loss ₹ 10 lakh includes depreciation on revaluation of assets to the tune of ₹ 1 lakh

Brought forward losses and unabsorbed depreciation as per books of the company are as follows: (₹ in lakh)

Previous Year	Brought Forward Losses	Unabsorbed Depreciation
2013-14	1	4
2014-15	1	1
2015-16	10	5

Compute the book profit of the company as per Section 115JB for the assessment year 2018-19. **(5 marks)**

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**Answer:**

**(a) Computation of Tax Liability of Amar for Assessment Year 2018-19**

Particulars	Amount (₹)	
<b>Income under head Business &amp; Profession</b>		
Gross fees for services rendered in Pakistan on 17.08.2017	2,90,000	
Gross fees for services rendered in Pakistan on 04.03.2018	1,90,000	
Less: Expenditure incurred	(2,40,000)	2,40,000
Income from other sources	3,00,000	3,00,000
<b>Gross total Income</b>		<b>5,40,000</b>
Deduction u/s 80C		
Payment towards LIC	70,000	(70,000)
Total Income		4,70,000
Tax Liability		
Tax on first 2,50,000	Nil	
Tax on remaining 2,20,000@5%	11,000	
Cess @2%	220	
SHEC @ 1%	110	11,330
Tax Relief		(3,156)
Tax Payable		8,174
Rounded off		8,175



**Note:**

1. Gross professional fee = Payment after TDS + TDS  
 Thus, professional fee on 17.08.2017 = ₹ (2,40,000 + 50,000)  
 Professional fees on 04.03.2018 = ₹ (1,60,000 + 30,000)
2. Tax Relief u/s 91  
 Income for services rendered in Pakistan taxed in India  
 = (2,40,000 + 50,000 + 1,60,000 + 30,000) - 2,40,000  
 = ₹ 2,40,000  
 Income assessed in Pakistan  
 = (2,40,000 + 50,000 + 1,60,000 + 30,000)  
 = ₹ 4,80,000  
 Tax paid in Pakistan = (50,000 + 30,000) = ₹ 80,000  
 (i) Tax on double taxed Income in India  
 = (20,600 × 2,40,000/4,70,000)  
 = ₹ 10,519  
 (ii) Tax on double taxed Income in Pakistan  
 = (80,000 × 2,40,000/4,80,000)  
 = ₹ 40,000  
 Tax relief u/s 91 will be lower of (i) or (ii)  
 Tax relief = ₹ 10,519

**(b) Computation of Books Profits of Apple Industries Ltd.  
for FY 2017-18**

Particulars	Amount (₹ in lakhs)	
	Net profit as per P & L A/c	120
Add:		
Proposed dividend	30	
Provision for Income Tax	18	
Provision for deferred Tax	10	
Provision for permanent diminution in value of investments	3	

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Depreciation debited to P/L statement	10	71
Less:		
Depreciation (excluding dep. on revaluation)	9	
Aggregate unabsorbed depreciation (4+1+5)	10	(19)
Book Profit U/s 115JB		172

**Note:** Since, unabsorbed depreciation is less than brought forward losses, unabsorbed depreciation is taken.  
Profit from unit established in SEZ is not deductible.

**2015 - June [2A] (Or)** (i) (a) Tinoo Ltd. is eligible to claim deduction of ₹ 2 crore under section 80-IA. It has filed its return of income after the due date as specified in Section 139(1). Discuss the allowability of deduction under section 80-IA. **(2 marks)**

**(b)** Sahil sold a residential house on 15<sup>th</sup> March, 2018 to Neeraj for ₹ 30 lakh of which value applied by stamp valuation authority was ₹ 38 lakh. Sahil purchased this house in March, 2007 for ₹ 12 lakh but the stamp duty value of the same was ₹ 15 lakh. In the context of these transactions, compute the following —

(i) Income out of this transaction, if any, in the hands of Neeraj.

(ii) Cost of acquisition to Neeraj. **(2 marks)**

**(c)** An HUF, resident in India, has a gross total income of ₹ 5,40,000 for the assessment year 2018-19. It made a payment of ₹ 50,000 for life insurance premium of one of its members. Whether the HUF is entitled to claim the rebate as per Section 87A? **(1 mark)**

**Answer:**

**(a)** No deduction shall be allowed to the assessee unless he furnishes a return of his income of the relevant assessment year on or before the due date specified under **section 139(1)**.

**(b)** (i) In order to prevent tax avoidance by transferring immovable property at prices significantly lower than the circle rates **Section 56 (2)(vii)**

has been amended with effect from Assessment Year 2015-16 to provide that where any immovable property is received for a consideration which is less than the stamp duty value of the property by an amount exceeding fifty thousand rupees the difference between the stamp duty value and the consideration shall be chargeable to tax in the hands of the individuals or HUF as “Income from other sources.”

(a) In this case, Sahil has sold the residential house to Neeraj at ₹ 30 lakhs whereas the stamp value ₹ 38 lakhs thus the difference amount i.e. ₹ 8 lakhs would be chargeable as income from other sources in the hands of Neeraj.

(b) As per the provisions of **Section 49(4)** the cost of acquisition of residential property in the hands of Neeraj shall be taken as ₹ 38 lakhs.

(ii) Cost of acquisition is the price which the purchaser has paid. Therefore, the cost of acquisition to Neeraj is ₹ 30 lakh.

(c) No. Rebate under section 87A is available only in the case of a resident individual if his/her taxable income is ₹ 3,50,000 or less.

**2015 - Dec [1]** (a) Jatin submits the following information relevant for the assessment year 2018-19:

	₹
Short-term capital gains	1,25,000
Income from owning and maintaining race horses	20,000
Income from units of mutual fund	17,000
Long-term capital gains in respect of buildings	7,000
Business profits	14,000
The following items have been brought forward:	
Long-term capital loss in respect of assessment year 2015-16	30,000
Brought forward business loss from assessment year 2016-17	15,000

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Brought forward loss from the activity of owning and maintaining race horses from the assessment year 2014-15 27,000  
 Speculation losses of the assessment year 2015-16 35,000  
 Calculate the gross total income of Jatin for assessment year 2018-19.

**(5 marks)**

**(c)** Alfa Ltd., a domestic company purchased its own unlisted shares on 4<sup>th</sup> July, 2017. The consideration for buy-back amounting to ₹ 10.50 lakh was paid on the same day. The amount received by the company two years back for issue of such shares was ₹ 6.5 lakh. The Assessing Officer has issued a notice to tax the gains on shares to which company denies. State the correctness of the contention of Assessing Officer and also compute the tax payable, if any. Also, compute the amount of interest, if any, payable by company assuming that the tax due is paid to the credit of the Central Government on 29<sup>th</sup> September, 2017.

**(5 marks)**

**Answer:**

**(a) Computation of Gross total Income of Mr. Jatin for the Assessment Year 2018-19:**

Particulars	Amount in (₹)	Amount in (₹)
A. Profits and Gains of Business & Profession		
Business Profits	14,000	
Less: B/F Business Loss from the AY 2015-16	(15,000)	
Loss to be C/F to next Year	(1,000)	
B. Capital Gains		
Short-term Capital Gains	1,25,000	
Long-term Capital Gains	7,000	
Less: B/F Long-Terms Capital Loss from AY 2014-15	(30,000)	
Loss to be C/F to next Year	(23,000)	1,25,000

C. Income From Other Sources			
Income from owning and maintaining Race Horses	20,000		
Less: B/F Loss from owning and maintaining Race horses from AY 2013-14	27,000		
Balance loss cannot be C/F as the limit of 4 Years expired with this AY	(7,000)		
B/F Speculative losses from the AY 2014-15	(35,000)		
Less: Speculative Incomes	-		-
Speculative losses carried forward	(35,000)		
D. Gross Total Income			1,25,000

(c) As per **Section 115QA** of the **Income Tax Act, 1991**, any amount of distributed income by the company on buy-back of shares (not being shares listed on a recognised stock exchange) from a shareholder shall be charged to tax.

Further, such company shall be liable to pay additional income-tax at the rate of 20% on the distributed income.

Thus, the contention of the Assessing Officer relating to taxability of the resulting from the buy back of shares is correct.

#### Computation of Tax Payable by Alfa Ltd.

Particulars	Amount (in ₹)
Consideration for Buy Back	10,50,000
Consideration received for issue of shares	(6,50,000)
Distributed Income	4,00,000
Additional Tax @ 20%	80,000
Surcharge @ 12%	9,600
Cess & SHEC @ (2% + 1%)	2,688
Total Tax Payable	92,288

The above tax should be paid on or before 18<sup>th</sup> July, 2017.

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However, it was paid on 29<sup>th</sup> September, 2017.

Thus, for this delay interest is payable @ 1% per month for each month in whole or part. Therefore, interest is payable for 3 months.

$$\begin{aligned}\text{Interest} &= ₹ (92,288 \times 1/100 \times 3) = ₹ 2,768.64 \\ &= ₹ 2,769\end{aligned}$$

**2016 - June [1]** (a) A company wants to raise capital of ₹ 40,00,000 for a project wherefrom earnings before tax would be 30% of the capital employed. The company can raise debt finance @ 12% p.a.

The following three alternatives for raising capital are available for the company:

- (i) ₹ 40,00,000 by equity capital
- (ii) ₹ 20,00,000 by equity capital and ₹ 20,00,000 by loans
- (iii) ₹ 8,00,000 by equity capital and ₹ 32,00,000 by loans.

Assume that the company would distribute the entire amount of profits as dividend. The tax rate is 30.9% and dividend distribution tax rate is 20.358%. Work out which one of the above three alternatives should the company opt to minimise its tax liability? **(5 marks)**

**(c)** Comment with reasons on the taxability or otherwise of the following incomes for the year ended on 31<sup>st</sup> March, 2018 as per the Income-tax Act, 1961:

- (i) Akhil, a not ordinarily resident, earned ₹ 65,000 from a business in Australia when he was in Australia. Later the profits were remitted to India.
- (ii) Birender, an ordinarily resident and a financial consultant, received a fee of ₹ 50,000 from an Indian company carrying on business in Canada for the services rendered there. The fee was directly deposited in a bank in Canada.
- (iii) Chandan, an ordinarily resident, earned agricultural income of ₹ 25,000 from land in England. He spent the entire income for his son's education in India.
- (iv) Dinesh, a citizen of India, got employment in Burma. He left India on 1<sup>st</sup> September, 2016 after earning ₹ 5,00,000 in India. He earned

₹ 7,00,000 in Burma during the previous year.

- (v) Girish, a resident, brought to India, his income earned in 2012-13 in Sri Lanka which was not taxed in Sri Lanka. **(5 marks)**

**Answer:**

**(a)**

Analysis of total tax liability of the Company under various financing options.

Particulars	Amount in ₹		
	Option 1	Option 2	Option 3
Share capital	40,00,000	20,00,000	8,00,000
Debt @ 12%	–	20,00,000	32,00,000
Total capital	40,00,000	40,00,000	40,00,000
PBIT (Expected Rate of Return @ 30% of total Capital Employed)	12,00,000	12,00,000	12,00,000
Less: Interest on Loan @ 12%	–	(2,40,000)	(3,84,000)
Profit Before Tax	12,00,000	9,60,000	8,16,000
Less: Tax @ 30.9% on PBT (a)	(3,70,800)	(2,96,640)	(2,52,144)
Net Profit After Tax	8,29,200	6,63,360	5,63,856
Dividend Distribution Tax @ 20.358% (b)	1,68,808	1,35,047	1,14,790
Total Tax liability			
Income Tax (a)	3,70,800	2,96,640	2,52,144
Dividend Distribution Tax (b)	1,68,808	1,35,047	1,14,790
Total tax liability (a+b)	5,39,608	4,31,687	3,66,934

As the tax liability is minimum in option 3, therefore company should go for option 3.

**Answer:**

- (c)** (i) Akhil, a not ordinarily resident have to pay taxes in Australia, due to income earned in Australia.
- (ii) **Taxable in India:** An individual, qualifying as resident and ordinarily resident in India would be liable to pay tax on his/ her Global Income. Therefore, the fee of ₹ 50,000 received by Mr. Birender from an Indian company carrying on business in Canada for the services rendered

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there would be chargeable to tax in India.

- (iii) **Taxable in India:** An individual, qualifying as resident and ordinarily resident in India would be liable to pay tax on his / her Global Income. Therefore, the agriculture income of ₹ 25,000, from a land in England, would be taxable in India. Further Mr. Chandan may be eligible to claim deduction with respect to the expenditure incurred for his son's education in India subject to the provisions of Section 80C of the Income tax Act, 1961.
- (iv) As Dinesh, Citizen of India, has left India for the purpose of employment outside India, present in India for less than 182 days during the previous year and therefore qualifying as non-resident 'NR' in India. Accordingly, he would be liable to pay tax on source based income in India. Therefore, Income of ₹ 5,00,000 earned in India would only be taxable in India. Income of ₹ 7,00,000 earned outside India i.e. in Burma would not be taxable in India.
- (v) **Not Taxable in India:** Since, the Income accrued and received during the year 2012-13 and not during the previous year i.e. 2011-12 and therefore not taxable in India during the previous year i.e. 2011-12. Further, the subsequent remittance of the fund to India would not deemed to be received in India.

**2016 - June [2A] (Or)** (ii) From the following information, determine the tax payable under section 115-O by a domestic company on the dividend distributed by it where the rate of dividend distribution tax is 20.358%:

- It received dividend of ₹ 5,00,000 on 20<sup>th</sup> November, 2017 from its subsidiary company which paid dividend distribution tax under section 115-O.
- It distributed dividend of ₹ 33,00,000 on 14<sup>th</sup> December, 2017 to its shareholders.
- Out of ₹ 33,00,000, the company paid dividend of ₹ 3,00,000 to a person on behalf of the New Pension System Trust. **(3 marks)**

**Answer:**

(₹)

Net dividend on which DDT is payable	
Amount of dividend to be distributed to shareholders	33,00,000



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Less: Dividend received from subsidiary company on which DDT has already paid	5,00,000
	28,00,000
Less: The company paid dividend to a person on behalf of the New Pension System Trust	3,00,000
Net dividend liable to pay	25,00,000
Computation of DDT	
<b>Alternative I</b>	
₹ 25,00,000 × 20.358% (effective rate)	5,08,950
<b>Alternative II</b>	
₹ 25,00,000 × 100/85	
Gross amount of ₹ 29,41,176	
DDT payable on ₹ 29,41,176 @ 17.304%	5,08,941

**Note:** There is a nominal difference between Alt I and Alt II, therefore, any can be paid.

**2016 - Dec [1]** (a) Global Ltd. is a widely-held company engaged in power generation in Assam. At present, the company is having a capital of ₹ 10 crore in fully paid equity shares. The company is considering a proposal to increase its power generation capacity which will require ₹ 5 crores. The additional capital required can be raised either by issue of fully paid equity shares or by issue of 10% debentures. Directors of the company want to raise the funds through equity shares as the company can have fully owned capital. Will you accept the proposal at 20% rate of return (pre-tax) and 30% rate of tax? Give reasons in support of your answer. **(5 marks)**

**(c)** Brisk Ltd. incurred ₹ 52.75 lakhs during the period April, 2017 to June, 2017 on advertisement, professional fees, administration cost, etc. for the purpose of public issue of ₹ 555 crores in July, 2017 and had, therefore, accounted all such expenses under the head 'share issue

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expenses'. However, the clearance for the public issue was not given by SEBI. The company in its return of income filed for the year ended 31<sup>st</sup> March, 2018 had claimed such expenses as revenue expenses which were disallowed by the Assessing Officer.

The company seeks your opinion. Advise.

**(5 marks)**

**Answer:**

**(a) Computation of Expected Rate of Return on Capital Employed**

Particulars	Amount in (₹)	
	(Proposal I) Issue of Equity Shares	(Proposal II) Issue of 10% Debenture
Equity Share Capital	1,50,000,000	1,00,000,000
10% Debenture	—	50,000,000
Total Capital Employed	15,00,00,000	15,00,00,000
PBIT (Expected Rate of Return @ 20% of total Capital employed)	3,00,00,000	3,00,00,000
Less: Interest on Debenture @ 10%	—	(50,00,000)
Profit Before Tax	3,00,00,000	2,50,00,000
Less: Tax @ 30% on PBT	(90,00,000)	(75,00,000)
Net Profit After Tax	2,10,00,000	1,75,00,000
Expected Rate of Return to Share Holders	14.00%	17.50%

**Conclusion:** The proposal of deriving additional capital by issuing fully paid up equity shares is not acceptable as it will give lesser rate of return to share holders in future. Therefore, it is beneficial to raise the additional funds through the issue of 10% debentures as it will increase the rate of return to shareholders from 14% to 17.50%.

**(c) MASCON TECHNICAL SERVICES LTD. V. CIT (Madras High Court):**

**Share issue expenses cannot be allowed as revenue expenditure even when shares could not be issued due to non-approval by SEBI:**

In the instant case the assessee incurred expenditure for issuing shares. However, on account of non-clearance from the SEBI, shares could not be issued. It claimed deduction for share issue expenses as revenue expenditure by contending that since the expenditure did not yield any

desired result, the character of the expenditure had to be decided on the basis of the result that would yield benefit in assessee's business. The Assessing Officer and the CIT (A) disallowed such expenses. The Tribunal also affirmed the view of the Assessing Officer. Aggrieved assessee filed the instant appeal.

**The High Court held in favour of revenue as under:**

- The impugned expenses were incurred by the assessee for the purpose of widening its capital base. The assessee, admittedly, took steps to go in for public issue and after incurring expenditure, just before the public issue, by reason of the orders from the SEBI, the assessee could not go in for public issue. Thus, the efforts were aborted.
- There was no justifiable ground to accept the plea of the assessee that on account of the abortive efforts, the expenditure incurred would lose its character as capital expenditure for the purpose of allowing it as a revenue expenditure.

**2016 - Dec [2]** (a) Explain in brief the treatment as to the taxability and/or allowability, in the context of provisions contained under the Income-tax Act, 1961 for the assessment year 2018-19, in the following cases:

- (i) Aroma Ltd., an investment company, received dividend of ₹ 3,00,000 on equity shares from listed domestic companies. It paid interest of ₹ 2,00,000 on the borrowed funds utilised for making investment in such shares of these companies.
- (ii) Chetan Ltd. did not have any active business carried on by it during the previous year ended on 31<sup>st</sup> March, 2018 and had incurred capital expenditure on scientific research amounting to ₹ 2,00,000 related to its subsidiary company. **(5 marks)**

**Answer:**

- (i) The dividend income earned by Aroma Ltd. on the shares held as investment is exempt under the provisions of Section 10(34). As per Section 14A, no expenditure is allowable in respect of income which does not form part of total income. The interest paid on borrowed capital is an expenditure incurred in respect of shares purchased for investment. Since the dividend income received on shares is exempt

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and does not form part of total income of Aroma Ltd., the interest expenditure is not allowable as deduction in view of Section 14A. [The quantum of disallowance must be in accordance with Rule 8D of the Income-tax Rules, 1962.]

- (ii) **As per Section 35(1)(iv)**, deduction in respect of capital expenditure on scientific research would be admissible under the provisions of **Section 35(2)** only if the scientific research relates to the business carried on by the assessee.

However, in the given case, Chetan Ltd., did not have any active business carried on by it to which the said scientific research related to. The capital expenditure incurred by Chetan Ltd. related to its subsidiary company. Therefore, Chetan Ltd. is not eligible for deduction under the provisions of **Section 35(1)(iv) read with Section 35(2)**.

**2016 - Dec [2A] (Or)** (i) Mohan owns a house located in Varansi. The construction of the house was completed in July, 2013. One-fourth floor area of the house is utilised by him for his own residence. He is running his own clinic in another one-fourth floor area of the house. The remaining floor area is let-out for residential purposes on a monthly rent of ₹ 8,000.

The let-out portion of the house remained vacant for two months during the previous year 2017-18. Other details of the entire house are as under:

	₹
Standard rent	1,60,000
Municipal valuation	1,40,000
Municipal tax paid by Mohan	20,000
Interest payable on loan taken for construction of the house	60,000
Repairs and maintenance	8,000
Insurance	4,000
Compute income from house property of Mohan for the assessment year 2018-19.	<b>(5 marks)</b>

- (ii) Arvind, a textile merchant and resident Indian is doing business in India and abroad. During the previous year 2017-18, he disclosed the following information:

	₹
Income from business in India	27,00,000
Income from business in Country-A with which India does not have agreement for avoidance of double taxation	15,00,000
Income-tax levied by government in Country-A	5,00,000
Loss from business in Country-B with which also India does not have agreement for avoidance of double taxation	(4,00,000)
Contribution to public provident fund	1,50,000
Payment of life insurance premium on the life of his father and mother	20,000

Compute the tax liability of Arvind for the assessment year 2018-19.

**(5 marks)**

- (iii) Nandita Traders, engaged in manufacturing activity, was in receipt of sales-tax subsidy of ₹ 5 lakh from State Government as its manufacturing unit was located in a backward area. The subsidy is related to the sales of its products and was payable only after the commencement of production. Nandita Traders claimed that the subsidy so received is in the nature of capital receipt and hence, cannot be taken as chargeable to tax for the assessment year 2018-19. How will you deal with the situation in the context of provisions of the Income-tax Act, 1961?

**(5 marks)**

**Answer:**

(i)

**Computation of Income from House Property of Mohan for the AY 2018-19**

Particulars	Amount in (₹)
Annual Value of 1/4 portion used for his own profession	Nil

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Annual Value of $\frac{1}{4}$ portion used for his own residence	Nil	
Less: Municipal Taxes	Nil	
Net Annual Value	Nil	
Less: Interest on Borrowing ( $\frac{1}{4} \times ₹ 60,000$ )	(15,000)	
Loss from house property (Self Occupied)		(15,000)
Gross Annual Value of let-out portion ( $₹ 8,000 \times 10$ )	80,000	
(a) Expected Rent = Fair Rent or Municipal Value whichever is higher subject to Standard Rent i.e. $₹ 1,40,000/2 = 70,000$		
(b) Gross Annual Value = Expected Rent or Actual Rent whichever is higher i.e. $₹ 70,000$ or ( $₹ 8,000 \times 10$ ) = $₹ 80,000$		
Less: Municipal Tax ( $₹ 20,000 \times \frac{1}{2}$ )	(10,000)	
Net Annual Value	70,000	
Less: Standard Deduction (Section 24b) ( $₹ 70,000 \times 30\%$ )	(21,000)	
Less: Interest on Borrowing ( $₹ 60,000 \times \frac{1}{2}$ )	(30,000)	
Income from let out house property		19,000
<b>Income under the head house property</b>		<b>- 4,000</b>

**Note :** Expenses on Repair and Maintenance and Insurance would not be allowed as deduction in computing the income under the head house property.

**(ii) Computation of Taxable Income of Mr. Arvind for assessment year 2018-19:**

	(₹)	(₹)
Income from business in India		27,00,000

Income from business in country A	15,00,000	
Loss from business in country B	4,00,000	11,00,000
Gross Total Income		38,00,000
Less: Deduction under Sec. 80C		
Public provident fund	1,50,000	
Life Insurance premium	20,000	
	1,70,000	
Max. Relief permissible		(1,50,000)
Tax on total income		36,50,000
Tax Liability on first ₹ 2,50,000 - NIL		
₹ 2,50,001 - ₹ 5,00,000 - 5%		12,500
₹ 5,00,000 - ₹ 10,00,000 - 20%		1,00,000
Balance @ 30% (₹ 26,50,000 × 30%)		7,95,000
Total Tax (excluding EC & SHEC)		9,07,500
Education Cess & SHEC @ 3%		27,225
Total Tax		9,34,725
Relief under section 91 (Note 1)		(3,84,150)
Tax payable in India		5,50,575

**Note 1****Computation of Relief under section 91 of the Income Tax Act, 1961**

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Average rate of Tax in India ₹ (9,34,725/36,50,000 × 100) = 25.6089%  
Average rate of tax in foreign country (5,00,000/15,00,000 × 100) = 33.33%  
Doubly Taxed Income 15,00,000  
Relief under section 91 (on ₹ 15,00,000 @ 25.61%) i.e. rate 25.6089% or 30% whichever is lower 3,84,150

(iii) Section 4 brings to charge tax on total income *prima facie* in order to come within the scope of the charging provisions. The receipt in question should normally be a revenue receipt. Capital receipt are normally exempt. However capital receipt has been specifically included in the definition of income as under:

Assistance in the form of subsidy or grant or cash incentive or duty drawback or waiver or concession or reimbursement (by whatever name called) by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee other than:

- (a) The subsidy or grant or reimbursement which is taken into account for determination of the actual cost of the asset in accordance with the provision of explanation 10 to clause (1) of Section 43; or
- (b) The subsidy or grant by the Central Government for the purpose of the corpus of a trust or institution established by the Central Government or a State Government as the case may be.

Therefore, Nandita Traders, can't be exempted and will be chargeable to tax for the assessment year 2018-19.

**2017 - June [2] (b)** How will you decide the residential status of the following companies or firms for the Previous Year 2017-18 under the provisions of Income Tax Act, 1961? Give brief reasons for your answer:

- (i) XYZ Pharma Ltd., a company registered in India under the Companies Act, 2013.
- (ii) PQR Ltd., a company incorporated in Germany, of which the control and management of the affairs of the business is situated wholly in India.
- (iii) SVR Ltd., a French company of which the control and management of



- the affairs of the business is situated wholly outside India in Sapin.
- (iv) ABC Ltd., a company incorporated in Australia, of which the control and management of the affairs of the business is situated partly outside India and partly in India.
  - (v) PCR & Co., a partnership firm is doing its business activities in Chennai, India. All the meetings of the partners during the year for decision-making took place in Singapore and Malaysia. **(5 marks)**

**Answer:**

As per the provision of **Section 6(3)** of the Income tax Act, **1961** for the Financial Year 2017-18. All Indian companies within the meaning of **Section 2(26)** of the Act are always resident in India regardless of the place of control and management of its affairs. Further, in the case of a foreign company, for the FY 2017-18, the place of control and management of its affairs is the basis on which the company's residential status is determinable. Accordingly a company shall be said to be resident in India in any previous year, if:

- (i) it is an Indian company; or
- (ii) the control and management of its affairs is wholly situated in India.
  - (a) XYZ Pharma Ltd., a company registered in India under the Companies Act, 2013 is an Indian company and therefore is always resident in India.
  - (b) PQR Ltd., a company incorporated in Germany, of which the control and management of the affairs of the business is situated wholly in India. As the control and management of the affairs of the business of PQR Ltd. is situated wholly in India and accordingly PQR Ltd. shall be a resident in India.
  - (c) SVR Ltd., a French Company, of which the control and management of the affairs of the business is situated wholly in Spain. As the control and management of the affairs of the business of SVR Ltd. is situated wholly in Spain and accordingly SVR Ltd. shall be a non-resident company.

- (d) ABC Ltd., a company incorporated in Australia, of which the

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control and management of the affairs of the business is situated partly outside India and partly in India. As the control and management of the affairs of the business of ABC Ltd. is situated partly outside India and partly in India and accordingly ABC Ltd. shall be a non-resident company.

- (e) The Partnership firm is non-resident in India, if control and management of its business affairs is wholly situated outside India as per **Section 6(2)** of the Income tax Act, 1961. Accordingly, PCR & Co. shall be non-resident in India.

**2017 - June [2A] (Or)** (iii) The profit and loss account of XYZ Ltd. for the year ended 31-3-2018 showed a net profit of ₹ 80,00,000 after making of the following adjustments:

- (a) Depreciation ₹ 24 lakh (including depreciation on revaluation of assets of ₹ 4 lakh).  
(b) Provisions for unascertained liabilities ₹ 2 lakh.  
(c) Transfer to General Reserve ₹ 9 lakh.  
(d) Agricultural Income ₹ 15 lakh.  
(e) Amount transferred to profit and loss account from general reserve ₹ 3 lakh. Brought forward business losses and unabsorbed depreciation as per books of accounts were ₹ 15 lakh and ₹ 11 lakh respectively.

Compute book profits and Minimum Alternate Tax (MAT) under section 115JB payable by XYZ Ltd. for A.Y. 2018-19. **(5 marks)**

**Answer:**

**Computation of Book Profit of XYZ Ltd. under section 115JB**

	₹	₹
Net profit as per profit and loss account		80,00,000
<i>Add:</i>		
Transfer to General Reserve	9,00,000	
Provision for unascertained liabilities	2,00,000	
Depreciation	<u>24,00,000</u>	<u>35,00,000</u>
		<b>1,15,00,000</b>

Less:

Amount transferred from reserve and credited to profit and loss account	3,00,000	
Depreciation (excluding revaluation)	20,00,000	
Agriculture Income [Exempt under section 10(1)]	15,00,000	
Loss brought forward (₹ 15 lakhs) or unabsorbed depreciation (₹ 11 lakhs) as per books, whichever is less	<u>11,00,000</u>	49,00,000
<b>Book Profit for computation of MAT under section 115JB</b>		<b><u>66,00,000</u></b>

**Computation of Minimum Alternation Tax (MAT)  
under section 115JB**

	₹	₹
18.50% of book profit (18.50% of ₹ 66 lakh)		12,21,000
Add: Education Cess @ 2%	24,420	
SHEC @ 1%	<u>12,210</u>	36,630
Minimum Alternate Tax payable under section 155JB		<u>12,57,630</u>

**2017 - Dec [1]** (a) Discuss the taxability or otherwise of the following income in the context of provisions contained under the Income Tax Act, 1961:

- (i) Agricultural Income of ₹ 2,50,000 earned by Ms. Divita, a non resident from land in Barmer in Rajasthan.
- (ii) Amount of ₹ 7,00,000 withdrawn by Mr. Rajesh, a resident individual, from Public Provident Fund as per relevant rules.
- (iii) Mr. Abhiman received ₹ 1,30,000 on 31.03.2018 towards maturity proceeds of the insurance policy issued on 1.04.2014. The annual premium and capital sum assured are ₹ 23,000 and ₹ 1,20,000 respectively.
- (iv) Mr. Dinesh received ₹ 3,60,000 as partner share of profit in the income of limited liability partnership.
- (v) ₹ 2,50,000 received by Mr. Rohan from Central Government as compensation on account of disaster taken place in Utrakhand.

**(1 mark each)**

**Answer:**

- (i) Agriculture Income is totally exempt as per **[Sec. 10(1)]**, if land is situated in India.
- (ii) Any payment from a provident fund to which the Provident fund Act, 1925 applies or from any other provident fund set-up by the Central Government and notified by it in this behalf shall be exempt. Public Provident Fund Scheme 1968 has since been notified under this cause vide notification No. 502430, dated 02.07.1968. as per **[Sec. 10(11)]**.
- (iii) If the premium payable during any previous year for a policy issued on or after 01.04.2012 exceeds 10% / 5%, of the actual capital sum insured, the entire amount received under such policy shall be taxable **[Sec. 10(10D)]**.  
However, the above provision shall not apply to any sum received on the death of a person.  
Therefore, in the said question Mr. Abhiman will be taxed.
- (iv) In case of a person being a partner of a firm (including LLP), his share in the total income of the firm or LLP shall be exempt from tax. **[(Sec. 10(2A))]**.  
However, profit will be taxed in the hands of LLP.
- (v) Any amount received or receivable from the Central Government or a State Government or a local authority by an individual or his legal heir by way of compensation on account of any disaster shall be exempt. **[Sec. 10(10BC)]**.

**2017 - Dec [1]** (b) Work out the taxable income and the tax payable thereon for A. Y. 18-19 of a partnership firm engaged in retail trade business from the following particulars:

- (i) Net profit of ₹ 3,65,000 arrived at after debit of interest on capital of partners of ₹ 1,80,000 and salaries paid to the working partners of ₹ 4,80,000.
- (ii) Total capital of the partners on which interest paid as debited in the

profit and loss account was ₹ 10,00,000.

- (iii) Both the payments of interest on capital and the salary to the working partners have been authorised by the deed. **(5 marks)**

**Answer:**

**Computation of taxable income of the firm for A.Y. 2017-18**

	₹	₹
Net profit as per profit and loss account		3,65,000
Add: Interest on capital	1,80,000	
Less: 12% of capital i.e. ₹ 10,00,000	<u>1,20,000</u>	<u>60,000</u>
Salaries to Partners		<u>4,80,000</u>
Book Profits		9,05,000
Less: Salary allowed (See note below)		<u>4,80,000</u>
<b>Total Income</b>		<u>4,25,000</u>
<b>Note:</b> On first ₹ 3,00,000 of book profits – 90% on ₹ 1,50,000 whichever is more		2,70,000
Next ₹ 6,05,000 of book profit – 60%		<u>3,63,000</u>
		<u>6,33,000</u>
Actual Salary paid to ₹ 4,80,000		
<b>Tax Payable –</b>		₹
<b>Total Income</b>		<u>4,25,000</u>
Tax @ 30% on ₹ 4,25,000		1,27,500
Add: Education Cess @ 2%		2,550
SHEC @ 1%		<u>1,275</u>
Total Tax Liability		<u>1,31,325</u>

**2017 - Dec [2]** (a) Discuss the deductibility or otherwise of the following expenditure incurred by Sumit Agro Industries, while computing its business

income for the year ended 31.03.2018.

- (i) Land & Building acquired for scientific research related to the business in September, 2017 for ₹ 22,50,000 consisting of cost of land ₹ 9,50,000 and balance for building. **(2 marks)**
- (ii) Contribution to the account of employees as per pension scheme referred to in Section 80CCD amounted to ₹ 35,00,000. Amount above 10% of the salary of employees in ₹ 5,80,000. **(2 marks)**
- (iii) Tax on non-monetary perquisites provided to the employees and borne by the employers of ₹ 4,50,000. **(1 mark)**

**Answer:**

- (i) As per **section 35(1)(iv) read with section 35(2)**, if any capital expenditure (other than expenditure on acquisition of land) is incurred on scientific research related to the business carried on by the assessee, the whole of such capital expenditure is allowable as deduction in the previous year in which it is incurred.  
Therefore, ₹ 13,00,000 (i.e. ₹ 22,50,000 – ₹ 9,50,000 being the cost of land) is allowable as deduction for the AY 2017-18.
- (ii) The employer's contribution to the account of an employee under a pension scheme referred to in section 80CCD, is allowable as deduction under Section 36(1)(iva) while computing business income only upto 10% of salary of the employee in the previous year. Accordingly, ₹ 29,20,000 would be allowed as deduction under section 36(1)(iva).  
Disallowance under section 40A(9) would be attracted only in respect of the amount in excess of 10% of salary. Therefore, ₹ 5,80,000 would be disallowed as per section 40(A)(9).
- (iii) The income chargeable under the head 'Salaries' of an employee below sixty years of age inclusive of all perquisites is ₹ 4,50,000 out of which, ₹ 50,000 is on account of non-monetary perquisites as per provision.

**2017 - Dec [2A] (Or)** (i) Mr. Bewaja, grows sugarcane and uses the same for the purpose of manufacturing sugar in his factory. 35% of the sugarcane produce is sold for ₹ 20 lacs and the cost of cultivation of such sugarcane is

₹ 7 lacs. The cost of cultivation of the balance sugarcane (65%) is ₹ 13 lacs and the market value of the same is ₹ 35 lacs. He after incurring ₹ 3.5 lacs in the manufacturing process on the balance sugarcane, sold the sugar for ₹ 45 lacs. Is he liable to tax on any income for A. Y. 2018-19 and if, yes, compute the taxable income and the agricultural income? **(5 marks)**

**Answer:**

Sugarcane is an agricultural produce and therefore, income from the sale of sugarcane gives rise to pure agricultural income.

However, in case of cultivation of sugarcane and use of sugarcane to manufacture sugar, the income would be partly business and partly agricultural. As per Rule 7 of the Income-tax Rules, 1962, taxable business income would be computed after deducting market value of any agricultural produce utilised as a raw material in such business, and no further deduction shall be made in respect of any expenditure incurred by the assessee as a cultivator or receiver of rent-in-kind.

The relevant workings as under:

**Business Income:** Sales – Market Value of 65% of sugarcane produce – manufacturing expenses.

45 lakhs – 35 lakhs – 3.5 lakhs = 6.5 lakhs

**Agriculture Income:** Market Value of sugarcane produce – Cost of cultivation of the sugarcane

= [20 lakhs + 35 Lakhs] – [7 lakhs + 13 Lakhs]

= 55 lakhs – 20 lakhs

= 35 lakhs

**2017 - Dec [2A] (Or)** (ii) Define the term 'Mat Credit' under section 115 JAA of the Income Tax Act. And also calculate the tax payable by the company in the assessment year 2018-19, if the book profits of a company in the previous year 2017-18 computed in accordance with Section 115 JB is ₹ 20 Lakhs. The total income computed for the same period as per the provisions of the Income Tax Act, is ₹ 7.5 Lakhs. You are also required to indicate whether the company is eligible for any tax credit. **(5 marks)**

**Answer:**

**Mat Credit:**

**Section 115JAA** provides that where any amount of tax is paid under **Sec. 115JB(1)** by a company for any assessment year beginning on or after 1.4.2008, credit in respect of the taxes so paid for such assessment year shall be allowed on the difference of the tax paid under **Section 115JB** and the amount of tax payable by the company on its total income computed in accordance with the other provisions of the act.

**Mat Credit shall be computed as under:**

Mat credit available = Tax paid under **Section 115JB** – Tax payable on the total income under normal provision of the act.

However, no interest shall be allowed on the amount of tax credit available under **Section 115JAA**.

**Computation of tax payable in the A.Y. 2017-18**

	(₹)
(A) Total Income	7,50,000
(B) Book Profit	20,00,000
(C) Tax on (A) (30.9% of ₹ 7,50,000)	2,31,750
(D) Tax on (B) (19.055% of ₹ 20,00,000)	3,81,100
(E) Difference between C and D	<u>1,49,350</u>
(F) MAT credit available	<u>1,49,350</u>

**2018 - June [1]** (a) (ii) An assessee has purchased a car for business purposes on 10<sup>th</sup> June, 2016 for ₹ 10 lakhs. This is the only asset in the block of assets. In the previous years 2016-17 and 2017-18, 25% of the usage of car was for personal purposes. What is the depreciation allowable for the assessment year 2018-19? You may take the rate of depreciation as 15%.

**(2 marks)**

**2018 - June [1]** (a) (iii) Vikas, a resident in India, has received divided of ₹ 13 lakhs from A Ltd., an Indian company, on which the company has paid DDT under section 115-O of the Income-Tax Act, 1961. He has incurred expenditure of ₹ 1 lakh for earning such dividend. What is the tax payable by him in respect of such dividend income?

**(2 marks)**

**2018 - June [2]** (a) Shakshitha Pvt. Ltd., furnishes the following summarized



position of its profit and loss account and pertinent additional information thereto, for the year ended 31-3-2018:

(All amounts are ₹ in lakhs)

(i) Net profit as per books		26
(ii) Share income from an AOP		6
Expenditure debited in books for earning such income		0.8
(iii) Provision for income-tax		2
(iv) CSR expenditure debited to P & L Account		14
(v) Royalty received relating to business (Chargeable at 10%)		6
(vi) The brought forward business loss and depreciation are as under:		
	<b>As per books</b>	<b>As per IT Act</b>
Business loss for AY 2017-18	4	12
Depreciation	3	11
(vii) The members as well as their shares in the AOP in which Shakshitha Pvt. Ltd. is a member, are specific and determinate.		
(viii) In the current year, the depreciation charged as per books is the same as that of the one allowable as per Income-Tax Act, 1961, before considering the provisions of section 32(2).		

Compute the book profits of the company and the tax on book profits under section 115JB for the AY 2018-19.

The company is not an Ind-As compliant company

(5 marks)

**2018 - June [2]** (c) From the following particulars relating to Mrs. Sridevi for the assessment year 2018-19, compute the deduction available under Chapter VI-A of the Income-Tax Act, 1961:

Gross total income	₹	11,90,000
Above includes the following:		
Short-term capital gains from sale of listed shares	50,000	
Long-term capital gains from sale of vacant site	1,50,000	
Winnings from crossword puzzles (gross)	90,000	

**Other information:**

Contribution to PPF

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in the name of son, a software engineer	80,000
Stamp paper and registration expenses relating to residential house purchased during the year	85,000
Donation to National Defence Fund	40,000
Donation given to Bhhodhan Charitable Trust recognised for section 80G purposes	80,000
	<b>(5 marks)</b>

**2018 - June [2A] (Or)** (ii) On 11.5.2017, Rama Ltd. purchased its own shares having face value of ₹ 10. Amount offered to shareholders was ₹ 80 per share. Total amount distributed by Rama Ltd. on buy back of 15,000 shares is ₹ 13,50,000. These shares were issued in the year 2004-05 at a premium of ₹ 15. Kaka one of the shareholder holding 1,500 shares (cost of acquisition ₹ 25 per share, year of acquisition 2007-08) got ₹ 1,35,000. Determine tax consequences in the hands of Kaka (Shareholder) and Rama Ltd. under section 115QA for AY. 2018-19, assuming shares are unlisted.

**(5 marks)**

**TOPIC NOT YET ASKED BUT EQUALLY IMPORTANT FOR EXAMINATION**

**Salary and Allowances**

**Q.1** J, a citizen of India, employed in The Indian Embassy at Tokyo, Japan. He received salary and allowances at Tokyo from the Government of India for the year ended 31.03.2018 for services rendered by him in Tokyo. Besides, he was allowed perquisites by the Government. He is a non-resident for the assessment year 2018-19. Examine the taxability of salary, allowances and perquisites in the hands of J for the assessment year 2018-19.

**Answer:**

As per **Section 9(I)(iii)**, salaries payable by the Government to a citizen of

India for services rendered outside India shall be deemed to accrue or arise in India. As such, salary received by J is chargeable to tax even though he is a non-resident for A.Y. 2018-19.

As per **Section 10(7)**, all allowances or perquisites paid or allowed as such outside India by the Government to a citizen of India for rendering services outside India is exempt from tax.

Therefore, the allowances and perquisites received by J are exempt as per **Section 10(7)**.

**Q.2** Mr. Kadam is entitled to a salary of ₹ 25,000 per month. He is given an option by his employer either to take house rent allowance or a rent free accommodation which is owned by the company. The HRA amount payable was ₹ 5,000 per month. The rent for the hired accommodation was ₹ 6,000 per month at New Delhi. Advise Mr. Kadam whether it would be beneficial for him to avail HRA or Rent Free Accommodation. Give your advice on the basis of "Net Taken Home Cash Benefits."

**Answer:**

**Computation of tax liability of Kadam under both the options:**

Particulars	Option I HRA (₹)	Option II RFA (₹)
Basic Salary (₹ 25,000 × 12 months)	3,00,000	3,00,000
Perquisites value of rent free accommodation (15% of ₹ 3,00,000)	NA	45,000
House Rent Allowance (₹ 5,000 × 12 months) ₹ 60,000		
Less: Exempt u/s 10(13A) least of the following		
- 50% of Basic Salary	<u>1,50,000</u>	
- Actual HRA	60,000	
- Rent less 10% of salary	<u>42,000</u>	
	18,000	
Income taxable under the head "Salaries"	3,18,000	3,45,000

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Less: Deduction under chapter VI A	–	–
	3,18,000	3,45,000
Tax on total income	3,400	4,750
Less: Rebate u/s 87A (Since, total income is less than ₹ 3,50,000)	2,500	2,500
	900	2,250

**Cash Flow Statement**

Particulars	Option I – HRA	Option II – RFA
Inflow: Salary	3,60,000	3,00,000
Less: Outflow: Rent paid	(72,000)	–
Tax on total income	Nil	Nil
Net Inflow	2,88,000	3,00,000

Since, the net cash inflow under option II (RFA) is higher than in option I (HRA), it is beneficial for Mr. Kadam to avail option II, i.e., Rent Free Accommodation.

**Q.3** Explain in brief about the treatment to be given in the following case under the Income Tax Act, 1961, for A.Y. 2018-19:

Pankaj, a salaried employee, received from his employer medical allowance of ₹ 12,000 and reimbursement of ₹ 16,000 on account of medical facilities.

**Answer:**

The medical allowance of ₹ 12,000 received by Pankaj from his employer shall be chargeable to tax under the income from salary as per **Section 17(1)**.

However, according to Clause (V) of proviso to **Section 17(2)**, out of reimbursement of ₹ 16,000 on account of medical facilities an amount of

₹ 15,000 will be exempt and only the balance of ₹ 1,000 will be the chargeable value of perquisites.

**Q.4** Ranjit has taken an interest free loan of ₹ 10 lacs from his company. The amount is utilized by him for purchasing a house on 30.06.2016. The house is self occupied. As per the scheme of the company, loan would be recovered in 40 equal monthly installments recoverable immediately after completion of 18<sup>th</sup> month from the date of purchase. Assuming the SBI lending rate of similar loan on 01.04.2017 was 9.75%. Calculate the perquisite value of such loan in the hands of Ranjit for the assessment year 2018-19, is it possible to get deduction of perquisite value of interest under section 24(b)? Does it make any difference, if the house is given on rent?

**Answer:**

First installment will be due on 1<sup>st</sup> January 2018. Amount of installment will be ₹ 10,00,000 ÷ 40 = ₹ 25,000

Therefore, value for perquisite for interest free loan will be calculated by applying the interest rate charged by the State Bank of India on the first day of the relevant previous year on the outstanding amount of loan as reduced by the interest, if any, actually paid by the employee.

Therefore, the value of perquisites will be as follows:

		₹
From April 17 to Dec 17	$10,00,000 \times 9.75\% \times 9/12$	73,125
For the m/o Jan 18	$9,75,000 \times 9.75\% \times 1/12$	7,922
For the m/o Feb 18	$9,50,000 \times 9.75\% \times 1/12$	7,719
For the m/o Mar 18	$9,25,000 \times 9.75\% \times 1/12$	7,516
	Total	96,282

Therefore, the perquisite value of interest free loan will be ₹ 96,282.

Interest on capital borrowed for the purchase, construction, re-construction, repair or renewals of house property is deductible under **section 24(b)**. In this case, capital is borrowed from the employer without interest. There is no interest paid or payable in respect of the amount of loan of ₹ 10 lacs. Consequently, no deduction under **section 24(b)** would be available,

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whether the house is self occupied or let out.

**House Property**

**Q.5** How do you deal with the following issue under the respective provisions of the Income Tax Act, 1961?

The assessee who was deriving income from 'house property' realized a sum of ₹ 52,000 on the account of display of advertisement hoarding of various concerns on the roof of the building. He claims that this amount should be considered under the head "house property" and not under "other sources".

**Answer:**

The question came up for consideration before the Calcutta High Court in ***Mukherjee Estate (P) Ltd. v CIT (2000) 244 ITR I***. It was decided that the assessee let out the roof for advertisement for hoarding and that the income cannot be considered as income from house property as hoarding do not form part of the building. Such, income is chargeable under the head "income from other sources".

**Capital Gain**

**Q.6** Explain in brief about the treatment to be given in the following case under the Income Tax Act, 1961 for the A.Y. 2018-19:

A farmer (resident of Jaipur) sold his rural agricultural land situated in Nepal and received Indian rupees 2 lacs over the cost of acquisition of this land.

**Answer:**

The definition of capital assets under **section 2(14)**, specifically excludes rural agricultural land in India. Therefore, it follows that if such land is situated outside India, it would fall within the definition of capital assets under **section 2(14)**. Accordingly, capital gains on sale of rural agricultural land

situated in Nepal would be subject to tax in the hands of the farmer, since he is a resident in India.

**Q.7** A shareholder of demerged Indian Company received listed shares from the resulting company in the scheme of demerger. The shareholder want to transfer the said shares received subsequent to the demerger for consideration. Your advice is sought on the tax consequences as to the shares received on demerger and sought to be transferred.

**Answer:**

As per the provisions of the **Section 47(vid)** any transfer or issue of shares by the resulting company to the shareholders of the demerged company in a scheme of demerger is not regarded as transfer for the purpose of capital gains under **section 45** if the transfer is made in consideration of the demerger of the undertaking.

As a consequence of the demerger, the existing shareholders of the demerged company will receives shares in a resulting company. When the shareholder subsequently intends to transfer the said shares, the cost of such shares will have to be arrived at as per the provisions of **Section 49(2c)**. According to the said provision the cost of acquisition of shares in the resulting company will be the amount which bears to the cost of acquisition of shares held by the assessee in the demerged company, the same proportion as the net book value of the assets transferred in a demerger bears to the net worth of the demerged company immediately before such demerger.

As per the provisions of **Section 2(42A)(g)**, for determining the period of holdings of such shares, the period for which shares of the demerged company was held by the assessee would also be considered.

If the listed shares are held for more than one year and transferred through a recognized stock exchange and securities transaction tax has been paid on such sale, the long-term capital gain arising there from would be exempt under **section 10(38)**. If the total holding period does not exceed one year, then the short-term capital gains arising on sale of such shares would be taxable @ 15% under **section 111A**.

**Income from Other Sources**

**Q.8** Dhaval is in business of manufacturing customized kitchen equipments. He is also the Managing Director and held nearly 65% of the paid up share capital of Aarav (P) Ltd. A substantial part of the business of Dhaval is obtained through Aarav (P)Ltd. for this purpose, Aarav (P) Ltd. passed on the advance received from its customer to Dhaval to execute the job work entrusted to him.

The Assessing officer held that the advance money received by Dhaval is in the nature of loan given by Aarav (P) Ltd. to him and accordingly is deemed dividend within the meaning of provisions of Section 2(22)(e) of the Income Tax Act, 1961. The assessing officer, therefore, made the addition by treating advance money as the deemed dividend income of Dhaval.

Examine whether the action of the Assessing Officer is tenable in law.

**Answer:**

As per **Section 2(22)(e)** in case a company, not being a company in which the public are substantially interested, makes payment of any sum by way of advance or loan to a shareholder holding not less than 10% of voting power/share capital of the company then, the payment so made shall be deemed to be dividend in the hands of such shareholder to the extent to which the company possesses accumulated profits.

In the present case Dhaval is holding 65% of the paid-up capital of Aarav (P) Ltd. has passed on advance received from its customer to Dhaval for execution of job work entrusted to Dhaval.

Since Aarav (P) Ltd. is not a company in which public are substantially interested, the applicability of the provisions of **Section 2(22)(e)** in respect of such transaction has to be examined in **CIT V Rajkumar (2009) 318 ITR 462 (Del.)**, it was held that trade advance given to the shareholder which is in the nature of money transacted to give effect to a commercial transaction, would not be deemed to be dividend in the hands of the shareholder under **section 2(22)(e)**. The Delhi High Court ruling in **CIT v Ambassador Travels (P/Ltd. (2009) 318 ITR 376** also support the above view).



In the present case, the payment is made to Dhaval by Aarav (P) Ltd. for execution of work is in the course of commercial transaction and therefore, it shall not be deemed as dividend in the hands of Dhaval under **section 2(22)(e)**. Hence, the action of Assessing Officer is tenable in law.

**Q.9** M N Q Ltd. is a company in which the public are not substantially interested. K is the shareholder of the company holding 15% of the equity shares. The accumulated profits of the company as on 31.03.2017 amounted to ₹ 10,00,000. The company lent ₹ 1,00,000 to K by an account payee bank draft on 1.10.2017. The loan was not connected with the business of the company. K repaid the loan to the company by an account payee bank draft on 30.03.2018. Examine the effect of the borrowal and repayment of the loan by K on the computation of his total income for the assessment year 2018-19.

**Answer:**

As per **Section 2(22)(e)**, any payment made by a company in which the public are not substantially interested, by way of advance or loan to the shareholder being a person who is the beneficial owner of shares holding not less than 10% of the voting power shall be treated as dividend to the extent to which the company possesses accumulated profits.

In The instant case MNQ Ltd., is a company in which public are not substantially interested. The company has accumulated profits of ₹ 10,00,000 on 31.03.2017. The loan given by the company to K was not in the course of business. K holds more than 10% of the equity shares in the company. Therefore assuming that K has voting power equivalent to his shareholding **Section 2 (22)(e)** comes into play and the sum of ₹ 1,00,000 representing the amount lent by the company to K, is includible as dividend in the total income of K for the assessment year 2018-19.

Under **section 2 (22)(e)** the liability arises the moment loan is borrowed by the shareholder and it is immaterial whether the loan is repaid before the end of the accounting year or not. Therefore the repayment of loan by K to the company on 30.03.2018 will not affect the taxability of the sum of ₹ 1,00,000

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as dividend in his hands.

**Q.10** Parimal Managing Director of Heavens Engineering Pvt. Ltd., holds 70% of its paid up capital of ₹ 20 lacs. The balance as at 31.03.2017 in general reserves was ₹ 6 lacs. The company on 1.07.2017 gave an interest - free loan of ₹ 5 lacs to its supervisor having salary of ₹ 4,000 p.m. who in turn on 15.08.2017 advanced the said amount of loan so taken from the company to Shri Parimal. The assessing officer had taxed the amount of advance in the hands of Parimal. Is the action of Assessing officer correct?

**Answer:**

The company had advanced a loan to an employee who in turn had advanced the same to the Managing Director of the company holding 70% of the capital. By virtue of the provisions of **Section 2 (22)(e)**, the same shall be treated as the payment by a company in which public are not substantially interested on behalf of, or for individual benefit of any such share holder (who holds not less than 10% of the voting power), to the extent to which the company possesses accumulated profits.

In this case the company has reserve of ₹ 6 lacs on 31<sup>st</sup> March, of the preceding year and the amount of loan advanced on 15<sup>th</sup> July 2017 is ₹ 5 lacs. Therefore the payment is to be treated as deemed dividend. The amount of interest free loan of ₹ 5 lacs given by the company to the supervisor who in turn had given the same to Mr. Parimal shall be construed as the amount given for the benefit of Mr. Parimal and is treated as deemed dividend chargeable to tax in the hands of Mr. Parimal. This has been held by the Supreme Court in the Case of **L. Alagsunderam Chettiar V CIT (2001) 252 ITR 893**.

**Assessment of Companies**

**Q.1** XYZ Limited's Profit & Loss Account for the period ended 31<sup>st</sup> March, 2018 shows a net profit of ₹ 75 lacs after debiting/crediting the following items:

- (i) Depreciation ₹ 24 lacs (including ₹ 4 lacs on revaluation).

- (ii) Interest to financial institution not paid before due date of filing return of income ₹ 6 lacs.
- (iii) Provision for doubtful debts ₹ 1 lac.
- (iv) Provision for unascertained liabilities ₹ 2 lacs.
- (v) Transfer to General Reserve ₹ 5 lacs.
- (vi) Net-Agricultural Income ₹ 6 lacs.
- (vii) Amount withdrawn from Reserve created during 2014-15 ₹ 3 lacs. (Book profit was increased by the amount transferred to such reserve in Assessment year 2016-17).

**Other information:**

Brought forward loss and unabsorbed depreciation as per books are ₹ 12 lacs and ₹ 10 lacs, respectively.

Compute minimum alternate tax under section 115JB for A.Y. 2018-19.

**Answer:****Computation of Book Profit of XYZ Limited under section 115JB:**

Particulars	₹	₹
Net profit as per profit and loss account		75,00,000
<i>Add:</i> Net profit to be increased by the following amounts as per explanation 1 to Section 115JB		
Transfer to General Reserve	5,00,000	
Provision for unascertained liabilities	2,00,000	
Provision for doubtful debts	1,00,000	
Depreciation	24,00,000	32,00,000
		1,07,00,000

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Less: Net profit to be reduced by the following amount as per explanation 1 to Section 115JB		
Amount transferred from reserve and credited to profit and loss account (since the book profit was increased by the amount transferred to such reserve in the assessment year 2016-17)	3,00,000	
Depreciation (excluding revaluation )	20,00,000	
Net Agricultural Income [exempt under section 10(1)]	6,00,000	
Loss brought forward (₹ 12 lacs) or unabsorbed depreciation ( ₹ 10 lacs) as per books, whichever is less	10,00,000	39,00,000
Book profit for computation of MAT under section 115JB		68,00,000

**Computation of Minimum Alternate Tax (MAT) under section 115JB:**

Particulars	₹	₹
18.50% of Book Profit (18.50% of ₹ 68 lacs)		12,58,000
Add: Education cess @ 2%	25,160	
Secondary & higher education cess @ 1%	12,580	37,740
Minimum Alternate Tax payable under section 115JB		<b>12,95,740</b>

**Note:** Explanation 1 to **Section 115JB** does not require adjustment of interest not paid before due date of filing return of income while computing book profit.

**Q.2** XYZ Private Limited is engaged in manufacture and sale of ceramic tiles. The net profit of the company as per its profit and loss account for the year ended 31<sup>st</sup> March, 2018 is ₹ 150 lacs after debiting or crediting the following items:

- (i) One-time license fee of ₹ 20 lacs paid to people Ltd. (an Indian company) for obtaining franchise on 1<sup>st</sup> June, 2017.
- (ii) ₹ 29,000 paid A & Co. a goods transport operator, in cash on 31<sup>st</sup> January, 2018 for carrying company's product to the warehouse.
- (iii) Rent of ₹ 6 lacs received from letting out a part of its premises. Municipal tax in respect of the said part of the building is ₹ 15,000 remains unpaid due to court litigation.
- (iv) ₹ 2 lacs, being contribution to a university approved and notified under section 35(1)(ii).
- (v) ₹ 3 lacs being loss due to destruction of machinery caused by a fire due to short circuit. The Insurance company did not admit the claim of the company.
- (vi) ₹ 5 lacs paid to contractor for repair work at the company's factory. No tax was deducted on such payment.
  
- (vii) Dividend of ₹ 0.10 lac from P Ltd. on 1,000 equity shares of ₹ 10 each purchased at ₹ 100 per share on 10<sup>th</sup> October, 2017. The rate of dividend declared is 100% the record date being 10<sup>th</sup> December, 2017. The share were sold on 1<sup>st</sup> March, 2018 at ₹ 80 per share. Loss of ₹ 0.20 lac has been debited to Profit & Loss Account.
- (viii) Depreciation on tangible fixed assets ₹ 1.10 lacs.

**Additional Information:**

- (i) Depreciation on tangible fixed assets as per Income tax Rules ₹ 1.75 lacs.
- (ii) The company has obtained a loan of ₹ 2 lacs from ABC Private Limited in which it holds 16% voting rights. The accumulated profits held by ABC Private Limited on the date of loan was ₹ 0.50 lac.

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Compute total income of XYZ Private Limited for the assessment year 2018-19 indicating reasons for treatment of each item.  
Ignore the provisions relating to minimum alternate tax.

**Answer:**

**Computation of total income of XYZ Private Ltd. for the year 2018-19:**

Particulars	₹	₹
Income from House Property (Note 1)		
Gross Annual Value (GAV) (Rental income has been taken as GAV in the absence of other information)	6,00,000	
Less: Municipal taxes (not deductible since it has not been paid)	Nil	
Net Annual Value (NAV)	6,00,000	
Less: Deduction under section 24(30% of NAV)	1,80,000	4,20,000
<b>Profits and gains of business or profession:</b>	1,50,00,000	
Net profit as per profit & Loss account		
Add: Licence fee for obtaining Franchise (Note 2)	20,00,000	
Municipal taxes in respect of let-out part of office premises (Note 1)	15,000	
Contribution to approved and notified university (treated separately) (Note 4)	2,00,000	
Loss due to destruction of machinery by fire (Note 5)	3,00,000	
Amount paid to contractor without deduction of tax at source @ 30% of ₹ 5 lacs (Note 6)	1,50,000	
Short term capital loss on sales of shares of P Ltd. (Note 7)	20,000	

Depreciation on tangible fixed assets (Note 8)	1,10,000	
	1,77,95,000	
Less: Depreciation under section 32 (Note 8) 1,75,000 Intangible assets (Franchise) 25% of ₹ 20,00,000 (Note 2) 5,00,000	6,75,000	
Weighted deduction under section 35(1)(ii) (Note 4) ₹ 2,00,000 X 150% (Contribution of University)	3,00,000	
Rental income to be taxed under income from house property (Note 1)	6,00,000	
Dividend credited to Profit & Loss account to be excluded (Note 7)	10,000	1,62,10,000
Capital Gain (Note 7) short term capital loss (₹ 20 × 1000 share)	20,000	
Less: Dividend exempt under section 10(34)	10,000	
Short term capital loss to be carried forward to A.Y. 2019-20 Income from other sources	10,000	
Deemed dividend under section 2(22)(e) (Note 9)		50,000
<b>Total Income</b>		<b>1,62,60,000</b>

**Notes:**

- Rental income from letting out a part of the office premises is taxable under 'income from house property'. Therefore, it has to be deducted while calculating business income since the income has been credited to profit & loss account. Likewise municipal taxes due in respect of such property, debited to profit & loss account has to be added back to compute business income.*

*There is an alternate view that rental income from letting out part of the excess premises by an assessee who is engaged in business is only exploitation of the commercial asset by an assessee who is*

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*engaged in business and hence, the same constitutes business income only. In such case also municipal taxes is not allowable as deduction since the same has not been paid on or before the due date of filing of return of income as required under **section 43B**.*

- 2. Franchise is an intangible asset eligible for depreciation @25%. Since one time licence fees of ₹ 20 lacs paid for obtaining franchise has been debited to profit and loss account, the same has to be added back. Depreciation @ 25% has to be provided in respect of the intangible asset since it has been used for more than 180 days during the year.*
- 3. ₹ 29,000 paid to A&Co., a goods transport operator in cash is deductible while computing business income, as the limit for disallowance under **section 40A(3)** would be attracted in case of payment to a transport contractor only when it exceeds ₹ 35,000. Since, it is already debited to profit and loss account, no further adjustment is required.*
- 4. Contribution to a University approved and notified under section 35(1)(ii) is eligible for a weighted deduction of 150%. Therefore, the contribution of ₹ 2 lacs debited to profit & loss account has been added back and ₹ 3.00 lacs (being 150% of ₹ 2 lacs) has been deducted while computing business income.*
- 5. Loss of ₹ 3 lacs due to destruction of machinery caused by fire is not deductible since it is capital in nature.*
- 6. Payment to contractor would attract disallowance @ 30% of the expenditure.*
- 7. As per **Section 94(7)**, where any person buys any shares within 3 months prior to the record date and sells such shares within 3 months after such date and the dividend received on such shares is exempt, then the loss arising out of such purchase and sale of shares shall be ignored to the extent of dividend income.*

₹



Loss on purchase and sale of shares (₹ 100 - ₹ 80) × 1000 shares	20,000
Less: Dividend exempt under section 10(34)	10,000
Short term capital loss	10,000

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

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

**Q.3** ABC Limited has claimed exemption on the income from long-term capital gains under section 54EC by investing in bonds of National Highway Authority of India within the prescribed time, in the computation of 'book profit' under section 115JB. The company claimed exclusion of long-term capital gains because of exemption available on it by virtue of Section 54EC. The Assessing Officer reckoned the book profit including long-term capital gains for the purpose of levy of

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minimum alternate tax payable under section 115JB.  
In the action of the Assessing Officer justified in law?

**Answer:**

The issue under consideration in this case is whether long-term capital gain exempted by virtue of **Section 54EC** can be included in the book-profit computed under **section 115JB** for levy of minimum alternate tax.

It may be noted that minimum alternate tax is attracted under **section 115JB**, on account of tax on total income being less than 18.5% of book profit. Chapter XII-B is a self contained code for computation of book profit. The net profit as per the profit and loss account for the relevant previous year prepared in accordance with Schedule III of the **Companies Act, 2013**, as increased/reduced by the specific adjustments provided for in Explanation I to **Section 115JB** would be the book profit for levy of MAT under **section 115JB**. Therefore, if an assessee has claimed exemption under **section 54EC** by investing in bonds of National Highway Authority of India within the prescribed time, the long-term capital gain so exempt would still be taken into account for computing book profit under **section 115JB** for levy of MAT. Since, Explanation I to **Section 115JB** does not provide for such deduction. As long as long-term capital gains are part of the profits included in the profit and loss account prepared in accordance with Schedule III of the **Companies Act, 2013**. Capital gains cannot be excluded unless provided under Explanation I to **Section 115JB**. It was so held by the Kerala High Court in **N.J. Jose and Co. Ltd. v ACIT (2010) 321ITR0132**.

Therefore, the action of Assessing Officer is justified in law.

**Q.4** ABC (P) Ltd. made a provision of ₹ 30 lacs for doubtful debts by debit to profit & loss account. The Assessing Officer while computing book profit under section 115 JB, wants to add back the provisions. Is the Assessing Officer justified in making such addition for computing book profit?

**Answer:**

Explanation (1) below **Section 115JB (2)** has been amended to provide that the net profit should be increased by inter alia, the amount set aside as provision for diminution in the value of any asset, if the same has been debited to profit and loss account, for computing the book profit.

Therefore, the Assessing Officer is justified in adding back the provisions of ₹ 30 lacs for doubtful debts while computing book-profit.

**Q.5** Yaman Limited is a company in which 60% of the shares are held by Piloo Limited. Yaman Limited declared a dividend amounting to ₹ 35 lacs to its shareholders for the financial year 2016-17 in its Annual General Meeting held on 10<sup>th</sup> July 2016. Dividend distribution tax was paid by Yaman Limited on 21<sup>st</sup> July, 2017. Piloo Limited declared an interim dividend amounting to ₹ 50 lacs on 15<sup>th</sup> October 2017.

Compute the amount of tax on dividend payable by Piloo Limited.

What would be your answer if 58% shares of Piloo Limited are held by Kafi Limited an Indian Company?

**Answer:**

As per **Section 115-O**, dividend distribution tax @ 17.304% (i.e. 15% plus surcharge @ 12% education cess @ 2% and SHEC @ 1%) is leviable on dividend declared, distributed or paid by a domestic company. As per Schedule 115-O (1A) a holding company receives dividend from its domestic subsidiary company can reduce the same from dividend declared, distributed or paid by it. The dividend from its domestic subsidiary company should be received in the same financial year in which the holding company declare distributes or pays the dividend. Further, the dividend shall not be considered for reduction more than once.

The conditions to be fulfilled for this purpose are as follows:

- (1) The domestic subsidiary company should have paid the dividend distribution tax which is payable on such dividend;
- (2) The recipient holding company should be a domestic company.

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For this purpose, a holding company is a company which holds more than 50% of the nominal value of equity shares of another company.

**Section 115-O(1B)** provides that for the purposes of determining the tax or distributed profits payable in accordance with **Section 115-O**, any amount by way of dividends referred to in **Section 115-O(1)**, as reduced by the amount referred to in **Section 115-O (1A)** [referred to as net distributed profits], shall be increased to such amount as would after reduction of the tax on such increased amount at the rate specified in **Section 115-O(1)**, be equal to the net distributed profits.

On the basis of the aforesaid provisions dividend distribution tax payable by Piloo Limited shall be computed as follows:

Particulars	₹ in lacs
Dividend distributed by Piloo Ltd.	50
<i>Less:</i> Dividend received from subsidiary Yaman Ltd. (60% of ₹ 35 lacs)	21
Net distributed profits	29
<i>Add:</i> Increase for the purpose of grossing up of dividend $29 \times 100/85 = 34.12 - 29.00$	5.12
Gross dividend	34.12
Additional income-tax payable by Piloo Ltd. u/s 115-O [15% of ₹ 34.12 lacs]	5.12
<i>Add:</i> Surcharge @ 12%	0.61
	5.73
<i>Add:</i> EC @2% and SHEC @ 1%	0.17
	5.90

In order to remove the cascading effect of DDT in a multiplier corporate structure, **Section 115-O** was amended by the **Finance Act, 2012**.

Accordingly in case any domestic company (Piloo Ltd. in this case) and such subsidiary company (Yaman Ltd.) Has paid the DDT as payable on such dividend, then, dividend distributed by the holding company (Piloo Ltd.) in the same year to the extent of dividend received from the subsidiary (Yaman Ltd.), shall not be subject to DDT under **section 115-O**, irrespective of whether the holding company (Piloo Ltd.) is a subsidiary of any other company (Kafi Ltd., in this case).

Therefore inspite of the fact that Piloo Ltd. is a subsidiary of Kafi Ltd. it can reduce the amount of dividend received from Yaman Ltd. for computation of dividend distribution tax. Therefore dividend distribution tax payable by Piloo Ltd. shall be 17.304% of ₹ 34.12 lacs (grossed up amount) i.e. ₹ 5.90 lacs.

### Limited Liability Partnership

- Q.1** (i) Who shall verify the return of income of a limited liability company?  
(ii) XYZ LLP is liquidated. What is the liability of partners of XYZ LLP in respect of its tax dues?  
(iii) PQR LLP has a profit of ₹ 500 lacs after charging interest on capital for P amounting to ₹ 15 lacs calculated at 15% p.a. as per the agreement, but before considering remuneration to partners. What is the maximum admissible amount of remuneration to partners assuming all the partners are working partners and remuneration is authorised by the LLP instrument?

**Answer:**

- (i) Under **section 140** in the case of Limited Liability Partnership (LLP), the return of income shall be verified by the designated partner. Where for any unavoidable reason such designated partner is not able to verify the return, or where there is no designated partner as such the return of LLP can be verified by any partner.
- (ii) **Section 167C** provides for the liability of partners of LLP in liquidation. In the case of liquidation of an LLP and where tax due from the LLP

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cannot be recovered, every person who was partner of the LLP at any time during the relevant previous year will be jointly and severally liable for payment of tax unless he proves that non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the LLP.

**(iii) Computation of maximum admissible remuneration to working partners:**

Particulars	₹ in lacs
Net profit before considering partner's remuneration	500
Add: Interest to partner, P in excess of 12% p.a. [ $₹ 15 \times 3/15$ ]	3
Book profit under section 40(b)	503
Maximum amount admissible as remuneration to working partners under section 40(b)	
On first ₹ 3 lacs of book profit 90%	2.70
On balance book profit i.e. ₹ 500 lacs at 60%	300.00
<b>Maximum admissible remuneration</b>	<b>302.70</b>

**Tax planning**

**Q.2** Explain the doctrine of form and substance in the context of tax planning?

**Answer:**

The following are certain principles enunciated by the courts on the question as to whether it is the form or substance of a transaction, which will prevail in income-tax matters.

**(i) Form of transaction is to be considered in case of genuine**

**transactions:** It is well settled that when a transaction is arranged in one form known to law it will attract tax liability whereas, if it is entered into in another form which is equally lawful it may not. Therefore, in considering whether a transaction attracts tax or not, the form of the transaction put through is to be considered and not the substance. However, this rule applies only to genuine transactions. [*CIT v. Motor and General Stores (P) Ltd. (1967) 66 ITR 692 (AP)*].

- (ii) **True legal relation is the crucial element for taxability:** It is open for the authorities to pierce the corporate veil and look behind the legal facade at the reality of transaction. The taxation authority is entitled as well as bound to determine the true legal relation resulting from a transaction. The true legal relation arising from a transaction alone determines the taxability of a receipt arising from the transaction [*CIT v. BM Kharvar (1969) 72 ITR 603(SC)*].
- (iii) **Substance (i.e. actual nature of expense) is relevant and not the form:**
  - (a) In the case of an expenditure, the mere fact that the payment is made under an agreement does not preclude the department from enquiring into the actual nature of the payment [*Swadeshi Cotton Mills Co. Ltd. v. CIT (1967) 63 ITR (SC)*].
  - (b) In order to determine whether a particular item of expenditure is of revenue or capital nature the substance and not merely the form should be looked into. [*Assam Bengal Cement Co. Ltd. v. CIT (1955) 27 ITR 34 (SC)*].

**Q.3** Specify with reason whether the following acts can be considered as (i) tax management; or (ii) tax planning; or (iii) tax evasion:

- (i) Mr. P deposits ₹ 1 lac in PPF account so as to reduce his total income from ₹ 3.40 lacs to ₹ 2.40 lacs.
- (ii) PQR Industries Ltd. installed an air conditioner costing ₹ 75,000 at the residence of a director as per terms of his appointment; but treats it as fitted in quality control section in the factory.  
This is with the objective to treat it as plant for the purpose of computing depreciation.

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- (iii) SQL Limited maintains register of tax deduction at source effected by it to enable timely compliance.
- (iv) R Ltd. issue a credit note of ₹ 90,000 for brokerage payable to Suresh, who is son of R, Managing Director of the company. The purpose is to increase his total income from ₹ 1,60,000 to ₹ 2,50,000 and reduce its income correspondingly.

**Answer:**

- (i) It is a case of tax planning, since depositing money in PPF and claiming deduction under **section 80C** is as per the provision of law.
- (ii) It is a case of tax evasion as the air conditioner fitted at residential place is furniture depreciable @ 10% whereas the rate of depreciation applicable for plant and machinery is higher. The wrong treatment unjustifiably increases the amount of depreciation and consequently, reduce profit.
- (iii) It is a tax management because maintaining register of payment subject to TDS helps in complying with the obligation under the **Income Tax Act, 1961**.
- (iv) Net effect of the transaction is reduction of tax liability of the company by improper means. The company is liable to tax at a flat rate of 30% whereas Suresh would not be liable to pay tax. Since his income does not exceed the basic exemption limit of ₹ 2,50,000. The issue of credit note to reduce the liability of company amounts to tax evasion.